Nassau County Interim Finance Authority

NIFA

REVIEW OF NASSAU COUNTY'S PROPOSED MULTI-YEAR FINANCIAL PLAN FISCAL 2012 – 2015

October 6, 2011

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INTERIM FINANCE AUTHORITY

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I. OVERVIEW

On September 16, 2011, the County submitted the Proposed Multi-Year Financial Plan, Fiscal 2012-2015 (the "Proposed Plan"), the first year of which is the Proposed Budget for FY 2012 (the "Proposed Budget"). The following discussion reflects our views of their submission.

The Proposed Plan recognizes that the County is in a fiscal crisis that will take many years to solve and requires multiple solutions. NIFA agrees.

Unfortunately, the County has not presented an adequate number of solutions that are realistic, reliable or sufficient to meet the crisis. For example, many initiatives rely on union concessions or legislative actions; others will undoubtedly be litigated.

The high degree of uncertainty and lack of strategic direction in the Proposed Plan, as well as the magnitude of tenuous gap closing initiatives, greatly concerns us as a Control Board monitoring the County's finances. Hence, we conclude that the Proposed Plan and its FY 2012 Budget do not meet the standards of prudence necessary for us to project budget balance.

BACKGROUND

NIFA's position on the Proposed Plan should come as no surprise. Similar concerns and findings were what led NIFA, on January 26, 2011, to (1) impose a control period based on the likelihood and imminence of a major operating funds deficit of more than one percent for FY 2011, and (2) direct the County Executive to submit a financial plan that was balanced in accordance with the requirements outlined by State law in the NIFA Act.

It wasn't until June 24, 2011, that the County Executive submitted to NIFA his Multi-Year Financial Plan (Update) Fiscal 2011-2014 (the "Midyear Plan"), which purported to reflect balance on a "budgetary basis of accounting," whereas the County is required by law to have a financial plan that is balanced according to Generally Accepted Accounting Principles ("GAAP"). The Update was the first four-year financial plan delivered to NIFA since the imposition of the control period.

Subsequent to submission of the Update, NIFA adopted a Staff Report on the Update, which showed that the County continued on a path that would not achieve the fiscal balance required by law in FY 2011, FY 2012 or in the Out-Years. Consequently, on July 14, 2011, NIFA adopted a resolution disapproving the County's Update and ordering the County to submit a revised Update with a prescribed format for FY 2012, including removal of questionable revenues or equivalent adjustments of $225 million for FY 2012.

On July 28, 2011, the County submitted to NIFA a revised Update containing the projected revenues already rejected by NIFA. On July 29, 2011, NIFA issued a statement that the County had ignored NIFA's direction to remove questionable revenues or make equivalent adjustments of $225 million for FY 2012.

Most recently, on September 2, 2011, the NIFA Board passed an additional resolution officially disapproving the July 28, 2011 revised Update. The resolution stated that the County had failed to comply with NIFA's specific directions to remove questionable revenues or make offsetting adjustments, and prescribed a format and supporting information for the Proposed Plan, which is the subject of this report.

To further assist the County in preparing its Proposed Plan, NIFA hired an outside consulting firm, Grant Thornton, to review County operations and make suggestions to the County. A comprehensive draft of the Grant Thornton report, which included suggestions for budgetary savings, was delivered to the County before its submission of the Proposed Plan.

While it appears from several entries in the Proposed Plan that the Grant Thornton report was carefully reviewed, many of the easiest remedies were not embraced. Therefore, it is surprising that the County incorporated over $100 million in labor related savings that would require the passage of novel legislation and/or the opening of collective bargaining agreements.

II. DISCUSSION OF FY 2011

Before examining the Proposed Plan we need to discuss the projected operating results for FY 2011 because they form the baseline for future years and, therefore, are paramount in our analysis of the County's revenue and expenditure assumptions for FY 2012 and the Out-Years.

FY 2011 RISKS

Our analysis of revenues and expenditures indicates that the County could end FY 2011 with an operating deficit of approximately $153 million and a significant related shortfall in cash resources. This estimate, which is consistent with the County Comptroller's estimates released on October 3, assumes that no other actions are taken to realize additional revenue or reduce spending during the final three months of the year. See "Projected FY 2011 Operating Results" table on the following page.

The projected year-end deficit is driven primarily by significant shortfalls in County revenues, which we estimate could be $134 million below budget. The major projected shortfalls include $48 million in unrealized revenue from red light camera violations and other traffic fines.

We are also concerned that failure to timely close on the proposed sales of County land and Mitchel Field leases would put a combined $47.5 million in expected cash proceeds at risk. Additionally, notwithstanding the successful execution of the Mitchel Field lease transaction, it is unclear how much of the proceeds would be counted as revenue in FY 2011 under GAAP. Regardless of the accounting treatment, the proposed transaction is a one-shot, which provides upfront resources to benefit taxpayers only in FY 2011 and does nothing to mitigate the County's persistent structural imbalance between recurring revenues and expenditures.

The projected revenue shortfall also includes: $13 million in unrealized departmental revenues; $14 million in sales tax collections; $5 million from the County's proposed LIE ticket surcharge initiative which has repeatedly failed to garner authorization from the State, and almost $3 million in OTB revenues.

The projected year-end deficit also reflects unbudgeted expenditures that could total almost $20 million. The projected overspending is primarily driven by: the County's need to fund certiorari payments in the operating budget; its failure to obtain the $61 million in budgeted savings it sought from labor concessions; as well as from $15 million in unbudgeted overtime expenditures.

While the County did not capture savings it sought from labor concessions, it did realize other savings from not filling vacant positions, implementing layoffs of 128 full-time employees, and effectuating a NIFA-imposed wage freeze. The County will also likely realize $10 million in savings from reductions in contractual services, $7 million in reduced fringe benefits, and will reallocate its $70 million budgeted contingency reserve to cover variances throughout the budget.

Projected FY 2011 Operating Results			
($ in millions)	**Adopted Budget**	**Current Projection**	**Surplus/(Risk)**
Revenues:			
Fines and Forfeitures	**$95.6**	**$47.4**	**($48.2)**
Red Light Camera	*61.7*	*25.2*	*(36.5)*
Other	*33.9*	*22.2*	*(11.7)*
Investment Income	**7.4**	**2.3**	**(5.1)**
Rents and Recoveries	**82.5**	**36.2**	**(46.3)**
Sale of County Land	*25.1*	*10.0*	*(15.1)*
Mitchel Field Leases	*36.0*	*7.0*	*(29.0)*
Other	*21.4*	*19.2*	*(2.2)*
Department Revenues	**122.6**	**109.3**	**(13.3)**
Ambulance Fees	*29.1*	*18.9*	*(10.2)*
Advertising Fees	*1.0*	*0.0*	*(1.0)*
Other	*92.5*	*90.4*	*(2.1)*
OTB Revenue	**6.5**	**3.6**	**(2.9)**
LIE Ticket Surcharge	**5.0**	**0.0**	**(5.0)**
Sales Tax	**1,023.4**	**1,009.4**	**(14.0)**
Other Revenue	**1,357.6**	**1,358.4**	**0.8**
Total Revenues	**2,700.6**	**2,566.6**	**(134.0)**
Expenditures:			
Salaries and Wages	**811.9**	**851.5**	**(39.6)**
Salaries and Wages	*746.3*	*770.9*	*(24.6)*
Overtime	*65.6*	*80.6*	*(15.0)*
Fringe Benefits	**444.5**	**437.5**	**7.0**
Contractual Services	**127.6**	**117.4**	**10.2**
Tax Certiorari Payments	**0.0**	**70.0**	**(70.0)**
Contingency Reserve	**70.3**	**0.0**	**70.3**
Other Expenditures	**1,246.4**	**1,243.9**	**2.5**
Total Expenditures	**2,700.6**	**2,720.3**	**(19.6)**
Total Risk			**($153.6)**

The following discussion explains the major variances in more detail.

Fines and Forfeitures – The County will collect significantly less revenue from fines and forfeitures than was budgeted. We project that Red Light Camera revenue will fall short by $36.5 million, of which $23.4 million results from the County not securing State authorization to expand the program to an additional 50 intersections. We also project that revenue from other traffic fines will be $12.3 million below expectations based on an extrapolation of year-to-date actuals.

($ in millions)	FY 2011 Budget	Projection	Surplus/(Risk)
Red Light Camera Phase I	$38.3	$25.2	($13.1)
Red Light Camera Phase II	23.4	0.0	(23.4)
Fines	31.6	19.3	(12.3)
Other	2.3	2.9	0.6
Total	$95.6	$47.4	($48.2)

Investment Income – The County will realize less revenue from investing available cash than it budgeted. Interest rates have remained lower than assumed and we have no reason to believe rates will be rising in the near term. Consequently, we project a shortfall of $5.1 million based on an extrapolation of year-to-date actuals.

Rents and Recoveries – We are currently projecting a shortfall of $46.3 million related to the County's efforts to sell surplus County property as well as securitize the rental income from the Mitchel Field leases. The County's most recent estimate is that it expects to close on both these transactions in the next 60 days. However, in addition to execution risk, it appears that the County will realize only $10 million in FY 2011 from the sale of the former Grumman property (and $5 million in FY 2012) and may be unable to recognize as current year revenue all of the $37.5 million in cash proceeds anticipated from the Mitchel Field lease securitization. The latter concern, which stems from a provision of the NIFA Act requiring that revenues be recognized in accordance with GAAP, has been communicated to the County repeatedly and was a factor in NIFA's determination to impose a control period.

Department Revenues – We are currently projecting a $13.3 million shortfall in departmental revenues. The negative variance is driven primarily by current weakness in ambulance fee collections. While the County maintains that it is making progress in collecting fees at the higher rates approved by the County Legislature, we estimate that they will fall $10.2 million below budget. We also project shortfalls in Parks revenue, including $1 million from a proposed advertising initiative.

OTB Revenue – We project a shortfall of $2.9 million in revenue from the Nassau Regional Off-track Betting Corporation ("OTB"). No profits are expected in FY 2011 and there has been a decrease in wagering subject to the 5% surcharge.

($ in millions)	FY 2011 Budget	Projection	Surplus/(Risk)
OTB Profits	$1.5	$0.0	($1.5)
OTB 5% Surcharge	5.0	3.6	(1.4)
Total	$6.5	$3.6	($2.9)

LIE Ticket Surcharge – Once again, the County has failed to secure State authorization for a surcharge that would enable the County to raise revenue to offset the costs associated with patrolling the Long Island Expressway, the Seaford-Oyster Bay Expressway, and portions of Sunrise Highway. Consequently, the $5 million in budgeted revenue will not be realized.

Sales Tax – As shown below, after experiencing a relatively strong first quarter, sales tax receipts have been weak during the subsequent months. Year-to-date collections are up only 1.6% (excluding the sales tax on residential energy which was repealed effective June 1, 2010) over the comparable period in 2010. Consequently, the County needs sales tax growth of 5.1% in the remaining months to reach budget. If sales tax growth in the remaining months were to continue at the current pace, the County would fall short of the FY 2011 adopted budget by approximately $14 million.

2011 Adjusted Sales Tax Growth Over Same Period 2010 (excluding tax on residential energy)	
1st Quarter	3.9%
2nd Quarter	(0.2%)
3rd Quarter (partial)	0.8%
YTD	1.6%

Salaries and Wages – Our analysis indicates that expenditures for salaries and wages may exceed budget by $39.6 million. The negative variance is driven by the County's failure to realize most of the $61 million in anticipated labor savings included in the budget. While the County realized savings from not filling certain budgeted, but vacant positions, the implementation of a wage freeze in March, and the implementation of 128 layoffs in June, it did not secure concessions from any of its unions. The County also failed to control overtime spending, particularly in the police department, adding a projected $15 million in unbudgeted costs.

Fringe Benefits – We project expenditures on fringe benefits to be $7 million below budget. Savings are driven by lower than budgeted health insurance costs for active employees.

Contractual Services – The County projects that spending on contractual services will be $10.2 million below budget. This is driven by savings of more than $15 million from reductions to miscellaneous contracts in several departments and program agencies. Included in this projection is also more than $6 million in savings expected to be realized in the Traffic and Parking Violations Agency ("TPVA"), primarily from not expanding its red light camera program (Phase II) because of a failure to secure State authorization. The County estimates that the aforementioned savings will be partially offset by $5 million in additional unbudgeted expenditures for outside legal services contracted by the County Attorney.

($ in millions)	FY 2011 Budget	Projection	Surplus/(Risk)
Miscellaneous (net of TPVA)	$34.4	$25.3	$9.1
TPVA	15.9	9.8	6.1
Legal	1.4	6.4	(5.0)
Other	75.9	75.9	0.0
Total	$127.6	$117.4	$10.2

Tax Certiorari Payments – The County did not budget for the payment of any property tax refunds in FY 2011, which could total approximately $70 million. To date, the County has paid out $22.8 million in property tax refunds.

The County originally planned to fund this operating cost with long term bond proceeds, which is a practice that NIFA has repeatedly criticized and one which NIFA has indicated will no longer be acceptable or approved. Furthermore, the NIFA Act clearly states that the use of cash raised through the issuance of debt (bond proceeds) to make these payments cannot be considered revenue when calculating budget balance.

The County currently has a substantial unpaid liability for cert claims, which are awaiting payment in the Treasurer's Office. At last count, this amount exceeded $30 million with an unknown, but significant, liability pending in the County Attorney's office.

While we do not encourage the use of bond proceeds to pay certs, we recognize the availability of approximately $35 million of unused proceeds from prior borrowings and the County's desire to use these funds. We will not, however, count its expenditure as revenue in balancing the budget for FY 2011.

It is worth noting that notwithstanding the County's belief that NIFA has acted arbitrarily in addressing the County's current desires regarding the funding of cert refunds, NIFA's position in this matter has been upheld by the State Supreme Court. See *In re County of Nassau*, 920 N.Y.S.2d 873 (Sup. Ct. Nassau County 2011).

Contingency Reserve – The County plans to use its $70.3 million budgeted contingency reserve to cover negative variances throughout the budget.

Cash Flow – If the FY 2012 Budget is not passed in a timely manner, there is serious doubt that the County would be able to complete a Tax Anticipation Note ("TAN") borrowing in 2011. This would present the County with a very serious year-end cash flow problem since issuing a TAN in 2011 is critical for the County's cash flow needs, especially given the significant projected shortfalls in revenues in FY 2011.

TANs are short term debt that will be retired with taxes to be collected at a future date. Consequently, without a budget, a TAN issuance would be highly doubtful since it is unlikely that anyone would purchase the TAN without an assurance that it would be repaid from subsequent taxes, which would normally require an enacted budget for 2012.

We recognize that if by October 30 a budget is not adopted by the County Legislature, the County Charter does provide that the Clerk of the Legislature may file certain papers with the Board of Assessors thereby triggering an "exigency" tax." The "exigency tax" is an amount equal to one hundred percent of the amount that was levied for County purposes for the current fiscal year" with some minor exceptions.

It is noteworthy that the "exigency tax" could not be used for a cash flow ("TAN") borrowing without a subsequent appropriation by the County Legislature. All of this may occur too late in 2011 for the TAN to be completed.

III. DISCUSSION OF FY 2012

NIFA has reviewed the Proposed Budget for FY 2012. Our analysis indicates that the County could end FY 2012 with a deficit of approximately $282.9 million if no other actions are taken, as shown below. The seriousness of this risk is obvious when juxtaposed against the $26 million deficit which is needed to trigger a control period.

Analysis of Proposed FY 2012 Budget					
($ in millions)	**FY 2011 Projection**		**FY 2012 Proposed**	**FY 2012 Projection**	**Surplus/(Risk)**
Revenues:					
Fines and Forfeitures	**$47.4**		**$59.3**	**$47.4**	**($11.9)**
Red Light Camera	*25.2*		*29.3*	*25.2*	*(4.1)*
Other	*22.2*		*30.0*	*22.2*	*(7.8)*
Investment Income	**2.3**		**3.6**	**2.3**	**(1.3)**
Rents and Recoveries	**36.2**		**19.1**	**16.7**	**(2.4)**
Sale of County Land	*10.0*		*7.4*	*5.0*	*(2.4)*
Mitchel Field Leases	*7.0*		*2.4*	*2.4*	*0.0*
Other	*19.2*		*9.4*	*9.4*	*0.0*
Department Revenues	**109.3**		**127.0**	**112.3**	**(14.7)**
Ambulance Fees	*18.9*		*29.1*	*18.9*	*(10.2)*
Advertising Fees	*0.0*		*1.0*	*0.0*	*(1.0)*
Other	*90.4*		*96.9*	*93.4*	*(3.5)*
OTB Revenue	**3.6**		**3.2**	**3.2**	**0.0**
Sales Tax	**1,009.4**		**1,056.2**	**1,054.0**	**(2.2)**
Other Revenue	**1,358.4**		**1,371.0**	**1,338.0**	**(33.0)**
Total Revenues	**2,566.6**		**2,639.4**	**2,574.0**	**(65.4)**
Expenditures:					
Salaries and Wages	**851.5**		**747.8**	**879.4**	**(131.6)**
Salaries and Wages	*770.9*		*720.4*	*802.0*	*(81.6)*
Overtime	*80.6*		*27.4*	*77.4*	*(50.0)*
Fringe Benefits	**437.5**		**412.2**	**479.8**	**(67.6)**
Contractual Services	**117.4**		**99.5**	**114.5**	**(15.0)**
Tax Certiorari Payments	**70.0**		**70.0**	**70.0**	**0.0**
Contingency Reserve	**0.0**		**0.0**	**0.0**	**0.0**
Other Expenditures	**1,243.9**		**1,309.9**	**1,313.2**	**(3.3)**
Total Expenditures	**2,720.3**		**2,639.4**	**2,856.9**	**(217.5)**
Total Risk	**($153.6)**				**($282.9)**

FY 2012 RISKS

The following discussion explains the major projected variances in more detail.

Fines and Forfeitures – The County has budgeted $59.3 million for fines and forfeitures, of which more than half is expected to result from the continued operation of its existing Red Light Camera program. Based on estimated results in FY 2011, and a projected decline in the number of violations due to increased public awareness of the monitored intersections, we estimate that the County will collect $4.1 million less than anticipated in FY 2012.

We also project that the County will miss its target for non-red light camera fines by $7.8 million. We base this estimate on the substantial decline in the number of tickets being issued in 2011 and see no reason to expect an increase in FY 2012.

Investment Income – We project that the County will be unable to realize the budgeted level of investment income, which they assume will derive from an average daily cash balance of $700 million invested at 50 basis points. Based on FY 2010 actual results, FY 2011 projections, and general indications that short term interest rates will remain low, we project a shortfall of $1.3 million in FY 2012.

($ in millions)	FY 2010 Actual	FY 2011 Projection	FY 2012 Proposed	Surplus/(Risk)
Investment Income	$2.4	$2.3	$3.6	($1.3)

Rents and Recoveries – The County has budgeted $19.1 million in rents and recoveries, which is a category of revenue that includes the sale of County property, rental income from tenants that occupy County facilities, recoveries generated by the reversal of prior year appropriations, and recoveries associated with the settlement of claims brought by the County against defendants.

The County expects to realize $7.4 million from the sale of County property in FY 2012, including the receipt of $5 million stemming from the sale of the former Grumman property in FY 2011 (in addition to $10 million received in FY 2011). This projection is consistent with the terms of the proposed transaction; however, the County also anticipates that it can realize an additional $2.4 million from the sale of other properties, including the potential sale of two police precincts that are proposed for elimination. We consider the additional revenue to be at risk until the contractual and legislative hurdles related to the police consolidation and redeployment initiatives are resolved and potential purchasers are identified.

Department Revenues – The County has budgeted $127.0 million in departmental revenue, of which we project $14.7 million to be at risk. Most of this risk stems from a projected shortfall in ambulance fees, which we base on the County's current collection experience in FY 2011. The County is also projecting an increase in cabana fee revenue in the Parks Department. The County expects to generate $1 million more in cabana fees in FY 2012 than currently projected in FY 2011 by building an additional 400 new cabana rental units at Nickerson Beach. We are concerned about execution risk.

Sales Tax – Sales tax is the largest revenue source for the County, comprising approximately 40% of all revenues in the major funds, and is budgeted at $1.1 billion for 2012, including $12.1 million earned in 2010, but for technical reasons not accounted for until 2012.("Deferred Sales Tax").

The County projects that sales tax revenues will grow by 3.2% in FY 2012. However, after adjusting for the impact of Deferred Sales Tax, the sales tax is actually projected to grow by a more modest rate of 2.2% in FY 2012, as shown below. While this assumption appears reasonable, we are concerned that current economic weakness may negatively impact sales tax collections in FY 2011 more than the County assumes, and would concomitantly impact collections in FY 2012.

($ in millions)	FY 2011 Budget	FY 2012 Proposed	Change
Current Sales Tax	$1,021.7	$1,044.1	2.2%
Deferred Sales Tax	1.6	12.1	
Total Sales Tax	$1,023.3	$1,056.2	3.2%

As discussed earlier, year-to-date growth in FY 2011 is only 1.6% and has weakened in recent months. Consequently, we believe that projected sales tax revenues may be slightly overstated in all years.

Other Revenue – We are holding at risk $33 million in other "revenue" related to the County's assumption of bonding $18 million in non-cert judgments and realizing $15 million in restructuring savings.

Refunding and Restructuring NIFA Debt – The Plan includes $15 million for refunding and restructuring of NIFA debt. Current indications are that on a present value basis there is far less than this amount available from an economically advantageous NIFA refunding and the Directors have not consented to any refunding or restructuring, especially a restructuring that would merely postpone debt and have minimal present value savings or would upfront the savings rather than employ a level savings structure.

Borrowing for Non Cert Related Judgments and Settlements – The County has included $18 million in borrowed funds for this item in the 2012 Budget even though NIFA has repeatedly criticized the County for borrowing for judgments and settlements. In addition to this practice being fiscally imprudent, the bond proceeds are not considered revenue under GAAP. Proper budgeting anticipates a certain number of lawsuits as the cost of doing business.

The County had made some progress in this area, but has now reverted to the practice of bonding substantially all of its judgments and settlements. NIFA does not approve this practice except under the most unusual and unanticipated circumstances.

Salaries and Wages – The County's budget for salaries and wages inclusive of full-time, part-time and seasonal positions is approximately $748 million. We believe this amount is understated by approximately $132 million. This variance is attributable to our assessment of what the County has identified as: "savings from initiatives;" a drastic reduction in overtime funding; savings from a continuation of the NIFA imposed wage freeze; and, zero funding for terminal leave payments.

"Savings from Initiatives" – The County has identified $51.6 million in savings that would be realized by means of a lay-off plan for 700 employees. Although the County did not delineate which positions would be targeted for lay-off, the reduction has been distributed throughout all departments including the Police Department.

While the County does have the authority to lay-off employees in the CSEA, other public safety unions' contractual agreements contain provisions limiting the use and utility of lay-offs as an expenditure reduction tool. The County believes it can proceed with lay-offs within all unions in spite of such provisions by means of passing a "Fiscal Crisis Reform Act." The Act would allow the County-wide lay-off plan to supersede present contractual agreements. We question whether there is sufficient support to enact this legislation and believe that its implementation will likely be challenged by the unions.

Overtime – We believe that the County will experience a shortfall of at least $50 million in overtime. Overtime costs have historically been underfunded and, year after year, have resulted in significant deficits of as much as $15 million. Most of the deficits have occurred in the public safety departments; namely, the Police District, Police Headquarters and the Correctional Center.

The County's significant reductions in funding for overtime in 2012 compound the overtime risk since the County proposes to slash overtime funding for these three departments by nearly $37 million. The County believes that the Fiscal Crisis Reform Act would empower them to re-open existing public safety labor contracts and amend items that contribute to overtime costs, such as minimum manning.

Based on historical spending and the unlikelihood that the County can legally re-open existing contracts to make these amendments, we expect that the County will continue to spend significant overtime dollars; hence, we believe that the overtime risk of $50 million is conservative.

Wage Freeze – The County has estimated that it would save approximately $34 million in FY 2012 by continuing the wage freeze that was imposed in 2011 and would save an additional $10 million in FY 2012 by extending the freeze for an additional year. As discussed in "savings from initiatives," above, the County believes that it can legislate the right to continue the wage freeze in FY 2012, with or without NIFA approval, by means of the Fiscal Crisis Reform Act.

We have placed $10 million of this item at risk for FY 2012 for two reasons: 1) it will require either legislative action or NIFA approval and 2) the current wage freeze is under litigation and should a determination be made in favor of the unions, it could not be extended by NIFA for future budget years.

Terminal Leave – Terminal Leave refers to the payment to employees upon termination or retirement for unused vacation time and sick leave accruals. However, despite the significant headcount reductions assumed in the Proposed Budget, the County has provided zero funding for Terminal Leave. The County plans to finance the entire cost of termination pay through the issuance of debt.

In order to bond this expense, the County must receive approval from NIFA and, even if approval were granted, we question whether this funding source can be recognized as revenue according to GAAP. Consequently, we project a risk of at least $20 million. The actual risk will be driven by the level of attrition and the County's success in executing its lay-off plan.

Headcount – The Proposed Budget contemplates 7,400 full-time positions. This level is 1,010 positions below the FY 2011 Adopted Budget allocation of 8,410. The majority of the planned headcount reduction results from a proposed lay-off of 700 employees. See Appendix A.

While the County has distributed "salary savings from initiatives" throughout various departments, it has not broken out the associated headcount reduction within these departments; rather, it has simply taken the reduction from the bottom line. Since the bump and retreat analysis which will impact the savings has not been conducted, it is difficult to ascertain how many full-time positions will ultimately need to be eliminated.

The County's on-board full-time headcount as of September 2011 was 7,978, which is already 432 positions below the 8,410 positions contained in the FY 2011 Adopted Budget. This reduction is due to a number of factors that include budgeted vacancies, the retirement of employees who elected to participate in an early retirement incentive program, a hiring freeze, and the lay-off of 128 employees within 5 departments in 2011.

Since the current headcount is only 578 full-time positions above the County's 7,400 target, it is unclear as to whether the County will need to lay-off fewer than 700 employees or if, in the process of filling vacancies that it deems to be critical or revenue producing, the County will need to adhere to its full lay-off plan.

Fringe Benefits – We project a net shortfall of approximately $67.6 million in fringe benefit savings. The County has expressed its intention to require employees and retirees to make a 25% contribution towards the cost of health insurance. As discussed in a number of proposed salary savings initiatives which we have risked, the County believes it can impose this contribution on its employees by means of the Fiscal Crisis Reform Act.

We have risked the entire amount of the County's proposed savings of $69.2 million because they can only be realized if the County wins the right to re-open contracts and we are doubtful that this will occur. It is also unclear if the County has the right impose this change on retirees.

The County also projects savings of $36.6 million through the amortization of the increase in pension costs that it would otherwise be required to pay on behalf of certain of its active employees. The County plans to take advantage of this State authorized provision for the first time in 2012.

Based on our review of the paperwork that the County has received from the State Comptroller regarding the County's required pension contributions, we believe that the County may have underestimated the savings from amortization by $1.6 million. Furthermore, we note that while the use of this provision will yield considerable budget relief in FY 2012, the effect of the amortization is to extend current liabilities into the future.

Contractual Services – The County has budgeted $99.5 million for contractual services. Although we believe the County can continue to realize savings in the Proposed Budget by constraining the number and dollar amounts awarded to various vendors, we are projecting a deficit of $15 million tied to the County's "Strategic Sourcing Initiative."

While this initiative was identified by Grant Thornton, an independent consultant group retained by NIFA to make suggestions for operational and financial initiatives to help the County, we have no indication of how it would be implemented. We will reevaluate this initiative once the County determines how it would become part of a streamlined process within its Purchasing Department and provides a timeline for implementation.

Utilities – We project that the County will exceed its $36 million utilities budget by a little over $3 million. We see no basis to expect these costs to decline from FY 2011 projected levels. Additionally, the County will not continue to receive previously issued credits from the Long Island Power Authority (LIPA) as it did in late FY 2009 and early FY 2010.

Tax Certiorari Payments – The County has budgeted $70 million for property tax refund payments in 2012. This tacit acknowledgement of NIFA's position regarding borrowing for certiorari claims is noted. We hope that this estimate of liability is accurate and will be sufficient to meet new expenses and possibly eliminate some of the accumulated backlog.

Contingency Reserve –The Proposed Budget does not provide funding for contingencies as it has in the past. We are concerned that within a budget that contains so many risks there is nothing provided to mitigate additional or unanticipated shortfalls or judgments that could emerge in FY 2012.

Other Concerns

Revenue Anticipation Notes ("RANs") / Tax Anticipation Notes ("TANs") – The County plans to use approximately the same level of TAN borrowing in 2012 as it anticipates using in 2011 to meet its cash flow needs; however, it plans to greatly increase its RAN borrowing from $230 million in 2011 to $325 million in 2012.

This increased RAN borrowing is simply a further indication of the precarious nature of the County's budget and revenue estimates as well as its liquidity. Furthermore, even though interest rates are low, it will cost the County to borrow this money, even if only for a limited time period.

Contingency Plan

The County has identified five initiatives as contingencies for slippage in its gap closing plan, but has not included any savings resulting from these actions in the Proposed Budget. The initiatives total $306.1 million and include $135 million in revenue to be raised in 2012 from its proposed Public-Private Partnership transaction, $120 million in expenditure reductions from additional labor savings, and $51.1 million in other actions requiring State approval.

Public-Private Partnership ("P3") - A major component of the Proposed Budget's Contingency Plan is a proposal to enter into a P3 with a private entity to lease, on a long-term basis, the County's wastewater system. The transaction would be governed by a concession agreement (GASB standards refer to it as a "Service Concession Arrangement").

The County would retain ownership of the asset(s) with a right to reclaim the asset(s) if the standards established in the agreement are not met (or presumably at the end of the term of the agreement). Certain risks and responsibilities would transfer to the private entity. The County has retained the services of Morgan Stanley & Co. LLC as sell-side advisor to assist in evaluating the proposed transaction.

When the County first presented this proposal in the 2011-14 MYP Update, it estimated that this transaction could generate total budgetary relief of $375 million beginning in FY 2012 through FY 2014. In the Proposed Budget the County has revised its estimate upward to $500 million in net revenue and also states that it would have the ability to retire nearly $500 million of debt.

Based on our understanding of the County's proposal, the entire amount received in cash might not, under GAAP, be considered "revenue," but would likely be amortized over the life of the financing. We are also concerned that the ramifications of transferring substantially all of the assets to a private entity have not been thoroughly considered or presented to the public and involve significant policy questions and decisions. Finally, we also believe that any proceeds from a privatization should be used for capital purposes or to reduce planned borrowings and not for operating expenses, which would perpetuate the structural deficit in the same amount.

Furthermore, notwithstanding the accounting treatment of a public-private partnership for wastewater treatment, the County has a long way to go to demonstrate that this initiative is even feasible. P3 deals are complicated and expensive to orchestrate. Among other costs would be the assistance of professional advisors to ensure the protection of the County's interests. A P3 deal from inception to signing can take more than a year to complete and we see little movement on the part of the County to take the steps necessary to find counterparties and effect such a transaction. Indeed, the County states "A typical Public-Private Partnership would take approximately 12-18 months to complete…." NIFA believes even this 12-18 month estimate is overly optimistic.

Labor Actions – The County states that if it is unable to achieve labor related savings, primarily with respect to labor concessions with its unions, it will have to implement other cost savings initiatives specifically tied to pairing down labor costs. The County has proposed two contingency labor actions for FY 2012 totaling $120 million. The first initiative would be to lay-off 600 additional employees for an estimated savings of $60 million ("Contingency Labor Plan One"). The second initiative is to institute unpaid furlough days whereby employees not working in critical areas of public safety and health, would work a mandatory four-day week. The estimated savings for this initiative is also estimated to be $60 million.

With respect to the Contingency Labor Plan One, the County has not identified which positions and departments would be affected, but coupled with the 700 employee reduction built into in the Proposed Budget, the total number of employees slated for lay-off would be 1,300.

It is not clear how the County will be able to achieve a reduction of this magnitude. As discussed previously in this report, with the exception of the CSEA, other unions' labor agreements contain provisions that limit the use of lay-offs as a tool to reduce expenditures. Therefore, the bulk if not all of the lay-offs would occur in departments that are primarily staffed with CSEA union employees thereby limiting distribution throughout departments County-wide. Consequently, certain departments could experience severe reductions in staff while other departments would see very little reduction. While the overall effect this measure would have on service delivery is difficult to quantify, clearly the consequences to services delivery and operations would be extreme and extensive.

In terms of unpaid furlough days, the County may experience the same legal challenges to this initiative as it has already experienced with litigation opposing the wage freeze. The cost of litigation may offset achieved savings even if the County were to prevail; and if the County did not win the lawsuit, the lost savings plus the cost of litigation would doubly impact the budget.

Actions Requiring State Approval – The County identified three actions that require State approval before they can be implemented: elimination of the County's payment for MTA station maintenance; expansion of the red light camera program (Phase II); and imposition of a LIE ticket surcharge.

MTA Station Maintenance – The County has listed as one of its contingency measures, savings of $27 million through the elimination of its payment to the MTA for maintenance at LIRR stations. The base amount for Nassau County is set and is adjusted based on the change in the regional Consumer Price Index (CPI) each year. This measure would require State legislation.

Red Light Camera Phase II – The County proposes to double the number of intersections included in its Red Light Camera program by adding cameras to an additional 50 intersections. The County projects that the expanded program will yield an additional $18 million in net revenue in 2012. We consider this initiative to be at risk since the expansion requires State approval. We also have concerns that delays experienced in rolling out of the existing program could recur and thereby negatively impact projected revenues even if State approval is granted.

LIE Ticket Surcharge –The County proposes to impose a surcharge on moving violations to reimburse the County for the costs of patrolling the Long Island Expressway and Sunrise Highway, both of which are State roads. We consider these initiatives to be at risk since it requires State approval. This initiative has repeatedly been rejected at the State level.

Other Concerns

Long Island Bus Contract with Veolia Transportation – The County budgeted $2.5 million in subsidies to Long Island Bus, which includes $1.9 million in payments for fixed routes and $0.6 million for Able-Ride paratransit routes. It plans to end its relationship with the Metropolitan Transportation Authority ("MTA"), the parent corporation of Long Island Bus, on December 31, 2011 and enter into an agreement with Veolia Transportation to operate the system. To date, the contract with Veolia has not been submitted to the Legislature for approval after which it would require NIFA approval.

County Guarantee –We note that the County has passed legislation ("cert legislation"), currently being litigated, that ends the County's obligation to indemnify towns and villages for errors in the assessment process. It is important for the County to recognize that if the cert legislation is not upheld in the courts, the County will have a massive and unbudgeted liability, beginning in 2013. The County should be considering how they will address this problem if the plaintiffs' positions are affirmed.

IV. THE OUT-YEAR GAPS: FY 2013 – FY 2015

This section of our report discusses the projected Out-Year gaps and the County's plan for ensuring balance in these years.

Sizing the Out-Year Gaps – The County projects that baseline gaps of $136.4 million in FY 2013, $129.1 million in FY 2014, and $174.8 million in FY 2015 will remain in the Out-Years even if it can successfully implement its entire 2012 gap-closing plan, which has been fully incorporated into the Proposed Budget. These gaps were calculated by the County using growth rate assumptions listed in Appendix B. See "County Gap Closing Plan" table below.

However, based upon our review of the Proposed Budget and the County's baseline assumptions, our analysis indicates that the County's projections of Out-Year gaps may be understated by almost $250 million in FY 2013, $280 million in FY 2014, and $315 million in FY 2015, if the risks we identified in FY 2012 are not satisfactorily addressed with recurring solutions. The additional risks stems primarily from the ambitious labor savings targets built into the County's baseline projections, as discussed in "Salaries and Wages" earlier in this report.

Closing the Out-Year Gaps – We are concerned that the County's gap closing plan repeats many of the same initiatives already proposed in earlier financial plan submissions, almost all of which contain considerable risk or require outside approval.

County Gap Closing Plan				
($ in millions)	FY 2012	FY 2013	FY 2014	FY 2015
Baseline Gap:	**-**	**($136.4)**	**($129.1)**	**($174.8)**
Gap Closing Options				
Financing Options/Asset Sales				
Surplus Land Sales		5.0	10.0	10.0
Public Private Partnership (Sewer System)	135.0	125.0	50.0	25.0
Expense/Revenue Actions				
NYS Actions				
Elimination of MTA Station Maintenance	28.1	29.0	30.0	31.0
Red Light Camera Phase II	18.0	12.0	9.0	7.0
LIE Ticket Surcharge	5.0	5.0	5.0	5.0
Tax Certiorari Savings				
Guarantee Removal Savings		14.0	28.0	42.0
Assessment Grievance band (Addition to Guarantee Removal)		-	6.0	12.0
Continuation of NIFA Wage Freeze		27.3	61.9	100.2
Value of New Construction		3.0	6.0	9.0
Total Gap Closing Options		**$220.3**	**$205.9**	**$241.2**
		$83.9	**$76.8**	**$66.4**

Financing Options/Asset Sales – Commencing in FY 2012, the County is counting on the receipt of revenue from sales of County land as well as from the proceeds it expects to realize from a public-private partnership transaction involving the assets of the County's sewer system. While there may be merit to both of these types of gap-closing initiatives, they clearly are one-shots that only help to bridge the deficit between recurring revenues and expenditures in the short term, but do nothing to address the persistent structural imbalance. We discuss the proposed sewer transaction and the attendant risks in more detail in "Contingency Plan" earlier in this report.

Expense/Revenue Actions – The County has outlined several initiatives that it is pursuing and that it projects could generate additional revenue or reduce expenditures in the Out-Years.

NYS Actions – Among the initiatives are three proposals that would require State approval before they could be advanced: elimination of MTA station maintenance support; expansion of the red light camera program (Phase II); and imposition of a LIE ticket surcharge. The County has proposed the latter two initiatives in the past without success.

It is unclear if the County can get the requisite approvals for the three proposals and therefore we hold the projected savings at risk. We discuss these actions in more detail in "Contingency Plan" earlier in this report.

Tax Certiorari Savings –The County has also identified two initiatives that it projects will reduce the cost of its annual tax certiorari liability: savings from the elimination of the County Guarantee; and imposition of an "assessment grievance band."

The County is banking very heavily on its success in eliminating its guarantee of certiorari refunds, which would simply shift the burden of improper assessments back to other jurisdictions rather than solve the underlying problem. The County will still be handling the cert claims, but as evidenced by the recent layoffs in 2011, with a greatly diminished number of personnel.

We do note that even if the initiative is successful, the County's share of cert claims will still be approximately 17% and that it will still have full responsibility for the current backlog, which the County estimates to be $152.3 million as of December 31, 2010. The Out-Years of the Plan have made some accounting for this continued liability; however, we are unable to decipher their methodology.

In conclusion, because this matter is being litigated, we will not comment further except to say that the success or failure of this initiative will have a major impact on the Out-Years of the Plan.

The County also projects that the imposition of an assessment grievance band could generate savings of $6 million in FY 2014 and $12 million in FY 2015. This idea, apparently borrowed from the Grant Thornton report, would establish a margin of error below which a taxpayer would be prohibited from filing a grievance. We cannot verify the accuracy of the savings in the Plan from this proposal or predict what Legislative authority or authorities would have to pass upon it.

Continuation of NIFA Wage Freeze – The County has projected that it could realize savings of $27.3 million in FY 2013, $61.9 million in FY 2014, and $100.2 million in FY 2015 from the continued imposition of a wage freeze. These savings would result from County employees not receiving cost of living adjustments and salary step increases in those years. It should be noted that these savings are in addition to those that the County estimated it would realize from a continuation of the current wage freeze in 2012, and which have already been reflected by the County in its baseline projections.

We emphasize that any savings generated by the continuation of a wage freeze require that NIFA annually make a determination that a fiscal crisis exists and that a wage freeze is essential to the County's adoption and maintenance of a budget balanced in accordance with the NIFA Act. Consequently, the County should not assume that NIFA will take this action.

Value of New Construction:

The County anticipates increasing the size of its property tax levy by $3 million annually, beginning in FY 2013. This would add $9 million to the tax levy by FY 2015. The County maintains that this revenue represents the additional taxable value of properties being added to the roll or improved through new construction.

V. CONCLUSION

The County's adoption of its Proposed Budget and Multi-Year Plan are at least a month away. During that time, hearings will take place to assist the Legislature in its deliberations.

Regardless of what happens in the hearings, concessions from the County's unions as well as important State legislation will be necessary if this budget is to stand any chance of being balanced. We see no signs of progress in either of those key areas; in fact, the State Legislature is not scheduled to come back into session until 2012.

We recommend that the Directors consider passing a resolution that adopts this staff report and indicates to the County that absent significant progress in the key areas outlined in this report, the Plan will be rejected by NIFA because of its failure to conform to the requirements of the NIFA Act.

VI. APPENDICES

Appendix A

FY 2012 PROPOSED BUDGET FULL-TIME HEADCOUNT (HC) COMPARISON TABLE

Department	2011 Adopted HC	On-Board (9-8-11)	2012 Proposed HC	2012 Proposed to 2011 Adopted Inc/Dec	2012 Proposed to Sept On-Board Inc/Dec
AC - DEPARTMENT OF INVESTIGATIONS	0	0	0	0	0
AR - ASSESSMENT REVIEW COMMISSION	43	31	29	(14)	(2)
AS - ASSESSMENT DEPARTMENT	216	169	169	(47)	0
AT - COUNTY ATTORNEY	135	112	112	(23)	0
BH - DEPT OF MH, CHEM DEPEND & DISABLE SVCS	62	51	0	(62)	(51)
BU - OFFICE OF MANAGEMENT AND BUDGET	27	26	24	(3)	(2)
CA - OFFICE OF CONSUMER AFFAIRS	33	32	32	(1)	0
CC - NC SHERIFF/CORRECTIONAL CENTER	1,235	1,211	1,227	(8)	16
CE - COUNTY EXECUTIVE	26	21	21	(5)	0
CF - OFFICE OF CONSTITUENT AFFAIRS	44	43	43	(1)	0
CL - COUNTY CLERK	103	97	103	0	6
CO - COUNTY COMPTROLLER	88	74	87	(1)	13
CS - CIVIL SERVICE	55	56	53	(2)	(3)
DA - DISTRICT ATTORNEY	369	375	361	(8)	(14)
EL - BOARD OF ELECTIONS	129	143	143	14	0
EM - EMERGENCY MANAGEMENT	7	7	7	0	0
FC - FIRE COMMISSION	107	94	101	(6)	7
HE - HEALTH DEPARTMENT	210	201	204	(6)	3
HI - HOUSING & INTERGOVERNMENTAL AFFAIRS	3	2	2	(1)	0
HP - PHYSICALLY CHALLENGED	4	5	0	(4)	(5)
HR - COMMISSION ON HUMAN RIGHTS	9	8	8	(1)	0
HS - DEPARTMENT OF HUMAN SERVICES*	0	0	96	96	96
IT - INFORMATION TECHNOLOGY	121	73	81	(40)	8
LE - COUNTY LEGISLATURE	95	82	94	(1)	12
LR - OFFICE OF LABOR RELATIONS	5	5	5	0	0
MA - OFFICE OF MINORITY AFFAIRS	6	6	7	1	1
ME - MEDICAL EXAMINER	53	56	58	5	2
PA - PUBLIC ADMINISTRATOR	7	7	7	0	0
PB - PROBATION	216	206	236	20	30
PD - POLICE DISTRICT	1,680	1,658	1,654	(26)	(4)
PD - POLICE HEADQUARTERS	1,626	1,534	1,567	(59)	33
PE - DEPARTMENT OF HUMAN RESOURCES	9	9	9	0	0
PK - PARKS, RECREATION AND MUSEUMS	148	173	172	24	(1)
PL - PLANNING	22	22	0	(22)	(22)
PR - PURCHASING DEPARTMENT	17	16	16	(1)	0
PW - PUBLIC WORKS DEPARTMENT	526	452	471	(55)	19
RE - OFFICE OF REAL ESTATE SERVICES	7	8	10	3	2
RM - RECORDS MANAGEMENT	12	12	12	0	0
SA - COORD AGENCY FOR SPANISH AMERICANS	4	5	5	1	0
SC - SENIOR CITIZENS AFFAIRS	34	27	0	(34)	(27)
SS - SOCIAL SERVICES	820	782	814	(6)	32
TR - COUNTY TREASURER	37	34	35	(2)	1
TV - TRAFFIC & PARKING VIOLATIONS AGENCY	47	46	46	(1)	0
VS - VETERANS SERVICES AGENCY	8	3	3	(5)	0
YB - NASSAU COUNTY YOUTH BOARD	5	4	0	(5)	(4)
	8,410	**7,978**	**8,124**	**(286)**	**146**
2012 POSITION REDUCTION NOT REFLECTED AT DEPARTMENTAL LEVEL				**(724)**	**(724)**
Grand Total				**(1,010)**	**(578)**

Appendix B

Expense/Revenue Category	FY 2012-15 Plan	FY 2012- FY 2015 Plan Explanations
Expenditures		
Wages	Variable	Terms of existing contracts
Non-Police Pension	State Rates	Reflects State Comptroller's effective rate, and preliminary 2012 estimates
Police Pension	State Rates	Reflects State Comptroller's effective rate, and preliminary 2012 estimates
Health Ins. – Active	5.87%, 5.87%, 5.87%	Reflects NYSHIP'S estimated increase for 2012 adjusted for Headcount assumptions
Health Ins. – Retirees	8.27%, 8.27%, 8.27%	Reflects NYSHIP'S estimated increase for 2012 adjusted for Headcount assumptions
Other Than Personal Services	2.9%, 2.9%, 2.9%	
Utilities Light and Power Brokered Gas Trigen Fuel Water Telephone	 1.00%, 2.00%, 2.00% 4.94%, -2.78%, 4.92 2.00%, 2.00%, 2.00% -17.4%, -14.4%, -11.20% 1.00%, 1.00%, 1.00% 1.00%, 1.00%, 1.00%	 For 2013-2015repsectively, .S. Dept. of Energy Estimates For 2013-2015repsectively, .S. Dept. of Energy Estimates For 2013-2015repsectively, .S. Dept. of Energy Estimates Reflects current market expectations Reflects current market expectations Reflects current market expectations
Medicaid	\$3m, \$3m, \$3m	Reflects most current caseload information
Social Services Entitlements	Variable	Reflects most current caseload information
Special Education	Variable	Reflects most current caseload information
Revenues		
State Aid	Variable	Variable based upon reimbursement formula
Federal Aid	Variable	Variable based upon reimbursement formula
Sales Tax	2.90%, 2.90%, 2.90%	
Property Tax	None	No property tax increase in the baseline