Nassau County Interim Finance Authority

NIFA

REVIEW OF NASSAU COUNTY'S PROPOSED MULTI-YEAR FINANCIAL PLAN FISCAL 2015 - 2018

October 15, 2014

NASSAU COUNTY
INTERIM FINANCE AUTHORITY

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I. OVERVIEW

On September 15, 2014, the County submitted to NIFA its Proposed Multi-Year Financial Plan, Fiscal 2015-2018 (the "Proposed Plan"), the first year of which is the Proposed Budget for FY 2015 (the "Proposed Budget"). The following discussion reflects staff's views on its submission.

The Proposed Plan contains significant projected deficits, including approximately $243 million in FY 2015, when calculated in accordance with Generally Accepted Accounting Principles and without using "other financing sources" (such as bond proceeds) to support operating expenses (hereinafter, deficit on a "GAAP Basis"). The control period will continue as long as there is at least a 1% deficit (on a GAAP Basis) in the County's Major Funds (defined herein).

On a non-GAAP, budgetary basis the County's financial outlook appears to be improving, but this "improvement" can be attributed to the following major causes, not all of which are positive or representative of structural change.

The causes include:

1. County borrowing for expenses that should normally be paid for out of operating income (*e.g.*, tax certiorari refunds, judgments and settlements, and termination expenses) – and which are paid for out of operating revenues by other comparable municipalities;
2. County actions (*e.g.*, reductions in headcount, increases in the property tax levy and fees, and the installation of school-zone speed cameras);
3. State actions (*e.g.*, State authorization to amortize retirement contributions); and
4. NIFA's previously imposed wage freeze (cumulatively saved approximately $231 million through the end of FY 2013), which has now been lifted.

Some of the County's fiscal discipline has been self-generated, but often it has come at the urging of rating agencies or the direction of NIFA. A good example is NIFA's restriction on certain types of non-essential borrowing (cumulatively, since the beginning of the control period, NIFA has rejected borrowings of approximately $200 million). NIFA also required the County to identify savings and other sources of revenue to fund its labor contracts as a condition of lifting the wage freeze.

FY 2014 was supposed to be a critical year for the County in its efforts to ensure GAAP balance in FY 2015; unfortunately, our analysis indicates that GAAP balance in FY 2015 will not be achieved. In fact, it appears that the County has abandoned its efforts to achieve GAAP balance through the end of the Proposed Plan. For example, the County wants to borrow $151 million in 2015 and $118 million per year through 2018, to fund judgments and settlements, terminal leave, and its tax certiorari liability, which will create GAAP Basis deficits of the same amounts.

II. Discussion of FY 2014

Before examining the Proposed Plan we need to discuss the projected operating results for FY 2014 because they form the baseline for future years and are the foundation of our analysis of the County's revenue and expenditure assumptions for FY 2015 and FY 2016 – FY 2018 (the "Out-Years").

FY 2014 RISKS

Our analysis of revenues and expenditures indicates that the County could end FY 2014 with a substantial operating deficit when examined using both the budgetary basis and GAAP Basis, as required by State law.

We project a FY 2014 deficit of approximately $135 million on a budgetary basis and $173 million on a GAAP Basis if the risks we have identified all break unfavorably against the County. Likewise, the projections assume that no favorable variances develop in addition to those already identified. See "Projected FY 2014 Operating Results" table on page 5. It should be noted that these risks include almost $100 million in operating expenditures that the County proposes to fund with proceeds from proposed borrowings. The borrowings have not yet received NIFA approval and would not reduce the GAAP Basis calculation even if they are approved.

NIFA's projections of County deficits could result despite the County's multi-year efforts to increase revenues and reduce expenditures, including the realization of significant savings from the NIFA imposed wage freeze, which has now been lifted. The County estimates that the wage freeze cumulatively saved approximately $231 million. Significant, unanticipated shortfalls in projected sales tax revenues have exacerbated the fiscal challenges confronting the County.

The persistent projected GAAP Basis deficit results primarily from the County's continued reliance on bonding certain operating expenses, such as tax certiorari refunds, judgments and settlements, and employee termination expenses. It is important to note that even if the proposed borrowings for these operating expenses were approved, the GAAP Basis deficit would be unchanged.

The GAAP Basis deficit in FY 2014 could end up being smaller if (for example) fewer tax certiorari refunds are settled or paid, sales tax revenues pick up in the remaining months of the year, school-zone speed cameras generate more fines than assumed, and additional prior-year encumbrances are reversed. Alternatively, operating results could be worse than projected if sales tax revenues do not rebound in the remaining months of FY 2014. At best, the GAAP Basis deficit for FY 2014 will likely exceed by multiple times the control period trigger of a 1% deficit in the County's Major Funds.

Some of the major projected *budgetary revenue variances* in FY 2014 include the following:

- Fines and Forfeitures are projected to surpass budget by $12.4 million. The surplus is driven primarily by unbudgeted revenue from the school-zone speed camera program, which will offset lower than assumed ticket revenue for traffic and parking infractions, red light camera violations, and alarm permit fines.

- Rents and Recoveries are projected to surpass budget by approximately $27.8 million. The favorable variance results primarily from the recovery of prior year appropriations for unused Foster Care expenses in connection with the Persons in Need of Supervision, Juvenile Delinquency and Early Intervention and Preschool programs. The County has also been notified that it will receive $12.7 million in Community Development Block Grant ("CDBG") funding to cover FEMA expenses from Superstorm Sandy.

- Departmental revenues are projected to fall below budget by $9.8 million. The projected shortfall includes: at least $7.7 million in mortgage recording fees, $1.5 million in the Assessment Department because of its delay in implementing its tax map verification fee; $1.3 million in parks revenue; $1.3 million in tow truck franchise fees in the Police Department; and $1.0 million from a delay in implementing the Clerk's online registration fee.

- Federal and State aid will be $16.1 million lower than budget primarily due to lower reimbursable expenses for Early Intervention/Preschool Special Education and Direct Assistance services.

- Sales tax revenue this year, through the sales tax distribution on October 10th, is down 5.8% from the same period last year. Assuming that sales tax growth in the remaining months rebounds to historical rates for this period (2.3%), we project total year-end receipts to be $63.3 million lower than budget. If sales tax revenue does not grow during this period, then the year-end shortfall would reach $70.8 million. If sales tax revenue continues to decline, the shortfall will be ratably larger. Actual collections will depend on the timing and strength of any economic recovery in Nassau County and will not be known with certainty until after the last sales tax revenues related to FY 2014 are received in February 2015.

Projected FY 2014 Operating Results on a Budgetary Basis			
($ in millions)	**Adopted Budget**	**Current Projection**	**Surplus/(Risk)**
Revenues:			
Fines and Forfeitures	**$67.9**	**$80.3**	**$12.4**
Rents and Recoveries	**22.4**	**50.2**	**27.8**
Departmental Revenues	**165.8**	**156.0**	**(9.8)**
Federal and State Aid	**367.7**	**351.6**	**(16.1)**
Sales Tax	**1,165.8**	**1,102.5**	**(63.3)**
Other Revenue	**1,000.2**	**1,002.6**	**2.4**
Total Revenues	**2,789.8**	**2,743.2**	**(46.6)**
Expenditures:			
Salaries and Wages	**809.5**	**852.7**	**(43.2)**
Overtime(Police and Corrections)	*66.2*	*86.2*	*(20.0)*
Terminal Leave	*31.2*	*46.7*	*(15.5)*
VSIP and other payments (excluding term pay)	*0.0*	*6.6*	*(6.6)*
Other	*712.1*	*713.2*	*(1.1)*
Fringe Benefits	**480.4**	**472.2**	**8.2**
Contractual Services	**237.2**	**243.1**	**(5.9)**
Debt Service	**167.7**	**157.0**	**10.7**
Tax Certiorari Payments	**10.0**	**75.0**	**(65.0)**
Judgments and Settlements	**3.0**	**13.7**	**(10.7)**
Early Intervention/Special Education	**139.5**	**134.0**	**5.5**
Direct Assistance	**181.9**	**178.6**	**3.3**
Other Expenditures	**760.6**	**751.9**	**8.7**
Total Expenditures	**2,789.8**	**2,878.2**	**(88.4)**
Total Risk			**($135.0)**

Some of the major projected *expenditure budgetary variances* in FY 2014 include the following:

- <u>Expenditures for salaries and wages</u> are projected to exceed budget by approximately $43.2 million. The projected variance primarily comprises approximately $20.0 million in overspending on overtime (primarily in the Police Department), $15.5 million in unbudgeted terminal leave expenditures, and $6.6 million in incentive-related payments. These unfavorable variances, plus unbudgeted payroll costs incurred because the wage freeze was lifted, are partially offset by projected savings arising from vacant full-time positions, and other smaller favorable variances.

The County had requested authorization to bond up to $28.5 million in termination expenses, which are payments to separating employees for unused vacation and sick leave balances, and other VSIP-related costs (*e.g.*, separation incentive, longevity payments and previously lagged wages); however, we are currently projecting needs of only $22.1 million ($15.5 million plus $6.6 million) in FY 2014, as noted above. The County plans to use excess bond proceeds to cover deferred termination payments it must make to certain VSIP participants over the next three years (some participants elected this payout option) as well as to fund FY 2014 operating expenses. NIFA must approve all County borrowings.

In an effort to stem the increased use of police overtime, the County hired a class of 131 police officers in May and a second class of 67 police officers at the beginning of October. However, due to the length of training and ongoing attrition, it is unlikely that the new police officers can significantly impact overtime usage in FY 2014. The County also plans to hire an additional 100 police officers by the beginning of 2015 and potentially a second class sometime later in 2015.

- Fringe benefit savings of $8.2 million, which are driven primarily by health insurance premiums rising by less than the amount budgeted and vacant positions, will partially offset excess salaries and wages. It should be noted that fringe benefits costs would have been $71.5 million higher than currently projected had the County paid its full pension liability in FY 2014 rather than opting to amortize a portion of these costs over the next 12 years (this impacts budgetary basis accounting, only, and does not affect the timing or amount of GAAP pension expenses).

- Contractual costs are projected to be approximately $5.9 million more than budget due, in part, to new vendor costs associated with the school-zone speed camera program, higher costs for the Veolia Bus contract and greater outside counsel fees.

- Debt service costs are projected to be approximately $10.7 million less than budget due to lower than assumed debt issuances and interest rates on outstanding bonds. It should be noted that lower borrowing is partly due to the fact that NIFA has not approved certain borrowings requested by the County since declaring a Control Period (approximately $200 million in such borrowing has been rejected to date).

- Tax certiorari payments from operating funds are projected by the County to be only $10 million in FY 2014, even though the average commercial liability has been approximately $75 million per year. To make up for this shortfall and to pay some of the liability backlog, which was estimated by the

Comptroller to be $325 million at the end of 2013, the County assumes that it will borrow up to $75 million in 2014. The County has made the refunds contingent on receiving authorization to bond these costs to avoid booking an unfunded expense. The borrowing requires approval by the Legislature and NIFA.

- Judgments and Settlements expenditures are estimated by the County to be $13.7 million in 2014 (not including the recently decided "utilities" lawsuit) of which only $3 million has been budgeted from operating revenues and the remainder anticipated to be paid with borrowed monies. Amounts borrowed for judgments and settlements requires approval by the Legislature and NIFA.

- Expenditures for Early Intervention/Preschool Special Education services are projected to be approximately $5.5 million less than budget due to lower service rates and a decline in caseloads.

- Direct assistance costs, which include expenditures for recipient grants, purchased services, and emergency vendor payments, are projected to be $3.3 million less than budget. These costs are down primarily as a result of lower caseloads under the Temporary Assistance for Needy Families, Safety Net, Foster Care and other social services programs.

III. DISCUSSION OF FY 2015

As required by the County Charter and NIFA Act, the County submitted its Proposed Multi-Year Financial Plan, Fiscal 2015-2018 (see Appendix A) the first year of which is the Proposed Budget for FY 2015. Our analysis of the Proposed Budget indicates that the County could end FY 2015 with an operating deficit of approximately $209.2 million on a budgetary basis, or $242.8 million on a GAAP Basis, if all of the risks we have identified are not resolved. See "Analysis of Proposed FY 2015 Budget" table on page 10.

The projected risks include $25.3 million in higher property taxes (requires approval by the Legislature) and $151 million in proposed borrowings for operating expenses (requires approval by the Legislature and NIFA). The projected GAAP Basis results would be unchanged even if the proposed borrowings are approved since these resources are not revenues.

The absence of balance on a GAAP Basis (as mandated by the NIFA Act) is disconcerting as NIFA had required, and the County had previously committed, to achieving this requirement by FY 2015. The projected GAAP Basis results are more than eight times the $29.8 million deficit which would otherwise trigger a control period. Consequently, we do not expect the control period to be terminated.

FY 2015 RISKS

The risks in FY 2015 fall into two main categories:

A. Category One Risks – **Implementation Risks** ($32.9 million).

These are risks from actions that our analysis indicates may be difficult to execute and/or may result in fewer savings or less revenue than assumed.

For example, the County plans to sell certain properties for which no contracts currently exist. In addition, the County projects an increase in the amount of departmental revenue as well as a decrease in police overtime compared to projected FY 2014 levels.

B. Category Two Risks – **Requires NIFA or County Legislative Action** ($176.3 million).

These are risks that cannot be implemented until the County Legislature or NIFA takes a favorable action(s).

For example, the County proposes to bond almost all payments for tax certiorari refunds, judgments and settlements and termination expenses.

Analysis of Proposed FY 2015 Budget on a Budgetary Basis			
($ in millions)	FY 2015 Proposed	FY 2015 Projection	Surplus/(Risk)
Revenues:			
Fines and Forfeitures	**103.7**	**103.7**	**0.0**
Rents and Recoveries	**21.8**	**17.9**	**(3.9)**
Departmental Revenues	**170.8**	**163.8**	**(7.0)**
Bond Proceeds for Operations	**151.0**	**0.0**	**(151.0)**
Tax Certiorari Payments	*100.0*	*0.0*	*(100.0)*
Judgments & Settlements	*18.0*	*0.0*	*(18.0)*
Termination Payments	*33.0*	*0.0*	*(33.0)*
OTB Profits	**9.0**	**1.8**	**(7.2)**
Property Taxes	**832.3**	**807.0**	**(25.3)**
Sales Tax	**1,146.1**	**1,134.2**	**(11.9)**
Other Revenue	**549.0**	**549.0**	**0.0**
Total Revenues	**2,983.7**	**2,777.4**	**(206.3)**
Expenditures:			
Salaries and Wages	**849.3**	**867.4**	**(18.1)**
Overtime (PD and CC)	*69.4*	*84.4*	*(15.0)*
Savings from Initiatives	*(6.2)*	*(3.1)*	*(3.1)*
Other Salaries and Wages	*786.1*	*786.1*	*0.0*
Fringe Benefits	**496.1**	**493.9**	**2.2**
Workers' Compensation	**26.3**	**28.3**	**(2.0)**
Contractual Services	**254.3**	**254.3**	**0.0**
Tax Certiorari Payments	**100.7**	**100.7**	**0.0**
Judgments & Settlements	**21.2**	**21.2**	**0.0**
Other Expenditures	**1,235.8**	**1,235.8**	**0.0**
Total Expenditures	**2,983.7**	**3,001.6**	**(17.9)**
Subtotal of Risks			**($224.2)**
Contingency			**15.0**
Total Net Risk			**($209.2)**

The following discussion explains in greater detail what NIFA staff considers to be the major projected risks.

Fines and Forfeitures – The County has budgeted $103.7 million in anticipated revenue from fines and forfeitures. At this time, our analysis indicates that the County's revenue target is achievable. The greatest risk to this revenue, as well as the greatest upside potential, stems from anticipated ticket revenues from school-zone speed camera violations. The County expects to roll out the program to all 56 school districts by the end of the year, and has seen success at locations where it has already been implemented. Although very early results indicate that the County will meet its estimates, there is insufficient data to gauge its ultimate success, especially since violations will probably diminish as the public becomes more aware of the program.

Rents and Recoveries – The County has budgeted $21.8 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. Of this amount, the County expects to realize $3.9 million from the sale of County property in FY 2015. We consider the additional revenue to be at risk until specific parcels and potential purchasers are identified, contractual agreements are reached, and the legislative approvals are secured.

Departmental Revenues – The County has budgeted $170.8 million in departmental revenue, of which we project $7.0 million to be at risk. Most of this risk stems from five sources: a Geographic Information Services ("GIS") tax map verification fee initiative, which was approved by the Legislature in 2013, but not implemented; Clerk fees from a web-based document access initiative, which was also approved by the Legislature in 2013, but not implemented; projected shortfalls in Parks revenue; ambulance collection fees and police tow truck franchise fees, which have never met the County's expectations.

Bond Proceeds for Operations – The County has budgeted the use of $151.0 million in bond proceeds to pay operating expenses in FY 2015. These uses include $100.0 million for tax certiorari refunds, $18.0 million for judgments and settlements, and $33.0 million for employee termination costs. The borrowings require approval by the Legislature and NIFA and are subject to risk until the requisite authorizations are secured.

The County should be paying its operating costs with operating revenues as is done in other municipalities. The practice of financing these expenditures, which add to the GAAP Basis deficit, burdens future taxpayers with debt service costs for a benefit obtained solely by current taxpayers. These concerns have been noted many times by NIFA in past years and are also discussed elsewhere in this report.

OTB Profits – The County is projecting $9 million in profits from the installation of up to 1,000 video lottery terminals ("VLTs"), which were authorized by State legislation in July of 2013. The net revenue, after distributions for education, lottery administration and marketing, and New York Racing Association initiatives, is to be used to subsidize operations at the VLT gaming facility. Any remainder is to be remitted to Nassau County to "defray property costs." Although there is data which suggests the County can achieve its targets when implemented, we are concerned that delays are likely to reduce the amount that can be realized in FY 2015. The County has stated that the site selection should be announced in the coming weeks.

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 $1.146 billion for FY 2015, including $2.9 million in sales tax earned in 2013, but for technical reasons not accounted for until FY 2015. ("Deferred Sales Tax"). Our analysis indicates that sales tax revenue may be overstated by $11.9 million.

The County projects that sales tax revenue will grow in FY 2015 by 3.0% over the amount projected in FY 2014. We consider this growth rate assumption to be reasonable. Projected sales tax revenues could be greater or smaller to the extent that sales tax revenues in FY 2014 vary from assumed levels. This revenue source requires close monitoring and the County must be prepared to quickly mitigate shortfalls that would likely materialize if the current weakness in sales tax collections continues through the end of FY 2014.

Property Tax – Property tax revenue, which provides a dependable source of recurring revenues, is projected to account for almost 30% of all revenues in the Major Funds. It is budgeted at $832.3 million, which is an increase from the $807.0 million budgeted in FY 2014. The increase must be approved by the Legislature.

Salaries and Wages – The County projects that salaries and wages will total $849.3 million in its Major Funds, which are defined as the General Fund, the Police District Fund, the Police Headquarters Fund, the Fire Commission Fund, and the Debt Service Fund. In contrast, our analysis indicates that salaries and wages may be underfunded by $18.1 million and must be closely managed.

The County's projections reflect: (1) the cost of the recently lifted NIFA imposed wage freeze and the impact of the union settlements (CSEA, PBA, DAI, SOA and COBA) through 2017, and (2) optimistic budgeting of overtime expenses and attrition savings.

In regard to overtime expenses, although the Proposed Budget increases funding by $5 million over FY 2014 budgeted levels, our analysis indicates that this will likely be insufficient. The County has consistently exceeded its overtime budget. For example, it was exceeded by $20 million in FY 2013 and we are projecting a comparable deficit in FY 2014. Therefore, in spite of the new police hires and management's continued promises to control overtime usage, we anticipate the County will exceed its overtime budget by approximately $15 million.

Additionally, the Proposed Budget includes approximately $6 million for savings from attrition. Although the County will experience attrition, due to workforce reductions achieved through multiple Voluntary Separation Incentive Programs ("VSIPs") in recent years, many of the attritted positions will likely need to be backfilled in order to continue providing key services. Consequently, we believe that only approximately half of the projected savings are achievable.

Headcount – The County's Proposed Budget maintains headcount ("HC") at the same level as the FY 2014 Adopted Budget of 7,395 full-time positions (see Appendix B). The County's on-board HC as of early September was 7,224, or 171 positions below the budgeted HC. An additional 198 separations also occurred due to the VSIP recently offered to CSEA employees. As of this writing, it is unclear how many of these positions will need to be backfilled since the County has not provided us with its plan.

Fringe Benefits – The projected expenditures for health insurance for current employees and retirees appear to be reasonably stated but must be carefully monitored to assess increased budgetary pressure in the event that the County backfills positions which, despite required contributions by new employees, would result in an increase in health insurance costs to the County.

For the fourth consecutive year, the County is taking advantage of a State authorized provision that allows the County to amortize certain pension costs. This provision translates to savings of approximately $48.3 million in FY 2015. As we have warned in previous years, while the use of this provision will yield considerable budget relief in FY 2015, the effect of the amortization is to merely extend current liabilities into the future.

Workers' Compensation – the projections for Workers' Compensation in the Proposed Budget reflect a 2.8% decrease from the County's FY 2014 projections of $27 million. Therefore, we feel that the Proposed Budget allocation is optimistic and, based on current trends, may fall short by approximately $2.0 million.

Contractual Services – the County uses outside contractors for many different services. Within the Major Funds, approximately $34.5 million per year are for Health and Human Services and Social Services. Additionally, outside vendors provide medical and psychiatric services in the Correctional Center with costs averaging $15.5 million per year. The Traffic and Parking Violations Agency is projected to spend $22 million, a majority of which is for the provision of red light camera and school-zone speed camera monitoring and enforcement. The County could see savings in this area if school-zone speed cameras do not generate the assumed levels of fines since the vendor receives a percentage of collected revenues. Finally, the Veolia contract costs approximately $123.8 million for the provision of bus transportation services.

Tax Certiorari Payments –The County has acknowledged over $300 million in tax certiorari liability. The County is proposing to repay this entire amount, plus all new liability, out of borrowed funds. This liability has been allowed to languish in recent years, out of public view, as a way to preserve operating income. To this amount must be added between $200 and $300 million which may be payable under the recently decided "utilities" lawsuit.

In June, the State Assembly and Senate passed legislation that created a "Disputed Assessment Fund" by which commercial property owners will, in essence, self-fund refunds that are due for contested property assessments. We acknowledge this as a major accomplishment and hope that the Governor will sign the bill. However, assuming all goes as planned, this new legislation will have no effect on the County's tax certiorari liability until calendar year 2017 and no impact on the County's budget until 2018. In the meantime, old cases will languish and new cases will arise.

NIFA recognizes that prior to 2017 the County must pay down much of its backlog of tax certiorari claims and liability without any new, foreseeable revenue sources. We also understand that it may be an unfair burden to current residents to have to pay all of the backlog through the use of operating income since this liability has accrued over many prior years. However, it is not unreasonable for current residents to be asked to pay for new liability that will be created in the coming years.

Consequently, we will look to the County to propose some kind of equitable distribution of the liability between bonding and current income. This has been our position since NIFA was created and we thought that it had become a policy of the County. Once we receive a reasonable and carefully constructed plan, we may then be in a position to allow for the judicious use of borrowed funds.

Judgments and Settlements – Every municipality encounters judgments and settlements in the normal course of business. Within a limited range, these costs are predictable. Consequently, they should be budgeted as part of the operating budget, as they are in the budgets of other municipalities in New York State. However, although the County has estimated a need of approximately $21 million for judgments and settlements, it proposes to borrow $18 million to pay substantially all of these expenses in FY 2015. The County makes similar expense and borrowing assumptions for the Out-Years. Therefore, the County is only providing approximately $3 million within the operating budget to cover these costs.

As we have stated in the past, only in the case of extraordinary judgments or settlements should they be funded through borrowing or from an appropriate reserve. Borrowing for these expenditures merely defers the impact of the current year's operating costs to future periods and sidesteps NIFA's earlier directive to fund these costs in the operating budget after FY 2014. The borrowing requires authorization by the Legislature and NIFA, which had previously directed the County to stop using this fiscally imprudent funding practice.

Other Expenditures – We project that the County has reasonably estimated its other expenditures. While variations are likely to develop during the year, we expect the County to be able to identify offsetting savings.

Contingency Reserve – The Proposed Budget allocates $15 million for contingencies. Although our analysis indicates that the Proposed Budget contains fewer risks, other than proposed borrowings, than in recent years, the amount appropriated for contingencies may be insufficient to mitigate unanticipated shortfalls that could emerge in FY 2015, such as from lower revenues from sales taxes or speed camera violations. The County's decision to not maintain any reserve for contingencies in the Out-Years is even more disconcerting and fiscally imprudent.

Other Major Concerns

In addition to these risks, there are two major concerns that we have not included on the risk table, but are important factors in achieving and maintaining GAAP balance.

Fund Balance – The Proposed Budget includes as "revenue" a draw of $15 million against its unreserved fund balance, as was done in FY 2012, FY 2013, and FY 2014. The County has informed us that it would take this action only if, and to the extent, that the $15 million is needed to mitigate budgetary variances.

Fund balance "resources" are not considered revenue under GAAP and, therefore, its use does not help to advance the County's effort to achieve GAAP Basis balance. Of equal importance is that the County Comptroller has noted previously that the County's unreserved fund balance, including the County-wide Special Purpose Funds, should be replenished and increased, not reduced. Fund balance should be preserved in case of unforeseen budgetary emergencies, and reductions could potentially lead to a downgrade in the County's credit rating.

Sewer and Storm Water Resource District – Although the Sewer and Storm Water Resource District is not one of the five Major Funds, as defined in the NIFA Act, we have concerns regarding the sustainability of its business model. Simply stated, projected baseline revenues are insufficient to support projected baseline expenditures and, absent other gap-closing measures and the depletion of remaining fund balance, will likely necessitate future increases in the sewer tax levy.

In 2003, at the request of the County, the New York State Legislature created the Nassau County Sewer and Storm Water Finance Authority and a consolidated County-wide Sewer and Storm Water Resource District. The primary purposes of the Authority are to refinance outstanding sewer and storm water resources debt issued by the County and to finance future County sewer and storm water resources projects.

The Statute required the County to transition down to three Zones of Assessment within the Sewer and Storm Water District by 2014 (the "System"). The tax levy for all the Zones of Assessment has been as high as $138.9 million in 2004, 2005 and 2006 and as low as $103.9 million in 2008. The decrease was due to a shift of certain parts of the levy to the Major Operating Funds. The levy was $117.3 million in FY 2014.

The Proposed Plan reflects projected savings from four major County initiatives. The County maintains that these actions, combined with other budget modifications, will make up for projected deficits in the System which, in the FY 2014-2017 Multi-Year Plan, it estimated to be $50 million in FY 2015, $53 million in FY 2016 and $50 million in FY 2017.

- The County has entered into an agreement with United Water to operate and maintain the System. The County expects United Water to operate the System more efficiently and at a lower cost than it could by itself, indicating a net savings each year of $10 million, including savings from lower payroll, general expenses, and utility costs that offset the contractual annual payments to United Water.
- The County has proposed to raise the sewer tax levy by $6 million in FY 2015.
- The County has proposed a debt refunding transaction that would reduce debt service costs by $4.2 million in FY 2015 ($5.3 million in overall present value savings) and eliminate the requirement to maintain a reserve for operations and maintenance of approximately $26 million.
- The County has increased its projection of revenues it expects to realize from the imposition of a service charge on tax exempt users. The service charge would bring in needed revenue to pay for services currently received by these entities for free, but paid for by other residential and commercial property owners in the County. In total, the County estimates that the service charge will generate $12.6 million in FY 2015, $18.1 million in FY 2016, $19.0 million in each of FY 2017 and FY 2018.

NIFA believes that savings and revenue from the first three sources can materialize. However, NIFA does not believe that revenue from the imposition of a service charge on tax exempt users will become available in the near term since this matter is being litigated and a preliminary injunction has prevented the County from implementing its plan.

IV. THE OUT-YEAR GAPS: FY 2016 – FY 2018

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

Sizing the Out-Year Gaps – Even if it can successfully implement its entire 2015 gap-closing plan, the County projects (on a budgetary basis) that baseline gaps of $49.8 million in FY 2016, $72.6 million in FY 2017, and $92.3 million in FY 2018 will emerge prior to implementing new gap-closing initiatives.

Projected Out-Year Gaps on a Budgetary Basis			
($ in millions)	**FY 2016**	**FY 2017**	**FY 2018**
County Estimated Baseline Gap*	**($49.8)**	**($72.6)**	**($92.3)**
NIFA Risks	**(210.0)**	**(223.2)**	**(233.5)**
NIFA Estimated Baseline Gap	**($259.8)**	**($295.8)**	**($325.8)**

*The baseline gaps were calculated by the County using growth rate assumptions listed in Appendix C.

However, our analysis indicates that if the risks we identified in FY 2015 are not satisfactorily addressed with recurring solutions, the County's projections of Out-Year gaps may be understated by approximately $210.0 million in FY 2016, $223.2 million in FY 2017, and $233.5 million in FY 2018. Most of these risks are carried forward from our analysis of projected revenues and expenditures in FY 2015 and are described in detail earlier in this report, beginning on page 9.

One major risk in FY 2015, related to borrowing for termination expenses, does not continue in the Out-Years since the County plans to begin paying these operating costs with operating revenues. In contrast, three new major risks arise (see below) related to the elimination of the contingency reserve, the elimination of the County's historic mission payment to the Nassau Health Care Corporation, and the projected growth in expenditures for providing health insurance to current employees and retirees.

Contingency Reserve - We advise the County to fund contingency reserves in each of the Out-Years with operating revenues rather than the current practice of using fund balance. Robust contingency reserves are necessary because of the probability that certain assumptions will break unfavorably against the County each year. Even a modest contingency reserve could buffer the otherwise disruptive impact on operations caused by unforeseen increases in expenditures or unanticipated shortfalls in revenues.

Historic Mission Payment – The FY 2014-2017 Multi-Year Plan had indicated the County's intention to end its annual $13 million historic mission payment to the Nassau Health Care Corporation ("NHCC") after its legal obligation expired in FY 2014. Notwithstanding that decision, the County reinstated the payment in the Proposed Budget but has eliminated its commitment in the Out-Years. The County's only remaining assistance would be limited to its guaranty of NHCC's outstanding long-term debt, which was $247 million as of December 31, 2013.

We are concerned about the fiscal stability of NHCC and the effect that any disruption in its services would have on the residents of Nassau County. However, the County should look first to its legal obligations and if it gives money to NHCC it should be convinced that the money will be spent in a targeted manner and for its highest and best uses.

Health Insurance - Our analysis indicates that the County's projections for health insurance costs may be understated by approximately $9 million in FY 2016, $16 million in FY 2017, and $23 million in FY 2018. We recommend that the County use more conservative growth rate assumptions to project the Out-Year costs of this fringe benefit, over which it has limited control for current employees and retirees.

*** * ***

The following discussion describes the County's plan to close the baseline gaps it has projected. However, as discussed above and illustrated in the table on page 17, our analysis indicates that the County's projections of baseline gaps are understated.

Closing the Out-Year Gaps – Our analysis indicates that the projected value of the County's gap-closing plan will be insufficient to close the NIFA estimated baseline gap (NIFA's projected risks plus the County's estimated baseline gap). See "County Gap Closing Plan" table on page 19. If successful, the projected gaps would still be $205.0 million in FY 2016, $215.4 million in FY 2017 and $233.4 million in FY 2018. Moreover, we think it is unlikely that the full savings from the proposed gap-closing initiatives can be realized.

County Gap-Closing Plan			
($ in millions)	**FY 2016**	**FY 2017**	**FY 2018**
NIFA Estimated Baseline Gap	**($259.8)**	**($295.8)**	**($325.8)**
County Gap-Closing Options			
Expense/Revenue Actions			
Suez Energy NA (TRIGEN)		$10.0	$20.0
Health Insurance Cost Reduction	$1.0	10.9	11.3
Workforce Management	10.4	10.8	11.2
United Water Synergy Savings	8.7	9.0	9.2
Advertising Revenue	6.0	8.0	8.0
Office Consolidation	2.0	3.0	4.0
Taxi Limousine Commission	2.0	2.0	2.0
Strategic Sourcing	2.0	2.0	2.0
BOE Reimbursement	2.0	2.0	2.0
ERP Implementation		2.0	2.0
Financing Options/Asset Sales			
Sale of Surplus County Property	5.0	5.0	5.0
NYS Actions			
Mandate Reform	10.0	10.0	10.0
LIE Surcharge	5.7	5.7	5.7
Total Gap-Closing Options	**$54.8**	**$80.4**	**$92.4**
Remaining Surplus/(Deficit)	**($205.0)**	**($215.4)**	**($233.4)**

Expense/Revenue Actions – The County has referenced several initiatives that it is pursuing and that it projects could generate additional revenue or reduce expenditures in the Out-Years. While this may be true, there are no detailed plans of implementation for us to evaluate.

Suez Energy NA (TRIGEN) Privatization – The County owns the cogeneration plant in Uniondale. There is an agreement between the County and Suez Energy NA to manage and operate the plant in Uniondale, which expires in 2016. The County believes that opportunities exist to generate additional revenue through expansion or monetization of the facility, which currently has excess capacity. Unfortunately, they have not outlined their plans and there is no indication that this concept is acceptable to the County Legislature.

Health Insurance Cost Reduction – The County refers to the concessions made by the labor unions where new employees would contribute 15% toward the cost of their health insurance. However, savings from this milestone achievement are already incorporated into the County's baseline projections. Reference is also made by the County to the Affordable Care Act, but no specifics are given to how the Act, implemented in 2010, would provide substantial savings in 2017 and 2018.

Workforce Management – The County claims that savings can be derived from eliminating vacant positions and filling other vacancies with employees earning lower salaries. Our analysis indicates that these savings have already been incorporated into the County's baseline projections. It is unclear if the County is proposing to contract part of its workforce, which could provide unbudgeted savings to the extent that funded vacancies remain unfilled.

United Water Synergy Savings – The projected gap-closing savings represents a combination of expenditure savings and revenue increases. The County anticipates that it can realize additional cost savings as Sewer and Storm Water employees leave the County's employment and are not replaced. The County also anticipates that it can generate additional revenue after it transfers some of the unneeded Sewer and Storm Water employees to revenue-generating tasks in certain other County departments that had been shorthanded in the past.

Advertising Revenue – The County expects to generate revenue through roadside and other forms of advertising. The County stated that an announcement is forthcoming, but we are skeptical since this idea has been floated and then unsuccessfully implemented, for many years.

Office Consolidation – The County claims that reductions in its workforce during the past few years have provided opportunities for reduction of office space and centralization of its staff. They also state that they have lagged in consolidation efforts, which they claim will generate savings. We question whether there would be significant savings without the transfer of employees out of leased space to County-owned facilities.

Taxi and Limousine Commission – The County intends to increase enforcement of current regulations and to expand existing laws regulations affecting businesses providing taxi, livery and limousine services to generate incremental revenue.

Strategic Sourcing – The County intends to continue pursuing efficiencies and savings through this initiative. They claim, without substantiation, that savings have already been realized and intend to expand this initiative in upcoming years.

BOE Reimbursement – As allowed by law, the County intends to allocate the cost of elections with local municipalities, which is a decision that the Nassau County Legislature must make. The Legislature did not pursue this for 2015, but may do so in 2016.

ERP Implementation – The County intends to pursue efficiencies and saving through by streamlining core business processes. No further details are known.

Financing Options/Asset Sales

Sale of Surplus County Property – Continuing from FY 2014, the County is counting on the receipt of revenue from sales of unidentified County properties. While there may be immediate value from the sale of land or buildings as a gap-closing initiative, it is a one-shot cash infusion that bridges the deficit between recurring revenues and expenditures but does nothing to address the persistent structural imbalance.

New York State Actions

Among the initiatives are two proposals that would require State approval before they could be advanced: (1) mandate reform; and (2) LIE surcharge.

Mandate Reform-The County believes that fraud and inefficiencies exist within State-mandated programs and intends to uncover those frauds and eliminate the inefficiencies.

LIE Surcharge-The County intends to seek permission from New York State to share the cost of patrolling State roads with Nassau County police officers. At this time, there is no sponsor in Albany in order to move this initiative forward and it has been repeatedly rejected in the past.

V. CONCLUSION

While the projected budgetary deficit may be manageable if all of the proposed borrowing is approved, the GAAP Basis deficit (the statutory standard by which NIFA is required to measure balance) continues to be well in excess of the trigger point for the continuation of a control period for every year of the Proposed Plan.

The County must cut back on its borrowing if it is ever going to free itself of a control period and regain its place among the pre-eminent counties in the Country. We have intentionally refrained from selecting from among key policy alternatives, leaving those decisions to the County's elected officials; however, the most obvious areas for reform are those that other municipal entities typically fund through operating income.

The County also has certain advantages and protections afforded to it through the NIFA Act. Some of these have been successfully utilized in the past, but the County has not proactively generated new ideas or legislation that might inure to its benefit despite suggestions from NIFA. We remain ready to partner with the County in considering new initiatives.

Finally, we remind the County that approval of the Proposed Plan is not approval of each single item in the Plan. It is solely an indication that after weighing all of initiatives in the Plan we believe that, on balance, it appears to be in substantial compliance with the requirements of the NIFA Act.

VI. APPENDICES

Appendix A

OBJECT	2015 PROPOSED BUDGET	2016 PLAN	2017 PLAN	2018 PLAN
EXPENDITURES				
AA - SALARIES, WAGES & FEES	849,268,675	875,451,927	903,231,324	909,782,197
AB - FRINGE BENEFITS	496,065,443	515,737,893	533,449,382	553,738,442
AC - WORKERS COMPENSATION	26,276,829	26,276,829	26,276,829	26,276,829
BB - EQUIPMENT	2,274,166	2,308,278	2,342,903	2,378,046
DD - GENERAL EXPENSES	35,201,389	35,439,763	35,800,973	36,235,021
DE - CONTRACTUAL SERVICES	254,280,075	257,891,289	259,732,996	261,606,291
DF - UTILITY COSTS	41,692,740	41,836,159	42,075,436	42,814,076
DG - VAR DIRECT EXPENSES	5,000,000	5,000,000	5,000,000	5,000,000
FF - INTEREST	100,721,845	116,413,351	127,752,474	138,183,797
GA - LOCAL GOVT ASST PROGRAM	68,501,853	70,183,149	71,906,478	73,672,890
GG - PRINCIPAL	80,260,000	92,060,002	107,565,000	120,914,999
HC - NHC ASSN EXP NASSAU HEALTH CARE ASSN	13,000,000	0	0	0
HH - INTERFD CHGS INTERFUND CHARGES	30,773,043	30,559,620	30,342,770	30,101,687
MM - MASS TRANSPORTATION	43,175,746	44,352,309	45,562,993	46,808,786
NA - NCIFA EXPENDITURES	1,900,000	1,950,000	2,000,000	1,925,000
OO - OTHER EXPENSE	366,301,231	341,518,396	326,587,039	314,254,915
PP - EARLY INTERVENTION/SPECIAL EDUCATION	135,000,000	137,700,000	140,454,000	143,263,080
SS - RECIPIENT GRANTS	60,550,000	61,761,000	62,996,220	62,996,220
TT - PURCHASED SERVICES	68,402,576	69,770,628	71,166,040	72,589,361
WW - EMERGENCY VENDOR PAYMENTS	52,755,000	51,699,900	51,182,901	51,182,901
XX - MEDICAID	252,255,731	252,571,349	252,571,349	257,115,874
TOTAL EXPENDITURES	**2,983,656,342**	**3,030,481,843**	**3,097,997,108**	**3,150,840,413**
REVENUES				
AA - FUND BALANCE	15,000,000	0	0	0
BA - INT PENALTY ON TAX	29,100,000	29,100,000	29,100,000	29,100,000
BC - PERMITS & LICENSES	16,274,987	15,274,987	16,274,987	15,274,987
BD - FINES & FORFEITS	103,748,400	106,797,574	106,797,574	106,797,574
BE - INVEST INCOME	2,118,700	2,118,700	2,118,700	2,118,700
BF - RENTS & RECOVERIES	21,751,615	18,364,232	21,564,232	21,564,232
BG - REVENUE OFFSET TO EXPENSE	11,412,000	11,412,000	11,412,000	11,412,000
BH - DEPT REVENUES	170,826,359	176,826,359	176,826,359	176,826,359
BI - CAP BACKCHARGES	0	0	0	0
BO - PAY LIEU TAX PAYMENT IN LIEW OF TAXES	11,663,465	11,663,465	11,663,465	11,663,465
BQ - D/S FROM CAP DEBT SERVICE FROM CAPITAL	122,224,000	121,816,000	121,816,000	121,816,000
BS - OTB NON-TAX REVENUE	9,000,000	22,000,000	25,000,000	25,000,000
BW - INTERFD CHGS INTERFUND CHARGES REVENUE	113,406,234	78,968,180	81,652,737	84,464,087
FA - FEDERAL AID REIMBURSEMENT OF EXPENSES	135,988,686	138,223,548	140,503,107	140,503,107
SA - STATE AID REIMBURSEMENT OF EXPENSES	209,891,279	212,410,917	214,982,287	216,463,776
TA - SALES TAX CO SALES TAX COUNTYWIDE	1,056,147,928	1,082,551,626	1,109,615,417	1,137,355,802
TB - PART COUNTY SALES TAX PART COUNTY	90,044,005	89,311,923	91,544,721	93,833,339
TL - PROPERTY TAX	832,277,017	832,277,017	832,277,017	832,277,017
TO - OTB 5% TAX	2,557,667	2,301,274	2,070,751	1,863,465
TX - SPECIAL TAXS SPECIAL TAXES	30,224,000	29,224,000	30,224,000	30,224,000
TOTAL REVENUES	**2,983,656,342**	**2,980,641,802**	**3,025,443,353**	**3,058,557,910**
PROJECTED SURPLUS/GAP	**0**	**(49,840,041)**	**(72,553,754)**	**(92,282,503)**

Appendix B

FY 2015 PROPOSED BUDGET FULL-TIME HEADCOUNT (HC) COMPARISON TABLE

Department	Sum of 2014 Adopted HC	Sum of 2015 Proposed HC	Inc/Dec	On-Board Sept 4, 2014	Inc/Dec
AR - ASSESSMENT REVIEW COMMISSION	29	30	1	28	(2)
AS - ASSESSMENT DEPARTMENT	158	148	(10)	149	1
AT - COUNTY ATTORNEY	107	98	(9)	93	(5)
BU - OFFICE OF MANAGEMENT AND BUDGET	25	25	0	24	(1)
CA - OFFICE OF CONSUMER AFFAIRS	27	25	(2)	25	0
CC - NC SHERIFF/CORRECTIONAL CENTER	1,134	1,072	(62)	1,041	(31)
CE - COUNTY EXECUTIVE	18	18	0	15	(3)
CF - OFFICE OF CONSTITUENT AFFAIRS	38	38	0	37	(1)
CL - COUNTY CLERK	84	84	0	84	0
CO - COUNTY COMPTROLLER	86	83	(3)	74	(9)
CS - CIVIL SERVICE	51	51	0	51	0
DA - DISTRICT ATTORNEY	375	373	(2)	366	(7)
EL - BOARD OF ELECTIONS	139	169	30	169	0
EM - EMERGENCY MANAGEMENT	9	11	2	10	(1)
FC - FIRE COMMISSION	95	93	(2)	93	0
HE - HEALTH DEPARTMENT	173	170	(3)	171	1
HI - HOUSING & INTERGOVERNMENTAL AFFAIRS	12	14	2	14	0
HR - COMMISSION ON HUMAN RIGHTS	8	8	0	8	0
HS - DEPARTMENT OF HUMAN SERVICES	77	70	(7)	70	0
IT - INFORMATION TECHNOLOGY	79	82	3	77	(5)
LE - COUNTY LEGISLATURE	102	95	(7)	85	(10)
LR - OFFICE OF LABOR RELATIONS	5	4	(1)	5	1
MA - OFFICE OF MINORITY AFFAIRS	6	6	0	6	0
ME - MEDICAL EXAMINER	72	75	3	69	(6)
PA - PUBLIC ADMINISTRATOR	6	6	0	6	0
PB - PROBATION	200	190	(10)	190	0
PD - POLICE DEPARTMENT	3,052	3,092	40	2,971	(121)
PE - DEPARTMENT OF HUMAN RESOURCES	9	9	0	9	0
PK - PARKS, RECREATION AND MUSEUMS	151	156	5	149	(7)
PR - PURCHASING DEPARTMENT	11	9	(2)	11	2
PW - PUBLIC WORKS DEPARTMENT	418	401	(17)	411	10
RM - RECORDS MANAGEMENT	14	12	(2)	12	0
SA - COORD AGENCY FOR SPANISH AMERICANS	4	4	0	4	0
SS - SOCIAL SERVICES	640	616	(24)	616	0
TR - COUNTY TREASURER	32	31	(1)	27	(4)
TV - TRAFFIC & PARKING VIOLATIONS AGENCY	43	47	4	47	0
VS - VETERANS SERVICES AGENCY	7	7	0	7	0
SubTotal	**7,496**	**7,422**	**(74)**	**7,224**	**(198)**
Unallocated HC Reduction	**(101)**	**(27)**	**74**	**0**	**27**
Grand Total	**7,395**	**7,395**	**0**	**7,224**	**(171)**

Appendix C

Expense/Revenue Category	FY 2016-18 Plan	FY 2016- FY 2018 Plan Explanations
Expenditures		
Wages		
Non-Police Pension	NYSERS, 0%, 4.62%	Estimates provided by the NYS Retirement System
Police Pension	NYSERS%, 3.27%, 3.52%	Estimates provided by the NYS Retirement System
Health Ins. – Active	4.46%, 4.46%, 4.46%	Highest average increase over last 3, 5, or 8 years
Health Ins. – Retirees	4.33%, 4.33%, 4.33%	Highest average increase over last 3, 5, or 8 years
Other Than Personal Services	1.5%, 1.5%, 1.5%	
Utilities Light and Power Brokered Gas Trigen Fuel Water Telephone	 1.11%, -0.65%, 1.57% -4.33%, 1.41%, 1.76% -2.03%, 1.82%, 2.05% -2.43%, -0.62%, 1.06% 3.18%, 3.18%, 3.18% 2.65%, 2.65%, 2.65%	 EIA (DOE) 2014 Annual Energy Outlook Price Projection for Mid-Atlantic Region Commercial Customers (June 2014) Base reference case) Blended (2/3 weighting for natural gas for electric power [EIA 2014 AEO] & 1/3 weighting for the 10 yr avg CPI [2.65%]) EIA (DOE) 2014 Annual Energy Outlook Price Projection for Mid-Atlantic Region Commercial Customers (June 2014) Base reference case) Historical Trend
Medicaid	Flat, Flat, Flat +1 Week	Reflects most current caseload information
Social Services Entitlements	Variable	Reflects most current caseload information
Special Education Program	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	2.5%, 2.5%, 2.5%	