NIFA Nassau County Interim Finance Authority

MEMORANDUM

TO: NIFA Directors

FROM: Richard L. Luke

RE: Review of Adopted FY 06 – FY 09 Financial Plan

DATE: December 1, 2005

Introduction

On October 14, 2005 the Directors accepted the Proposed Multi-Year Financial Plan for Fiscal Years 2006 – 2009 (the "Proposed Plan") submitted to NIFA by the County Executive. Consistent with the NIFA Act ("Act"), the County Executive submitted the Adopted Financial Plan ("Plan") to NIFA upon its final enactment on November 10, 2005.

The County provided NIFA with the details of the changes to the FY 2006 budget ("Budget"), along with the ordinances adopting the Budget and Plan and indicated that various other documents required by the Act would be provided to NIFA within 30 days. We have reviewed this submission and based upon the factors discussed below, we recommend that you take the final actions and make the necessary findings required by the Act to approve the Plan. While we recommend that the Board approve the Plan, we also believe that the Plan is more risky than the Proposed Plan submitted by the County Executive because: none of the risks identified in our October 14, 2005 report were dealt with; an annual growth rate of 3.6%, rather than the 3.2% assumed in the Proposed Plan, is needed to achieve the sales tax estimate in the Budget; several revenue projections have been increased; and several vacant and funded positions have been eliminated from the Budget thereby reducing an implicit reserve. The comments contained in this Memorandum need to be read in conjunction with our October 14, 2005 report.

Legislative Changes

On October 30, 2005 the County Legislature took action to modify the County Executive's Proposed Plan and FY 2006 Budget. The revised budget was unanimously approved, while the out-years of the Plan were approved 10-9, along party lines. On October 31, 2005 the County Executive signed the revised Budget and revised Plan into law. The Legislature committed to bringing the sworn officer headcount to 2,750 at a cost of $0.5 million in FY 2006, provided additional funding of $3.5 million for various programs, re-estimated debt service and Medicaid costs, and took two one time actions that were not material. In order to fund these additional costs, the Legislature reduced funded vacancies by approximately $1.4 million and increased various revenue projections by $7.8 million, including a one time recovery of $3.4 million of Medicaid reimbursement. In addition, even though the County projects that FY 2005 sales tax revenues will be $4.7 million less than the amount budgeted, the sales tax revenue estimates for FY 2006 and beyond remain unchanged. As a result, the County now needs annual growth of 3.6% in FY 2006, rather than the 3.2% originally projected in the Proposed Plan. Year to date growth for FY 2005 is only 2.1%.

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Major Changes from Proposed Budget to Adopted Budget

Expenditure Changes	**Amount** (in millions)
Staffing Changes	
Add 100 police officers (1/4 year in FY 2006)	$0.5
New staff	0.1
Sub-total	$0.6
New Program Costs	
SPCA initiative	$0.1
Home Energy Assistance Program (HEAP)	0.3
HHS programming	3.0
Human rights summer program	0.1
Sub-total	$3.5
Other Actions	
Debt service adjustments	$1.6
Lost Sewer and Storm Water chargeback revenue	0.4
Medicaid caseload re-estimate	2.5
Other adjustments (net)	(0.2)
Sub-total	$4.3
One Time Actions	
Police staffing analysis (FY 2006 only)	$0.3
Medicaid fraud adjustment (FY 2006 only)	0.5
Sub-total	$0.8
Total Expenditure Changes	**$9.2**

Funding Sources	**Amount** (in millions)
Vacancy Reductions	$1.4
Revenue Increases	
Investment income	$1.6
Medicaid 621 recoveries (FY 2006 only)	3.4
Insurance adjustments	0.5
Mitchell Field reimbursements	0.3
Surplus contractual services (County Executive and Budget)	0.3
Hotel/motel adjustment	0.1
Ambulance billing revenue	0.3
E911 surcharge revenue	0.6
State aid for telephone services to Courts	0.4
Federal aid for HEAP	0.3
Sub-total	$7.8
Total Funding Sources	**$9.2**

The following is a discussion of the major changes that were made to the Budget and the Proposed Plan by the Legislature:

Cost Increases

- **Police hiring –** The Budget appropriates an additional $450,000 in FY 2006 to hire 38 new police officers in the 4th quarter of the fiscal year. The County estimates that these October hires, which will augment an anticipated mid-year police class of 140 police officers, will raise the sworn police force level to 2,750, or 100 positions above the previously authorized level of 2,650. The County plans to maintain this higher level of sworn police strength in the out-years of the Plan. The Plan provides an additional $2.4 million in FY 2007, $3.6 million in FY 2008, and $5.1 million in FY 2009 to cover the costs associated with the additional 38 police officers.

  The County maintains that it only needed to accommodate the cost of an additional 38 police officers (rather than 100 police officers) to reach the new headcount target of 2,750 because the Proposed Plan had already included sufficient funding to cover a sworn strength level of 2,712. While our analysis indicates that the County's revised estimates are not unreasonable, we are concerned that the County has effectively appropriated, in advance, resources that would have otherwise become available, through attrition, to cover known risks and unforeseen events. This action provides another example of the County's recent departure from its past practice of utilizing prudent conservatism in its budgeting practices.

- **New program initiatives** - The Legislature increased funding for the following programs: Youth Board $1.1 million; Mental Health $1.3 million; Drug and Alcohol $0.8 million; Health Department $0.1 million; Social Services $0.4 million; Senior Citizens $0.4 million; Domestic Violence $0.1 million; and Legal Services $0.3 million.

- **Debt service adjustments –** For FY 2006 the County has increased debt service costs by $1.6 million, but shows cumulative savings of $6 million in the out years of the Plan, with savings of $1.3 million in FY 2007, $1.9 million in FY 2008, and $2.8 million in FY 2009. These changes are the net result of the County increasing its estimate of interest costs in FY 2006 for its planned TAN borrowing, reducing the size of the Fall 2005 NIFA borrowing, and increasing the amount of capital borrowing in the out years of the Plan.

- **Medicaid re-estimate –** Based upon higher caseloads in FY 2005, the County believes that Medicaid costs will increase by $2.5 million starting in FY 2006.

Funding Sources

- **Vacancy reductions** - The Legislature eliminated 19 funded vacancies with a value of $1.4 million, including fringe benefits. The vacancies included 5 positions in the Office of Management and Budget and 5 civilian positions in the Police Department. In prior years the County has used its discretion to limit mid-year hiring in order to generate requisite budget relief to offset increased overtime costs, particularly in the Police Department and the Correctional Center. The County still has a number of funded vacancies in the Budget and does not assume any turnover savings. However, the removal of these 19 vacant positions to fund new costs will reduce the County's flexibility to manage the Budget.

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- **Revenue increases** – The Legislature increased 2006 revenue projections by $7.8 million, including a one time recovery of Medicaid costs of $3.4 million, and recurring increases of $4.4 million. The recurring revenue increases included $1.6 million for investment income, $0.6 million for E911 surcharge, $0.5 million for insurance adjustment, and $0.3 million for increased reimbursements for the Nassau Coliseum. While most of these changes are not significant, the revised projections are less conservative then those contained in the proposed budget. NIFA is concerned with the Legislature's decision to change estimates of revenues rather than reduce expenditures.

Out-Years

In addition to projecting the out-year impact of the above actions, the Legislature also increased the amount of projected savings it will seek from police labor concessions by $1.2 million in FY 2007, $1.8 million in FY 2008, and $2.5 million in FY 2009. The presumption is that future police labor negotiations will generate additional savings equal to 50% of the cost of the additional police officers. While the County obtained various savings in the prior police contract, we are concerned that increasing the projected savings from future police negotiations is less conservative than earlier assumptions regarding the financial plan.

Conclusion

The Legislative changes are troubling as they have increased the level of risk in the Budget and Plan. In particular the Legislative changes: did not take any actions to address any of the risks discussed in our October 14, 2005 report; increased certain revenue projections; assumed a higher growth rate for sales tax revenues; and reduced the level of conservatism in the budget by eliminating some of the vacant positions that were funded in the budget. While our October 14, 2005 Report indicated that these risks were manageable within the context of a $2.4 million budget, the Legislative changes have increased the level of risk contained in the Budget.

In addition, the County is projecting that the FY 2005 will end with a surplus of $66 million. This projection assumes the receipt of $7.5 million of transitional State aid which has not yet been released by the State of New York. Should this $7.5 million not be released, this would reduce the projected FY 2005 surplus.

NIFA believes that the Budget contains risks in the amount of $29.3 million, which represents more than 1% of the County's FY 2006 operating budget. On November 18, 2005, the New York State Health Insurance Plan notified the County of its health insurance rates for FY 2006. The rates are scheduled to increase approximately 11% for active employees and more than 5% for retirees, rather than the 8% for active employees, and 5% for retirees assumed in each year of the Plan. As a result NIFA believes that FY 2006 health insurance costs could be understated by approximately $3 million. If health insurance rates continue to grow at the same rate, the risk increases to $6 million in FY 2007, $10 million in FY 2008, and $15 million in FY 2009. In addition we are concerned that the recent financial performance of the Nassau Health Care Corporation could require that the Corporation and County make hard choices about the future direction of the Corporation. Some of those choices could involve additional County resources. Some of these risks could be offset depending upon actual employee turnover, and how many vacant positions the County actually chooses to fill.

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- Hotel/motel tax - $1.5 million
- Sales tax - $5.5 million
- Health insurance costs - $3 million
- Overtime - $7 million
- ShOA savings - $5.7 million
- Consumer affairs revenue - $1.2 million
- HHS consolidation - $0.8 million
- Revenue extenders - $4.6 million (Legislation to extend these revenues has been passed by the State Legislature and on November 18, 2005 it was sent to the Governor for his signature.)

While we believe that FY 2006 is likely to end without a deficit, we are concerned that the Legislative changes will make it more difficult to achieve a surplus and therefore, closer monitoring will be required throughout the year. While the Legislature has previously shown wisdom in offering additions with real expenditure cuts, the trend towards revenue adjustments is worrisome. Because of these concerns we are recommending that the Board require the County to submit an update of the Plan no later than April 1, 2006, rather than June 1, 2006 as previously approved by the Directors.