NIFA Nassau County Interim Finance Authority

October 14, 2005

Hon. Thomas Suozzi
Nassau County Executive
Office of the County Executive
One West Street
Mineola, NY 11501-4895

Hon. County Executive Suozzi:

Pursuant to the Nassau County Interim Finance Authority ("NIFA") Act, we have completed our review of the Proposed Multi-Year Financial Plan - Fiscal 2006-2009 ("Proposed Plan"). Our review is transmitted to you in the attached report entitled, "Nassau County Interim Finance Authority Review of the Proposed Multi-Year Financial Plan – Fiscal 2006-2009" ("Report").

The Report has been reviewed and adopted by the NIFA Directors. NIFA formally accepts the Proposed Plan and finds that it is in substantial compliance with the requirements laid out in the NIFA Act. The County Legislature will now review NIFA's Report and either adopt, reject, or modify the Proposed Plan. The adopted plan will then be returned to NIFA for final action.

Before we summarize our Report, we wish to commend the County on its continued progress in restoring Nassau County to fiscal health. NIFA looks forward to working with the County in the coming year to help maintain this positive momentum.

Briefly summarized, our Report finds that:

FY 2005 – NIFA concurs with the County that it should achieve an operating surplus.

FY 2006 - This first year of the Proposed Plan, which is the County's proposed 2006 Budget, is reasonable; however NIFA has identified a number of risks that must be considered when adopting the plan.

FY 2007 - FY 2009 (the "Out-Years") – The County continues to have large out-year gaps, although they have been reduced significantly by the State-enacted Medicaid cap and the use of several less conservative revenue and expenditure assumptions. We acknowledge that Nassau County is not alone in confronting these gaps, but their resolution will be more difficult now that NIFA aid is substantially completed.

The NIFA Act requires that during the Interim Finance Period, which does not terminate until the end of 2007, a high level of oversight be maintained. We intend to follow that statutory mandate and to constructively assist in the County's recovery.

In the past four years, the County has submitted an update of its financial plan. NIFA believes that these updates have been useful for both NIFA and the County. Therefore, NIFA is again requesting that the County submit a financial plan update no later than June 1, 2006.

Sincerely,

Ronald A. Stack
Chairman

cc: Presiding Officer Jacobs
Minority Leader Schmitt
Comptroller Weitzman
NIFA Directors
Richard Luke

Nassau County Interim Finance Authority

NIFA

REVIEW OF THE PROPOSED MULTI-YEAR FINANCIAL PLAN FISCAL 2006 – 2009

October 14, 2005

NASSAU COUNTY INTERIM FINANCE AUTHORITY

Table of Contents

I. Overview

We are pleased to report that by combining the County's conservative budgeting and NIFA's assistance together with a series of administrative and legislative actions, continued progress has been made toward restoring fiscal health to Nassau County. NIFA now believes that structural budgetary balance, where recurring expenses are offset by recurring revenues, is possible. While the County has made enormous strides the County must continue to be vigilant as continuing out-year gaps which the County estimates at $175.3 million in 2007, $230 million in 2008, and $272.3 million in 2009 continue to exist.

As of the close of 2004, the County had an undesignated fund balance of $90.5 million. This milestone was achieved through major County initiatives and NIFA assistance. The County's initiatives since 2002 have included: increasing property taxes by 20%; reducing the workforce; realigning the County's debt burden; implementing Smart Government Initiatives; and implementing new management practices that provide greater control.

NIFA, through its statutory authority and credit rating, has also played a significant role in the County's recovery. NIFA has provided $92.7 million of unrestricted State Aid; budgetary relief of $236.1 million by financing maturing debt; and debt service savings of $146.6 million by restructuring and refinancing County debt to bring savings forward and take advantage of favorable interest rates.

NIFA has also helped to impose better budgetary practices through a series of initiatives and statutory mandates. NIFA's oversight responsibility will continue until the end of the Interim Finance Period in 2007 and, to a lesser degree, until NIFA no longer has bonds outstanding.

Nassau County – the Executive and Legislative branches - deserve credit for moving the County forward and strengthening its finances. NIFA looks forward to a continued partnership with the County as it moves into 2006 and 2007.

Findings

NIFA staff is recommending acceptance of the Proposed Plan. This does not mean that NIFA agrees with all the estimates and assumptions contained in the Proposed Plan, or endorses all the initiatives and policy choices. Acceptance means that the Proposed Plan, in total, is reasonably likely to lead to balanced operating results in the first year (the Budget Year) and adequately recognizes and addresses out-year revenues, expenses and gaps.

NIFA is making the following general findings:

1. The Proposed Plan continues to be presented in a professional, comprehensive and well thought out fashion.

2. NIFA has identified a number of risks; however, most appear to be manageable within the context of the $2.4 billion budget.

3. The County used $95.1 million of non-recurring resources to balance the FY 2006 budget and reduced some of its future gap-closing savings from workforce management and smart government initiatives while leaving projected property tax increases unchanged.

4. The County's out-year assumptions regarding sales tax collections and health insurance costs are less conservative than in prior years.

5. While the County has begun to make progress in dealing with the tax certiorari dilemma, much more work needs to be done to avoid future problems.

6. Capital expenditures for infrastructure remain very low considering the extent of the needs in this area.

7. The Nassau Health Care Corporation ("NHCC") is still operating at a deficit and only has two weeks of operating cash which could significantly impair its operations. Of particular concern is the operation of the A. Holly Patterson nursing home.

8. The County has not provided an update of its information technology plan; therefore, NIFA cannot evaluate this component of the County's program.

NIFA is making the following findings about the specific years of the Proposed Plan.

FY 2006 - This first year of the Proposed Plan, also known as the proposed FY 2006 budget (the "Budget") is reasonable.

FY 2007 - FY 2009 (the "Out-Years") – The County continues to have large out-year gaps, although they have been reduced significantly by the State-enacted Medicaid cap and the use of several less conservative revenue and expenditure assumptions.

CONCLUSION

Nassau County has made significant headway in reducing near-term gaps and we believe that the Proposed Plan is reasonable. If the County makes any changes to the Proposed Plan, offsetting changes of equal value must be made to ensure that budgetary balance is maintained. NIFA staff will study their impact on the Adopted Plan before making its final recommendation to the Directors.

The discussion that follows and transmittal letter constitute the NIFA staff's review and recommended findings regarding the County Executive's Budget and Proposed Plan. It is proposed that this document be adopted by NIFA as the Report of the Directors and that copies of this document be transmitted to the Nassau County Executive, the Presiding Officer of the Nassau County Legislature, the Minority Leader of the Nassau County Legislature, the Nassau County Comptroller and Clerk of the Nassau County Legislature for distribution to members of the County Legislature.

II. Risk Assessment

This section presents NIFA's analysis and conclusions regarding the proposed FY 2006 Budget and the major underlying initiatives designed to ensure year-end budgetary balance. The County's ability to achieve its fiscal objectives for FY 2006 is directly dependent on the actions that the County takes in the remainder of FY 2005 and its ability to fully implement its FY 2006 gap-closing actions.

Since any budget or financial plan is a set of estimates, the actual results will differ from initial expenditure and revenue estimates. Risk assessment attempts to identify what these differences will be and whether they will ease or worsen budget pressures. Normally, the emergence of offsets can cover routine risks, but rigorous and timely monitoring can reduce the possibility that risks may break disproportionately against the County and require significant gap-closing actions near the end of a fiscal year.

The County will be confronted with a wide range of fiscal problems to solve during the next several years and there is always the possibility that baseline estimates may prove incorrect or that reasonable gap-closing initiatives will not be achieved. Risk assessment identifies those areas where corrections need to be made, or those areas where monitoring can allow for earlier identification of potential problems so that corrective action can be taken as soon as possible. For the purpose of NIFA's analysis, risks have been classified into two major categories.

The *first* category is the quantifiable risks that affect the Proposed FY 2006 Budget and include items that may be:

- difficult to execute and/or may result in fewer savings or less revenue than assumed; and
- errors or omissions that occurred during preparation of the Budget.

The *second* category of risks are those that cannot be quantified but have the potential to negatively impact all years of the Proposed Plan. These risks are highlighted during our discussion of the specific action or initiative.

FY 2006 Budget Risks

NIFA has identified a number of actions or initiatives that may be at risk and the County must monitor closely. The upper panel of Table 1 identifies the portion of the item that NIFA believes is unlikely to occur or is in error.

For example, if NIFA believes that a particular expense is incorrect, the amount of understatement will be identified. In those cases where NIFA believes that the full amount of a savings initiative will not be realized, NIFA will identify the amount that it believes will not be realized. In both cases, the County Legislature must weigh the risks and have substitute initiatives ready for enactment. This concept holds true for any other changes that may be made by the County Legislature. If any new programs, services or costs are added by the County Legislature, offsetting recurring actions must be identified to ensure that the Budget and Proposed Plan remain balanced.

FY 2006 – FY 2009 Financial Plan Risks

The lower panel of Table 1 presents those risks that cannot be easily quantified and primarily affect the County's ability to achieve the results projected in the out-years of the Proposed Plan.

(Table 1)
BUDGET RISKS AND OFFSETS

		Estimated Risk ($ in millions)	Page
FY 2006 Budget Risks	**Risks**		
	Medicare Part D	$10.4	18
	Overtime (net of ShOA risk)	7.0	17
	ShOA Savings	5.7	16
	Sales Tax	5.5	11
	Revenue Extenders	4.6	14
	Hotel/Motel Tax	1.4	14
	Consumer Affairs Revenue	1.2	35
	HHS Consolidation	0.8	31
	Subtotal	**$36.6**	
	Less Contingency Reserve	(5.0)	12
	Total	**$31.6**	
FY 2007 – FY 2009 Financial Plan Risks	Sales Tax- See page 11		
	Health Insurance– See page 18		
	Utility Costs – See page 21		
	Nassau Health Care Corporation – See page 25		
	Workforce Reduction Sustainability – See page 37		
	Tax Certiorari – See page 38		

While NIFA has identified the risks set forth above, we believe that most of them are manageable within the context of a budget of approximately $2.4 billion.

III. Proposed FY 2006 - FY 2009 Financial Plan

FY 2005 RECAP

Before discussing the Proposed Plan we need to discuss the projected operating results for FY 2005 because this forms the baseline for future years. The Administration submitted a FY 2005 Budget that was reviewed by NIFA and thought to be reasonable. The County's June 30, 2005 Budget Status Report projected a positive operating result of $54.8 million. The County Comptroller's Mid-Year Budget Report projected a positive operating result that could range from $48 million to $70 million. Included in these projections is approximately $55.6 million of non-recurring resources that the County has earmarked for gap-closing purposes in FY 2006 – FY 2008. This practice is consistent with prior years where the County has used surplus funds to pre-pay future expenses and fund reserves. This is a prudent fiscal policy that is supported by NIFA.

The June 30, 2005 Budget Status Report described a number of projected variances that largely offset each other. The major variances from the budget include increased overtime costs, reduced health insurance costs, reduced Medicaid costs, reduced sales tax collections, and the recognition of several non-recurring resources. The major non-recurring resources, totaling $53.5 million, include:

- $24.9 million in prior years' funds that have accumulated in the Capital Projects Fund to pay debt service on specific projects.

- $15.1 million of General Fund relief by transferring 2003 storm water costs to the Sewer and Storm Water Resource District Fund.

- $13.5 million from the reversal of the year end Medicaid accrual because of the new cap on Medicaid expenditures.

The projection presumes that the County will receive $7.5 million of State transitional aid this year. In order to receive the transitional aid, the authorizing legislation provides "that the Nassau county has demonstrated by October 1, 2005 that such funds are necessary to address a 2005 county budget deficit". On September 30, 2005 the County submitted its request for the $7.5 million based upon its new projection of an $8.6 million deficit in the Police District Fund. The Police District Fund is a separate tax district (excluding the cities, villages or police districts in Nassau County that maintain their own police forces) that is supported by a separate property tax levy different from the General Fund. The County's request is in the process of being reviewed.

Earlier in the year the County reduced its sales tax projection by $7 million because collections through the end of May 2005 were almost 2% below prior year's collections. The Proposed Plan now assumes that full year sales tax collections will grow by 2.6% to meet its FY 2005 budget estimate of $964.7 million. In order to achieve 2.6% growth for the full year, this year's remaining payments must grow by 3.9% over last year's collections which is above the 2.07% growth rate experienced so far this year. NIFA is particularly concerned about the likelihood that the County will achieve the projected growth because of recent reports that holiday sales may be slowed as a result of recent economic events, resulting in reduced collections for the balance of the year. Assuming that the remaining payments grow by the same 2.07%, the County will receive $959.4 million, or $5.3 million less that the budgeted amount.

Based upon historical data, analysis to date, and discussions with various County officials, NIFA concludes that for 2005:

- The County should end the year with a surplus. The major source of the surplus comes from non-recurring resources. Without these non-recurring resources the County would end the year essentially even.

- The County's request for the $7.5 million of transitional State aid is being reviewed.

- NIFA is concerned that sales tax revenues will not grow at a rate sufficient to achieve the budgeted amount of $964.7 million. Assuming that the remaining payments grow by the same 2.07%, the County will receive $959.4 million, or $5.3 million less that the budgeted amount.

- This will be the third year since the creation of NIFA that the County should have an operating surplus without NIFA and State assistance.

CLOSING THE FY 2006 BUDGET GAP

The June Update submitted by the County projected a gap of $148.6 million, which was reduced by $55.9 million from the gap projected in the Adopted Plan, primarily because of the benefit of the State-enacted cap on Medicaid expenditures. The Proposed Plan successfully closes the budget gap in FY 2006 and page 14 of the County's Proposed Plan identifies the most significant actions taken to close the gap. As shown in Table 2, the $148.6 million gap was closed with County actions totaling $117.8 million, of which $95.1 million are non-recurring actions.

Since the June Update, the County changed its FY 2006 gap-closing program in several ways. The revised gap-closing program eliminates the workforce reduction savings of $22.3 million and reduces the value of the Smart Government Initiatives by $8.9 million. In order to offset these changes the County increased its 2006 sales tax estimate by $10 million, will use an additional $6.5 million from the pension reserve, recognizes $7.4 million of non-recurring savings from prior NIFA borrowings, and $5 million of pre-payments. The County needs to be cautious because a number of recurring actions were replaced with gap-closing measures that are non-recurring in nature. When combined with the use of $55.3 million of non-recurring items used to balance the FY 2005 Budget, the County will have used $150.4 million of non-recurring actions, excluding tobacco proceeds, to close the FY 2005 and FY 2006 budgets.

(Table 2)
FY 2006 GAP-CLOSING ACTIONS

Type of Action	**Amount**	**%**
County Actions - Recurring		
Smart Government Initiatives	$10.0	
State Reimbursement Indirect Costs	7.0	
Labor Concessions	5.7	
Sub-total	**$22.7**	**14.9**
County Actions - Non-Recurring		
Certiorari PAYGO Funding	$50.0	
Pension Reserve	29.2	
Bonded Indebtedness Reserve	10.9	
Prepayment of Expenses	5.0	
Sub-total	**$95.1**	**62.2**
Other actions		
Medicare Part D	$10.4	
Improved Sales Tax Collections	10.0	
Debt Service Savings	7.4	
Reduced Health Insurance Rates	4.6	
Medicaid Cap	2.6	
Sub-total	**$35.0**	**22.9**
Total	**$152.8**	**100.0**

Excessive reliance upon non-recurring resources was one of the problems that contributed to the County's fiscal instability. Reduced reliance upon recurring actions also means that the out-years gaps are not reduced as quickly as possible. This conclusion is supported by the fact that even though the County took actions necessary to close a $148.6 million gap for FY 2006, the gaps contained in the June Update were only reduced by $56.3 million in FY 2007, and $72 million in FY 2008.

THE OUT-YEAR GAPS – FY 2007 – FY 2009

This section discusses the growth rates used by the County to project revenues and expenditures in the Proposed Plan as well as the actions proposed by the County to close the projected Out-Year gaps. The County has previously pointed to rising mandates such as Medicaid, health insurance, and pension contributions as the cause of the gaps. To this list we would add salary costs that have grown faster than inflation. There are other uncertainties, such as NHCC and the projected certiorari settlements that may significantly affect future gaps. With implementation of the Medicaid cap and pension costs leveling off, these costs should be more controllable in the future.

Sizing the Out-Year Gaps

The County projects gaps of $175.3 million in FY 2007, $230.0 million in FY 2008, and $272.3 million in FY 2009. These gaps were calculated based upon the growth rates set forth in Table 3. Based upon our review of the growth rates used by the County, and the underlying assumptions, we believe that the projections of out-year gaps are reasonable, except for health insurance. As discussed in the section on health insurance we believe that the growth rates used may be understated. While the gaps have declined since our October 5, 2004 report on the FY 2005 – FY 2008 financial plan, it should be noted that the major cause of the decline is the implementation of the State-enacted Medicaid cap, and the use of several assumptions that are less conservative than previously used by the County.

When compared with the Adopted Plan, the growth rates for the following significant items have been changed, reducing the projected gaps:

- Health insurance rates have declined from 12% for all employees, to 8% for active employees and 5% for retirees.
- Early intervention growth rates have been reduced from 4.9% to 3.3%
- Special education growth rates have been reduced from 5.5% to 3.3%.
- Sales tax growth rates have increased from 3% to 4%.

(Table 3)
MULTI-YEAR PLAN GROWTH RATE ASSUMPTIONS

Expense/Revenue Category	FY 2005-08 Plan	FY 2005-08 Update	FY 2006-09 Plan	FY 2006- FY 2009 Plan Explanations
Expenditures				
Wages	Contracts	Contracts	Contracts	Reflects terms of existing contracts
Non-Police Pension	13.4%	13.4%	11.7%	0.50% rate reduction for payment in 2007
Police Pension	19.2%	19.2%	17.6%	0.07% rate increase starting in 2007
Health Ins. – Active	12%	9.9%	8.0%	Higher than State optimistic estimate
Health Ins. – Retirees	12%	11.2%	5.0%	Higher than State optimistic estimate
OTPS	1.3%	1.3%	1.125%	Commitment to contain admin expenses
Utilities	2%	2.0%	6.2%, 3.1%, 2%	US Department of Energy estimate
Medicaid	12.9%	Capped	Capped	Based on approved State Medicaid cap
Social Services Entitlements	4.5%	3.0 - 4.4%	4.4 – 5.0%	Most current information
Early Intervention	4.9%	3.5%	3.3%	Most current information
Special Education	5.5%	5.5%	3.3%	Most current information
Revenues				
State Aid	Variable	Variable	Variable	Based upon reimbursement formula
Federal Aid	Variable	Variable	Variable	Based upon reimbursement formula
Sales Tax	3%	3%	4%	3.2% growth in 2006, 4% thereafter
Property Tax	Flat	Flat	Flat	No increase in baseline
Other Revenues	Flat	Flat	Flat	

CLOSING THE OUT-YEAR GAPS

The County has chosen to modify its gap-closing program by reducing the value of certain recurring gap-closing actions. The following are some of more significant revisions from the June Update:

- The workforce management savings have been reduced by $15.3 million in FY 2007, and $12.5 million in FY 2008, while no workforce savings are contained in the FY 2006 Budget.

- The expected savings from smart government initiatives have been reduced by $19.5 million in FY 2007 and $39.9 million in FY 2008, even though only $9.6 million of smart government initiatives were incorporated into the FY 2006 budget.

In addition, the out-year gap-closing program assumes the following non-recurring actions to help balance the financial plan:

- The use of the remaining $14.9 million from the pension reserves.

- The use of $50 million of expected FY 2005 surplus funds to pre-pay debt and transition to PAYGO for certiorari settlements.

We are concerned that while the out-year gaps are increasing, the value of certain gap-closing measures has been reduced, and the County is using various reserves to help balance the Budget. In particular, the County has reduced the projected savings from workforce management and smart government initiatives. The need to balance the Budget and Proposed Plan with recurring actions that provide continuing budgetary relief is essential. The County should be more aggressive in pursuing its smart government initiatives, restructuring government operations, and continuing its planned workforce reduction in order to achieve structural budgetary balance. Section IV discusses the major elements of the County's gap-closing program.

REVENUES

The County has four major revenue sources: sales tax, property tax, Federal and State aid, and other revenues (primarily departmental revenues). The Proposed Budget estimates $2.4 billion of revenues, excluding interdepartmental transfers. The County also projects that baseline revenues will be $2.4 billion in FY 2007, $2.4 billion in FY 2008, and $2.5 billion in FY 2009, as shown in Table 4. Consistent with the New York State's plan to return Nassau County to fiscal stability, this is the first year that Nassau County is not entitled to receive any transitional State aid. The following sections discuss the major revenue sources.

(Table 4)
BASELINE REVENUES
FYS 2006-2009

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009
Sales Tax	$1,001.8	$1,027.7	$1,060.5	$1,094.5
Property Tax	738.7	738.7	738.7	738.7
Federal and State Aid	285.7	293.2	301.7	310.5
All Other	371.0	339.8	327.3	329.3
Total	**$2,397.2**	**$2,399.4**	**$2,428.2**	**$2,473.0**

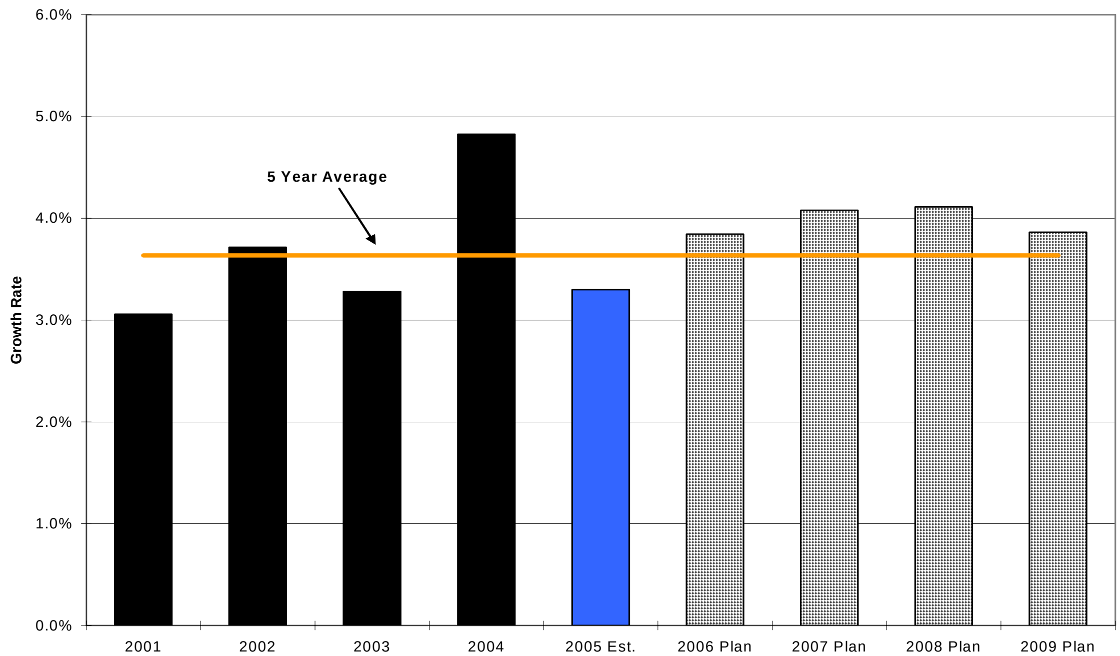
Sales Tax

Sales tax is the largest revenue source for the County, comprising 41.8% of all revenues covered in this analysis, and is budgeted at $1,001.8 million for FY 2006. The current sales tax rate in Nassau County is 8.625%, of which 4% is the State's share, 4% is the County's share, 0.375% is allocated to the Metropolitan Transportation Authority, and the remaining 0.25% is distributed to the towns and cities in the County.

Earlier in the year the County reduced its projected sales tax revenue by $7 million because payments through the end of May were almost 2% less than prior year's receipts. Since May 2005 collections have increased and now through October 12 they total $668.8 million, or 2.07%, ahead of last year's pace. The County now believes that sales taxes will grow by 2.6% and meet its budgeted revenue estimate of $964.7 million. In order to achieve 2.6% growth for the full year, this year's remaining payments must grow by 3.9% over last years collections, which does not appear unreasonable based upon the long-term historical growth of approximately 4%. However, for the last five years, annual growth has averaged only 3.6 %. We continue to be concerned because year-to-date collections remain below the projected 2.6% growth assumed in the FY 2005 budget. Assuming that the remaining payments grow by the same 2.07%, the County will receive $959.4 million, or $5.3 million less that the budgeted amount.

The Proposed Plan projects that baseline sales tax revenues of $964.7 million will grow by 3.2% in 2006. Since the FY 2005 budgeted sales tax may not be achieved, we believe that the FY 2006 sales tax estimate may be overstated by $5.5 million. In addition, the County's gap-closing program assumes that sales tax growth will reach 4%, generating additional sales tax of $15 million in 2007, $25 million in 2008 and $33 million in 2009, beyond the amounts contained in the baseline. Because the FY 2005 estimated sales tax may not be achieved, the County should consider reducing its out-year sales tax projections. As shown in Chart 1, sales tax revenues have actually grown by an annual average of 3.6% over the last 5 years. While 4% is not unreasonable based upon long-term historical experience, it is above the most recent 5 year average, and less conservative than previous year growth rate assumptions.

(Chart 1)
ANNUAL SALES TAX GROWTH HAS AVERAGED 3.6 PERCENT DURING THE LAST FIVE YEARS

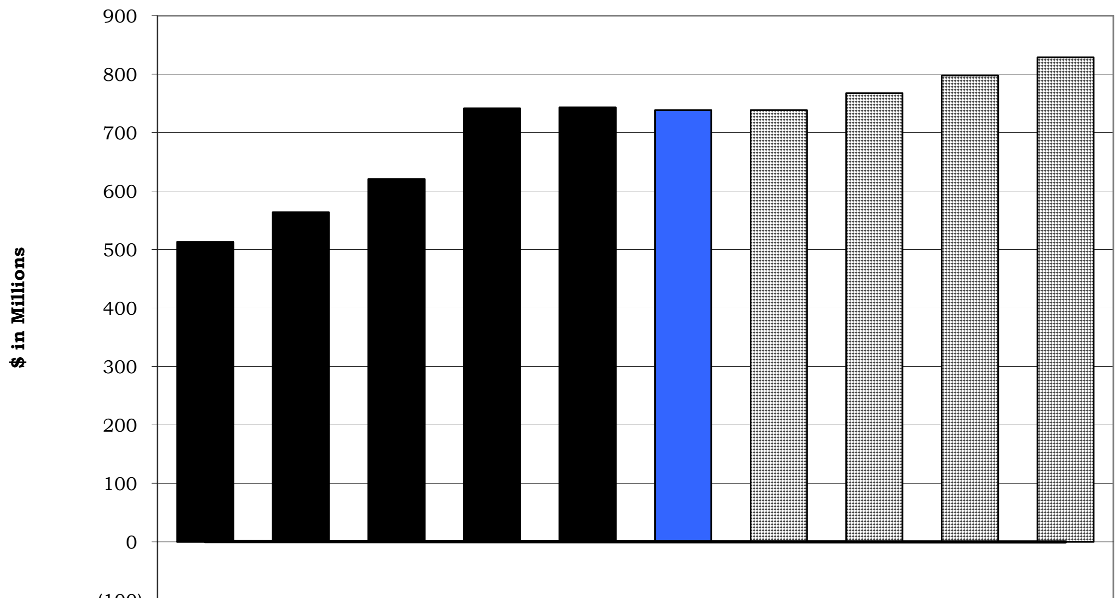


In recent years the County has benefited from a number of positive economic events such as strong jobs growth and rising housing prices. However, 2005 has been a challenging year from an economic perspective. Sales tax growth in 2005 has lagged prior years, as evidenced by the fact that year to date sale tax collections are only 2.07% ahead of last year. In addition, recent economic events, such as rising energy costs, rising interest rates and the economic affects of Hurricane Katrina could negatively affect the economy. Recent news reports have also raised concerns that consumer spending may be weak for the upcoming holiday season, which would result in lower sales tax collections. The County is aware of these concerns and it has established a $5 million contingency reserve in the FY 2006 Budget in order to compensate for any possible adverse economic events.

Property Taxes

Property taxes are the second largest revenue source for the County. They comprise nearly 31% of total revenues and are budgeted at $738.7 million in FY 2006. This represents the third consecutive year that there has been no increase in the property tax levy. Chart 2 depicts the property tax collections from FY 2000 - FY 2004 and the property tax levy from FY 2005 - FY 2009, which includes the County Executive's intention to implement annual property tax increases of 3.9% beginning in FY 2007. These increases are much larger than the increases proposed in the Adopted Plan, which only called for a 1.5% increase in 2007 and a 1.9% increase in 2008 if a cap on Medicaid costs was implemented. This will raise additional property tax revenues of $28.9 million in FY 2007, $30.0 million in FY 2008, and $31.1 million in FY 2009. This course of action would result in cumulative tax levy increases of $315.4 million (61.4%) since FY 2000.

(Chart 2)
PROPERTY TAXES
FY 2000 – FY 2009



	00 Actual	01 Actual	02 Actual	03 Actual	04 Actual	05 Budget	06 Plan	07 Plan	08 Plan	09 Plan
Annualized	513.3	563.6	620.7	741.8	743.0	738.7	738.7	767.6	797.6	828.7
Growth Rate	9.9%	9.8%	10.1%	19.5%	0.2%	-0.6%	0.0%	3.9%	3.9%	3.9%

Years

While NIFA recognizes the need for structural balance, it views property tax increases as a last resort. NIFA continues to urge that the County to carefully review, and to implement where feasible, previously intended workforce reductions and smart government initiatives that have been deferred, using further tax increases only as a last resort.

State and Federal Aid

Combined State and Federal Aid totals $285.7 million in the FY 2006 Budget, which comprises 12% of total revenues. The lion's share of State and Federal aid serves as reimbursement for health and human services programs. The FY 2006 Budget represents a reduction of approximately $50 million, due in large part to implementation of the Medicaid cap, which changes the way that statewide Medicaid costs are reimbursed. Absent the change in Medicaid funding, the FY 2006 Budget is relatively unchanged from FY 2005. The out-years of the Proposed Plan contain average increases of 3% for State and Federal aid, with such revenues growing to $293.2 million in FY 2007, $301.7 million in FY 2008, and $310.5 million in FY 2009.

State and Federal aid projections are developed on a program basis in conjunction with the County's operating departments. Salaries and wages are slated to grow on average in excess of 5% over the Proposed Plan from FY 2005 projections. This is greater than the rate of anticipated State and Federal aid reimbursements and reflects conservative budgeting by the County.

It also should be noted that FY 2005 is the final year that NIFA assistance is available to the County, therefore the County cannot budget for any such aid in FY 2006. The FY 2005 budget contained $11.8 million ($7.5 million for transitional aid and $4.3 million for tax certiorari reform).

Other Revenue

The remaining revenues are budgeted at $371.0 million in FY 2006, and represent approximately 15.5% County revenues. The more significant revenues included in this category are: departmental revenues; special taxes; rents and recoveries; fines and forfeits; interest and penalty on taxes; permits and forfeits; and investment income. Two major components of this revenue source are departmental revenues, which are budgeted at $81.5 million, and rents and recoveries which are budgeted at $50.5 million in FY 2006. Departmental revenues are expected to decrease by $1.3 million (1.6%) from the FY 2005 Budget and projected actual receipts of $82.8 million. Rents and recoveries are expected to remain essentially unchanged from the FY 2005 Budget. Rents and recoveries are expected to decline by $9 million in FY 2007, and another $14.6 million in FY 2008 as the tobacco proceeds are depleted. Other than the major changes highlighted above, the County has chosen to conservatively keep most other revenues essentially flat in the out-years of the Proposed Plan.

The FY 2006 Budget, and the out-years of the Proposed Plan, assume approximately $28 million of special taxes. Among these taxes are the hotel/motel tax, an entertainment tax, accident report fees and parking ticket surcharges, all of which expire on December 31, 2005. For FY 2006 the hotel/motel tax is budgeted at $1.4 million, however, the New York Legislature has not passed a bill authorizing the extension of this tax. Therefore, NIFA is risking the full amount of this revenue. The budget also includes $.6 million for accident report fees, $3.0 million for the entertainment tax and $1.0 million for parking ticket surcharges. The State Legislature has passed a bill extending these fees; however, this bill has not yet been sent to the Governor for his signature. Until such time as this bill is signed into law, NIFA is putting these revenues, which total $4.6 million, at risk.

In the past NIFA has recommended that the County periodically review all of its fees and charges to determine whether they should be adjusted. The County should be complemented for developing a revenue manual, which is a consolidated statement of its revenues. The revenue manual contains detailed descriptions, legislative authorizations, financial data and rate schedules for each revenue generated by the County. The manual should prove to be a useful resource to assist it in reviewing and assessing the myriad of revenue sources.

EXPENDITURES

The Proposed Budget consists of $2.4 billion of expenditures, excluding interdepartmental transfers.[1] The County projects that baseline spending will grow to $2.6 billion in FY 2007, $2.7 billion in FY 2008, and $2.7 billion in FY 2009. As shown in Table 5, these expenditures are composed of the following categories of spending: Personal Services ("PS") expenditures include the cost of salaries and wages as well as fringe benefits for employees and retirees; Other-than-Personal-Services ("OTPS") expenditures include charges for contractual services, pre-school special education, early intervention, utility costs, local government assistance, mass transportation, and payments to the Nassau Health Care Corporation; Direct Assistance includes payments for public assistance, Medicaid, day care programs, and institutional expenses; and Debt Service refers to both principal and interest costs for County and NIFA issued debt, including debt that will be reimbursed by the Sewer and Storm Water District Fund.

(Table 5)
COMPOSITION OF EXPENDITURES
FYS 2006-2009

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009
PS	$1,202.8	$1,290.4	$1,342.2	$1,401.5
OTPS	499.5	551.4	564.3	577.2
Direct Assistance	404.9	418.6	432.1	446.5
Debt Service	290.0	314.3	319.7	320.1
Total	**$2,397.2**	**$2,574.7**	**$2,658.3**	**$2,745.3**

Personal Services

The County projects that personal services expenditures will be $1.2 billion in FY 2006 and will reach almost $1.3 billion in FY 2007, $1.3 billion in FY 2008, and more than $1.4 billion in FY 2009, as shown in Table 6. These expenditures are driven by changes in the size of the workforce, changes in contractual salaries, and changes in the underlying cost of providing employee benefits.

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[1] The analysis contained in this report is limited to the five major operating funds within the Nassau County budget. These funds consist of the General Fund, Police Headquarters Fund, Police District Fund, Fire Commission Fund, and County Parks Fund. In FY 2003 the County created a Debt Service Fund to clarify the presentation of debt service expenses.

(Table 6)
PERSONAL SERVICES EXPENDITURES
FYS 2006-2009

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009
Salaries and Wages	$833.2	$870.7	$901.2	$937.2
Fringe Benefits:				
Health Insurance	197.3	210.2	224.0	238.8
Pension Contributions	76.1	109.2	112.6	116.7
Social Security	56.8	58.9	61.2	63.5
Workers' Compensation	17.6	18.8	20.2	21.6
All Other	21.8	22.6	23.1	23.8
Subtotal Fringe Benefits	369.6	419.7	441.1	464.4
Total	**$1,202.8**	**$1,290.4**	**$1,342.3**	**$1,401.6**

Salaries and Wages

Salaries and wages, the largest component of PS expenditures, are projected to total $833 million in FY 2006, or $10.5 million more than had been projected in the June Update. The County states that its revised estimate reflects the funding of all on-board employees, recognition of overtime needs in the Correctional Center and Police Department, and additional resources to cover new hiring needs identified in select departments, such as Assessment, Assessment Review, Corrections, Information Technology, Police, and Social Services.

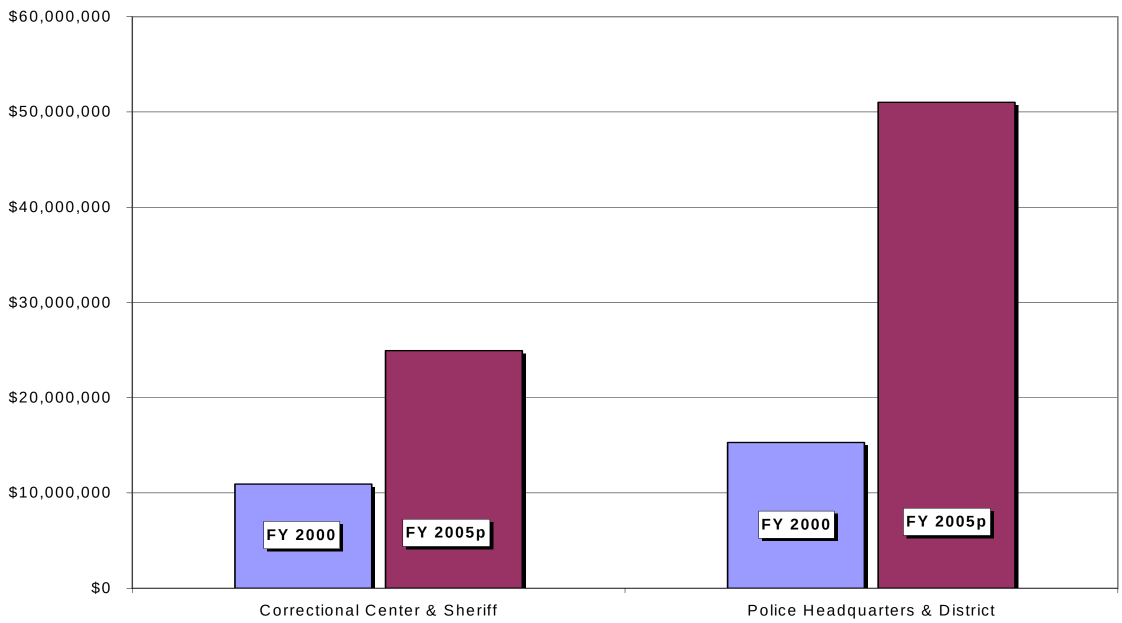
The terms and conditions of the recently rejected ShOA contract are reflected in the salaries and wages baseline. The County estimated that the ShOA contract would have provided baseline savings of $5.7 million in FY 2006, $3 million in FY 2007, $7.1 million in FY 2008, and $5.9 million in FY 2009. Therefore, the Legislature's decision to reject the ShOA contract creates equally-sized holes in the Proposed Plan, which NIFA expects will be addressed before the Proposed Plan is adopted. NIFA's analysis of the proposed ShOA contract was detailed in a separate memo dated September 13, 2005. The analysis questioned the County's ability to realize savings from civilianization, sick leave management, and 207c reforms.

The County's other baseline projections (other than for ShOA), which assume that successor labor agreements negotiated with each of its unions will contain terms and conditions that are consistent with current agreements, are not unreasonable. In fact, the County could realize salaries and wages savings in FY 2006 should it not fill all of its funded, though currently vacant, positions before the end of FY 2005. In addition, the baseline does not capture turnover savings that will accrue through the normal attrition/replacement hiring cycle. Furthermore, while the baseline assumes a stabilized workforce in the out-years of the Proposed Plan, the County intends to reduce its aggregate workforce through carefully managed attrition of its CSEA-represented headcount. These salary and wage savings are included in its gap-closing program for FY 2007 - FY 2009.

Overtime Control

A significant portion of the County's overtime expenditures occurs in the Police Department and Correctional Center. These costs have grown largely unchecked, as the County's attempts to control overtime in these departments have mostly failed. As shown in Chart 3, Correctional Center overtime has more then doubled (130%) between FY 2000 and FY 2005. Similarly, Police overtime has more than tripled (230%) over the same period.

(Chart 3)
OVERTIME EXPENDITURES HAVE GROWN RAPIDLY



The County attributes the rapid growth of these costs, in part, to its decision to let these departments shrink through attrition. While Correctional Center overtime has soared in recent years, the County stated that it is cheaper to use overtime to meet its operational staffing needs rather than hiring additional correction officers to perform these duties. In contrast, the Office of Legislative Budget Review released an analysis which concluded that the County could save $21.5 million over the next five years by hiring an additional 91 correction officers. Since the County has not provided us with its long-promised cost/benefit analysis, NIFA believes that the County should reexamine its staffing policies to determine the most efficient use of its resources.

The State Commission of Correction prepared a position and staffing analysis of the County's Correctional Center in 1995, which indicated that the Correctional Center requires the full time equivalent of 919.11 staff. Since the Correctional Center's headcount currently exceeds this level (1,035 correction officers), the County should request that the Commission update this ten year old analysis to help it better determine its current minimum staffing needs. The County should utilize this information in its ongoing efforts to identify and mitigate the Correctional Center's overtime drivers.

The County's chronic pattern of overspending budgeted overtime levels has been exacerbated by its inability to implement its civilianization initiatives, a management prerogative granted explicitly in its collective bargaining agreements negotiated with both the PBA and ShOA membership. For example, the Correctional Center has only filled 18 of the 55 positions that the County has been authorized to fill since 2001. NIFA projects that overtime expenditures may exceed proposed levels by approximately $4 million in the Correctional Center, if significant new controls are not immediately implemented, and $6 million in the Police Department, despite a new $2.5 million Police overtime reduction initiative. Approximately $3 million of NIFA's Correctional Center overtime risk stems from the rejection of the ShOA contract. Public Works overtime could also exceed proposed levels should snow removal costs approach the levels incurred in FY 2005.

The rejection of the ShOA contract, which included significant overtime reduction reforms, combined with contractual raises and step increases in the Police Department will exert upward pressure on overtime costs in future years. The County should monitor these expenditures closely and continue its efforts to develop new overtime control strategies.

<u>Fringe Benefits</u>

Fringe benefits costs are projected to reach $369.6 million in FY 2006 and grow to $464.4 million in FY 2009. These costs are projected to grow more slowly than in previous years. In fact, after adjusting for $30 million in off-budget reserves the County is tapping to pay for its FY 2006 pension obligations, these costs are projected to grow annually by a manageable 5%. While health insurance costs are projected to grow faster than inflation, adding an additional $41.5 million in County costs by FY 2009, the County actually realized significant financial plan relief by revising downward its health insurance growth rate assumptions to generate savings of almost $4 million in FY 2007, $16 million in FY 2008 and $30 million in FY 2009.

Health Insurance

The County assumes that health insurance costs for active employees and retirees will grow annually by 8% and 5%, respectively. These assumptions are significantly lower than the 12% growth rate used for active employees and retirees in the Adopted Plan and it continues a County pattern of reducing projected out-year gaps by virtue of using less conservative assumptions.

In addition, the County separately accounts for the receipt of $10.4 million in reimbursement revenue related to the new Medicare Part D subsidy. The subsidy relates to prescription drug coverage for Medicare-eligible retirees enrolled in the Empire Plan. It is NIFA's understanding that the County will not receive these monies as assumed, but rather the New York State Health Insurance Plan will use the Medicare Part D subsidy as a credit against County health insurance liabilities. The change in how the subsidy is implemented will have no net impact on the Proposed Plan because the "loss" of revenue will be offset by an equal reduction in expenditures. There are recent reports that implementation of Medicaid Part D may be delayed.

The County's out-year growth rate assumptions are mid-way between the "optimistic" and "best estimate" range of Civil Service expectations for FY 2006, which is a notable departure from the County's past practice of budgeting for the "pessimistic," or worst-case, scenario. While the growth rate of retiree health insurance costs slowed in FY 2005 and FY 2006, it is likely that these costs will resume their more typical growth patterns, which are more consistent with active employee costs, beginning in FY 2007. If retiree costs keep pace with active employees, health insurance expenditures could exceed County projections by $2.9 million in FY 2007, $6.1 million in FY 2008, and $9.7 million in FY 2009.

Pension Contributions

The County's contribution rates to both the Employees' Retirement System ("ERS") and the Police and Fire Retirement System ("PFRS") are expected to remain fairly constant during the Proposed Plan.[2] The County has reasonably budgeted these expenditures at $76 million in FY 2006, $109 million in FY 2007, $113 million in FY 2008, and $117 million in FY 2009.[3] However, should weak year-to-date pension investment performance continue, pension contribution rates may increase in future years, which would result in pension contribution payments exceeding planned assumptions.

The County has stated its desire to pre-pay its FY 2006 pension contribution obligation in FY 2005 to avoid the 8% interest rate otherwise charged by the retirement system through the February 1st due date. The County projects that it could realize approximately $800,000 in savings by using proceeds raised from a tax-anticipation note it would issue in December 2005 to make this prepayment. We note that while the "cash" payment would be made in December 2005, there would be no FY 2005 budgetary impact since the County Comptroller would account for these costs as prepaid FY 2006 expenditures.

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2 The County participates in the New York State and Local Employees' Retirement System ("ERS"), the New York State and Local Police and Fire Retirement System ("PFRS"), and the Public Employees' Group Life Insurance Plan. The local participating employer contribution rates for each retirement system are set by the State Comptroller and are now payable by the County each February 1st. The State Comptroller recently released the rates that will be used to determine the pension payment due February 1, 2007, and they are approximately 0.5 percent lower for ERS and approximately 0.07 percent higher for PFRS than the rates used to calculate the pension payment due February 1, 2006.

3 The County estimates that its FY 2006 pension bill payment will be approximately $105 million, of which $76 million is accounted for in the Proposed Budget and $29 million will be drawn from the pension reserve the County established in FY 2004. The County plans to use the remaining $15 million held in the pension reserve to mitigate pension costs in FY 2007.

Other Than Personal Services

County OTPS expenditures are composed of several large categories of spending, as shown in Table 7. These categories include: pre-school special education, local government assistance, early intervention services, mass transportation, utility costs, payments to the Nassau Health Care Corporation, and suits and damages.

(Table 7)
OTHER THAN PERSONAL SERVICES EXPENDITURES
FYS 2006-2009

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009
Pre-School Special Education	$98.1	$101.3	$104.7	$108.1
Local Government Assistance	59.7	61.6	63.6	65.6
Early Intervention Services	46.0	47.5	49.1	50.7
Mass Transportation	46.0	46.8	47.6	48.4
Utility Costs	33.2	36.4	38.8	41.1
Payments to NHCC	13.0	13.0	13.0	13.0
Suits and Damages	2.8	52.8	52.8	52.8
All Other	$200.7	$192.0	$194.7	$197.5
Total	**$499.5**	**$551.4**	**$564.3**	**$577.2**

The Early Intervention program provides specialized services to families with children under age three with developmental delays and disabilities. As children get older, they become eligible for partner components of the program, such as the Pre-School Program for ages 3-5 and the School-Age Program for ages six and older.

The County projects that these costs will grow by 3.3% annually, which will increase expenditures for Pre-School Special Education from $98.1 million in FY 2006 to $108.1 million in FY 2009. Similarly, the County projects that expenditures for Early Intervention Services will increase from $46.0 million in FY 2006 to $50.7 million in FY 2009. While NIFA believes that these estimates are not unreasonable, it is noteworthy that the County has reduced its growth rate assumptions for these expenditures from approximately 5%. The County should closely monitor these costs to identify changing trends and concomitant variances in a timely manner.

The County remits to the towns and cities sales tax revenue resulting from the 0.25% portion of the sales tax charged on purchases made within Nassau County borders. The payments to these local governments, projected to be $59.7 million in FY 2006, $61.6 million in FY 2007, $63.6 million in FY 2008, and $65.6 million in FY 2009 are an expenditure offset to the sales tax revenue collected by the County from its aggregate 8.625% sales tax rate.

The County projects that it will spend $46.0 million on mass transportation in FY 2006. These expenditures are composed of $10.5 million in subsidies to the MTA Long Island Bus, including $3 million for Able Ride, its transportation service for the handicapped. In addition, the County is providing $23.9 million in payments for Long Island Railroad station maintenance and $11.6 million for Long Island Railroad operating assistance. The Proposed Plan inflates the Long Island Railroad station maintenance by 3.3% annually in the out-years while holding its other subsidies and assistance expenditures flat.

The County has budgeted $33.2 million for utility costs in FY 2006, or 6% more than included in the FY 2005 Budget due to the continuing rise in electricity, fuel and heating costs. The Proposed Plan reflects the County's assumption that these costs will grow by more than 9% in FY 2007, and more than 6% in each of FY 2008 and FY 2009. NIFA believes that while the out-year growth rates are not unreasonable, these costs may be understated beginning in FY 2006. In the quarter ending September 30th, the prices of gasoline, heating oil, and natural gas have risen 44%, 23%, and 80%, respectively. While we can not quantify a specific risk, the County will need to monitor these costs closely because utility costs are subject to the volatility of world energy prices.

The County estimates that its FY 2006 payments to the NHCC will be $38.1 million, including $13 million in historic mission payments as well as the cost of retiree health insurance and termination pay for certain employees of the NHCC. The cost of retiree health insurance and termination pay is accounted for in fringe benefits and salaries and wages, respectively. The County projects that these costs will grow to $41.8 million in FY 2009. The County is currently negotiating a successor agreement with NHCC. If the County provides additional resources to NHCC under the new agreement, the County will be required to identify an equal amount of savings to maintain budgetary balance.

The Proposed Plan reflects the County's required transition to funding certiorari refunds out of its operating budget. The County projects that it will reduce the size of its certiorari refund backlog to a level that will translate into the need to make annual property tax refund payments of $50 million. This is accounted for in the suits and damages component of OTPS. We discuss the County's efforts to reform its certiorari process in more detail in "Certiorari," beginning on page 38.

The "All Other" component of OTPS is composed mostly of contractual spending. There are myriad contracts, of which the largest are related to medical and psychiatric services in the correctional center, funding for program agencies, and miscellaneous spending on such programs as community health centers, brownfield redevelopment, and medical and public assistance.

The County continues to squeeze OTPS spending by applying an annual inflator of only 1.125% on certain administrative expenditures. The County previously used a 1.3% growth rate in the June Update. The County has reasonably estimated these costs in FY 2006, but we are mindful that even in a low inflationary environment, limited nominal growth translates into real cuts in the out-years of the Proposed Plan. It is unclear if the County can sustain the limitations it has placed on these expenditures. The County should closely monitor spending during FY 2006 to ensure that resources are not being depleted more rapidly than assumed and/or that operations are not being impaired by a failure to procure necessary goods and services.

Direct Assistance

The County projects that spending on direct assistance will grow from $404.9 million in FY 2006 to $446.5 million in FY 2009. These costs cover social service entitlement benefits for clients enrolled in a variety of support programs within the County. As shown in Table 8, these expenditures are made within four major categories: Medicaid, Title XX, Temporary Assistance to Needy Families ("TANF"), and Safety Net Assistance ("SNA"). The remaining expenditures, grouped in "All Other", consist of spending on the County's other major social service program areas, including foster care, children in institutions, education for handicapped children, and juvenile delinquents. NIFA's analysis indicates that the County has reasonably estimated these costs, but that each program should be monitored closely to ascertain if the impact of a weakened local economy results in a greater than assumed demand for social service programs and direct assistance spending.

(Table 8)
DIRECT ASSISTANCE EXPENDITURES
FYS 2006-2009

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009
Medicaid: Local Share	$212.4	$219.1	$225.3	$232.1
IGT	$39.6	$39.6	$39.6	$39.6
Title XX	$46.0	$48.0	$50.2	$52.4
TANF	$29.1	$30.5	$31.9	$33.6
Safety Net Assistance	$18.5	$19.5	$20.4	$21.4
All Other	$59.3	$61.9	$64.7	$67.4
Total	**$404.9**	**$418.6**	**$432.1**	**$446.5**

Medicaid

Expenditures for Medicaid recipients cover a wide range of services, including payments for nursing homes, hospitals, home health care, and pharmaceuticals. The County assumes that the cost of its local share of these expenditures will increase from $214.6 million in FY 2006 to $234.4 million in FY 2009, before the application of other savings that are presented separately in the gap-closing program.

These projections are significantly below previous County estimates since the County will benefit from the State's decision to enact a cap on the local share of Medicaid spending. The Cap formula will ensure that the County's share of Medicaid costs grow in FY 2006 by no more than 3.5% above the FY 2005 Cap base. Similarly, the County's expenses will be constrained to additional growth of 3.25% in FY 2007 (cumulative growth of 6.75%) and 3% in FY 2008 (cumulative growth of 9.75%). The County will be subject to 3% annual cost increases after FY 2008. This compares favorably with the County's prior baseline assumption of 13% annual growth.

The County estimates that the Medicaid Cap, combined with downward revisions in its projected FY 2005 Cap base, will result in financial plan savings of $43.6 million in

FY 2006, $76.3 million in FY 2007, $114.3 million in FY 2008, and $160.0 million in FY 2009.

NIFA believes that the County's assumptions are reasonable, although it continues to be cautious in its assessment of the County's Medicaid utilization initiative, which the County anticipates will yield an additional $2.6 million in annual savings, beginning in FY 2007. It is unclear how the savings will be of sufficient size to drive down Medicaid costs below the Cap in those years.

Public Assistance

The County is projecting that its expenditures for Temporary Assistance for Needy Families ("TANF") and Safety Net Assistance ("SNA") will grow by approximately 5% annually in the Proposed Plan. Combined, these costs are expected to increase from $47.6 million in FY 2006 to $55.0 million in FY 2009, driven higher by projected growth in caseloads, which have been rising after a long period of contraction. While TANF caseload has been fairly steady at around 2,500 for the past few years, SNA caseload has doubled to 2,309 after hitting a low of 1,184 in 2001.

Our analysis indicates that the County's estimates are reasonable. However, NIFA notes that changes in public assistance caseload and associated costs are difficult to predict since the linkage between fluctuations in the local economy and recipient grant demand may often be lagged by between 12 and 36 months. Compounding the complexity of this forecast is the Federal five-year limit on TANF benefits that results in many recipients switching into the SNA program at twice the cost. The County must continue to monitor its public assistance caseloads and associated costs closely to ensure that variances are accounted for in its model.

Debt Service

Once again we commend the County for achieving ratings in the "A" category. Each upgrade helps to reduce the County's cost of issuance and positions the County for its complete return to the capital markets under its own credit – one of NIFA's principal goals.

The County has regularly acknowledged the role that NIFA has played in its march toward self-sufficiency. For example, NIFA has issued in excess of $2.36 billion in bonds and $892 million in notes on behalf of the County of which over $1.99 billion in bonds are currently outstanding. These bonds have provided budgetary relief of $236.1 million by financing maturing debt, and debt service savings of $146.6 million by restructuring and refinancing County debt to take advantage of favorable interest rates. The County also continues to benefit from NIFA's variable rate bonds, the unhedged portion of which had a combined average interest rate of 2.15% in 2005.

The County projects that debt service will increase from $290.0 million in FY 2006 to $320.1 million in FY 2009, as shown in Table 9. This includes principal repayment and interest costs for NIFA-issued debt, County-issued debt, anticipated County TAN borrowings, and miscellaneous County expenses for future debt issuances.

(Table 9)
COMPOSITION OF DEBT SERVICE
FYS 2006-2009

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009
NIFA Debt	$146.6	$178.3	$194.0	$195.9
County Debt	140.8	130.9	120.4	118.9
TAN Interest	2.1	4.6	4.8	4.8
Expense of Loans	0.5	0.5	0.5	0.5
Total	**$290.0**	**$314.3**	**$319.7**	**$320.1**

The County has been conservative in estimating its debt service on variable rate NIFA bonds. For the first nine months of 2005, debt service on 2005 Series B and C was 2.13%. The County has assumed 4.0% for 2005 through 2006 and 4.75% for 2007 and beyond.

<u>**General Observations**</u>

Debt Issuance – The Proposed Plan appears to take full advantage of NIFA's borrowing capacity before it substantially sunsets in 2005. Notably, debt issuance in 2005 is increased because of the County's desire to use the remainder of NIFA's cert authorization.

Cash Flow Borrowing has returned to the County's Proposed Plan after a short hiatus. Notably, annual Tax Anticipation Note borrowings of $120 million have been reinstated in 2005 and remain throughout the Proposed Plan. The projected interest costs for cash flow borrowings for the County would increase dramatically from $522,670 in 2005, to $2,068,267 in 2006, to $4,570,133 in 2007, to $4,823,467 in 2008 and finally to $4,823,467 in 2009. These increases in interest expense (net of incremental interest earnings) are an added burden to the operating budget.

Increased cash flow borrowings could infer higher historical yearly maximum cash imbalances. Regardless of the justification for the increases in TAN borrowing amounts, the County will have to explain to the rating agencies and the market the need for such increased issuances.

Capital borrowing in 2005 is listed at $53.9 million and increases to $86 million in 2008. We agree that capital improvements and other capital spending is needed, but even with the limited amounts of capital that have been previously borrowed, a substantial amount has not been spent. Of the $31.1 million that was borrowed in the spring of 2005 on behalf of the County, nothing has been drawn down. In addition, almost $10 million remains unspent from the Spring 2004 capital borrowing that was made on behalf of the County.

County Building Consolidation Program. The Proposed Plan provides only skeletal information on the County's program to reconfigure and upgrade County offices and court facilities. We cannot comment on these borrowings until the County provides NIFA with a revised building consolidation plan. We note that of the $15 million raised in NIFA's Spring 2005 borrowing, nothing has been utilized to-date.

NASSAU HEALTH CARE CORPORATION

The financial health of the Nassau Health Care Corporation ("NHCC" or "Corporation") and its potential impact on Nassau County continues to be a major source of concern for NIFA, although we support the goals and progress that management has made during the past 8 months to decrease the 2005 projected loss from its 2004 level. While the results of the medical center have been contained at a $1 million loss through August 31, 2005, the nursing home loss of $5.7 million over the same period continues to bleed off resources from the combined institution. Gap-closing plans and DOH Approvals, plans for the A. Holly Patterson nursing home, cash flow, revenue cycle and receivables management, successor agreements and audit opinions all remain areas in which substantial further work remains to be done.

The County retained the consulting firm of Manatt, Phelps, and Phillips, LLP ("Manatt") to provide a report recommending the best course of action for NHCC. The report, released in January 2004, called for a modification of the NHCC Enabling Statute and a total restructuring of NHCC. The Manatt report was critical of NHCC's vision and stated "NHCC has failed to implement a strategic business financial plan based on a realistic assessment of its market position.

On September 8, 2004 the County and NHCC announced a five-point plan, as set forth below, to implement recommendations contained in the Manatt report:

1. **Operational improvements** designed to reduce costs, rightsize staffing consistent with industry standards, introduce affiliation agreements with neighboring hospitals, and improve the Corporation's revenue collection;

2. **Rate changes** approved by the New York State Department of Health as part of a comprehensive relief package;

3. **Relocation of the nursing home** to the NUMC campus, disposition of the Uniondale property, the sale of 300 excess beds at the nursing home, and the use of sale proceeds from the disposition of the property to reduce outstanding Corporation debt;

4. **The refunding of the Corporation's outstanding debt**; and

5. **An interim stabilization** agreement between the County and the NHCC intended to provide the Corporation with cash flow relief through the end of 2005, resolve

disputed charges, override certain unworkable language in existing agreements between the County and NHCC, and identify the principles to govern more comprehensive successor arrangements.

Recent Events

The County has taken further steps during FY 2005 to implement Manatt's five-point plan; however, much remains to be done in order for NHCC to attain financial health. In particular, we are concerned about the AHP which is projected to lose $7.6 million in 2005 and 2006. The Corporation has recently hired a new Chief Executive Officer, who has extensive experience in hospital and health care administration, to lead its implementation. An NHCC refinancing and new money debt issuance of approximately $300 million was completed in October 2004. In addition, the hospital has made substantial efforts to rightsize staffing consistent with the operating plan.

The refinancing served to avert an impending cash crisis and provided breathing room for the Corporation to implement the Manatt recommendations. The transaction resulted in the Corporation receiving approximately $41 million of cash, of which $26 million was available for working capital and $15 million for new capital project financing and approximately $22 million in net present value savings from lower debt service payments. However, it should be noted that even after realizing the benefits of the refinancing, NHCC ended FY 2004 with a cash balance of $30 million, approximately $5 million less than the prior year and only retains an average of two weeks operating cash on hand.

NHCC also entered into interest rate exchange agreements to hedge its floating rate debt exposure with commercial banks to convert the variable interest rate Series C Bonds to a fixed interest rate of 3.46% and a variable rate received based on LIBOR. Floating rate bonds can be redeemed more easily than alternative structures and proceeds from the sale of the Uniondale property may be used for this purpose. These swap agreements expire on August 1, 2029. We are told that monitoring by the County indicates that there have been no material deviations from previous projections or expectations to date.

Stabilization and Regulatory Agreements

In addition to the refinancing, NHCC's Board and the Nassau County Legislature approved new Stabilization and Regulatory agreements in September 2004. The Stabilization and Regulatory agreements supercede the Acquisition agreement from September 29, 1999 and redefine the relationship between the County and NHCC. The Stabilization agreement settled many long-standing disputes between the County and NHCC on items such as Correctional Center bills, and claims relating to longevity and early retirement. The Stabilization Agreement also limited certain potential exposures to the County (e.g., potential subsidy increases through arbitration and various capital obligations).

The Regulatory Agreement enhanced management accountability at NHCC and provided a framework for the recommendations contained in the Manatt report to be implemented. The Agreement established various reporting requirements for the Corporation and put forward policies whereby timely business plans must be submitted to address financial shortfalls. It also established standards of conduct for the members of the Board of Directors at NHCC, including attendance standards, disclosure of interests and avoidance of conflicts of interest.

The Regulatory Agreement also recognized NIFA's statutory role with respect to NHCC as a covered organization. NIFA is to receive quarterly reporting and is to be copied on all documents, reports or notices that are specifically required under the Stabilization and Regulatory agreements. NIFA has been calling for and supports the aggressive monitoring of NHCC. The controls outlined in the Stabilization and Regulatory agreements provide enhanced oversight for the County, NIFA and other fiscal monitors.

However, the economics of health care are extremely dynamic. A blueprint for providing health care to Nassau residents has been established, but drafting a plan alone will not cure the financial ills confronting NHCC. It is imperative that management at NHCC and the County continually monitor the progress of implementing the Manatt guidelines and stand ready to modify the course of action as needed. NIFA has concerns about several specific areas which are discussed below:

Gap-closing plans and DOH Approvals- The Adopted Plan initially projected a surplus for NHCC in the amount of $3.3 million which was subsequently reforecast as a $6.4 million deficit, after the fact, for a net negative change of $9.7 million. As a result, we have carefully reviewed the FY 2006-2009 Gap-closing plan and find there are several material "at risk" initiatives as follows:

"At Risk" Gap-Closing Measures

	2006-2009 Budget Impact
Bed Hold Reimbursement Approval	$7,113,000
Hospital Based Status Approval	$15,455,000
Chemical Dependency Rehabilitation Program	$4,620,000
Revenue Cycle Improvements	$18,826,000
Total	**$46,014,000**

The Proposed Plan, calls for gap-closing initiatives of $17.3 million in 2006 and $90.3 million in the out years for a total of $107.6 million for FY 2006-2009, many of which require DOH approval and funding to implement. The decertification of beds to obtain a "bed hold" reimbursement, hospital-based funding, and additional revenue from a chemical dependency unit all require DOH approvals. Based on recent Manatt progress reports and discussions, NIFA remains skeptical as to whether some of these initiatives can be successfully implemented in light of the dynamic changes taking place in the health sector regulatory arena, the Federal budget situation and competing resource needs, and in light of the impending 2006 elections and potential changes in State government. The gap-closing initiative for FY 2006 includes $4.5 million in revenue initiatives; however, more recently provided information indicates that savings may actually be closer to the $1-2 million dollar range. As a result, we believe that several gap-closing initiatives are "at risk" and may not come to fruition. These "at risk" initiatives are estimated at $46 million for FY 2006-2009, as shown in the above schedule and they constitute 42% of the total gap-closing initiatives. As a result, NIFA feels that there is an impetus for hospital management to develop alternative gap-closing measures should any of these risks, in fact, be realized.

Plans for the A. Holly Patterson nursing home- The plan to replace the home has taken an extensive amount of time, although losses continue to mount and are currently averaging $500,000 per month despite census increases. As of this writing, the certificate of need (CON) has not yet been submitted to the Department of Health (DOH), although verbal discussions have taken place. Although various plans such as sale or decertification of beds have been discussed with DOH, there has been no forward movement on their part. In light of current legislative changes such as the State plans to close down and eliminate beds, the window of opportunity to proceed with this negotiation, as well conceived as it may have been, might have been missed. NIFA recommends that hospital management and the County's consultant revisit this request with DOH at its earliest opportunity and develop or confirm a plan that will meet with approval.

Cash Flow- In light of continued concerns about potential cash flow problems, NIFA requested a FY 2006 budgeted cash flow forecast. NHCC's cash balance has declined by $15.6 million to $14.5 million between December 2004 and August 2005. Management has indicated that should certain State money not be received in the fourth quarter of FY 2005, cash currently classified as limited use assets, can be tapped. However, this would prevent the hospital from pre-paying its 2006 pension payment in December 2005 and they would incur approximately $0.8 million in interest costs that they had hoped to avoid. We are advised that NHCC will end the year with only a two week cash-on-hand position, which could significantly impair its operations.

Revenue Cycle and Receivables Management- As of August 2005, patient receivables have increased by $7.5 million since December 2004 and other receivables have increased by $7.3 million. At the same time, bad debt expense is $2.5 million less than August of the previous year and $0.3 million favorable to budget as of August 2005. The County Comptroller has requested that his audit staff review this receivable and the related reserve calculations to determine if the bad debt reserves are properly stated. It should be noted that the hospital has not yet successfully filled its Revenue Cycle management position, which has been open for several years, although this is one of the most critical and key revenue producing management positions. NIFA feels strongly that additional efforts need to be made in order to fill this vacancy. In addition, it should be noted that the hospital is now working with its second successive consultant at considerable expense, savings have yet to be fully realized, and in-house expertise still has to be developed, in order to eliminate the need for outside consultants.

Successor Agreements- NIFA was advised that negotiations to conclude a successor agreement are ongoing and that a term sheet is undergoing discussions as of this writing. Items requiring resolution are the amount of mission payments and the subsidy that the County will assume prison health services, County capital budget provision, and the level of County oversight. We have been advised that this agreement is expected to be completed by December 2005. However, if there is agreement to provide additional resources to NHCC, the County should identify an equal amount of recurring savings to maintain budgetary balance.

Certified Audit Opinions- The Nassau Health Care Corporation received a “Going Concern” audit opinion for FY 2004 by its outside public accounting firm Ernst and Young. This opinion potentially negatively impacts the NHCC’s ability to borrow, issue debt and obtain low cost rates for capital expansion and construction projects. As a result, it is likely that it would be unable to borrow on its own, without the County’s financial guarantees. In addition, the FY 2004 certified audit for the NHCC, Ltd. , incorporated in 1999 under Cayman Island law as a Class “B” insurer and wholly owned subsidiary of NHCC, also has a “going concern” opinion and was cited for having a shareholder deficiency. NIFA has been advised that FY 2005 claims experience has been reasonably low, however, that actuarial estimates have been relatively consistent at approximately $8 million per year.

Now that the NHCC and County have engaged new hospital leadership, we are hopeful that substantial progress can be made to resolve the issues noted above and meet these ongoing challenges during fiscal year 2006.

NASSAU COMMUNITY COLLEGE

The Proposed Plan for the Community College contains annual budget growth rates in excess of 5% to address anticipated salary costs, related fringe benefits, and other projected cost increases. Annual increases in tuition and property taxes are contemplated in order to support this projected growth.

Salary and fringe benefit costs account for approximately 87% of total expenses. The two teaching unions, the Nassau Community College Federation of Teachers (“NCCFT”), and the Adjunct Faculty Association (“AFA”) both have contracts that expire this fall and CSEA employees are in a long-term contract through December 31, 2007. The College will need to ensure that any settlements with its faculty are within the limits of what has been projected in the financial plan. Any settlement beyond what is contained in the financial plan would place additional fiscal pressure on the financial plan. Fringe benefit inflators for major items such as health insurance and pension contributions are in line with what the County has budgeted, and the estimates are reasonable.

Revenue for the College comes from three major sources: tuition, state aid, and funding from the County through property taxes. These three funding sources account for 87% of total revenues for the College. Property taxes in each year of the Proposed Plan increase by 3.9%. While this increase is always subject to County approval, recent history indicates a commitment to this funding source.

The College projected State Aid at $2,350 per full-time equivalent student (FTE), for FY 2006, which is based upon the amount contained in the adopted State budget. The out-years of the Plan assume that State aid will increase $50 in FY 2008 and FY 2009.

Tuition in each year of the Proposed Plan is scheduled to increase from the base year FY 2006 rate of $3140, by 5% to 8% depending actual enrollment levels and state aid provided in future years. In order to be conservative, the Proposed Plan assumes that student enrollment will be flat. While enrollment through the period of the plan is flat, enrollment for FY 2006 is 1.5% less than anticipated. If actual enrollment is less than projected, it may be necessary to identify actions that will maintain budgetary balance throughout the period of the plan.

SEWER AND STORM WATER SERVICES

In September 2003, at the request of Nassau County, the New York State Legislature created the Nassau County Sewer and Storm Water Finance Authority (SSWFA) and a consolidated County-wide Sewer and Storm Water Resource District, which is called the Sewer and Storm Water Resource District Fund (Fund).

The FY 2006 Budget and the Proposed Plan contain financial information regarding the Sewer and Storm Water Authority that can not be reconciled. The County indicated that the information was different because “different calculations” were used. The County will submit a technical correction to the County Legislature.

The County provided us with corrected information which shows that the Fund will spend $236 million in FY 2006 for sewer and storm water services. Included in this amount is $20 million of costs that will be reimbursed to the general fund for storm water related services. This reimbursement includes: salaries of $6.9 million, $4.2 million of fringe benefits (56% of salary costs), $5.6 million of debt service costs, $1.5 million of indirect costs and $1.8 million for other related expenses. The corrected information also shows that the Fund will use $32.3 million of fund balance for rate stabilization purposes. There appears to be a large increase in the number of employees whose cost is being transferred from the General Fund to the Sewer and Storm Water Resource District. Our current intention is to investigate this matter further in the coming year.

IV. Gap-Closing Program

This section of our report discusses the major elements of the County's gap-closing program including: Smart Government Initiatives; Labor Concessions; Workforce Management; and PAYGO Certiorari.

SMART GOVERNMENT INITIATIVES

NIFA continues to be concerned with the County's ability to achieve some of these initiatives. Some of these initiatives are again being pushed to the out-years of the County's Plan with reduced savings.

The County has reduced the overall value of its SGI's by approximately $10.4 million (51.5%) in FY 2006, $22.5 million (49.3%) in FY 2007 and $36.4 million (49.3%) in FY 2008, from the Adopted Plan. These decreases are, in part, because the County has again chosen to move those initiatives that require State Legislative approval into the out-years of the Proposed Plan and to eliminate several others.

The balance of this section discusses some of the specific changes that have been made to the Smart Government Initiatives. The major initiatives have been grouped as follows: those where the County has made a downward revision in the value of the savings or eliminated them entirely; and those that require State legislative approval and have all been moved to the later plan years. It should be noted, that for some initiatives, such as the Nassau Coliseum Redevelopment, there may be expenses associated with the potential income, such as the cost of providing direct services and infrastructure, which do not appear to be included as budgeted expenses.

Where NIFA is in agreement with the various initiative revisions that have been made by the County, no additional comments are noted. However, with respect to the items discussed below, more aggressive implementation and timely monitoring are necessary if the County is to achieve its projected savings.

Revised and Eliminated Initiatives

The County has scaled back the projected savings from the following initiatives:

- **eGovernment Revenues**

In the Adopted Plan, this initiative was projected to save $7.85 million and has now been eliminated.

- **HHS Administrative Consolidation**

In the Adopted Plan, savings for FY 2006-2008 were projected at $25 million. The Proposed FY 2006 Budget assumes savings of $1.7 million and additional out-year savings as set forth below. This initiative appears overstated based on prior year savings estimates and the methodology employed which utilized the experience of similar initiatives at other counties, instead of actual Nassau County cost structures. The revenue offset also appears to be understated, for example, FY 2006 uses a 35% reimbursement rate. As a result, we feel that 50% or $0.8 million of the FY 2006 budgeted savings is at risk.

2007	2008	2009
$1,778,544	$3,278,544	$3,278,544

- **Parks Revenue Enhancement Plan**

In the June 2005 update, FY 2006-2008 was reduced from the 2004 projected income amount of $15 million to $12.6 million. This has now been further reduced to $5 million for this same period and no savings are included in the 2006 Budget. This initiative was originally introduced in the Adopted Plan with increased program income of $21.2 million over a three-year period**.** The estimated revenue previously projected to be $15 million over the life of the Adopted Plan is now further reduced to $9 million for FY 2007-2009. To accomplish this the County had said it would focus on improving business processes such as accepting credit cards, actively soliciting grants, corporate sponsorships for events and engaging in target marketing to a wider audience. The County had identified facilities where it seeks to create partnerships with the general public, civic groups, other municipalities, recreation industry professionals and employee unions to maximize utilization and performance of selected park facilities. The County now expects to begin engaging consultants to review key issues in its plans. It must be noted that, by its own admission, the County has not been successful in attaining these goals to date.

2007	2008	2009
$2,000,000	$3,000,000	$4,000,000

- **Fee Increases**

The Adopted Plan had been reduced by $8 million in FY 2006 and FY 2007. The Proposed Plan increases revenue by $.7 million for FY 2007-2008. This initiative was originally introduced in the Adopted Plan with estimated revenue in excess of $10 million over a three-year period. The Proposed Plan indicated that OMB and the County Legislature were in the process of collaboratively developing a revenue manual which was published in June 2005. The purpose of the revenue manual was to enhance the process of annually reviewing the fee-based revenues and help evaluate whether incremental increases are appropriate. NIFA questions whether a consensus exists to raise fees to generate income at the projected levels. The County has not included fee increases in the FY 2006 Budget.

2007	2008	2009
$2,100,000	$3,600,000	$5,600,000

- **Cash and Receivables Management**

This initiative was originally introduced in the 2002 Multi Year Plan with estimated revenue in excess of $4.5 million over a three-year period but has been reduced to $.5 million in the FY 2006 Budget with no additional savings in the out years of the Proposed Plan**.** The Adopted Plan was reduced by $3 million in the out-years. However, the $1.5 million 2004 estimated savings projected over the life of the plan are now eliminated in 2005. This initiative proposed that the County Treasurer would coordinate the collection of receivables associated with ambulance fees, in addition to various other past due receivables. In June 2005 the County Legislature approved the hiring of NCO Systems Inc. to perform collection services. The Treasurer will monitor the performance of the selected agencies and award additional work based on prior performance. Updated estimates using historical data indicate there is an un-booked ambulance receivable of at least $2.5 million, but that $.5 million will be ultimately collected. It was noted that although this initiative was introduced in 2002, there is a long time period between identification of this initiative and implementation of the actual collection work which will not commence until October 2005. The County has indicated that as a result, these receivables have been written off during this interim period.

- **Fraud Hotline**

This initiative was originally expected to have $1 million in savings for FY 2007-2008 but has now been eliminated. Based on a review of the June 6, 2005 approved legislation, we agree that it is not possible to quantify potential savings, though they may in fact exist.

- **Energy Conservation**

This initiative was originally introduced in the 2002 Multi Year Plan with estimated savings in excess of $11 million over a three-year period. These savings are now being reflected in the 2006 utility budget in conjunction with the New York Power Authority Energy Savings Program and no longer appears in the Proposed Plan as an SGI. The estimated savings were originally projected to be $5 million over the life of the Adopted Plan. This initiative involved conservation to save on the County's $22 million annual bill for public utilities and develop an energy conservation plan in recognition of the fact that availability, reliability and affordable energy is essential to the operation of the County government. The work on this initiative has not yet begun although it was first proposed 3-4 years ago. While the County has reduced its savings projections for this initiative since the September 2003 Plan, we are hopeful that this plan will come to fruition in 2006, forming a basis for projecting future savings in the out-years of the Plan.

- **Health Insurance Coverage**

The $13.2 million included in the Adopted Plan for savings in FY 2008 has been moved to labor concession. The County offers employees and retirees health insurance known as Core Plus Enhancements, which includes certain enhancements that are rarely used, but represent a significant cost to the County. By changing the plan to Core Plus the County believes there will be minimal adverse effects to the insured. The Administration intends to negotiate this change in the health insurance coverage with the various unions in time to include the decreased cost to health insurance in the proposed 2008 budget. In the settlement with the CSEA in 2003 the County agreed to review health insurance cost savings options with union officials, however, no progress has been made even though there is a provision to share any cost savings between the County and CSEA. The County needs to determine to what extent revisions to retiree health insurance are permissible. This initiative is scheduled to provide savings in 2008 and the negotiations with the unions involved will be a formidable challenge.

- **Police Overtime**

Previous projected savings of $5 million per year have been eliminated from SGI and included in the baseline and a new $2 million annual savings initiative has been added. We question whether these savings will be realized based on historical overtime trends, usage and past results achieved in attempting to civilianize administrative positions.

2007	2008	2009
$2,000,000	$2,000,000	$2,000,000

- **Increased Federal Inmate Aid**

This assumes that 25 new prisoners will be added for FY 2007-2009. However, costs associated with this census increase such as additional staffing and direct costs do not appear to be included in the computation.

2007	2008	2009
$1,500,000	$1,500,000	$1,500,000

- **Automated Time and Leave**

This initiative was pushed back from 2006 to 2007. We are questioning this change in light of the recently discovered problems and improprieties regarding time and attendance internal controls in a number of departments, as well as management of overtime usage.

2007	2008	2009
$850,000	$1,700,000	$1,700,000

- **State Reimbursement for Police Training**

This was first added in the June Update and appears in the Proposed Plan. The County has informed us that other municipalities have been able to obtain State funding for this initiative, however, because this plan is still in the early stages, it is too soon to comment on whether this will be ultimately successful.

- **Consumer Affairs Revenue Initiative**

The Proposed FY 2006 Budget includes an initiative in the amount of $2,500,000 for Consumer Affairs revenue. The County plans to implement annual registration fees for all for-hire (taxis, limousines and livery) vehicles based in and operating in Nassau County. The County also plans to implement fees for non-bank ATM's located throughout the County. The Plan indicates that there are approximately 8,000 vehicles based in the 5 boroughs of New York City, 2,000 Nassau based vehicles and 6,000 non-bank ATM's for a total estimated fee base of 16,000. A straight line calculation indicated that the average fee would need to be $156.25 per registrant. NIFA questions whether the non-Nassau based vehicles can be registered and how this would be implemented. Based upon what the County has provided, this initiative appears similar to the one included in the 2005 Adopted Budget. As a result we feel that 50% of the FY 2006 projected savings or $1.2 million is at risk.

- **Initiatives Requiring State Legislative Approval**

The County has moved all initiatives requiring State legislative approval out of FY 2006 and into the later years of the financial plan. In addition, some initiatives such as LIE Reimbursement and Licensing Fees for Plumbers/Electricians have been removed. This action has the greatest impact in FY 2006 where savings from Smart Government Initiatives have been reduced by $20.4 million. The initiatives included in this revision are:

- Nassau Coliseum Redevelopment
- Ticket Processing Surcharge
- Commercial Tax Grievance Filing Fee
- Absentee Landlord Surcharge

<u>New Initiatives</u>

- **Persons In Need of Supervision**

This has been added in the Proposed Plan for estimated savings of $5.8 million in FY 2006-2009. This plan assumes that money can be saved by adding additional probation officers which will result in fewer residential placements. The County hopes to achieve savings thru a 65% reimbursement rate received by DSS providing service as opposed to the 20% Probation Department State reimbursement rate. It is hoped that this initiative will result in fewer costly residential placements.

2007	2008	2009
$1,457,072	$1,457,072	$1,457,072

- **Medicaid Cost Containment**

NIFA believes these savings are unlikely to be achieved. This initiative is discussed in "Medicaid" on page 22.

2007	2008	2009
$2,600,000	$2,600,000	$2,600,000

- **Nassau Coliseum Redevelopment**

This new initiative requires legislative approval prior to implementation.

2007	2008	2009
$1,500,000	$1,500,000	$1,500,000

- **Grant Fund Reimbursements**

The County receives approximately $100 million in grants annually from various State and federal agencies. Although Social Services has historically received indirect cost reimbursement from NYSOCFS and NYSTDA, other department grant proposals have not included a provision for the recoupment of indirect costs. As a result, based on Circular A-87, the County is estimating it has forfeited approximately $2 million annually due to lack of indirect cost reimbursement. NIFA encourages the Office of Grants Management to thoroughly scrutinize every grant agreement in a systematic manner and attempt to secure indirect cost reimbursement from all grantors wherever possible.

2007	2008	2009
$2,000,000	$2,000,000	$2,000,000

LABOR CONCESSIONS

The County projects in the Proposed Plan that it will secure labor concessions worth $24.6 million in FY 2007, $48.5 million in FY 2008, and $50.2 million in FY 2009. Specifically, the County expects to realize $24.6 million in recurring labor savings from the PBA and DAI beginning in FY 2007 and an additional $22.9 million in recurring savings from the SOA and CSEA beginning in FY 2008. These gap-closing targets are in addition to the $21.6 million in cumulative savings from ShOA that the County already assumed in its baseline projections. The County had expected to realize these savings in the recently rejected ShOA contract proposal.

NIFA's analysis of the proposed ShOA contract was detailed in a separate memo dated September 13, 2005. The analysis questioned the County's ability to realize savings from civilianization, sick leave management, and 207c reforms. It is our understanding that the County has restarted the collective bargaining process with ShOA and will attempt to negotiate new terms and conditions that will not trigger reopener clauses contained in other union contracts, a concern which was raised by the Office of Legislative Budget Review, NIFA, and the County Legislature.

The County anticipates generating a portion of the out-year labor concession savings target from a change in health insurance coverage, beginning in FY 2008. The County assumes that it can realize $13.2 million in savings through a reduction of benefits County employees currently have under Core Plus Enhancements by negotiating a switch to Core health insurance coverage.

The concept of achieving savings through a reduction of benefits, or employee contributions to health insurance premiums, is not new to the County. The current CSEA Memorandum of Agreement, FY 2003-2007, provided for the establishment of a committee to study alternative health insurance concepts. Even though the County has agreed that one-quarter of any cost savings resulting from implementation of the committee's recommendations will be shared with the CSEA, to date no savings have been identified. NIFA realizes that these savings are difficult to achieve, but urges the County to focus on the hard choices in the present rather than pushing them off to FY 2008.

WORKFORCE MANAGEMENT

The County's ability to attain long-term structural balance depends on its capacity for bringing its recurring expenditures in line with its recurring revenues. The County acknowledges that headcount reduction remains a critical tool within the County's control through which expenditure cuts can be made. While the Proposed Plan calls for hiring in select agencies, it also reflects the County's larger effort to further shrink its aggregate full-time workforce through attrition.

The County plans to reduce its full-time headcount from 8,709 employees as of August 18th to 8,506 by the end of FY 2009. The County projects that this initiative, when combined with normal turnover savings, will generate financial plan relief of $25.4 million in FY 2007, $38.7 million in FY 2008, and $51.4 million in FY 2009. The County did not budget any savings from this initiative in FY 2006.

The County plans to achieve its planned workforce reduction targets by adhering to a strict hiring control process which limits replacement hiring to only one out of every three separating CSEA-represented employees. If successfully implemented, this would reduce the CSEA-represented ranks by an additional 12% by FY 2009, a target that may be unachievable given the hiring priorities articulated by the County Executive. For example, the Proposed Plan calls for increasing the number of civilians in the Police Department and Correctional Center, in addition to the planned expansion of the uniformed headcount in these departments, to address operational needs, realize trumpeted civilianization savings contained in its labor agreements, and positively impact the County's rapidly rising dependence on overtime used to deliver services. Additionally, the County identified hiring needs in the Department of Assessment, Information Technology, Probation, and the Department of Social Services to name a few.

Since the County did not specify in the Proposed Plan how its headcount reduction targets would be allocated, we remain cautious in our assessment of the County's ability to maintain its workforce reduction objectives, its capacity to realize its concomitant out-year savings targets, and the extent to which services or revenue collections may be impacted.

Without a four-year departmental headcount plan, it is difficult to decipher what long-term policy choices have been made. NIFA has previously encouraged the County to develop department-level headcount plans in order to enumerate its long-term strategic vision. The planning process should include proactive and explicit County Executive decisions concerning which services to continue, scale back, and/or eliminate immediately and in the future. The level of authorized staffing and resources provided in each year of the financial plan should then be made consistent with these decisions.

CERTIORARI

From the outset, resolution of the certiorari ("cert") problem has been seen as essential to Nassau County's return to fiscal stability. The State Legislature recognized the severity of this problem. Under the legislation that created NIFA in June of 2000, Nassau County was given the ability, until December 31, 2004, to borrow up to $800 million for cert settlements and judgments. The County was also given $5 million of State aid to assist it in streamlining the tax cert claims process.

We join with the County in, once again, acknowledging certain achievements including:

- legislative reforms;
- annual updates of the assessment roll;
- correction of many assessments by ARC before they were appealed;
- settlement of more new cases, including the backlog of small claims cases;
- hiring of significant numbers of qualified staff; and
- not bowing to pressure to settle cases for more than they believe is their fair value.

It was the original intention of the State Legislature when it established NIFA that the County would fund its certiorari obligation on a "pay-as-you-go" ("PAYGO") basis beginning in 2005. That obligation has been postponed three times:

1. In the first instance, the County's right to borrow for certs was extended from 2004 to 2005.
2. In the second instance, the County right to borrow for certs was extended, in part, until 2007 when it was permitted to borrow $15 million for certs in 2006 and $10 million in 2007.
3. In the third instance, the unilateral refund program has allowed the County to pay for cert claims that would normally have been settled in 2006, with 2005 borrowed cert money by using the unilateral refund program.

Notwithstanding the County's receiving these extensions, NIFA still has many unanswered questions, many of which it has been pointing out in each of its reports.

1. <u>Unilateral Refunds</u> NIFA is concerned about the planned use of unilateral refunds because the County has been unable, during the past five years, to spend all the money it was permitted to borrow through NIFA.

We are still not sure why the County has had to resort to unilateral refunds considering the large increases in the budget of ARC and over five years of lead time. We believe that distributing large amounts of cert money in the last few months of 2005 will increase the possibility of errors and, at a minimum, will create an administrative burden which has not been properly anticipated. Perhaps the County should finally use some of the $4.8 million in State aid that NIFA has been holding since 2000 to staff-up for this one time event.

2. <u>PAYGO</u> The County has received several unanticipated one time resources that have allowed it to postpone its PAYGO policy. This has postponed the day, which had been

greatly anticipated, when payment of certs would come from and be a part of the regular operating budget. That was one of the main goals of the NIFA statute and until we see it accomplished, we consider that a major part of our mission has not been accomplished.

Furthermore, payment of the cert backlog with one time resources is not a benign event, because it takes away the ability to use the resources for other important County needs; however, NIFA consider this to be a policy decision by the County.

3. Backlog Size The County still lacks any empirical study or reliable methodology to accurately measure the size of the backlog and predict its growth in the future. We have repeatedly asked for such a methodology and been met with silence. In addition, acquiescing to use of the Comptroller's estimate is not a substitute for the County creating a reliable methodology of its own.

4. Internal Controls There is no discussion in the Plan of internal controls, a topic which should be of great concern to the County. Other than a preliminary audit by the Comptroller, no one has assured NIFA that the expenditure of nearly $800 million in taxpayer dollars has been properly managed and that there is sufficient oversight. It is noteworthy that the County's Department of Investigations has been allotted the paltry sum of $494,995 in the Budget for 2006 and that its main mission appears to lie with other departments.

5. Legislative Agenda Why is there no legislative agenda for the two biggest questions connected with certiorari: (1) unclaimed tenant refunds escheating to the County, and (2) the law requiring the County to indemnify the municipalities? While we recognize that earlier attempts to introduce these measures did not gain traction, that is no reason to abandon them in perpetuity.

6. Legal Department Other than a statement that "the County has faired well in the cases that were tried," we have no idea what has been done in the cert area by the County's legal department. Earlier reports had projections of increased staffs and caseloads. At this point we have no idea of the staffing, number of cases that have been tried and their outcomes, or what is the anticipated County exposure from cert litigation going forward.

7. Assessment Department We were somewhat assured after a meeting with the Assessor and his staff that there is positive activity in his Department. We were surprised to find that he was not a participant in developing the Proposed Plan or privy to the statements about his Department. This is very troublesome since the County continues to take credit for "addressing the problem of new liability through annual revaluations producing incrementally more accurate rolls each year."

8. Technology Every year we ask for the County to describe its efforts at improving technology in ARC and we receive no information. The ARC budget has only $40,000 for equipment in 2006, but we assume that there must be efforts in this area that are not apparent or described in the ARC write-up.

NIFA remains uneasy about the resolution of the cert problem. We intend to continue to monitor and comment about it as long as appropriate. In addition, although NIFA's bonding authority is rapidly expiring, it still must review the terms of and comment upon each proposed borrowing by the County. While we acknowledge that there are ambiguities in the NIFA statute, for example in the definition of a "certiorari judgment," NIFA will consider each situation and the County should assume that NIFA will vigorously uphold the intent of its statute.

V. Other

This section of our report discusses several other issues regarding the County. These issues include comments on the County's capital budgeting process, its cash flows, and reserves that have been established by the County.

Capital Budgeting

The County's Capital Budget does not account for all sources of funding. While reviewing certain technology related projects we noted that the Capital Budget did not include project funding that was being provided by the Technology Fund. Without all funding information in one place it is difficult to evaluate and monitor the progress of specific capital projects. We recommend that the County modify its capital budgeting process so that the full cost of each project is identified, along with the various funding sources, including borrowing, that will be used to finance the project.

Cash Flows

Accurate cash flow modeling and reporting permits the County to plan for spending and investment and to better manage its cash flow borrowings. Since 2000, cash flow modeling and forecasting had been handled by the County's outside financial advisor. The County has recently taken over the management of cash flow modeling. Over this period, the County has developed a greater understanding of factors affecting the timing of disbursements and receipts, and has better information about actual cash balances. This knowledge has, in turn, contributed to a reduction in annual cash flow borrowings. As a result the County has not issued a cash flow borrowing in several years. The Proposed Plan presumes that late in 2005 the County will resume annual cash flow borrowings of $120 million.

While the County has generally improved its cash flow reporting, problems still remain regarding the management of its capital program. NIFA has requested, but the County is unable to provide more accurate projections of its needs to draw down funds held by NIFA. As a result, NIFA can only invest bond proceeds for 30 days. If the County provided NIFA with better information about its projected needs, NIFA could invest for longer periods and increase its investment yield, resulting in additional income for the County.

The County is required to submit cash flow statements as part of the Financial Plan. The County will submit them after the Financial Plan is adopted.

Reserves

Over the last several years the County has created a number of reserves that would help mitigate unforeseen events. The County has established the following reserves: a reserve for retirement of indebtedness; a pension contribution reserve; and an employee accrued liability reserve. In addition, the County has established the Tobacco Trust Fund. Such reserves can provide short-term budget relief in a way that allows more time for deficit reduction to be orderly and consistent with budget priorities, without the need to impose large tax increases or abruptly curtail services. However, we caution that these reserves should not be used to adjust spending levels below the amount necessary to fully fund current needs. The County has chosen not to budget the full cost of certain operating expenses (pension, certiorari and debt service costs) in the FY 2006 Budget because these costs are being paid from other resources. While this practice does not affect the projected operating results, it has the effect of understating County costs and making it difficult to make comparisons or develop trend information.