NIFA Nassau County Interim Finance Authority

May 13, 2003

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

Hon. County Executive Suozzi:

Enclosed is NIFA's Review of the May 1, 2003 Update of the Nassau County Multi-Year Financial Plan for Fiscal Years 2003-2006. The Update was submitted at NIFA's request because of the uncertainties that NIFA saw in the Plan.

The Report comments on many key aspects of the Update. Briefly summarized, the Report finds that:

1) The Update continues to highlight the County's progress toward achieving structural balance. We concur with recent rating agency findings that the County has demonstrated progress in many areas including the implementation of a 19.4% property tax increase along with expenditure reductions. Its longer term efforts to achieve passage of legislation for a sewer and storm water authority, combine County offices, improve technology, reduce cash flow borrowing, and improve financial forecasting are all commendable.
2) Notwithstanding the many accomplishments of the County, the major challenges outlined in the Executive Summary of NIFA's October 7, 2002 report on the Plan have not changed. The County continues to face uncertain resolutions of key problems including labor costs, workforce reductions, the Nassau Health Care Corporation, the enactment of the sewer and storm water authority legislation, elimination of the certiorari backlog, increased termination costs, and limited capital expenditures.
3) According to the Update, the baseline gap, which is the difference between recurring revenues and expenditures, has remained substantially the same in the Out Years of the Plan. However, the County has proposed gap-closing measures to ensure budgetary balance.
4) The County still needs NIFA's monetary assistance, which includes borrowings through 2005, in order to fill its structural budget gap.
5) Based upon the proposed borrowing schedule in the Update, the "interim finance period," as defined in the NIFA Act, will continue until the end of 2005.

6) Fund balance and other non-recurring pockets of reserves exist, but there has not been a comprehensive plan proposed for their use.
7) The County has continued to minimize the impact of legislative changes (such as escheat legislation, which could end the unjust enrichment and the abusive practices) in the area of certiorari reform that NIFA has suggested and which it believes could generate significant additional revenues for the County.

The County has fulfilled the request of NIFA that it submit an update to the Plan. NIFA concludes that there has been significant activity, which we interpret positively, but major challenges still exist which if not met could jeopardize the County's fiscal future.

NIFA expects that a number of key uncertainties will be resolved one way or the other by the time the County has to submit its Plan for FY 2004 – 2007 in September. At that time we expect to see demonstrated planning (including timetables with benchmarks) and progress toward implementing the FY 2004 initiative.

Sincerely,

Frank Zarb
Chairman

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

Nassau County Interim Finance Authority

NIFA

REVIEW OF THE MAY 1, 2003 UPDATE OF THE NASSAU COUNTY MULTI-YEAR FINANCIAL PLAN FOR FISCAL YEARS 2003 – 2006

May 13, 2003

NASSAU COUNTY
INTERIM FINANCE AUTHORITY

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Robert W. Wallach

STAFF

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Executive Director

Evan L. Cohen
Deputy Director

Jane F. Cunneen
Deputy Chief Financial Officer

Carol S. Kostik
Chief Financial Officer

Laurie A. Leat
Corporate Secretary

Timothy P. Sullivan
Deputy Director

Jeremy A. Wise
General Counsel

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I. Introduction

At its October 31, 2002 meeting, the Directors of NIFA found that the County's Multi – Year Financial Plan for Fiscal Years 2003 – 2006 (hereinafter, the "Plan") was in compliance with the NIFA Act. Because of the many uncertainties in the Plan, the Directors mandated that the County Executive submit to NIFA an update of the Plan no later than May 1, 2003 (hereinafter, the "Update").

The Update was delivered to NIFA on May 1, 2003. What follows is a selective review and analysis of those parts of the Update that NIFA felt would be predictive of the County's future financial position. The report is divided into three sections: (1) risks, (2) the baseline, and (3) the gap-closing plan.

Summary of Findings

8) The Update continues to highlight the County's progress toward achieving structural balance. We concur with recent rating agency findings that the County has demonstrated progress in many areas including the implementation of a 19.4% property tax increase along with expenditure reductions. Its longer term efforts to achieve passage of legislation for a sewer and storm water authority, combine County offices, improve technology, reduce cash flow borrowing, and improve financial forecasting are all commendable.

9) Notwithstanding the many accomplishments of the County, the major challenges outlined in the Executive Summary of NIFA's October 7, 2002 report on the Plan have not changed. The County continues to face uncertain resolutions of key problems including labor costs, workforce reductions, the Nassau Health Care Corporation, the enactment of the sewer and storm water authority legislation, elimination of the certiorari backlog, increased termination costs, and limited capital expenditures.

10) According to the Update, the baseline gap, which is the difference between recurring revenues and expenditures, has remained substantially the same in the Out Years of the Plan. However, the County has proposed gap-closing measures to ensure budgetary balance.

11) The County still needs NIFA's monetary assistance, which includes borrowings through 2005, in order to fill its structural budget gap.

12) Based upon the proposed borrowing schedule in the Update, the "interim finance period," as defined in the NIFA Act, will continue until the end of 2005.

13) Fund balance and other non-recurring pockets of reserves exist, but there has not been a comprehensive plan proposed for their use.

14) The County has continued to minimize the impact of legislative changes (such as escheat legislation, which could end the unjust enrichment and the abusive practices) in the area of certiorari reform that NIFA has suggested and which it believes could generate significant additional revenues for the County.

Conclusion

The County has fulfilled the request of NIFA that it submit an update to the Plan. While the Update does contain critical information and reveal new initiatives, it would have been a more useful tool and more effective if it had been more succinct and focused solely on changes from the Plan.

NIFA concludes that there has been significant activity, which we interpret positively, but major challenges still exist which if not met, could jeopardize the County's fiscal future.

NIFA expects that a number of key uncertainties will be resolved one way or the other by the time the County has to submit its Plan for FY 2004 – 2007 in September. At that time we expect to see demonstrated planning (including timetables with benchmarks) and progress toward implementing the FY 2004 initiatives.

II. Risks Identified in the Update

In our October 2002 report, NIFA identified a number of risks. This section includes a selective discussion of current risks that NIFA believes are the most significant and/or imminent. Many of these risks are offset by opportunities (new and old) that the County has identified or through the County's "Plan B" (discussed elsewhere), which is primarily a bundling of several significant gap-closing measures from the original Plan.

1) **<u>Pensions</u>** This was the largest risk identified by NIFA in its October report. The County heeded the advice of NIFA and, unlike many other Counties, adequately budgeted for this risk in both the current and Out Years of the Plan. Ironically, if the Governor approves pending State Legislation designed to help municipalities that under-budgeted this expenditure, the County will reap a one time cost savings of approximately $25 million in FY 2003 and $12 million in FY 2004.

2) **<u>Labor Costs</u>** Of the five unions that represent the workforce covered in the Plan, four have expired contracts. While the County continues to believe that timely concessions will be obtained from these unions, it has recognized a $32.5 million threat to the Plan in FY 2003, which it has addressed in Plan B.

3) **<u>Workforce Reduction</u>**

   (a) <u>Monetary Risk</u> The County made a permanent reduction of 1,400 full-time positions by September of 2003 a cornerstone of the Plan. To date, only 1,021 full-time positions have been eliminated, primarily through normal attrition and retirements. The County is assuming in the Update that a reduction of only 1,200 positions may be achieved in FY 2003 without intervention, and has recognized a $21.7 million threat (which NIFA calculates at approximately $15 million) to the Plan in FY 2004, which it has addressed in Plan B. NIFA believes there is also a risk in FY 2003 that the County has not identified.

   (b) <u>Service Delivery Risk</u> The County has reiterated its commitment to utilize layoffs to ensure that its gap-closing targets are being achieved. If it were necessary to implement Plan B, the County would lay off an additional 250 employees, thereby raising its cumulative net headcount reduction target to 1,650 full-time positions. Measuring the impact of this initiative on service delivery must remain a priority for the Legislature and Executive.

4) **<u>Sewer and Storm Water Authority</u>** The County has enhanced its original proposal and continues to advocate for a Sewer and Storm Water Authority ("SSWA") to assume responsibility for all County wastewater

and storm water functions. NIFA continues to support the creation of this Authority as it is currently proposed. However, to-date required State legislation has not been enacted. If the SSWA is not created, the County is prepared to recognize a shortfall in excess of $23 million per annum, which it has addressed in Plan B.

5) **<u>Certiorari/Assessment Review Reform</u>** Even though NIFA acknowledges significant activity and progress by the County in satisfying its certiorari reform plan, it still has not demonstrated any improvement in the number of certiorari claims or in the total amount of monetary exposure for the County. This matter is discussed in greater detail elsewhere in this report.

6) **<u>Nassau Health Care Corporation</u>** ("NHCC") The Update indicates that the NHCC intends to reverse negative cash flow trends through labor concessions and restructuring efficiencies; however, they have not provided any specifics. We acknowledge the County's gesture of reserving an additional $9 million in both FY 2004 and FY 2005, to fund one year of NHCC's debt service requirements.

7) **<u>Police Termination Pay and Overtime</u>** The Update risks $15 million for termination pay and $5 million for overtime, part of which may become necessary as a result of the layoffs. While the County is correct to budget for the potential overtime expense, it highlights the complex interrelationships among different budgetary actions.

8) **<u>State Budget Shortfalls</u>** This fluid situation may not result in the large negative recurring impact that the County has reflected in its update ($52.8 million through 2006), but if certain items pass the legislature, they are likely to have negative effects on the County. The County properly risks this item, together with sales tax shortfalls, both of which will need to be closely monitored in the next few months.

9) **<u>NIFA Restructuring Assistance</u>** The County has budgeted NIFA restructuring aid totaling $57 million of which $40 million will be funded through NIFA's scheduled bond sale in May 2003. The remaining $17 million will only be issued if the restructuring is permitted by the provisions of the NIFA Act and deemed appropriate by NIFA. The NIFA decision whether to issue the additional $17 million will be based, in part, upon the County's willingness to make the difficult choices necessary to move toward structural balance.

10) **<u>Smart Government Initiatives</u>** The County has reduced its estimate of savings from existing initiatives and has identified several new initiatives resulting in a $10 million net increase in the value of the FY 2004 and FY 2006 initiatives.

11) **<u>Capital Planning</u>:** The proposed property consolidation plan, although laudable, should not be seen as the only major capital need in the County. We remain concerned about the slow pace of other capital spending, even when bond funds remain available. We look forward to a more detailed explanation of the County's progress with its entire capital plan in the near future.

III. Baseline Projections

The County developed a multi-year "baseline" forecast to measure the imbalance between its recurring revenues and expenditures. The imbalance is known as the "structural gap." An examination of the changes in the size of the structural gap, over time, can reveal how much progress the County is making toward achieving long-term financial stability. The Update shows that the County's estimate of its structural gap remains largely unchanged from the Plan and therefore continues to present a formidable challenge that must be addressed by the County in the coming years. In addition, we also comment on the multi-year plans submitted by the Nassau Health Care Corporation and the Nassau Community College.

FY 2003

For FY 2003, the County is projecting a $28.4 million structural deficit between recurring revenues and recurring expenditures. This gap is more than covered with the $72 million of budgeted NIFA assistance for State Aid and debt restructuring, which would create a virtual surplus of $43.6 million.

In addition, the County has identified a number of threats, together with contingencies and opportunities, largely items with non-recurring impacts, which could affect FY 2003. The County's financial results for FY 2003 will depend in large measure upon the outcome of these actions. These actions, which are more fully described later in this report, include:

- The State Comptroller's proposal to smooth FY 2003 pension costs.
- A State Legislative proposal for a one-time forgiveness of Medicaid advances.
- Closing out of encumbrances that have crossed fiscal years.
- Using excess FY 2003 resources to pay certain non-recurring costs.
- Paying, rather than bonding, the costs of the FY 2002 early retirement program. NIFA has declined to borrow for these costs under current financial circumstances.
- Pre-pay retirement debt service to provide relief in FY 2004 and FY 2005.
- Deferring the use of $12 million of budgeted tobacco revenues to FY 2004.

FY 2004 – FY 2006

The County's new baseline forecast is derived from certain economic assumptions which we regard as conservative, although not unreasonable. The County determined that few changes were required to the assumptions underlying the Plan when it crafted the Update. The assumptions were modified in only a limited number of situations where better information became available (e.g. pension contribution rates) and where the County's year-end (FY 2003) forecasts had changed, thereby resulting in different out-year projections (e.g. headcount-related salary savings). After these changes were factored, the County projected that its baseline gaps could reach \$152.4 million in FY 2004, \$304.7 million in FY 2005, and \$399.2 million in FY 2006 if no remedial actions were taken. After adjusting these projections for the level of NIFA restructuring assistance and State transitional aid contemplated in the Plan, we have determined that the County's estimate of its out-year baseline gaps have decreased by \$9.0 million in FY 2004, but increased by \$4.4 million in FY 2005 and \$22.0 million in FY 2006.

The major changes are discussed below.

Expenditure Adjustments

Salaries and Wages **–** The County reduced its projection of baseline salaries and wages to more accurately reflect the projected impact of savings resulting from its 1,400 full-time position workforce reduction program that commenced in FY 2002. This change is consistent with the analysis included in our October 2002 report, which indicated that the County's success in reducing its headcount during FY 2002 provided significant, but unrecognized savings beginning in FY 2003. The County's assumptions for baseline wage growth remain unchanged, reflecting the theoretical costs related to future salary step increases and collectively bargained raises patterned after historical labor agreements. The County currently reports that it has completed more than 70 percent of its workforce reduction target, having reduced its headcount by 1,021 full-time positions since January 1, 2002. The County expects to eliminate the remaining 380 positions by September 1, 2003 through attrition and/or layoffs.

Fringe Benefits **–** The County revised its baseline projection of fringe benefit costs for three major reasons. First, the County has better information regarding the magnitude of its pension contribution rates which, in the absence of State legislative changes (Hevesi proposal), are higher than budgeted due to the worse-than-assumed investment performance of the State's Common Retirement Fund. Second, the County's health insurance projections are now based on the actual premium increases that became effective January 1, 2003 which were lower than budgeted. Third, the County's new estimates of its health insurance needs and pension costs more accurately reflect the reduced size of its workforce, which is expected to contract by 1,400 full-time positions before the end of this year, a reduction that is larger than budgeted.

The County continues to conservatively assume that its out-year health insurance costs will grow by 15 percent annually, which is unchanged from the Plan. The County's baseline pension contribution rates assume that the State's Common Retirement Fund's aggregate investment performance reverts to the actuarially assumed rate of 8 percent (9 percent for equity investments) for the remainder of the plan period. The County must monitor its pension assumptions closely since future investment performance that deviates from the actuarial assumptions will favorably or unfavorably impact contribution rates and County pension costs.

Debt Service – The County has changed its formulation of baseline debt service and was unable to provide a reconciliation between the Plan and the Update. However, it appears that there were two areas in which the baseline changed: (1) movement of County debt service expense related to a 1993 retirement bond issue from the debt service fund to the departmental fringe benefit budget lines; and (2) eliminating planned NIFA borrowing for the $23 million cost of early retirement in FY 2002, with the cost instead paid over five years under a State Comptroller payment plan. The first change is an internal allocation decision that does not affect the County's overall budget. The second change will be offset by the County's "below-the-line" plan, articulated elsewhere, to use FY 2003 operating surplus to pay the entire $23 million bill in FY 2003. It should be noted that the County has also been unable to reconcile various debt service numbers within the Update to each other.

Other Expenditures – The County made changes to certain other expenditure assumptions that, in aggregate, had no material impact on the projected baseline gaps. For example, the County added $1.3 million to its annual equipment budget to cover the purchase of certain police vehicles on a pay-as-you-go basis, a sound departure from previous policy that capitalized similar operating expenses. Similarly, the County allocated $2 million for contractual needs in the Correctional Center to cover anticipated payments to the Nassau Health Care Corporation (NHCC) for medical services provided to County inmates. In addition, the County revised upward its estimate of payments to NHCC approximately $11 million by FY 2006. NIFA recognizes that some of the components in this indirect care subsidy will increase over time, such as health insurance for retirees. However, other variables such as termination pay are overstated in FY 2003 and should not be further inflated in the out-years. The County also added resources to cover new costs related to the annual property revaluation project that it offset, in part, by reducing its estimate of costs related to the automated valuation model used by the Assessment Review Commission. These net expenditure increases were principally offset by projected reductions in various social service spending categories driven lower by a downward revision of its projected caseload growth.

Revenue Adjustments

Sales Tax - The Update assumes a sales tax growth rate of 2.7%. This rate of growth is unchanged from the Plan. During the Adoption process the FY 2003 budget for sales tax was increased by $8.9 million, from $873.6 million to $882.5 million, to reflect higher than budgeted collections in FY 2002. The compounding value of this revision adds $9.6 million to the sales tax projection by FY 2006.

Year to date sales tax results are lagging behind collections in FY 2002, down 1.3% or $2.9 million. The Update does identify a risk of $10.3 million for FY 2003 and provides contingencies should this problem materialize. However, it should be noted that it is still very early in the year. The County needs a growth rate of 3.1% for the rest of the year to achieve its fiscal 2003 target and sales tax growth has averaged 4.5% for the seven-year period, 1996 through 2002.

State and Federal Aid - State and Federal aid are developed on a program basis in conjunction with the County's operating departments and generally parallel anticipated reimbursable expenditures. Since the County has been reducing its expenses it follows that the reimbursement for these expenses will be less. In FY 2003 the Update reflects a decrease of $19.4 million, mostly from removing $15 million of NIFA transitional aid from the baseline and reclassifying it as a gap-closing action. In addition, the Update accounts for reduced staffing and caseloads in the human services departments. While the Plan did not contain any growth, in the Update the County utilizes the recommendation of the Survey of Professional Forecaster and budgets an annual growth rate of 2.45%.

Department Revenues – The only material change relates to reduced funding for the Intergovernmental Transfer Program. This program has been the funding method used to provide enhanced federal aid for public hospitals and nursing facilities. The Update reflects a phasing out of funding for the County's nursing home, the A. Holly Patterson Geriatric Center. Since this revenue, estimated to be $39.7 million in FY 2006, flows to the nursing home, its loss is offset by reduced expenditures of the same amount.

Covered Organizations

We also comment upon the updated multi-year financial plans submitted by the Nassau Health Care Corporation and Nassau Community College.

Nassau Health Care Corporation

The Update submitted by the Nassau Health Care Corporation ("NHCC") projects operating losses of $8.8 million in FY 2003, $15.3 million in FY 2004, $22.9 million in FY 2005, and $31.9 million in FY 2006. Since its creation NHCC has incurred annual operating deficits. NIFA has continually expressed its concern with the financial outlook of NHCC and its subsequent impact on the County. Going forward there are numerous obstacles and challenges that the Corporation will have to contend with. Primary concerns include the ability of NHCC to attract new business necessary to meet the aggressive revenue targets set forth in the Update, the declining census at the geriatric center, increasing pension fund requirements, reduced State funding, and the lack of a labor contract with the workforce.

The Update submitted by NHCC does not offer adequate specifics on how it is going to deal with its losses. The County in the Update has recognized an exposure, which they estimate at $9 million in FY 2004 and FY 2005, to fund one year of NHCC's debt service. However, the increasing deficits at NHCC greatly exceed the exposure identified by the County. Absent major restructuring and enhanced efficiencies, NHCC will continue to pressure the County's finances. NIFA has requested a plan revision by

June 1, 2003 and the need for specifics for inclusion in the September 2003 financial plan.

Both NHCC and the County are aware of the risks discussed herein. NHCC has recently engaged a consultant to look at restructuring opportunities and the County is seeking a consultant to examine the delivery of health care services in Nassau County and the role of NHCC in this process. NIFA recognizes the importance of these studies and looks forward to their output.

Nassau Community College

The Update submitted by Nassau Community College (the "College") reflects changes due to the uncertainty of the State budget. The Plan contemplated annual tuition increases of $125. The Update factors in the potential loss of State Aid and increases tuition by an additional $150 in FY 2004. If enacted this would raise the annual tuition rate to $2,800.

The Update projects annual increases in salaries of 3.7%, to reflect contractual increases, and yearly increases of 3.9% in property taxes. Consistent with the County, the College Update increases fringe benefits to reflect the latest estimates of health insurance premiums and retirement system rates.

IV. Gap-Closing Program

The County has reviewed and modified its gap-closing program. While the major elements of the County's gap-closing program remain substantially unchanged, the County has identified opportunities that could provide limited current and out-year relief, set forth several new recurring initiatives, and provided substitutions for initiatives that may not achieve their expected results. Within the gap-closing program, the County has identified several actions that would be implemented only if certain other actions do not realize their projected savings. The County refers to these actions as Plan B.

While Plan B could be implemented should any actions fall short, the County has specifically associated their implementation with the three actions that it believes are most important to achieving the FY 2004 gap-closing program:

- Reducing the workforce by 1,400 employees.
- Negotiating $32.5 million in labor concessions.
- Securing enactment by the State Legislature of the Sewer and Storm Water Authority.

The next portions of this section discuss the more significant changes to the existing gap-closing program, the new recurring initiatives that have been identified, and the County's contingency program, which it calls Plan B. This report, however, does not reiterate discussions of ongoing concerns, which we addressed in our October 2002 report, regarding the sustainability of the County's workforce reduction objectives, the County's ability to extract significant savings from labor concessions, and some of the County's large, but speculative out-year gap-closing initiatives. This includes planned savings in FY 2006 from the County's proposed health insurance cost containment initiative that would require changes in both provider and benefit levels, changes which we believe may be, at best, subject to collective bargaining and, at worst, legally unfeasible. Likewise, we still question the likelihood of the State implementing a cap on the local share of Medicaid expenditures to generate savings beginning in FY 2006 as well as reimbursing the County for expenses associated with patrolling the Long Island Expressway.

The County will need to consider these concerns as well as other risks identified throughout this report during its preparation of the September 2003 plan.

Existing Initiatives

Sales Tax Rate Increase – The adopted financial plan contained a ¼ percent increase in the County's sales tax rate commencing, at a 50% discounted level, in FY 2004. The Update delays the implementation of this tax increase until FY 2005 and eliminates discounting. If enacted this increase is scheduled to yield additional revenue of $54.8 million in FY 2005 and $56.2 million in FY 2006. Under this scenario sales tax on most items purchased in Nassau County would increase from 8.5% to 8.75%, or 9% if current proposals for a ¼ percent increase are effectuated at the State level.

Residential Energy Sales Tax – The Update provides for the imposition of a 2.5% sales tax on residential energy beginning in FY 2005. It is scheduled to generate $21 million in FY 2005, and $21.7 million in FY 2006. While the County states that this is a delay of one year from the adopted financial plan, NIFA notes that the previous plan had also called for implementation in FY 2005, however at a rate of 4.25%.

Property Tax Levy – The Update proposes a property tax increase of $33.8 million in FY 2006 to pay tax certiorari refunds out of the operating budget. It also states that subsequent property tax increases would be capped at the rate of increase of the consumer price index. NIFA questions the appropriateness of linking increases in property taxes to the CPI, an index that measures changes in the prices paid by consumers for a representative basket of goods and services. If the County has made a policy choice to fund tax certiorari refunds through increased property tax increases, then future increases should be correlated with future estimates of tax certiorari liability.

Debt Service **–** Debt service initiatives proposed in the Plan, which were (1) reduced interest rate estimates and (2) proper allocation of NIFA sewer-related debt service to the sewer districts, have been implemented. The County's major debt service initiatives were introduced in its April 1, 2002 Plan. Important initiatives from that plan have been implemented, such as reduced borrowing for capital projects and NIFA variable rate debt issuance on the County's behalf.

New Initiatives

Automated Time and Leave System **–** We are concerned that the County's estimate of savings from this initiative ($1.7 million in FY 2004, $2.6 million in FY 2005 and $3.4 million in FY 2006) may be overstated. First, it is unclear if the new system can be operational by the beginning of FY 2004. Second, savings realized from reduced headcount needs are already captured in the County's baseline assumptions. Third, savings from reductions in unauthorized leave would be realized in the long term, rather than short term, from smaller termination payouts, which would eventually be based on more accurate leave balances.

Discretionary Program Reductions **–** This initiative seeks to reduce the level of funding earmarked for the County's discretionary programs in health and human services by approximately $1.2 million beginning in FY 2004. The County has identified reductions in day care salary enhancements, homemaker services, day care services, and one community center.

House Non-County Inmates **–** This initiative builds upon the County's existing successful efforts to maximize Correctional Center revenue by housing non-local inmates. The Update calls for filling unused jail capacity (24 beds) at the prevailing reimbursement rate of $142 per day to generate $1.2 million on an annual basis.

OTPS Freeze – The County has proposed a freeze on OTPS spending to realize savings of $1.8 million in FY 2004, $5.6 million in FY 2005, and $10.6 million in FY 2006. It is unclear how these savings can be achieved without impacting County operations since the majority of these expenditures relate to contractual services and programs, which are already subject to the discretionary program reduction initiative, nor does the Update specify any new or planned purchasing efficiencies that would facilitate a multi-year savings target of this magnitude.

Debt Service – The County identifies seven gap-closing initiatives, some of which are new in FY 2003 and some of which were incorporated in prior plans. The most significant new initiative is a reduction and delay in cert borrowing due to new estimates of liability. While the County has not yet completed its scientific sampling of the pending cases, preliminary results indicate to it that the backlog is closer to the low end of their estimate range. Prior borrowing assumptions had used the high end of the range to size debt issuance projections. This initiative, if borne out by actual borrowing, will save $2.2 million in FY 2003, rising each year to $19.6 million in FY 2006.

The second largest initiative is the use of unspent County bond proceeds to defease County debt, saving $6 million in FY 2003 and lesser amounts in later years, a total of $11.8 million from 2003 through 2020. This idea was presented previously but the substantial work with the County's financial advisor and bond counsel that was needed to implement this initiative was completed earlier this year. $4.2 million of the $6 million in 2003 is also included as a use of funds in the contingencies table on page 11 of the Update.

In addition, the County has further revised interest rate assumptions downward. The new assumptions are reasonable.

Several other initiatives are or appear to be repeats of prior initiatives. These include reallocation of NIFA's sewer-related debt to the sewer districts, which was included in the Plan and implemented in 2003; and reduced capital borrowing, which was a centerpiece of the County's April 1, 2002 Plan. There is no change in projected capital borrowing between the Plan and the Update.

Parks Revenue Enhancement Plan – This initiatives seeks to generate an additional $10 million in revenue in FY 2006 through a myriad of initiatives including seeking partnerships for selected park facilities, and improving business processes. While revenue from this initiative is in the final year of the Update, the goal of $10 million is ambitious and represents an increase of 57% over the current budgeted revenue of $17.5 million.

Reimbursement for Out-of-County Tuition – Counties in New York State issue "certificates of residence" to students who attend community colleges elsewhere in the State and pay "chargeback" rates for these community colleges. The initiative maintains that New York State Education Law permits counties to pass these costs on to the town and cities where the students live. The Update proposes to implement this mid-year in FY 2004, yielding savings of $2.6 million that annualize to $5.2 million in FY 2005 and FY 2006.

Ambulance Billing Revenue – The Update proposes to increase ambulance transportation rates in 2004 by 2.95%, their estimate of growth in the consumer price index. The County proposes that this initiative will generate additional revenue of $2.6 million in FY 2004. Ambulance fees are budgeted at $8.2 million in FY 2003, so applying this inflator will not yield the desired results. However, collections for FY 2003 are projected to exceed budget by $1.3 million. The net result of these actions will be that the initiative may fall short by approximately $1 million in FY 2004.

Certiorari and Assessment Review Reform

The elimination of the County's certiorari problem was one of the main reasons for the creation of NIFA and the October report outlined our continuing concerns. Since that time an exceptional amount of activity has taken place and progress has been made. However, the Update still does not provide sufficient empirical evidence to suggest that it will be able to solve this problem in the foreseeable future, and NIFA fears that the County has not budgeted adequate reserves for the years when NIFA funding will no longer be available.

NIFA's concerns include the following:

a) The County is unable to determine if its overall exposure has increased or decreased since NIFA was created.

b) There is still no accurate accounting of the size of the cert problem.

c) No effective means of auditing the settlement process has been drafted or implemented.

d) None of the legislative agenda items suggested by NIFA have been enacted, nor have there been serious efforts to build a consensus for their passage. Nevertheless, the County acknowledges that the escheat legislation "would likely result in fewer commercial tax cases being filed" and potential savings of millions of dollars. We have no way of verifying the numbers included for escheat in the Update, but suspect they are extremely low. Regardless, we consider any money that is not returned to its rightful owner to be unjust enrichment and legally indefensible.

e) Approximately $4.8 million of the funds given by the State to help the County streamline its cert process is still in NIFA's possession, pending evidence that significant actions have been taken to reduce the backlog of certiorari claims.

f) Contrary to the indications in the Update, relations between the Assessor and ARC do not appear to have improved. Without commenting specifically on the nature of the disagreements or taking sides, we are convinced that this disconnect has wasted County resources and deprived all sides of useful expertise.

g) The pressure on the County to settle cases will increase dramatically as the remedial ARC legislation sunsets and the ability of NIFA to bond for settlements is eliminated.

Opportunities

The Update highlights several significant non-recurring opportunities that, if realized in FY 2003, could be used to mitigate the impact of the identified threats and/or provide new resources that could be used to fund County-identified actions that generate recurring budgetary relief.

Pension Legislation – The State Legislature recently passed legislation containing a series of pension reforms, which if enacted, changes the manner in which the New York State Common Retirement Fund is funded. These reforms will ease the budgetary pressure confronting the retirement systems' participating employers, including Nassau County, to fund rapidly growing pension costs caused by the weak and/or negative investment returns experienced by the systems in recent years. The County estimates that the favorable impact of these reforms will result in approximately $25 million in savings in FY 2003 and generate an additional $12 million in budgetary relief in FY 2004 by setting the County's pension contribution rate at 4.5 percent of payroll (excluding local add-ons) rather than at the higher rate assumed in its baseline projections. It should be noted that this significant, but largely non-recurring benefit derives from merely delaying by one year the impact that weak and/or negative equity investment returns would have had on the County's pension contribution rates. Specifically, the County's normal contribution rates in the next few years will likely be significantly greater than the proposed minimum since the full impact of poor investment returns experienced by the Common Retirement Fund in recent years has not yet been fully reflected. While we believe that the Update provides an adequate level of resources to cover near-term pension costs, we urge the County to remain vigilant in monitoring its exposure to changing contribution rates caused by stock market volatility.

State Forgiveness of Medicaid Advances – The State budget currently under consideration allows for Nassau County to not repay prior advances in Medicaid and mental health services. The County estimates that this would generate savings of $18.3 million in FY 2003. NIFA believes that this is overstated by $3 million and that the savings in FY 2003 will be $15.3 million.

Closeout of Aged Encumbrances – In their Financial Infrastructure Reform section the County outlines a policy to cancel old encumbrances for which actual expenses are not expected. They estimate that the prior year disencumberances will provide a one-time benefit of $10 million in FY 2003. NIFA supports this policy of matching the operating budget with actual operating expenses within the same fiscal year.

Defer Use of Tobacco Securitization Funds – The County is stretching out receipt of the funds it received from tobacco securitization. In FY 2002 the County deferred its budgeted receipt of $18 million. The Update proposes to defer for one year $12 million of the $18 million that is currently budgeted in FY 2003 and it is also planning to defer $13 million of this funding scheduled for receipt in FY 2005.

"Fund Balance" – The Update states that the County wants to utilize fund balance to pre-pay future liabilities. In fact the County plans to use projected FY 2003 resources to make certain payments that will provide out year benefits. Among the uses contemplated are:

- Pre-payment of the 2002 early retirement incentive. This would cost $23 million in FY 2003, and save approximately $6 million a year through FY 2007. The September 2002 proposed plan requested that NIFA bond this payment, an idea that was largely rejected by NIFA.

- Prepay retirement debt service. This would cost $19.5 million in FY 2003, and save $9.9 million in FY 2004 and $9.6 million in FY 2005.

- Use $7.5 million to: purchase open land; engage consultants to advise the County on hospital restructuring issues, and health insurance cost-containment options; and pay an arbitrage rebate penalty.

The County's proposed uses of any excess FY 2003 resources are consistent with NIFA's previous recommendations that such excess resources be used to offset non-recurring expenditures or to provide longer term benefits. Therefore, we are supportive of the County's proposed efforts. However, the plan currently contemplates that NIFA will provide restructuring relief of $57 million during FY 2003. Of this $57 million, $40 million will be funded in our May borrowing. At the time of our fall 2003 borrowing, NIFA will review the County's financial position and make a decision whether or not to provide the additional $17 million of restructuring. That decision will be based, in part, upon our assessment of the County's resolve to make the difficult choices which are necessary to move toward structural balance as well as its willingness to implement some of the above actions.

Contingency Plan

The Update highlights several initiatives that, when grouped together, are characterized by the County as Plan B. The County has stated that Plan B includes the actions it will take, some of which were already included in the Plan and some of which are newly presented in the Update, to ensure multi-year budgetary balance should a combination of the identified threats materialize, potential opportunities not be realized, or certain gap-closing program targets not be achieved.

Layoffs

Plan B reiterates the County's commitment to utilize layoffs to ensure that its gap-closing program remains on track. The Update links the necessity of Plan B directly with the County's success or failure to implement its ambitious workforce reduction program and labor concession targets in their entirety. Unfortunately, the County's goal of permanently reducing the size of its full-time headcount by 1,400 positions by September 1, 2003 through normal attrition may be in jeopardy because of the slowing pace of voluntary separations in FY 2003. In addition, the County has been unable to report any measurable progress toward achieving its labor concession targets of $32.5 million in FY 2004, $65 million in FY 2005 and $78 million in FY 2006 that it expects to collectively realize from all of its unions (CSEA, PBA, ShOA, SOA, DAI). NIFA expects the County to adhere to the expenditure reduction targets delineated in the Update with the understanding that it will decisively move forward with Plan B should events break unfavorably against the County.

The County currently contemplates the need to layoff civilian employees to reach its original headcount target of 1,400 positions, since only 1,021 positions have been eliminated to-date and targeted hiring is scheduled to continue in the Department of Assessment, Assessment Review Commission, and County Attorney. The County acknowledges that the number of required layoffs will be contingent upon future attrition, labor concessions, and the approval of a Sewer and Storm Water Authority.[1] In fact, the County's Plan B describes the need to increase its workforce reduction target to 1,650 full-time positions, including the involuntary separation of police and corrections officers, if it fails to achieve the requisite savings from these gap-closing initiatives. Since the Update does not specify its layoff targets by department, it is unclear what impact these reductions will have on County operations.

Discretionary Program Cuts

The County identified a recurring savings target of approximately $35 million from reductions in discretionary programs in three broad areas: health and human services ($22.7 million), recreation and parks ($3.6 million), and transportation ($8.3 million). The County included in the Plan a detailed listing of the discretionary programs it currently provides in its health and human services and recreation and parks departments. While the Update and Plan are consistent for these two functional areas, this initiative now includes a proposal to eliminate entirely the County's fixed route and paratransit subsidies to the Long Island Bus. The County maintains that its legal obligation to provide a paratransit subsidy to the Long Island Bus for its Able-Ride program ceases if it doesn't subsidize any other operational component of the Long Island Bus.

Combined with the County's other discretionary reductions, this initiative would virtually eliminate the remaining resources supporting discretionary health and human

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[1] The County expects to transfer 136 full-time employees into the Sewer and Storm Water Authority.

services programs. Because of the dramatic impact that these combined reductions would have on County services, it will be important to have legislative support to implement this component of Plan B. While Plan B does contain credible gap filling options, the County should explore a broad array of measures that go beyond layoffs and social service reductions. Clearly, some out-year initiatives could be moved forward and others could be explored, including County/town consolidations, temporary reductions, or eliminations of non-essential services, to help the County achieve structural balance more quickly.