NIFA Nassau County Interim Finance Authority

October 10, 2001

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

Hon. County Executive Gulotta:

The Nassau County Interim Finance Authority (NIFA) has completed its review of Nassau County's Proposed Fiscal Year 2002 Budget and Multi-Year Financial Plan for Fiscal Years 2002-2005. The attached report presents NIFA's comments and recommendations concerning these documents as required by Chapter 84 of the Laws of 2000.

NIFA's report is entitled, "Nassau County Interim Finance Authority Review of Proposed Multi-Year Financial Plan for Fiscal Years 2002-2005." It has been reviewed and adopted by the NIFA Directors with the understanding that additional backup information might alter some of the report's findings.

The report speaks for itself and comments in detail on many key aspects of the proposed FY 2002 Budget and the Financial Plan. In sum, the NIFA report finds that:

1. The County was negatively affected by the tragic events of September 11, but the County had serious financial problems prior to that date.

2. Nassau County is likely to achieve a balanced FY 2001 Budget, but only because of $25 million in State aid, $88 million of debt restructuring through NIFA, and unusually strong economic conditions early in the fiscal year.

3. The proposed FY 2002 Budget contains a number of risks that could impair the County's ability to achieve a balanced budget. These risks are explained in the report and their existence places approximately $45.3 million in revenue and expenditure projections in jeopardy. There are additional high risk items amounting to $10 million.

4. The Multi-Year Financial Plan, which is more comprehensive than last year, requires the closing of out-year gaps of $129.8 million in FY 2003, $179.9 million in FY 2004, and $208.6 million in FY 2005. NIFA has identified a number of risks that must be addressed before adoption of the Plan.

Consequently, unless NIFA has confidence that there will be a resolution of the major risks that is has identified, both the Fiscal Year 2002 Budget and the Plan will be deemed unacceptable.

We are asking the County to work with the Legislature and NIFA staff to ensure that every effort is made to arrive at an acceptable FY 2002 Budget and a more complete Multi-Year Financial Plan. NIFA requests a written report on how the Legislature and County Executive plan to close the gap no later than October 23, 2001.

Although NIFA is ready to assist the County leaders in meeting their mandated fiscal goals and objectives, our authorizing statute also imposes upon us a responsibility to the people of Nassau County and the State of New York.

Sincerely,

Frank G. Zarb
Chairman

Attachment

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

Nassau County Interim Finance Authority

NIFA

REVIEW OF PROPOSED

MULTI-YEAR FINANCIAL PLAN FOR FISCAL YEARS 2002 – 2005

October 10, 2001

NASSAU COUNTY INTERIM FINANCE AUTHORITY

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I. Introduction

In response to a deterioration in the financial condition of Nassau County, in June of 2000 the New York State Legislature created the Nassau County Interim Finance Authority ("NIFA") or ("Authority"). NIFA's mission included:

- Overseeing County finances through new financial reporting requirements, which included reviewing and commenting on the County's budget, four-year financial plan, quarterly budget status reports and any proposed borrowings;
- Providing budgetary relief through the restructuring of County debt and, when requested, by issuing debt on behalf of the County; and
- Administering transitional State aid to the County.

During the first six months of the Authority, the County's FY 2000 budgetary outlook improved from initial deficit projections that reached $178 million earlier in the year. The improvement resulted from:

- NIFA issuing approximately $42 million of bonds to restructure County debt and approximately $212 million for other bondable purposes, including the payment of certiorari claims;
- NIFA releasing $25 million of transitional State aid to the County; and
- The County introducing initiatives worth at least $50 million annually.

In addition to the foregoing, on December 8, 2000 NIFA conditionally accepted the County's financial plan for the period from 2001 through 2004. The first year of the financial plan was the County budget for FY 2001.

During FY2001 the County undertook a number of actions that were not part of its financial plan, but which were designed to improve its fiscal operations. The following are some of the more important County accomplishments:

- Monthly meetings were held between NIFA, the County Executive, the Legislative Majority Leader, the Legislative Minority Leader and the County Comptroller to discuss issues of mutual concern. The purpose of the meetings was to improve communications among the Leaders and to monitor County operations on a monthly basis.
- Adoption of a capital plan to allow for the better planning of the County's capital needs.
- Improvement of cash flow reporting and monitoring systems.
- Implementation of improvements to the tax certiorari process that are intended to lead to a reduction of the backlog.
- Execution of a contract to operate the Cradle of Aviation Museum and share in its revenues.
- Institution of monthly meetings with key County departments to monitor financial performance and progress toward meeting the planned initiatives.
- Successful implementation of the FY2001 budget.

On September 17, 2001, the County Executive submitted a formal Multi-Year Financial Plan For Fiscal Years 2002-2005 (the "Plan") to the Clerk of the County Legislature and subsequently to NIFA.

The discussion that follows and transmittal letter constitute the NIFA staff's review and recommended findings regarding the County Executive's proposed FY 2002 Budget and Financial Plan. It is proposed that this document, together with the findings contained herein, 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. Overview

NIFA's authorizing statute (the "Act") requires that it comment about the sufficiency of the County's four year Plan. As a first step, this requires a review of the County Executive's FY 2002 Budget ("Budget"), which forms the first year of the Plan. Unless the Budget is in balance, the remainder of the Plan will be flawed.

In evaluating the Plan and Budget, NIFA looked for substantial permanent changes in spending and revenues. Recurring revenues had to match recurring expenditures. Budget balancing efforts that merely slipped costs into later years were deemed unacceptable.

In FY 2001 the County undertook a number of actions that improved its fiscal operations. NIFA's opinion of the efficacy of those actions, along with the County Executive's new proposals, form the basis of this report.

SUMMARY OF FINDINGS

NIFA's review has determined that:

- Nassau County is likely to achieve a balanced FY 2001 Budget, but only because of $25 million in transitional State aid and $88 million of debt restructuring through NIFA.

- The FY 2002 Budget, as proposed by the County Executive, continues a positive trend in the County's attempt to forecast revenues and eliminate one-shots. However, the Budget contains risk factors and errors of $55.3 million, which need to be addressed in order for the County to achieve a balanced budget. Some of the risks arose or were exacerbated by the events of September 11, 2001; however, NIFA and the County must address the situation as it is rather than as we wish it would be. The FY 2002 Budget also does not contain adequate reserves. A discussion of the County's reserves and a detailed accounting of the risks and errors are contained in the report, and including but are not limited to the following:

    1. A $16.5 million overstatement of sales taxes because of the failure to sufficiently recognize a downturn in the economy, which has been exacerbated by the tragic events of September 11, 2001.

    2. A $10 million overstatement of Social Services revenue because the revenue was not adjusted to reflect expenditure reductions.

    3. The underbudgeting of $8.7 million in several fringe benefit categories.

    4. An $8.0 million risk from understating overtime needs in the Correctional Center, Police and Parks Departments.

5. The understatement of pension costs by $7.5 million due to an overly optimistic projection of the investment performance of pension fund assets.

- The County was negatively affected by the tragic events of September 11, but had serious financial problems prior to that date.

- The Plan is not acceptable in its current form because of the need to modify the FY 2002 Budget. As currently presented, the Plan contains out-year gaps of $129.8 million in FY 2003, $179.9 million in FY 2004 and $208.6 million in FY 2005 which must be closed through a series of County initiatives. A discussion of the assumptions underlying the County's multi-year Financial Plan and selected gap closing initiatives is contained in the report.

CONCLUSION

The County Executive's proposed FY 2002 Budget contains errors and risks that must be resolved before the Budget can be approved by NIFA. It should also be noted that the events of September 11, 2001, will likely cause unanticipated negative consequences for the County. Constant monitoring will be essential, particularly in the early part of the year, before trends such as sales tax receipts, the demand for social services, and the potential for enhanced security needs become apparent.

For the reasons previously outlined and as elaborated herein, the out years of the Plan are not acceptable in their current form. Consequently, the Plan fails to satisfy the requirements of the Act.

The guidance provided in this report is intended to help the County's leaders as they explore their economic options. Failure to address the deficiencies discussed herein will result in budgets that will further erode the County's fiscal health and jeopardize its financial well-being. NIFA and its staff are ready to assist the County Executive and the County Legislature with any and all assistance.

III. FY2001 Recap

The Act requires that the County submit a quarterly summary of budget data within 30 days after the end of each quarter. On July 31, 2001 the County submitted to NIFA its report for the quarter ended June 30, 2001. The quarterly report projected that the County would end FY 2001 with an operating surplus of $21 million, which is approximately $9.5 million ahead of plan. Without NIFA restructuring assistance of $88 million, and State aid of $25 million, the County would end the year with a significant operating deficit.

The County Executive's proposed Financial Plan for FY 2002 – FY 2005 upwardly revises the projected FY 2001 surplus from $21 million to $25.9 million. The major changes to the projection include:

- Increasing the sales tax projection by $15 million consistent with information about year-to-date receipts.
- Assuming NIFA transitional aid for certiorari reform in the amount of $776,000.
- Increasing the projected salary costs by $6.9 million to reflect gross costs associated with the new ShOA agreement.
- Expenditures for the Nassau Health Care Corporation were adjusted upward by $6.8 million.

Several fortuitous events positively contributed to the County's FY 2001 budget including unanticipated increases in sales tax revenues, higher than expected investment income, reduced salary costs resulting from the delay in filling vacant positions, and lower social service costs.

The County has resources available in the debt service fund and from the projected FY 2001 operating surplus. The County plans to use the FY 2001 operating surplus as follows:

Proposed Use in Financial Plan	Amount
Establish Technology Fund	$10,000,000
Defease outstanding debt for budgetary relief	15,900,000
Total	$25,900,000

Should the FY 2001 results exceed the current projection, the County proposes that an additional amount up to $5 million be considered for further Technology Fund investments.

At the end of FY2000, the County transferred $49.4 million of excess FY 2000 resources to the debt service fund. The County plans to use the debt service fund monies to meet a planned shortfall in FY 2001 debt service of $14 million, prepay pension obligations of $27.9 million, and pay, rather than bond, $7.5 million of certiorari settlements. NIFA concurs that any additional resources that become available should be used in a manner that reduces the County's debt burden and provides long term recurring budget relief. As explained elsewhere in this report NIFA does not believe that the planned defeasance of $15.9 million of debt service meets this criteria because it is a one-shot designed to pay existing County debt service of $813,000 in FY 2002, $5.2 million in FY 2003 and $10.5 million in FY 2004.

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

- the County should end FY 2001 ahead of plan;
- the sales tax estimate of $835 million could be overstated;
- the projected surplus does not recognize the cost of any possible labor settlements for police contracts;
- the projected surplus presumes that the $10 million contingency reserve will be used during 2001, however we are not aware of any planned uses of this reserve;
- the estimate of certiorari assistance is overstated by up to $670,000; and
- the current risks that the County faces within the gap-closing program for FY 2001 should be controllable, with foreseeable baseline risks offset by planned under spending, better-than-expected revenues, and budget relief provided through a substantial debt restructuring and State assistance of $25 million.

Notwithstanding the foregoing conclusions, the impact of the tragic events of September 11, 2001 remains unclear. There is concern that, among other items, sales tax revenues will fall, and the demand for social service programs and the potential for enhanced security needs will increase thereby having a negative impact for the remainder of FY 2001 and into early FY 2002. Additionally, the County is incurring overtime costs associated with the deployment of personnel to the disaster. The County is unable to estimate the projected cost of this effort or any emergency assistance aid that may be available in the future to offset these costs.

IV. FY2002 Executive Budget

This section presents NIFA's analysis and detailed conclusions regarding the proposed FY 2002 Budget and the initiatives contained in the out years of the Plan. The proposed FY 2002 Budget, which represents the first year of the County's four-year Plan, incorporates a number of new initiatives designed to ensure year-end budgetary balance. The County's ability to achieve its fiscal objectives for FY 2002 is directly dependent on the actions that the County takes in the remainder of FY 2001 and its ability to quickly implement the FY 2002 gap-closing actions to help realize their full-year value.

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 must ensure that management systems are in place to implement and monitor the large number of new initiatives that have been, and will be, part of Nassau County's plan to restore financial stability. Inattention to proper implementation and monitoring of these initiatives could result in the County failing to achieve the planned results.

Implementation of the FY 2002 Budget will require special attention in light of the tragic events of September 11, 2001, which have raised concerns about the economic impact on the County and the entire Country. As a result of these events, it will be important for the County to manage and monitor the FY 2002 Budget very closely. This will be especially important during the early part of the fiscal year, before trends may become apparent regarding the level of sales tax receipts and the demand for a variety of social services and police needs.

RISK ASSESSMENT

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. For the purpose of NIFA's analysis, risks have been classified into two major categories.

The *first* category is implementation risks. These have been quantified and identified for the FY 2002 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 includes initiatives that require action or approval. For example, this would include actions or initiatives that require adoption of County or State laws or ordinances, or the agreement of a labor union. These risks will be highlighted during our discussion of the specific action or initiative.

Implementation Risks

Table 1 summarizes the results of NIFA's analysis, and identifies $55.3 million of actions or initiatives that NIFA believes cannot be accepted as currently proposed and must be either fully explained or reconfigured before the Budget is adopted. The County agrees with the areas of risk but they estimate the shortfall to be $10 million less. NIFA recognizes that the amounts of risk would have been less if the tragic events of September 11, 2001 had not occurred. The list 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, such as overtime 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.

(Table 1)
FY 2002 BUDGET RISKS AND OFFSETS

($ in millions)	Estimated Risk	Page
Risks		
Sales taxes may be overstated (reduce growth rate from 4% to 2%)	$16.5	9
Social Services revenues are overstated	10.0	12
Police, Corrections and other overtime is understated	8.0	20
Retirement costs are understated	7.5	23
Unfunded technology maintenance contracts	5.0	25
Unrealistic fringe savings	4.7	22
Investment income overstated (error)	4.4	13
Health insurance costs are understated	4.0	22
Interfund revenues are overstated	3.3	12
Investment income overstated (unrealistic interest rate assumption)	2.2	13
"One-shot" defeasance of County debt	0.8	35
Greens fees are overstated in Parks budget	0.7	12
NIFA Expenditures are understated	0.1	13
Offsets		
Understatement of Probation State Aid	($5.5)	12
Recoveries of prior year appropriations understated	(5.5)	12
Understated police transfer revenue	(0.9)	13
Net Risks	**$55.3**	

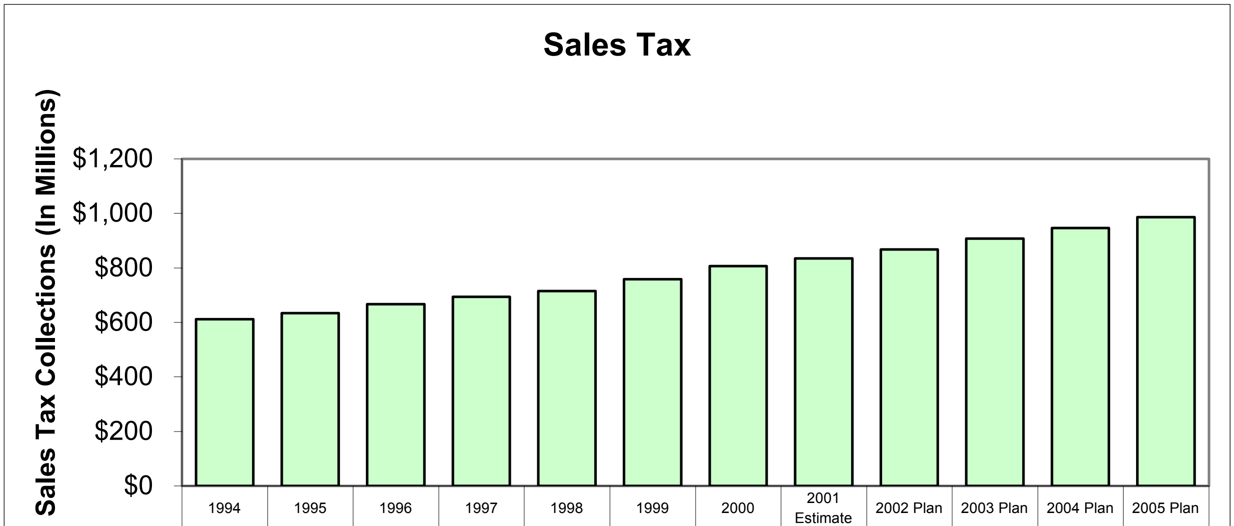
REVENUES

Sales Tax

Sales tax is the largest revenue source for the County, comprises 39% of all revenues covered in this analysis, and is budgeted at $868.2 million for FY 2002. The current sales tax rate in Nassau County is 8.5%, of which 4% is the State's share, 4% is the County's share, 0.25% is allocated to the Metropolitan Transportation Authority, and the remaining 0.25% is distributed to the towns and cities in the County. State legislation to increase the initial local authorization (3%) by an additional 0.75% and 0.5% has been enacted and is effective until November 30, 2003.

Chart 1 illustrates historical sales tax growth for the County. From a projection of $835 million for the current fiscal year, the budget for FY 2002 projects a net growth of 4.0%. Subsequent years in the financial Plan are projected to grow by 4.5% in FY 2003, 4.3% in FY 2004, and 4.2% in FY 2005.

(Chart 1)



	1994	1995	1996	1997	1998	1999	2000	2001 Estimate	2002 Plan	2003 Plan	2004 Plan	2005 Plan
Sales Tax (in Millions)	$611.97	$633.73	$666.54	$694.02	$715.52	$758.22	$807.03	$835.00	$868.17	$907.23	$946.24	$985.99
Growth Rate		3.6%	5.2%	4.1%	3.1%	6.0%	6.4%	3.5%	4.0%	4.5%	4.3%	4.2%

The County has diversified its economic base substantially over the past decade bolstered by the growth in technology industries. The growth of information technology, the biosciences, and telecommunications has fueled the region's economy by attracting highly skilled personnel, innovative businesses and a large influx of capital.

Sales tax growth has averaged 4.6% for the seven-year period 1995 through the estimate for 2001. However, the amount of future sales tax revenues to be collected depends upon various factors including the economic conditions in the County and the region.

While the historical growth provides some comfort, there are several factors that create concern. Recently, the economy has been experiencing a slowdown. The County's forecast of $835 million for FY 2001 represents growth of 3.5% from FY 2000 actual receipts of $807 million. Almost all of this growth in FY 2001 occurred during the first quarter of the year with second quarter results largely flat from the prior year. Given the recent slowdown in sales tax receipts, coupled with the uncertain aftermath of the terrorist attacks, it is difficult to justify a higher growth rate in FY 2002 than FY 2001. Subsequent to the recent terrorist attacks, a consulting economist retained by the County has revised sales tax projections downward to 2.5%-3% for FY 2002.

There is also concern that the FY 2001 projection for sales tax revenue of $835 million is overstated. Because of the foregoing, the County's sales tax estimate of 4% growth for FY 2002 is optimistic and overstated by $16.5 million. A more conservative estimate of 2% growth would be prudent.

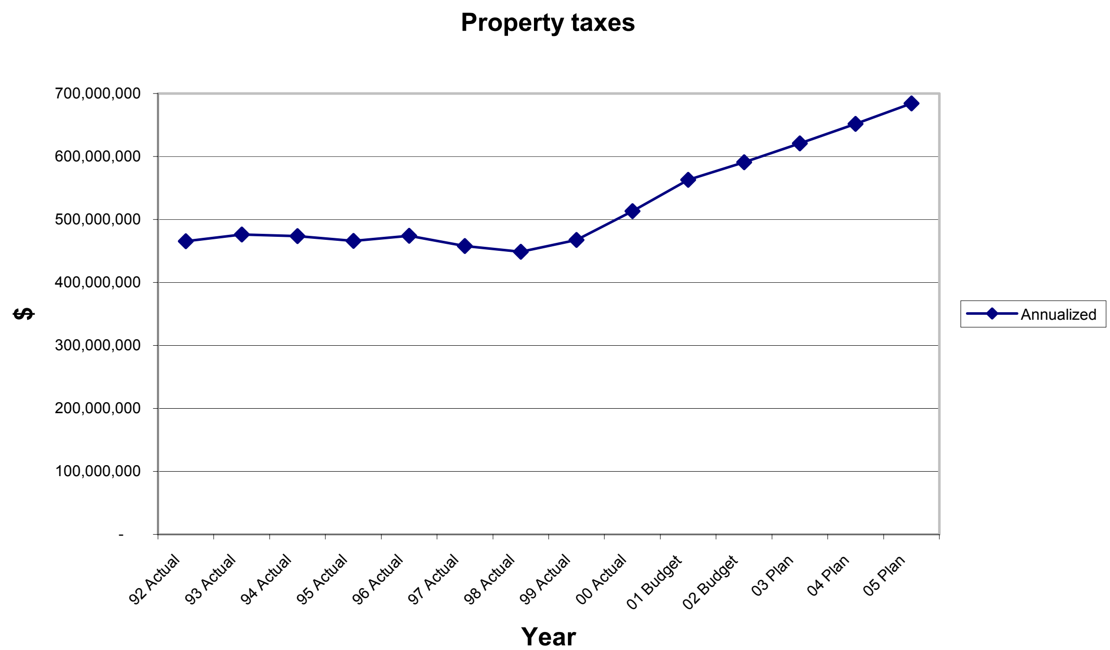
The out-years of the Plan contain growth rates ranging from 4.2% to 4.5%. The Consensus Addendum to the Multi-year Financial Plan adopted in November 2000 contained growth rates of 3% for all years covered in that analysis. Since that time, the economy has slowed and major uncertainties have arisen. Consequently, increasing the growth rates from last year's financial plan is not justified and a more conservative estimate would be appropriate.

Property Taxes

Property taxes are the second largest revenue source for the County, comprise 26% of all revenues covered in this analysis, and are budgeted at $591 million for FY 2002. The $591 million represents an increase of 5% from the FY 2001 budget. The financial plan assumes 5% growth for each of the out-years in the Plan. This growth rate is consistent with the currently adopted financial plan for FY 2001 – FY 2004.

Chart 2 shows property tax growth since 1992 for all major funds.

(Chart 2)



As evidenced from the graph, revenues from property taxes actually decreased by 3.6% from FY 92 through FY 98. While this revenue was declining, property tax certiorari refunds were escalating at an alarming rate. This dynamic of increasing expenses coupled with declining revenues significantly contributed to the structural operating gap. Table 2 illustrates the certiorari payments from 1990 to 2000.

(Table 2)
HISTORY OF CERTIORARI PAYMENTS

Year	Certiorari Payments
2000	$77,616,421.00
1999	$77,056,775.05
1998	$108,372,087.04
1997	$85,884,856.43
1996	$133,609,874.76
1995	$180,694,550.74
1994	$99,038,542.14
1993	$50,404,916.04
1992	$46,283,008.75
1991	$28,328,609.70
1990	$28,319,875.85
Total	**$915,609,517.50**

State and Federal Aid

State and Federal aid is budgeted at $304 million in FY 2002. This is 13.5% of revenues and represents a decrease of 3.6% from the FY 2001 budget. Out-year growth for State and Federal Aid is projected to grow at levels slightly higher than 5%. This contrasts with the FY 2001 – 2004 financial plan where State and Federal aid were projected to grow by less than half that amount, 2.5%. There are several factors which make the out-year growth projections overly optimistic including the recent passage of a "bare bones" budget by the State, the negative impact of the recent terrorist attacks on State and Federal revenues, and block grants.

As noted in the County's financial Plan, State and Federal aid are developed on a program basis in conjunction with the County's operating departments and generally parallel anticipated reimbursable expenditures. In the FY 2002 budget it appears that the County reverted to a prior practice of making expense reductions without adjusting the corresponding revenues. This practice results in revenues being overstated and is seen in departments such as Social Services where revenues appear to be overstated by approximately $10 million. Conversely, it appears that the County erroneously understated State aid in the Department of Probation by approximately $5.5 million as the revenue reimbursement level does not correspond to proposed expenditures. This additional revenue can be used to offset any other required adjustments.

Other Revenue

The remaining revenues make up 21.5% of the financial Plan. A major component is departmental revenue, which is budgeted at $143 million in FY 2002. This category is essentially unchanged from the FY 2001 budget and the projected actuals for the current year are largely on target. Of this total, $81 million relates to Medicaid reimbursements received from the Nassau Health Care Corporation, which is actually an offset against Medicaid expenditures.

The Department of Recreation and Parks contains $16 million in departmental revenue. While this represents no change from the current budget, the Department projects that in FY 2001 they will fall short of this revenue target by approximately $700,000, mainly due to a deficit in greens fees. The FY 2002 budget does not adjust for this deficit and a major surge in the number of golf rounds played would have to be realized in order to avoid a similar deficit.

Another significant issue relating to department revenues is an increase in ambulance fees by $1.5 million in FY 2002 which is discussed separately in the initiatives section on page 14.

The County Comptroller has indicated that recoveries of prior year appropriations, generated by the disencumbrance of old contract and purchase order balances, is understated by approximately $5.5 million in FY 2002. The County has not budgeted for recoveries in FY 2001 and a similar budgetary benefit should be realized. Other technical adjustments noted include an overstatement of interfund revenue, which

NIFA is risking by $3.3 million, an understatement of police transfer funds by $938,000, and underfunding NIFA operating expenses by $100,000.

Other revenues sources include fines and forfeits which remain constant from the FY 2001 budget and are in line with projections, and permits and licenses which are increasing by $500,000 to reflect better than anticipated fee results from alarm and pistol permits.

Investment Income

FY 2002 investment income is overbudgeted by $4.4 million due to an error. In addition, $2.2 million may be at risk due to interest rate assumptions which NIFA believes may be too high.

The County budgeted investment income in FY 2002 from four sources: (1) funds held by NIFA's bond trustee in set-aside and capital accounts; (2) County capital funds; (3) County operating cash balance; and (4) funds related to a potential tobacco restructuring. The Budget shows total general fund FY 2002 earnings of $13.2 million.

Correction to FY 2002 interest earnings. Back-up materials furnished to NIFA calculate total general fund-related earnings of $12.7 million, less than the budgeted amount. More significantly, the NIFA earnings of $3.8 million included in the total are also included as revenue to offset the NIFA set-asides. Both of these errors, which total $4.4 million, have been acknowledged by the County. The NIFA investment earnings have been left as a NIFA debt service offset (at a lower interest earnings assumption) and the investment income category is reduced.

Interest rate assumptions. The County Budget assumed a 3.8% earnings rate. This is well above rates currently being achieved by the County and NIFA, and a further reduction in short term interest rates by the end of FY 2001 is possible. A 25% reduction in the assumed investment earning rate, to 2.85%, would reduce earnings on the County investments by about $2.2 million. Interest forecasts are by definition uncertain and NIFA appreciates the County's effort to select an appropriate rate. However, the 3.8% rate appear highly unlikely.

Tobacco

The County is contemplating a restructuring of its prior tobacco securitization and a related new money issue to be secured by tobacco receipts. The transaction is proposed to be completed in FY 2001. NIFA has not been included in discussions about these financings. Nor has NIFA been formally notified and provided information for review and comment, as required by the NIFA Act. The limited back-up information recently furnished to NIFA in connection with the FY 2002 Budget and financial Plan review raises serious business and policy issues with respect to the proposed transaction. These issues include the structure and timing of the transaction and the application of proceeds, among other concerns.

FY 2002 Impact. As presented, the tobacco transaction, on a net basis, appears to be revenue neutral in FY 2002. The amount of the tobacco residual drops but is compensated for by a rise in investment income and the allocation of a portion of the transaction proceeds to replace the residual. If the transaction does not occur, the larger residual amount will remain available.

FY 2003 – 2005 Impact. The proposed transaction generates cash for the County from a combination of refinancing existing tobacco debt at lower interest rates (about one-third of the total cash provided) and issuing new debt backed by residual tobacco revenues (about two-thirds of the cash). As presented, the cash goes into the General Fund. This represents conversion of a long term resource into a "one shot" cash infusion. As such, this transaction may not be in the best interest of the County.

Debt-related

Capital backcharges. This revenue is essentially flat in FY 2002 despite the drop in projected capital spending in FY 2002, as discussed in the Debt Service section of this report beginning on page 32. The County has advised us that the level of charges reflects an increase in County staff and thus more in-house work that can be charged back to capital projects.

Debt service – CAP. This line is being phased out as NIFA takes over debt issuance. NIFA can reallocate unused bond proceeds to other County needs.

Revenue Initiatives

Additional Ambulance Revenues

In August 2001 the County issued a Request for Proposals to improve ambulance services billing and collection practices. They are anticipating that this will advance a previous initiative to increase this revenue source and have adjusted the impact to yield an additional $1.5 million, plus inflation, to each year in the financial Plan. The initiative is based on improved third-party reimbursement, increasing the County's collections rate from the current 40-45% of billings to levels above 65%, and developing a new fee structure. While the County and the representatives from the Police Department have presented a strong argument and methodology to support this gain, it should also be noted that this same item has been discussed for several years in the County without the achievement of any positive results. The County must monitor this initiative closely and take corrective action should the anticipated revenue not be realized.

Additional Privatization and Competition Savings

The County has put forward an initiative which seeks to achieve savings through privatization and competition. Areas which have been suggested include, workers' compensation programs, landscaping grounds maintenance, facilities management and janitorial services, and fleet management. This initiative is projected to yield savings of $1 million in FY 2003 and escalates to $5 million in FY 2005.

While the initiative makes sense in theory, the reality is that the County has continually neglected and reduced financial support to many of these identified areas thereby making additional savings unlikely. An example of this is facilities management and janitorial services. Several of the County's facilities are in desperate need of repair as the County has neglected to dedicate financial resources to maintain and properly clean its buildings. As such, privatization and competition may lead to operational improvements without yielding financial savings.

Cigarette Tax

The County is seeking State legislation to impose a $0.05 per pack tax on cigarettes. Based on 1999 purchase levels the County approximates that this would generate $4.3 million annually and the financial Plan contains discounted revenues from this tax beginning in FY 2004. While New York City collects an $0.08 per pack charge, the results of a new tax are difficult to estimate. Additionally, the County has unsuccessfully pursued the passage of State legislation for imposition of this tax for several years. While the County could continue to pursue this initiative, NIFA believes that it is uncertain and at risk in light of the County's previously unsuccessful efforts.

County Share of E-911 Surcharge for Cellular Telephones

Currently the State collects a surcharge of $0.70 monthly on each wireless phone. The revenue is used to offset the cost associated with emergency calls from wireless phones that are answered by State police. Nassau County, along with several other counties in the State with E-911 systems, have been answering these emergency calls. Legislation has been introduced, A00706, to remit cellular telephone surcharges to counties providing emergency 911 phone services. The initiative contains revenue of $1.2 million commencing in FY 2004. While there is rationale to this argument, the gain in revenues for the counties from this legislation represents a loss of revenue to the State. Consequently, the passage of the legislation is far from certain and the initiative is at risk.

Fee Increases for FY's 2003, 2004, and 2005

The financial Plan includes additional fee increases of $3.5 million for each of the out-years, FY's 2003, 2004 and 2005. The rationale is to periodically adjust fees to recoup the rising cost of providing specific services to the end users. The prospective fee increases range across several departments within the County including Recreation and Parks, Health, Social Services and Public Works.

The County's financial consultant has performed an extensive review of the fee structure within the County departments and identified potential sources of additional revenue. However, it should be noted that many of the County's fees increased in FY 2000 as part of the County's financial recovery plan. The County has historically failed to make timely adjustments to its fees and implementation of this policy decision is far from certain.

Grumman Site Lease Revenues

The Grumman property is a 105-acre site near Bethpage that is currently owned by the United States Navy. Discussions have taken place over several years regarding the transfer of this property to Nassau County for one dollar. According to the Nassau County Industrial Development Agency (NCIDA), the lead agency for the leasing of this property, 80 acres of the property are in condition to commence leasing. The initiative is scheduled to bring in revenues of $4 million on an annual basis commencing in FY 2003.

There are environmental concerns regarding this property. While NCIDA maintains that 80 of the 105 acres are cleared for commercial construction, issues relating to groundwater remediation remain. Disputes between the US Navy and Grumman concerning who is responsible for the groundwater remediation have bogged down the process.

Furthermore, one electric meter currently services the entire property so there would be an additional cost to run lines to provide separate metering. The County has indicated that they are scheduled to receive title to the property in FY 2002, however, the County has made this claim over several years without ever achieving it. Environmental concerns and certain logistical issues coupled with the County not having title to this property places this initiative at risk.

Improved TPVA Collections

Currently the Traffic and Parking Violations Agency is on target to meet their current year goal of $9.4 million in fines. The County is working on several initiatives to increase this revenue beginning in FY 2003. Primary among them are: establishing a third courtroom to increase the volume of hearings; implementing electronic data transmission to automate license suspensions; the use of handheld computer devices to minimize ticket errors; and an upgrade of the telephone system to improve call volume management. A question does exist as to whether adequate staffing exists to fully realize the potential revenue increases from these actions. However, additional revenues are not anticipated from these actions until FY 2003, which should allow ample time to institute the necessary changes. In total an increase of 12% in FY 2003 is not seen as unreasonable.

Increase County-Wide Property Taxes Collections by 5% Annually

The proposed FY 2002 Budget seeks to increase property taxes by 5% resulting in an increase of $28.1 million. Similarly, the out-years of the financial Plan contain 5% annual increases that result in an increase in property tax collections of $121.3 million by FY 2005. The County believes that this regular growth of the County's second largest revenue source, behind sales tax, is one of the keys to bringing long-term financial stability to Nassau County and is essential to keep pace with inflationary wage growth, increased cost of mandates, and escalation in the cost of utilities, fuel, etc. This initiative is consistent with the assumptions contained in the currently adopted financial Plan.

Increase Grants Recovery

Nassau County currently has a decentralized approach to grants management and recovery. The County has issued a Request for Proposals (RFP) to retain a firm to aid in the identification and management of grant opportunities. While the County has received a favorable response to the RFP, it is difficult to quantify the additional revenue that may result from this process. The lack of organization and strong management in the County has most likely resulted in the County missing opportunities in the past for additional grant revenues to offset costs currently incurred by the County. Since the firms that are ultimately hired to pursue these grants will be compensated from newly generated grant revenues, the idea is a good one and should be vigorously pursued.

The initiative assumes generating $1.5 million starting in FY 2003 and escalates to $4 million by FY 2005. Until some history is developed the success of the initiative is uncertain.

Increased E-911 Surcharge Rate

In FY 2000 Nassau County imposed a monthly surcharge of $0.35 per hard phone line for providing E-911 emergency police services system. State legislation exists which authorizes counties to impose this fee, however the fee is currently capped at $0.35. The County initiative seeks to increase the surcharge to $0.55 and projects revenue gains of $2.3 million commencing in FY 2004. While increasing costs to the E-911 system may justify an increase to the surcharge, in order to be successful this increase will require State and local legislation. Due to the uncertainty of passage of the required legislation the initiative is at risk.

Red Light Cameras

This initiative contemplates the installation of a red light camera system to identify vehicles that run red lights thereby increasing revenues for the Traffic and Parking Violations Agency. Currently, New York City is the only jurisdiction in New York State authorized to use red light cameras. The County initiative contains addition revenue of $1.6 million beginning in FY 2004.

While this initiative could generate significant revenue, the required capital costs to implement the system are high. The County has unsuccessfully pursued the passage of State legislation for imposition of this initiative for several years. While the County should continue to pursue this initiative, NIFA believes that it is uncertain and at risk in light of the County's previously unsuccessful efforts.

TPVA Surcharge Adjustments

Currently surcharges of $15 dollars per moving fine and $10 per parking ticket are in effect and used to cover a portion of the administrative costs for Traffic and Parking's adjudication and collection functions. The proposed financial Plan seeks a $5 increase to each surcharge to take effect in FY 2004. The County projects that this increase would yield an additional $1.1 million in fees. State legislation is required to approve these increases, which would also impact other counties in the State. Furthermore, the imposition of the parking surcharge was effectuated in August 2000 and it will be difficult to seek a further increase from New York State in this short time frame. This initiative is therefore at risk.

EXPENDITURES

The proposed FY 2002 Budget consists of $2.3 billion of expenditures.[1] As shown in the chart to the right, personal services ("PS") expenditures comprise 40% of the budget and include the cost of salaries and wages as well as fringe benefits for active employees and retirees. Other-than-Personal-Services ("OTPS") costs account for 19% of the Budget and include charges for contractual services, pre-school special education, utility costs, local government assistance, mass transportation, and payments to the Nassau Health Care Corporation. Direct Assistance, comprising 20% of the budget, includes payments for public assistance, Medicaid, day care programs, and institutional expenses. Debt Service, which represents 11% of the Budget, refers to both principal and interest costs for County issued debt. Interfund Charges are expenses charged between component funds that are, at the County level, offset by the recognition of interfund revenues.

Composition of Expenditures		
($ in millions)		
PS	$899.9	40%
OTPS	$438.8	19%
Direct Assistance	$441.1	20%
Debt Service	$251.9	11%
Interfund Charges	$233.8	10%
Total	**$2,265.5**	**100%**

Personal Services

The largest component of PS expenditures, salaries and wages, is projected to reach $692 million in FY 2002, as shown in the chart to the right. This estimate reflects savings from the County's workforce attrition assumptions, overtime control initiatives, prepayment of certain pension obligations, and salary increases stemming from collective bargaining agreements currently in place with ShOA and CSEA represented employees. No funding has been included in FY 2002 to pay for raises and step increases that may be granted to the employees represented by police unions (PBA, DAI, and SOA).

Elements of PS Spending	
($ in millions)	
Salaries and Wages	$692.0
Fringe Benefits:	
Health Insurance	$114.4
Social Security	$50.7
Workers' Compensation	$11.1
Pension Contributions	$13.1
All Other	$18.6
Subtotal Fringe Benefits	$207.9
Total	**$899.9**

[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.

Staffing Levels

Outside of collective bargaining savings, workforce management is the only major tool the County has available to control PS costs. After reducing the size of its workforce by 735 full-time employees between January 1, 2000 and January 1, 2001, the County began to replace vacant positions in targeted areas to better meet critical service needs during FY 2001. Through August 31, 2001, the County has added 315 full-time employees, with most hiring occurring in the Correctional Center and the Departments of Health, Probation, Social Services, Recreation and Parks, and Public Works.

The County has articulated that its goal is to maintain headcount at its August 2001 on-board level of 8,888 full-time employees; however, the FY 2002 Budget contains unspecified salary and fringe benefit savings targets that the County maintains were based on a 4% assumed level of attrition. Furthermore, while the County suggests that these savings can be realized through attrition and that the lack of specificity provides department managers flexibility in conforming to their reduced salary and fringe benefit appropriation levels, it contradicts its stated goal of maintaining staffing at current levels.

Since the County does not prepare a four-year headcount plan, it is difficult to decipher in which direction the County actually intends to move. In addition, since normal attrition occurs throughout the year and across positions at all salary levels, it is likely that in order to achieve a 4% salary savings, a higher than 4% level of attrition will be necessary.

NIFA believes that the County Executive must be proactive and make explicit decisions on which services to continue, scale back, and/or eliminate and then provide sufficient funding to staff departments at commensurate levels. NIFA encourages the County to develop a four-year headcount plan which is consistent with the financial plan. In the absence of an articulated headcount policy, the size and scope of County services will be shaped by the random nature of the attrition program. In addition, since achieving goals and objectives through attrition requires significant managerial sophistication, skill, and effort, NIFA remains concerned whether the necessary management processes are in place to effectuate the assumed expenditure reductions and revenue enhancements during the transition to a new administration.

On balance, NIFA's analysis indicates that the County could adhere to its aggregate base salary projections, though individual departments may have operational difficulties resulting from meeting the unspecified salary savings targets. In addition, any raises granted to employees represented by the PBA, DAI, and SOA will exacerbate the difficulty the County will experience in managing to its salary budget since funding has not been provided to cover collective bargaining increases for these groups. Moreover, NIFA's analysis assumes that County headcount on January 1, 2002 will not be higher than it was on August 31, 2001. It is now our understanding that the County headcount increased by an additional 100 full-time employees in September, a development which can only complicate the County's ability to meet its FY 2002 salary and fringe benefits targets.

Overtime

NIFA believes that the County's ability to control its overtime expenditures will be severely tested and presents a formidable risk to FY 2002 Budget balance, especially if attrition creates vacancies in traditionally overtime-intensive titles.

Police and Correctional Center overtime costs account for a significant portion of the County's overtime expenditures. Until FY 2000, these costs had grown largely unchecked, as actual overtime expenditures often exceeded adopted appropriation levels. FY 2000 marked a successful period of County restraint on overtime spending, especially in these two departments. The Police Department reduced its utilization of overtime through better staffing practices, reassignment of certain personnel into patrol duties, civilianization efforts, and a labor-management agreement involving payback time. The Correctional Center was able to rein in overtime spending through a number of efforts including the enforcement of a contractual provision on "over-the-cap" overtime earnings and optimally streamlining and consolidating inmate housing units based on inmate census.

Unfortunately, FY 2001 marked a return to the uncontrolled spending habits of the past as several overtime initiatives either slipped or failed, planned civilianization didn't occur, vacant positions remained unfilled, and an erosion of morale at the Correctional Center caused by a protracted round of collective bargaining led to increased sick leave usage and a greater-than-planned reliance on overtime to maintain Correctional Center security. The County currently estimates that FY 2001 Police and Correctional Center overtime expenditures will exceed FY 2000 actual levels by $11 million, and almost $6 million over FY 2001 adopted levels.

The County projects that its FY 2002 aggregate overtime needs will fall below $35 million, or more than $9 million less than currently projected in FY 2001, as shown in Table 3. NIFA's analysis indicates that the County may have understated its FY 2002 overtime needs by $8.0 million, of which $7.5 million derives from potential overspending in the Correctional Center and Police Department.

(Table 3)
OVERTIME MAY BE UNDERFUNDED BY $8.0 MILLION

($ in millions)	FY 2001 County Projection	FY 2002 Budget	FY 2002 NIFA Risk
Correctional Center	$16.2	$10.7	$5.0
Police	$20.5	$18.0	$2.5
All Other	$7.1	$6.0	$0.5
Total	**$43.8**	**$34.7**	**$8.0**

The County has proposed a number of new initiatives for FY 2002 aimed at reducing overtime usage in the Correctional Center. It estimates that these efforts will generate recurring savings that grow from $2.3 million in FY 2002 to $2.9 million in FY

2005. In addition, it assumes that the planned hiring of additional correction officers before the end of FY 2001 should mitigate the need to staff certain mandatory post assignments with officers on overtime. Furthermore, a new labor agreement (ShOA) includes a strengthened sick leave control policy, a requirement that provides compensatory time in lieu of cash overtime for the first 16 hours worked, and the addition of five training days for new hires. The County expects these measures to result in a reduction in overtime utilization and concomitant reduction in costs.

NIFA's analysis, however, indicates that Correctional Center overtime may be understated by up to $5 million in each year of the Plan. NIFA's conclusion is based on current spending trends in the Correctional Center, anticipated contractual raises for correctional officers in FY 2002, and NIFA's assessment of the impact that proposed overtime reduction initiatives and hiring plans will have on overtime usage at the Correctional Center.

The Police Department maintains that a portion of the increased cost of overtime in FY 2001 results from unanticipated police retirements in the detective and supervisory ranks, a failure to fully implement certain civilianization initiatives, and the expiration of a memorandum of agreement (MOA) which required the first 16 hours of overtime worked to be paid for with compensatory time. The Police Department planned to civilianize 177 positions in FY 2001, of which only 40 were accomplished through a PBA MOA. In January 2001, an arbitrator ruled that further civilianization beyond previously agreed upon positions could not take place outside of the collective bargaining process, thereby jeopardizing a major component of the Department's staffing and overtime control plans.

The Police Department states that overtime costs can be reduced in FY 2002 and controlled through such measures as promotions into the detective and supervisory ranks and planned new hiring to replace uniformed attrition that has left many funded positions vacant. While certain promotions were recently made that will positively impact overtime usage for detectives and supervisors due to minimum staffing requirements, the County has not yet authorized the hiring of 125 police officers already requested by the Department. The Department assumed that approximately 75 of these new officers would begin training in November 2001 and become available to mitigate overtime demands by May 2002.[2] Delays in hiring and/or changes to starting salaries may impact the Department's ability to adhere to its overtime budget.

Despite the Police Department's efforts, NIFA's analysis of current spending trends in the Department, anticipated salary step increases for police officers in FY 2002, and NIFA's assessment of the impact that proposed hiring plans will have on overtime usage at the Police Department indicates that Police overtime may be understated by approximately $2.5 million in each year of the Plan.

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[2] Police officer candidates receive 7 months of training at the Nassau County Police Academy.

Fringe Benefits

The cost of providing fringe benefits to County employees continues to exert upward pressure on the County's budget and financial plan. The County's fringe benefits costs are projected to grow by 6.9% annually over the term of the Plan. Fringe benefits costs are primarily driven by legal requirements and collective bargaining agreements. As shown in Table 4, health insurance costs, and retirement and Social Security contributions are responsible for much of the projected growth. Since the Federal government sets social security contribution rates and the State Comptroller sets retirement system employer contribution rates, the County has limited power to decrease its own exposure to increases in these costs.

(Table 4)
GROWTH IN FRINGE BENEFITS
FY 2002- FY 2005

($ in millions)	FY 2002	FY 2003	FY 2004	FY 2005	Cumulative
Employee Health Insurance	$6.1	$7.7	$7.2	$7.9	$28.8
Retiree Health Insurance	3.2	6.1	5.7	6.2	21.1
Police Retirement	2.7	8.1	0.8	0.8	12.5
Social Security	5.0	2.2	2.3	2.5	12.0
State Retirement	(12.7)	4.4	0.3	0.3	(7.8)
Other Fringe Benefits	(5.2)	0.9	1.0	1.1	(2.3)
Total Fringe Benefits	**$0.8**	**$29.3**	**$17.2**	**$18.7**	**$64.4**

The County included an unspecified $4.7 million fringe benefit savings target in its FY 2002 budget, a level which we believe to be unattainable. In fact, our analysis indicates while various fringe benefit categories appear reasonably estimated, the County's projections for health insurance and pension costs may be significantly understated.

Health Insurance

For the majority of County employees and retirees, their health insurance benefits are determined through collective bargaining. Currently, the County funds the entire cost of these benefits for both active employees and retirees, at a projected cost of $114 million in FY 2002, or 9% higher than projected in FY 2001. Aggregate health insurance costs are projected by the County to increase by an additional $49.9 million by FY 2005 based on an assumed growth of 12% in FY 2003 and more moderate growth of 10% in FY 2004 and FY 2005. Since these expenditures are not negotiable and are mandatory, the growing costs must be accommodated in the FY 2002 Budget and Plan, further straining other parts of the budget.

NIFA is concerned that the cost of providing health insurance coverage to County employees and retirees may be understated by up to $4 million in FY 2002, $5 million in FY 2003, $9 million in FY 2004, and $13 million in FY 2005. These risks stem from NIFA's assumption that the cost of health insurance may rise by as much as 12.5% annually, an amount currently anticipated by the State Department of Civil Service. In addition, NIFA's analysis indicates that the County's projection of FY 2001 health insurance costs, which serve as the base from which the County's FY 2002 projections are made, may be understated and not account for the additional health insurance costs associated with County hiring since June.[3]

NIFA is concerned that current labor agreements lock the County into funding the entire cost for health coverage at a time of significant fiscal instability. Moreover, in most cases, the current labor agreements oblige the County to support these expenditures beyond the expiration of the respective contracts; a highly unusual practice that NIFA believes is fiscally imprudent.

Moving the County closer to a defined contribution toward employee health coverage, a practice that exists in virtually all public entities, would enable the County to shift a portion of the budgetary risk that stems from rapidly rising costs to its employees. It could take the form of a percentage of premiums paid by workers, higher deductibles and co-payments, and/or changes in the core coverage provided.

The County proposes that non-union employees, who comprise approximately 5% of the County's workforce, begin to contribute toward the costs of their health insurance coverage beginning in FY 2003. The proposal calls for the County to phase-in a cost-sharing relationship with this group of employees and retirees and is patterned after the State's cost-sharing model, which requires employees to pay 10% of the cost of single coverage and 25% of the added cost of family coverage. The County estimates annual savings from this initiative could grow to $733,000 by the end of the Plan. We encourage the County to pursue these fringe benefit cost containment initiatives during the collective bargaining process as part of its comprehensive plan to control expenditures and attain structural balance.

Pensions

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 billed to the County each December. After years of declining costs due, in part, to favorable pension investment earnings, it is expected that the County's contribution rates to both the ERS and PFRS will rise in the coming years. The County assumes that after funding stable employer rates in FY 2002, the retirement systems will require an additional 1.5% of covered payroll for ERS and 2.5% of covered payroll for PFRS in FY 2003 as the impact of recent declines in the stock market permeate State actuarial calculations.[4]

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[3] New County employees are subject to a 6-month waiting period before receiving health benefits.

[4] Nassau County's employer contribution to ERS was set at 0.6% of covered payroll in FY 2001. Likewise, Nassau County's employer contribution to PFRS was set at 3.3% of covered payroll in FY 2001. By increasing these

The County estimates that it will be required to contribute $13.1 million towards employee pension benefits in FY 2002, or 43% less than it expects to pay in FY 2001 before growing by $14.7 million over the next three years. The anomaly in FY 2002 results from a County gap-closing initiative that seeks to prepay certain out year pension obligations in FY 2001.[5] This action will cost $27.9 million and be funded with reserves produced in FY 2000 and currently held in the debt service fund. The County estimates that this action will generate budget relief of $10.1 million in FY 2002, $8.2 million in FY 2003, $7.2 million in FY 2004, and $5.2 million in FY 2005.

NIFA believes that the County's assumptions for future pension costs are not sufficiently conservative to mitigate the additional costs that might stem from investment volatility and any economic and demographic changes that may be considered by the retirement systems during the Plan period. In fact, the County Comptroller stated on September 28, 2001 that the proposed FY 2002 budget understates retirement system costs by more than $7.5 million. The County's calculations assume that the State retirement systems' pension investments grow by approximately 8% between April 1, 2001 and March 31, 2002, a scenario that appears unlikely considering that the value of the equity-invested component of pension assets has fallen by approximately 10% midway through the investment period.[6] Moreover, should the State retirement systems' investments continue to under perform the assumed rates of return, NIFA analysis indicates that requisite pension contributions could significantly exceed planned levels between FYs 2003-2005.[7]

Other Than Personal Services

The County projects that it will spend $438.8 million on OTPS costs in FY 2002. As shown in the chart to the right, these expenditures are composed of several large categories of spending: pre-school special education, local government assistance, mass transportation, early intervention services, payments to the Nassau Health Care Corporation, and utility costs. In general, the County has reasonably estimated these costs,

Elements of OTPS ($ in millions)	
Pre-School Special Education	$70.3
Local Government Assistance	$51.0
Mass Transportation	$43.1
Early Intervention Services	$42.8
Payments to NHCC	$35.1
Utility Costs	$26.8
All Other	$169.7
Total	**$438.8**

rates by 1.5% and 2.5% in FY 2003, respectively, the County assumes that employer contributions will be 2.3% for ERS and 5.8% for PFRS in FY 2003 and remain flat thereafter.

5 The County has been amortizing over a five-year period the additional pension costs associated with each of the County's early retirement incentive programs offered to County employees in recent years. The retirement systems provide the option to defer these costs at an annual interest rate of 8%.

6 Domestic and international equity investments comprise approximately 65% of the combined retirement systems' investments as of March 30, 2000.

7 The State Actuary indicated that contribution rates could increase by 1.5% for ERS and 2.5% for PFRS in each year of the Plan rather than remaining flat in FY 2002 and flat again in FY 2004 and FY 2005 as assumed by the County.

although the underlying assumptions must be monitored closely throughout FY 2002 to ensure that potential budget variances are recognized immediately and that corrective actions are implemented in a timely manner.

The Early Intervention program, administered by the Department of Health, 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, the Pre-School Program for ages 3-5, administered by the Department of Mental Health, and the School-Age Program of the Department of Social Services for ages six and older. The County assumes that the number of children receiving benefits will remain relatively stable during FY 2002 with rate increases driving program costs in the out years.

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 $51 million in FY 2002, are an expenditure offset to the sales tax revenue collected by the County from its 8.5% sales tax rate.

The County projects that it will spend $43.1 million on mass transportation in FY 2002. These expenditures are composed of $21.2 million in payments for Long Island Railroad station maintenance, $11.6 million for MTA operating assistance, $5.9 million in subsidies to the MTA Long Island Bus, and $4.5 million for Able Ride, its handicap transportation service.

The County estimates that its FY 2002 payments to the Nassau Health Care Corporation will be $35.1 million. These expenditures include $13 million in historic mission payments and $5 million in Article 6 Public Health Activities costs as well the cost of retiree health insurance, retiree debt service, longevity payments, and termination pay for certain employees of the Nassau Health Care Corporation.

The County has budgeted $26.8 million for utility costs in FY 2002, or about 2.7% more than it anticipates spending in FY 2001. The County maintains that these estimates include additional costs associated with the LIPA surcharge and higher costs for Trigen-Nassau Energy Corporation, a company that provides hot and chilled water to the Nassau Coliseum, Nassau Community College, and the Marriott Hotel under a contract with the County. The County's assumptions for the growth in fuel and other utility costs is not without risk and must be monitored closely during FY 2002 and be revisited in the out years of the Plan should factors beyond the County's control drive these costs higher.

The County projects that all other OTPS expenditures will reach $169.7 million, including expenditures for contractual services in areas such as legal, medical and psychiatric services in the Correctional Center, and program agencies. Of particular concern is the County's removal of all funding from the Data Processing division of the Department of Recreation, Parks and Support Services for software contracts, communications equipment, disaster recovery services and support for systems and programming. Data Processing submitted an FY 2002 budget request for $8.3 million, of which the division recently testified that more than $5 million is required to maintain existing data processing operations. These resources are required to pay for the routine maintenance of software and hardware, some of which are license agreements. In fact, the department maintains that certain systems will stop functioning when existing contracts expire and the long term costs of resolving currently unknown problems will be much higher without having service agreements in place. Failure to include funding for these costs could place the County's computer operations at risk. NIFA considers these savings to be misguided and unachievable.

Direct Assistance

The County projects that it will spend $441.1 million on direct assistance in FY 2002. As shown in the chart to the right, these expenditures are composed of four categories of spending: Medicaid, purchased services, emergency vendor payments, and recipient grants. The expenditures for the County's major social service program areas, including public assistance, foster care, children in institutions, and Title XX services are spread among the elements of direct assistance. As discussed below, NIFA's analysis indicates that the County's FY 2002 estimate of these costs are not unreasonable, but should be monitored closely should a deterioration of the local economy result in increased demand for social service programs and direct assistance spending, which may be more likely because of the events of September 11, 2001.

Elements of Direct Assistance ($ in millions)	
Medicaid	$296.5
Purchased Services	$49.8
Emergency Vendor Payments	$48.7
Recipient Grants	$46.1
Total	**$441.1**

Medical Assistance

Expenditures for medical assistance ("MA") have been steadily rising in recent years. The County assumes this growth may accelerate, conservatively embedding nearly 11% growth into its projection for FY 2002 Medicaid expenditures. The County estimates that it will spend more than $296 million on this assistance category, a figure NIFA believes to be reasonable.[8] The State has introduced Family Health Plus, a new health care program designed to provide health coverage to those who do not have health insurance through their employers, yet have income that disqualifies them from Medicaid. This program will soon commence and will clearly add to the County's local Medicaid burden as the program phases in.

NIFA also believes that the County's estimate of slightly more than 8% growth in Medicaid expenditures in each of the out years of the Plan is less conservative though not unreasonable in the aggregate. The determinants of growth in past years are difficult to isolate as the analysis is clouded by the multitude of different State and local funding

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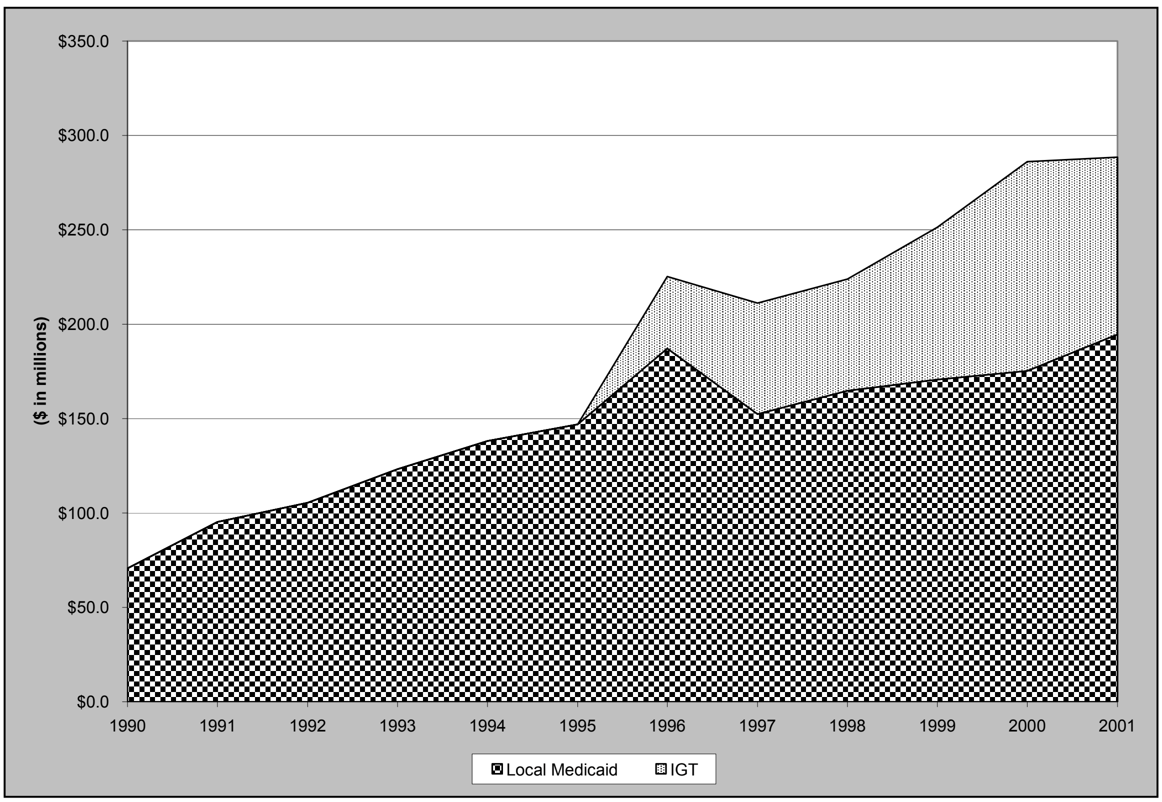
[8] This estimate is composed of County Medicaid obligations of $195 million and a $94 million Intergovernmental Transfer ("IGT") payment to the State. The IGT expenditure is actually a pass-through payment, which is fully recaptured through a reimbursement made to the County by the Nassau Health Care Corporation.

ratios across different Medicaid programs. It is clear, however, that changes to the program, which expanded coverage and increased reimbursement rates, have contributed greatly to the growth in spending on this area.

Medicaid caseloads continue to rise, growing by 50% since January 1990. As shown in Chart 3, local costs have grown by 175% over the same period, rising from $70.7 million in 1990 to a projected $194.5 million in FY 2001. This growth will continue to dictate policy to the degree that other programmatic choices must be prioritized so as to accommodate this large and growing mandated expense. Since the County lacks the authority to limit Medicaid coverage provisions and associated costs, it must be creative in finding measures to increase efficiencies and curb growth in these costs.

(Chart 3)
LOCAL MEDICAID COSTS
FY 1990-FY 2001



One such effort the County is pursuing is the introduction of mandatory Medicaid managed care. The program was originally scheduled to commence in January 2001. However, delays in receiving approvals prevented the County, until now, from beginning its process of enrolling its eligible Medicaid recipient population into one of five managed care programs on a mandatory basis.[9]

Managed care represents a step forward in cost containment since the capitated rates for managed care providers are lower than the traditional fee-for-service rates currently being reimbursed by the County through its local share of the Medicaid program. To date, the County has operated under a voluntary managed care program, with current enrollment levels reaching almost 9,000, or 22% of its total eligible recipient population, some of whom are exempted from the mandatory enrollment requirement.[10] The County is targeting 92% of the more than 31,000 non-exempted eligibles, phasing in their enrollment over a 12 to 14 month period.

The County has included savings of $1.8 million in FY 2002 and recurring savings of $2.9 million in the out years of the Plan from this initiative. NIFA believes these projections are reasonable based on the County's experience with its voluntary enrollment program and the State's estimate of savings that can be realized by switching from the traditional fee-for-service model to a Medicaid managed care model.

NIFA is cognizant of the impact that implementation of the mandatory Medicaid managed care initiative will have on the Nassau Health Care Corporation's ("NHCC") revenue base. The County and the NHCC are positioned on opposite sides of any initiative that modifies medical care reimbursement rates. Specifically, for every dollar the County saves on its local share of Medicaid expenditures, the NHCC will lose a multiple of these savings, since the NHCC captures State and Federal matching revenue as well. While movement toward mandatory Medicaid managed care has been discussed for many years, the NHCC has only recently requested that the County temporarily suspend its implementation to provide it more time to develop new and necessary strategies to mitigate the anticipated significant loss of Medicaid revenue. The County is currently evaluating this request. This report discusses the short- and long-term financial outlook of the NHCC beginning on page 49.

Public Assistance

In recent years, Nassau County's public assistance programs have changed considerably. Dramatic caseload declines and revised State and Federal welfare laws have had both important fiscal and policy implications. The "Personal Responsibility and Work Opportunity Reconciliation Act of 1996" introduced a comprehensive welfare reform plan that dramatically changed the nation's welfare system into one that requires work in exchange for time-limited assistance. The Act eliminated the open-ended federal entitlement program of Aid to Families with Dependent Children ("AFDC") and created

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[9] Nassau County began its mandatory Medicaid managed care enrollment process in late June with an anticipated effective date of October 2001.

[10] New York State began voluntary enrollment of Medicaid recipients into managed care programs in 1991. Key exceptions from managed care enrollment goals are residents of nursing homes, psychiatric centers, intermediate-care facilities for mentally disabled people, and recipients eligible for nursing home placement who are receiving home care or community-based services.

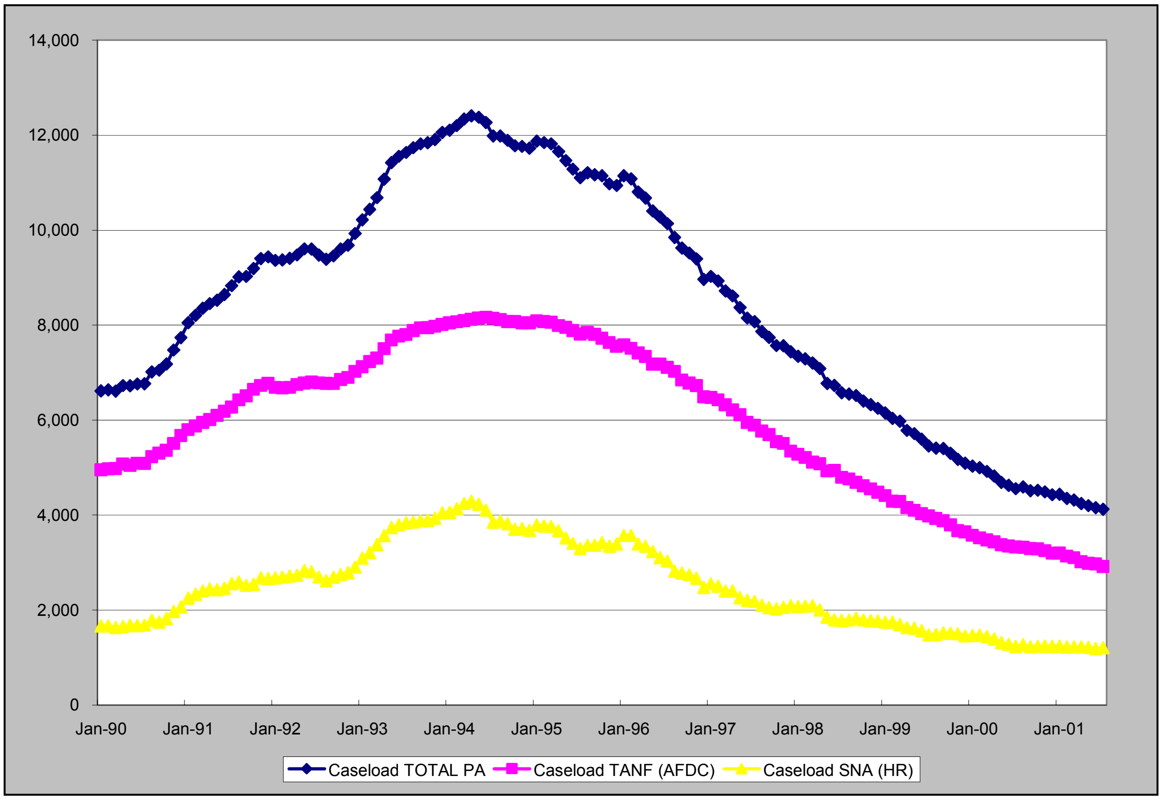
a new program called Temporary Assistance for Needy Families ("TANF"), which provides block grants for states to offer time-limited cash assistance. Under New York State's "Welfare Reform Act of 1997," Family Assistance ("FA") and Safety Net Assistance ("SNA") were created to administer and maintain a two-tiered system of public assistance at current benefit levels. Essentially, FA is New York's federally-funded public assistance program governing participants in TANF programs, including work participation quotas and a lifetime five-year limit on receiving aid. Likewise, SNA is New York's state- and locally-funded program for certain people not eligible for other assistance programs, including single adults, childless couples, and persons who have exceeded their five-year limit on assistance.

Funding for the new TANF block grant, authorized until 2002, was based on Federal contributions for AFDC, the Job Opportunities and Basic Skills ("JOBS") program, and Emergency Assistance programs in fiscal years 1992 through 1995. Because caseload levels have fallen relative to those base years, the State currently receives more TANF dollars than are required to maintain the programs that were incorporated into the block grant. The State allocates the TANF "surplus" among various programs and jurisdictions, including Nassau County.

The TANF surplus must be used for programs previously funded under the old welfare law and other social service laws that were replaced by TANF and other block grants. The State's maintenance of effort ("MOE") requirement was set at 80% of baseline spending (or 75% if they meet the Federal work participation requirements). If spending falls below the MOE requirement, the TANF grant is reduced in the subsequent year on a dollar-for-dollar basis equal to the level of non-compliance. The State is required to expend additional State funds in its TANF program equal to the amount by which the State fell short of meeting the MOE requirement. In addition, if the State received a Welfare-to-Work formula grant in the year in which it failed to meet the TANF MOE requirement, the TANF grant in the year after the failure will be reduced by the amount of the State's Welfare-to-Work formula grant.

While the block grant mechanism currently results in the State and local governments keeping the savings achieved by moving people off welfare and into jobs, it also means that the State and local governments will bear most of the increased cost if spending rises. As shown in Chart 4, public assistance caseloads rose significantly in the early 1990's, a time of economic contraction, almost doubling from 6,613 recipients in January 1990 to its peak of 12,406 recipients reached in April 1994. Since that time, welfare reforms and a robust economy led to a decline in caseloads by 67%, falling to 4,120 recipients in July 2001.

(Chart 4)
PUBLIC ASSISTANCE CASELOAD
FY 1990 – FY 2001

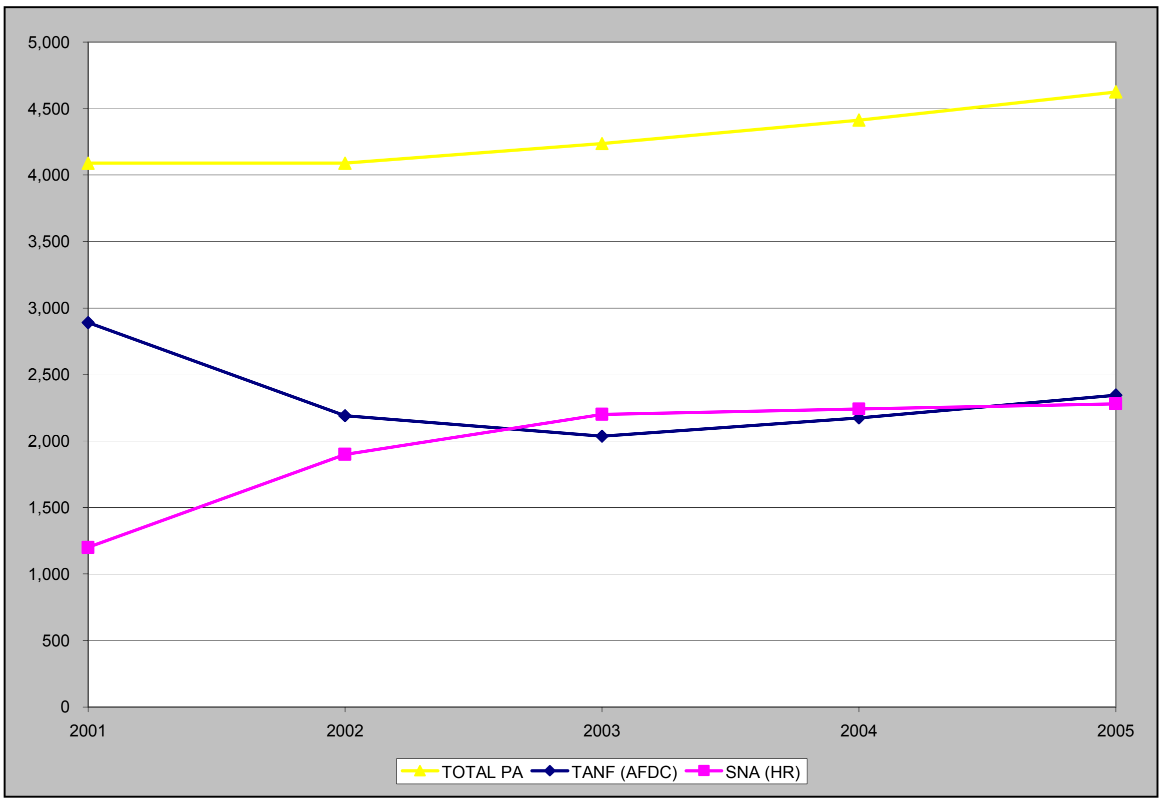


Changes in public assistance caseload and costs seem closely linked to fluctuations in the local economy. While predicting a turning point in the near-term direction of PA caseload would be speculative, it is reasonable to assume that the County will incur increased social services costs during the period of the Plan should there be a prolonged downturn in the local economy. County expenditures may be exacerbated once families begin to reach their five-year limit on FA, putting a further strain on local social services resources. Time-limited recipients will likely shift from Federally-funded TANF to State- and County-funded SNA. Since there is no Federal participation, the cost of this program to the State and its localities is twice as much as TANF. In addition, assuming the Federal government authorizes TANF funds beyond 2002, it is likely that the appropriation will be much lower since it will be based on significantly reduced caseloads, thus potentially forcing the State and its localities to increase their own level of funding.

While the County assumes that TANF caseload will decline by 700 in FY 2002 and an additional 264 per year beginning in FY 2003 due to time limits, it anticipates many of these cases will transfer to the State's Safety Net program resulting in an associated increase in SNA caseload and spending. In addition, the County assumes that baseline TANF caseload will begin to rise by between 5% and 10% for each percentage point rise in unemployment, lagged by 12-36 months, thereby also offsetting a portion of the savings from time-limited caseload declines associated with the TANF program. The County's projections assume a rise in the unemployment rate to 4.8% over the next three years.

As shown in Chart 5, the County estimates that aggregate PA caseloads will grow by 535 during the four years of the Plan. Specifically, net TANF caseload will continue to fall by nearly 700 in FY 2002 and 155 in FY 2003 before rising by 138 in FY 2004 and 171 in FY 2005. In recognition of the Federal five-year limit on TANF benefits and potential impact of the recent rise in unemployment, the County's SNA caseload is expected to climb by 699 in FY 2002, 302 in FY 2003, 239 in FY 2004, and 240 in FY 2005. Funding for these higher caseload projections has been factored into the Plan.

(Chart 5)
PROJECTED PUBLIC ASSISTANCE CASELOAD
FY 2002 – FY 2005



In total, the Plan contains \$44 million in FY 2002, \$46 million in FY 2003, \$48 million in FY 2004, and \$50 million in FY 2005 for TANF and SNA program expenditures. While these projections were reasonable when the Budget and Plan were constructed, they do not factor in any significant impact on the local economy, or increased demand for social services that might result from the tragic events of September 11, 2001. In addition, the County has not insulated itself from potentially negative consequences that would result from re-authorization of the TANF block grant at reduced levels, or a severe and prolonged downturn in the local economy. Should unemployment rise above County assumptions, or reach County assumptions more quickly than anticipated, additional unbudgeted costs may require that resources be redirected. The County must follow closely this highly uncertain program to guard against adverse changes in caseload and funding levels and be able to respond quickly to offset additional costs with new expenditure reduction and/or revenue enhancement initiatives.

Debt Service

Although many elements of the NIFA and County debt service figures have needed revision or correction, in NIFA's estimation the net effect of the changes is to leave the FY 2002 NIFA and County debt service close to the budgeted amounts. However, the actual County Budget document will need to be revised to properly attribute the various costs.

Principal changes to the budget and four year plan for NIFA set-asides and County debt service are detailed below. Related Capital Plan issues are also discussed.

NIFA Set-Asides. The NIFA debt service set-asides are presented in the FY 2002 Budget and Plan as reductions in sales tax revenue. The budgeted amount of $45.3 million is a net figure after deductions for proposed initiatives and NIFA investment income. NIFA believes that after making the corrections and adjustments discussed below, and reducing the projected NIFA investment income to reflect the current and forecast interest rate environment, the budgeted amount is appropriate.

Adjustments to the NIFA set-aside amount, before offsets, are as follows:

- <u>Shift RAN debt service to County budget</u>. This expense will be paid by the County, not out of NIFA sales tax set-asides as assumed in the Budget. The County has acknowledged this change.

- <u>Reconfigured Fall 2001 borrowing</u>. The County Plan assumes a November 2001 NIFA bond issue. Subsequent to Plan submission, a consensus has emerged that in lieu of this bond sale, NIFA can increase the size of its scheduled December note issue to include funding for items that would have been bonded in November. The County has sufficient funds to cover costs through December, between unspent NIFA proceeds ($40 million capital, $19.5 million working capital) and the proposed use of $7.5 million of FY 2000 surplus resources for pay-as-you-go financing of working capital needs. The reconfigured borrowing will reduce debt service set-asides in FY 2001 and FY 2002.

- <u>Change proposed amortization schedule for Spring 2002 NIFA borrowing</u>. Contrary to NIFA's established practice, the County plan assumes that NIFA bonds sold in May 2002 will not begin to have principal set-asides until November 2003, a one and one-half year period of interest only.

NIFA has determined that only a brief phase-in period, if any, is appropriate for general fund debt. The proposed Spring 2002 NIFA bonds should start principal set-asides in November 2002, just as the Spring 2001 NIFA bonds begin principal set-asides in November 2001. This will have a small cost impact in FY 2002 and a larger impact (approximately $4 million) in FY 2003. The correction must also be made for the proposed NIFA issues in Spring 2003 and 2004 and will further raise debt service amounts in FY's 2003-2005.

- Amortization of NIFA Restructuring Bonds. The amortization of the NIFA restructuring bonds has also been deferred beyond the level NIFA has previously determined to be prudent. The dollar impact of this deferral is smaller and mostly in the out years of the Plan. Although NIFA does not necessarily concur with this proposed restructuring bond amortization schedule it will consider the suggestion in the context of the sale of restructuring bonds.

- Shift offset of NIFA 2002 restructuring debt service to County debt service budget. NIFA's policy to date has been to provide restructuring savings to the County in the net amount agreed upon (i.e., net of the cost of related NIFA set-asides in the year in which the restructuring takes place). To achieve the net savings, NIFA refunds additional County debt service in an amount that compensates for the NIFA set-aside. The County Plan incorporates the offset amount in the NIFA debt category, but it needs to be built in to the County debt line. The amount will depend on the amount of restructuring NIFA performs.

NIFA has estimated, with the above adjustments, that NIFA 2002 set-asides before offsets are about $48.5 million. The County should re-run its NIFA debt issuance numbers to come up with more precise budget figures.

In the FY 2002 Budget, the amount of NIFA set-asides is reduced by projected earnings on funds held by the NIFA Trustee and by projected savings from County initiatives. Several facets of these offsets require comment:

- NIFA Investment Income. The County assumes a 3.8% earnings rate that is well above the rates currently being experienced or projected. If current rates hold, a 25% or $959,400 reduction in NIFA investment income is reasonable to expect and would be sustainable within the current budgeted net NIFA debt service amount. As detailed in the Investment Income section of the revenue analysis, the NIFA 2002 investment income is double-counted in the proposed 2002 Budget and Plan. The NIFA analysis assumes that the income remains here and therefore the County's projection for Investment Income should be reduced.

- Correct allocation of sewer debt service. We agree with this initiative, but it needs to be restated to: (1) correct the amount related to NIFA debt (as the County has acknowledged), and (2) allocate the total savings in the initiative between NIFA and County debt service. The NIFA-related sewer debt service is an offset to NIFA debt service. County debt that has been omitted from prior charge back to the sewer districts will offset County debt service amounts (see the County debt service section below).

- <u>Commercial Paper (CP) initiative</u>. The proposed commercial paper program, which NIFA would have to administer on the County's behalf, reduces NIFA set-asides in FY 2002 due to: (1) temporarily lower cost of borrowing (until floating rate CP is converted to long term bonds); (2) slower pace of debt issuance, as debt is rolled out in smaller monthly increments rather than as a lump sum in the first month; and (3) deferred amortization – the first principal payment on the proposed Fall 2001 CP-related debt is November 2004, versus a November 2003 principal payment for a conventional Fall 2001 borrowing. This last element is not acceptable.

  In response to the County proposal, NIFA has investigated the CP idea with our bond counsel, underwriters, trustee and other governmental issuers of CP. Our preliminary determination is that CP has merit as a general idea but will need further investigation by NIFA and by the new County administration in FY 2002. While we believe a CP program could be made to work, there are implementation issues with respect to NIFA's debt issuance framework and County and NIFA administrative responsibilities. In addition, NIFA is wary of creating a program that could be seen as compensating for the County's inability to accurately forecast spending needs. Finally, the reconfigured Fall 2001 borrowing plan, noted above, eliminates the potential use of CP for the Fall 2001 borrowing, and thus eliminates a substantial portion of the projected 2002 savings from NIFA CP. For all these reasons, we have taken CP out of our projection for FY 2002 NIFA debt service. We remain open to considering the idea in 2002.

Nassau County Debt Service. As with the NIFA debt service, after correcting for a series of countervailing errors and adjustments, the amount budgeted for County debt service appears reasonable though not precise. There will be some shortfall if the defeasance initiative is disallowed or the sewer debt service reallocation can not be made (see below).

The County long term bond debt service in the FY 2002 Budget and Plan conforms to debt summaries provided to NIFA in February 2001, except that sewer-related debt currently charged to the General Fund but omitted from the February data has been added back (it is proposed to be removed in accordance with initiative titled "Correctly allocate sewer debt service", discussed below). The reduction in FY 2002 County debt service to achieve net NIFA restructuring savings, discussed above, also needs to be reflected. The short term (RAN and TAN) debt service amounts require adjustment as follows:

- RAN interest. The 2002 RAN interest was originally stated as a hypothetical amount based on the 2000 RAN. However, the 2002 interest will be paid on RANs that have already been issued, so that the exact amount of the liability is known. Also, the RAN interest was originally added to the NIFA set-asides and must be moved to the County debt service line. The County has acknowledged the need to make these changes.

- TAN interest. The 2002 TAN interest expense projection was based on excessively high interest rates of 5.39% to 6.26%. NIFA's June note sale was at a 2.5% yield and rates have continued to fall. Following discussions with NIFA, the County has revised its interest rate projection for the December TAN to 2.5%. Their methodology also provides some room for higher interest expense. We believe the amount to be more than adequate for the current market.

- Sizing of RAN and TAN. Interest expense for the RAN and TAN also depends on the total amount borrowed. The County projects that the trend already begun since NIFA's creation, of lower cash flow borrowings due to improved County finances, will continue. To the extent that budget gaps recur and the County is not able to improve its financial position, these cash flow borrowings will not decrease as much as projected.

The financial Plan includes several initiatives to reduce County debt service in 2002:

- Reduction in RAN and TAN interest. It is appropriate and expected that a better County financial position and permanent gap-closing measures will reduce the need for cash flow borrowing. NIFA does not consider the reduced borrowing to be an "initiative." The amount the County can borrow is constrained by Federal tax law. While lower short term borrowing is a product of better finances and cash flow forecasting, it is not an independently implemented improvement.

- Correctly allocate sewer debt service. This initiative states that New York State Environmental Facilities Corporation (EFC) Series 1992B debt service which is currently being paid from the general fund should be reattributed to the sewer funds. The $456,728 EFC debt service in 2002 is included with a 20% "discount" to $365,383. Questions have been raised whether the 1992B debt was in fact sewer-related. If so, this initiative should be implemented as soon as possible and, as noted by the County Comptroller, should be fully reflected in the 2002 budget as well as in the financial Plan.

- Use $15 million of 2001 excess resources to defease County debt in 2003 and 2004. This proposal, which has an $813,700 effect in 2002 (interest that would otherwise have been paid on the defeased debt) is a one-shot, not an initiative. Money is being set aside to pay principal and interest, when due, on bonds that mature in FY 2003 and FY 2004. This provides one time budget savings of $5.2 million in 2003 and $10.5 million in 2004. The County argues that without freeing up budgeted debt service monies to fund new debt service, the capital program would have to be cut by $101 million in 2003 (eliminating capital borrowing that year) and $20 million in 2004. However, the resources needed to support the capital program are like all other County resources and should be evaluated as part of the total financial Plan. There is no reason to link this initiative specifically to the level of capital plan spending.

Capital Plan-related issues in the 2002 Budget and financial Plan. Embedded in the projected debt service numbers are assumptions about the County capital program. In April 2001, the County adopted a five year capital plan for 2002-2006 that included $157.56 million of general County capital and $22 million for sewers in 2002. Several aspects require comment:

- General purpose county capital. The County expects to pay for capital projects in 2002 through a combination of County and NIFA funds on hand and additional NIFA borrowing. Based on information provided in response to NIFA requests and the projected NIFA borrowing schedule in the four year plan, it appears that money available for capital projects in 2002 is well below the adopted capital plan level of $157.56 million. The County must further prioritize its capital spending.

- Cost of initiatives. The County's 2002-2006 capital plan includes $6.4 million to implement projects that appear as initiatives in the financial Plan. An additional $2 million of capital spending will be needed for the copier purchase initiative. These costs must be included in the scaled-back capital spending in 2002.

- Sewer-related capital needs. Since the inception of NIFA, sewer capital needs have been funded with NIFA bonds. However, NIFA has been advised that the financial Plan's projected debt issuance schedule does not include sewer needs. Economically, if the sewer-related NIFA debt service is correctly allocated in accordance with initiative titled "Correctly allocate sewer debt service," the additional NIFA debt for sewers will not change the bottom-line cost to the County general fund. However, provision must be made in the budget for additional NIFA expense and related offsetting interfund transfers.

Pay-as-you-go Initiative. A large part of the County's borrowing, historically and through NIFA, has been for costs that are more appropriately financed out of an operating budget. These costs, defined as "working capital" under the Federal tax code, include tax certiorari payments and other routine settlements and judgments. NIFA has criticized this practice.

Pursuant to the proposed initiative, the County will allocate $7.5 million of excess FY 2000 resources to pay working capital costs that would otherwise have been bonded. This represents a small first step towards better practices. NIFA would like to see any additional excess resources also applied in this manner.

Expenditure Initiatives

Meal Relief Schedule

The Correctional Center has modified its staffing schedule to maintain inmate supervision at the lowest cost while providing meal relief to correction officers assigned to a housing area. The Correctional Center assigned 21 correction officers to an 11am-7pm schedule in order to relieve officers working on the 8am-4pm and 4pm-12am shifts using straight time rather than overtime as had been done historically. The County estimates that this initiative can generate recurring overtime savings of $1.5 million in FY 2002 and almost $1.8 million by FY 2005. It is unclear if the Correctional Center can realize the full savings contemplated in the Plan. Since these savings are subsumed in the Correctional Center's overtime budget and, as discussed on page 20, our analysis indicates that the Correctional Center may exceed budgeted overtime levels by approximately $5 million, the County must closely monitor overtime spending and be prepared to immediately implement corrective measures to ensure budgetary balance.

Revise In-Service Training Schedule

The Correctional Center has rescheduled most training to take place during the 4pm-12am shift. Since fewer officers are required during this time compared with the 8am-4pm shift when training had been conducted historically, the County estimates that the Correctional Center can save $500,000 in avoided overtime costs in FY 2002 and greater amounts in each year of the financial plan. While this initiative is clearly designed to reduce overtime costs, it is uncertain if the Correctional Center can realize the full savings contemplated in the Plan. Since these savings are subsumed in the Correctional Center's overtime budget and, as discussed on page 20, our analysis indicates that the Correctional Center may exceed budgeted overtime levels by approximately $5 million, the County must closely monitor overtime spending and be prepared to immediately implement corrective measures to ensure budgetary balance.

Productivity Gains and Reduced Costs in Police Department

This initiative seeks to reduce staffing levels and realize savings within the Police Department's support functions by $2 million in FY 2002, $4 million in FY 2003, $6 million in FY 2004, and $8 million in FY 2008. The Department will look to utilize technology and consolidate commands to minimize any adverse service impact in non-patrol services. The County maintains that non-essential services will be curtailed to the extent that savings from these efforts are less than assumed in the Plan. Since the Department does not currently have an explicit plan designed to realize the FY 2002 savings target, NIFA encourages the County to articulate what tasks and milestones must be accomplished by the Department to support the significant budget relief required by this initiative.

Reduce County Copy Machine Inventory and Lease Costs

This initiative seeks to generate budget relief by reducing the number of copy machines in the County from 588 to 516 and by replacing leased machines with County-owned machines through a three-year capital program purchase. In addition, the County seeks to capture additional copy machine revenue by adding 14 public access copy machines in County offices under a concession contract in which a portion of revenues will accrue to the County. In aggregate, the County projects that it can realize $491,000 in budget relief in FY 2002 and higher annual amounts during the Plan. While the County states that it performed a purchase versus lease analysis in support of this initiative, we are generally wary of actions that capitalize operating expenses.

Reduce Long Island Bus Subsidy by $2 Million

The County proposes to reduce its annual subsidy to the MTA Long Island Bus by $2 million, taking it down from $7.9 million to $5.9 million. The County maintains that its contract with the MTA provides the County with the ability to limit its subsidy, with any resultant shortfalls being made up through improved operating efficiencies, reductions in service, or additional revenues such as State aid. While this reduction in funding may negatively impact service, it is a policy decision that the County has made and was already included in the consensus plan adopted on November 29, 2000.

Prepay Pension Obligations

The County has participated in a series of State early retirement incentive programs in recent years. Each program required that the resulting cost of the greater pension benefit be paid to the retirement system immediately or be amortized over a five year period with an interest charge of 8%. The County is proposing that it prepay in FY 2001 all remaining charges for these past programs and other benefit enhancements using available reserves from FY 2000. The prepayment will total $27.9 million, but result in budget relief of $10.1 million in FY 2002, $8.2 million in FY 2003, $7.2 million in FY 2004, and $5.2 million in FY 2005. We believe this initiative makes good use of the non-recurring reserves generated by the County in FY 2000 and currently held in the debt service fund.

Increase Revenues from Housing Federal Inmates

The County proposes to increase its revenues from housing Federal inmates at the Correctional Center. The County projects that a 10% increase in the current reimbursement rate of $142 per inmate per day combined with an increase in the number Federal inmates currently held by the County from a maximum of 150 to 200 could yield additional budget relief of $260,000 in FY 2003, $855,000 in FY 2004, and $1.4 million in FY 2005. These projections assume that a Federal audit of County Correctional Center housing costs leads to an increase in the reimbursement rate, that the Federal government continues to incarcerate Federal inmates in the County despite these higher costs, and that the Federal government needs to increase by 50 the number of inmates housed daily by the County. While NIFA believes that the County should maximize the revenue generated by housing Federal inmates at the Correctional Center, the audit's findings and the County's ability to land more inmates is unknown. It also appears that the projected budget relief from this initiative does not account for the increased costs of housing Federal inmates at the Correctional Center, an expense that reduces the net benefit to $65 per day per inmate.

Reduce Correctional Center Medical Costs

Correctional Center inmates receive medical care by the Nassau County Health Care Corporation under a contractual arrangement with the County. Under the contract, the County pays direct costs plus a 21% administrative charge for the operation of infirmary services at the Correctional Center and pays Medicaid rates for outpatient and inpatient services rendered at the hospital. The County maintains that these costs, which average approximately $8,600 per inmate, are high relative to other municipalities.

The County proposes that these costs can be brought down through better oversight, changes to the reimbursement rates, and other strategies including the use of insurance for catastrophic inmate medical care and increased reimbursements from third party insurers. The County assumes that these costs can be slowly lowered to $6,500 per inmate, generating savings that grow from $750,000 in FY 2003 to $3 million in FY 2005. While the County has significantly discounted the estimated savings in the first two years of implementation, in light of the NHCC's current fiscal distress, NIFA believes that the NHCC may be resistive to renegotiating rates downward since any savings that accrue to the County results in lost revenue to the hospital.

Local Certiorari Debt Service Savings

The County seeks to shift the burden of town and school district property tax refunds to the jurisdictions that levy the taxes. This has been opposed by the localities because, unlike other New York counties, Nassau handles the assessment function for all jurisdictions in the County. Implementation of this initiative would require State legislative action bolstered by local support, neither of which have been evident to date. The Plan assumes the shift is completed in FY 2003 and that financial benefits begin to be realized in FY 2004. NIFA believes the probability of success is very low.

Consolidate and/or Outsource Mainframe and Network Management

The County currently has a division of Data Processing in the Department of Recreation, Parks and Support Services which is charged with meeting countywide information technology (IT) needs. In addition, the County assigns certain IT personnel to specific agencies, thereby increasing costs for duplicative functions and equipment. The County proposes to consolidate and centralize its IT operations, realizing personnel savings, increased efficiencies, and improved service response. The County alternatively contemplates outsourcing data processing functions in order to realize these savings. The County estimates that savings of $750,000 in FY 2003, $1 million in FY 2004, and $2 million in FY 2005 can be realized from these actions. While any initiative which seeks to eliminate redundancies and, in the process, improve County efficiency and productivity has merit, it is unclear how savings can be realized from personnel savings when, at the same time, the County notes that implementation of the initiative will require additional personnel to fill budgeted positions.

Remit Town and School Taxes Upon Receipt

Under this initiative, which would require State legislation to implement, the County would remit taxes to towns and school districts only when received, rather than on a fixed schedule that may not reflect actual collections. This change would reduce the size of County cash flow borrowings, which are required for the County to be able to remit 100% of the amount of taxes in advance of their receipt, and allow greater County investment income. It is scheduled to begin in FY 2004 to allow time for State action.

In this case, the County's gain would be a loss to the towns and school districts, reducing the likelihood of State legislative action.

Establish Technology Investment Fund

The County plans to establish a $10 million Technology Fund in FY 2002 that will provide "seed" money to fund technology investment throughout the County on a pay-as-you go basis rather than relying on the use of long-term financing. The County anticipates using a portion of its projected $25 million FY 2001 year-end positive operating result to support the fund. The County stated that the Technology Fund's guidelines will require that projects provide a 2-for-1 return within five years and that funding cannot be used for recurring personnel costs.

In light of the County's glaring weakness in technology investment and utilization, NIFA actively supports the creation of the Technology Fund. NIFA is pleased that non-recurring resources generated from positive operating results will be used to reduce future borrowing needs and thereby generate recurring debt service relief, a cornerstone of County movement toward structural balance.

The County projects that this initiative will generate $2 million of budget relief in FY 2003 before growing to $4 million in FY 2004 and FY 2005. However, the County cites as examples projects that are expected to generate only $125,000 in annual savings. The County points to other opportunities for exploration including fleet management information systems, facility management software, energy conservation measures, and parks and public works maintenance equipment. NIFA believes these savings projections are overly optimistic until more detailed technology improvement plans are unveiled.

Professional Services Contract Cuts

This initiative seeks to reduce the County's reliance on outside consultants and projects savings of $3 million in FY 2003, rising to $4 million by FY 2005. The County represents that it aims to strengthen internal staffing and predicts that this will lead to a reduced need for personal services contracts with outside consultants. At the same time, however, the County is striving to achieve salary savings of 4% through attrition and has an initiative to reduce non-union positions by 15%. These actions will weaken internal staffing and NIFA questions the ability of the County to achieve this initiative.

Reduce Non-Mandated Expenditures by 1.5 Percent

The County proposes to reduce non-mandated expenditures by 1.5% in each year of the plan, reasoning that it can realize budget relief of $13.2 million in FY 2003, $26.8 million in FY 2004, and $41.2 million in FY 2005 from these cuts. The County has categorized the following expenses as mandated expenditures: fringe benefits, debt service, local government assistance, Early Intervention contracts, the Mental Health Pre-School program, purchased services, emergency vendor payments, Medicaid, indirect care, and subsidies to the Nassau University Medical Center. Also exempted are payments for rents, utilities, insurance, and suits and damages, expenditures for which the County has only limited control.

While the County characterizes the proposed reductions as something other than “across the board,” it is unclear what programmatic priorities, if any, the County Executive is setting. Although certain programs have been explicitly spared, individual department level targets have not been established. NIFA believes that managerial discretion to effectuate these savings through reductions to salaries, equipment, supplies, general expenses, reserves, MTA Long Island Bus, contracts for services other than Early Intervention, and contributions is limited by the lack of specificity, particularly since the targeted level of savings compounds in each successive year. NIFA encourages the County to develop a more comprehensive plan which lays out in greater detail where the cuts will be exacted, the major tasks and milestones essential for implementation, and an analysis of the impact these reductions will have on County services. At that time, both the County Executive and the County Legislature can make informed policy choices.

Reduce Ordinance Positions by 15 Percent

The initiative seeks to reduce the expenditures on non-union (Ordinance) employees by 15% resulting in planned savings of $2.7 million starting in FY 2003. Ordinance employees serve at the pleasure of the County Executive and are not represented by any collective bargaining unit. As discussed in NIFA’s report on the Adopted Financial Plan for Fiscal Years 2001 – 2004, effective management is required to ensure that necessary services are delivered to County taxpayers in an efficient and effective manner. Many Ordinance employees serve in managerial capacities. The initiative fails to discuss what departments would be reduced and how this would impact operations. Until a more focused and thoughtful analysis is provided the initiative is at risk.

Arbitrage Rebate Liability

Nassau County’s bond proceeds expenditure rate and investment policy have in some cases failed to meet the requirements of Federal tax law, thereby requiring it to rebate excess earnings to the IRS. A rebate payment of several million dollars is expected to be made in FY 2001. This payment covers only one set of transactions (in connection with the MTA) and the County has not established whether other rebate liability exists. The County needs to examine its entire financing portfolio to determine the timing and magnitude of any other rebate liability.

RESERVES

The NIFA Act requires that the Authority monitor the "fiscal management" of the County. As part of this responsibility, when reviewing the County's financial Plan, the Authority must ensure that "adequate reserves are provided to maintain essential programs in the event that revenues have been overestimated or expenditures underestimated for any period."

The County has several potential liabilities for which there are not adequate reserves or for which there has been inadequate planning. One example is the Nassau Health Care Corporation ("NHCC"). Even though "active efforts are underway" to solve its financial problems, NHCC has not presented any financial information to NIFA that demonstrates improvement in its financial condition. The County should not only be setting aside reserves to cover its legal obligations for debt service, it should also be evaluating its options, and continuing obligations, if the hospital is forced to close.

Another illustration of the inadequacy of reserves is the amount that the County has set aside in its FY 2002 Budget, and for each of the out years of the financial Plan. In each year of the financial Plan the County has included \$10 million, of which \$8.9 million is for unforeseen events in the Police District, and the remaining \$1.1 million is for contingencies that may arise in all other funds. The proposed Plan does not contain any salary increases for the settlement of police contracts. A one percent salary increase in the PBA contract would cost approximately \$2.5 million per year, which illustrates the inadequacy of the \$8.9 million reserve for the Police District.

A third example is the utilities lawsuit in which the State Supreme Court ruled that the County's method of taxing utilities violated the State law. If the County fails on appeal, liability has been calculated at \$99.1 million plus interest at 9% from January 1998. No reserve has been placed in the Plan for this possibility.

The County has taken the general position that it is not "prudent to dedicate specific contingency reserves to specific risks when active efforts are underway to mitigate potential County obligations associated with such matters." In the past it was necessary for the County to bond for unforeseen events because adequate reserves were not budgeted. That pattern of not living within its budget and borrowing for every contingency was a contributing factor in the deterioration of the County's fiscal health and to the need to create NIFA. In addition, the economic uncertainty caused by the tragic events of September 11, 2001, are one more reason why NIFA believes that the County should increase the reserves contained in the FY 2002 Budget and financial Plan.

V. FY's 2003-2005 Financial Plan

This section discusses the growth rates that were used by the County for revenues and expenditures in the Plan and the actions that the County proposes to take to close the out-year gaps. The growth rates used are prior to the implementation of any major policy changes and out year initiatives contained in the Plan (future property tax increases, phase out of Long Island Bus subsidy, etc.). In addition, the County has made several revisions to the out years of the Plan to correct errors and make technical adjustments. NIFA's analysis is based upon the information contained in the formal submission. Any such errors and technical adjustments should be reflected in the final adopted Plan.

OUT YEAR GROWTH RATES

Revenue Growth

For purposes of projecting revenues in the out years of the financial Plan (FY 2003 – FY 2005) the County used the following growth rates:

- Property taxes are projected to increase 5% per year, which is consistent with the currently adopted financial plan.
- Sales taxes are projected to grow 4.5% in FY 2003, 4.3% in FY 2004, and 4.2% in FY 2005, a significant increase from the 3% growth rate that is contained in the currently adopted financial plan.
- Special taxes are projected to grow 2.5% per year, which is consistent with the currently adopted financial plan.
- Interest penalty on taxes grow by 5% a year, which represents a change from the projection of zero growth contained in the adopted financial plan.
- Permits, licenses, fines and forfeits are projected to increase .4%, which is a decrease from the 1.1% growth projected in the currently adopted financial plan.
- Capital backcharges are projected to grow 5%, which represents an increase from the 2.5% that was projected in the currently adopted financial plan.
- Federal and State aid are projected to grow approximately 5% a year, which represents an increase from the 2.5% projected in the currently adopted financial plan.

Expenditure Growth

The following is a discussion of the growth rates used in the out years of the financial Plan for the more significant expenditure categories.

Salaries and wages represent the single largest expenditure category in the FY 2002 Budget. For employees covered by existing contracts, salaries are projected based upon their contracts, averaging approximately 4% per year. For employees without a current contract, the County is projecting no increase in salary or steps, generating a projected savings of approximately $12.5 million. In subsequent years, the County is projecting 2.5% increases for salary and 1.5% increases for steps.

Fringe benefits are projected to remain level between FY 2001 and FY 2002, and then grow by 14% in FY 2003, 7.3% in FY 2004, and 7.4% in FY 2005. Health insurance and pension costs are major components of fringe benefits. Health insurance costs are projected to grow by 12% in FY 2003, and 10% in FY 2004 and FY 2005 as compared with a projected annual growth rate of 8% in the adopted financial plan. Pension contributions are scheduled to increase significantly in FY 2003, due to the recent poor performance of the stock market, and then grow by a more modest 4% in FY 2004 and FY 2005. This represents an increase from the 3% annual growth rate projected in the currently adopted financial plan. In light of the recent poor performance of the pension fund assets, we believe that annual increases of 4% may be insufficient.

Medicaid costs are projected to grow by 8.3% in each of the out years, which is an increase from the 7% contained in the currently adopted financial plan. Other contracted services are projected to grow at an average rate of 4.5%, based upon a general cost escalation of 3%, adjusted upward to reflect higher historical growth in certain mandated social services programs, such as Childhood Early Intervention.

Most other expenditures are projected to grow by approximately 3% in each of the out years. Included in this category are the following items: equipment; supplies; general expenses and LIRR station maintenance. Utilities are scheduled to increase 5% each year.

OUT-YEAR GAP-CLOSING ACTIONS

Based upon the growth rates discussed above, the County has identified out year gaps of $78.8 million in FY 2003, $146.9 million in FY 2004, and $208.6 million in FY 2005, after consideration of NIFA debt restructuring and transitional State aid, and before implementation of County actions to close the gap. While there is no precise categorization of the County's initiatives, for discussion purposes they have been separated into three broad categories:

- Management actions, which represent decisions that impact County-wide issues such as staffing levels, and service delivery;
- Revenue actions, which are designed to increase revenues within the County through increases to established user fees, permits and licenses; and
- Expenditure actions, which are designed to reduce the cost of County operations.

These three categories are discussed below. Many of the more significant initiatives have been discussed earlier in the report.

Management Actions

The Plan to close the gap contains four initiatives with projected savings of $20.9 million in FY 2003, $37.1 million in FY 2004, and $52.1 million in FY 2005. This includes initiatives to cut non-mandated expenditures annually by 1.5% for a total reduction of approximately 4.5% over the three year period, reduce ordinance positions by 15% in FY 2003, and reduce the level of professional service contracts by $3 million in FY 2003, $3.5 million in FY 2004, and $4 million in FY 2005. These actions represent policy decisions that must be considered and addressed by the County Legislature during the adoption of the financial Plan.

Revenue Actions

The Plan also contains approximately 17 initiatives that are projected to increase County revenues by $40.3 million in FY 2003, $90.6 million in FY 2004, and $129.6 million in FY 2005. Among these initiatives are annual property tax increases of 5%, which are consistent with the currently adopted financial plan. The County also proposes to increase various fees by $3.5 million in each out year of the Plan, and improve collections in the Traffic and Parking Violation Agency by $1.2 million in FY 2003, and an additional $1.1 million in FY 2004. Other revenue initiatives requiring State Legislative approval include a cigarette tax, red light cameras, the sharing of the E-911 cellular surcharge, and a change in the way that taxes are remitted to the County.

Expenditure Actions

The Plan contains approximately 12 initiatives with projected savings of $4.9 million in FY 2003, $15.8 million in FY 2004, and $21.3 million in FY 2005, that are projected to reduce the cost of County operations in a variety of ways, including operational improvements, transferring costs to other governments, and privatizing certain functions. Among the larger initiatives are: reducing the cost of providing medical services to the Correctional Center to save $750,000, in FY 2003 and than growing to $3 million in FY 2005; requiring that school districts and towns be responsible for their share of the tax certiorari settlements which is projected to save $7 million in FY 2004 and FY 2005; and privatization efforts which are scheduled to save $1 million in FY 2003, and grow to $5 million in FY 2005.

CONCLUSION

The out-year gap-closing actions proposed by the County must be realistic, achievable, and part of a coherent effort to resolve the County's structural imbalance between revenues and expenditures. As currently written, the multi-year Plan is unacceptable because it is extrapolated from a flawed FY 2002 Budget. In addition, NIFA has the following concerns as it relates to the actions proposed in the out years of the Plan.

In order to reach a decision about the proposed management actions, the Legislature must have information about how such cuts will affect employee headcounts, its ability to manage the County, and the level of services that the County will be able to provide. The County must also have a plan to show how these cuts will be made and managed.

Four of the initiatives increase County revenues, which represent actions that have been discussed for several years but have not received support at the State level to have the necessary legislation enacted. These revenue initiatives have a value of $8.5 million for FY 2004, and $9.2 million for FY 2005. We continue to question the County's ability to have these initiatives enacted by the State Legislature.

The proposed expenditure actions include two of particular concern. These include the reduction of Correctional Center medical costs, and the requirement that school districts and towns pay their share of the tax certiorari claims. It is our understanding that the County is under a court order to provide adequate medical care to inmates, and the County Comptroller notes that the costs of providing such care are set forth in the transfer agreement between the County and the Medical Center and are subject to future negotiations. Consequently, the County may have limited ability to control these costs. As it relates to the school districts and towns paying their share of tax certiorari claims, the County has not demonstrated that there is support at the State or local level to enact such a change.

NIFA also questions the assumption contained in the Plan that any newly negotiated labor contracts will have no salary or step increases in the first year. The savings associated with this assumption are projected to be $12.5 million in FY 2003. While the County should strive to control all costs, including labor, we question the ability of the County to achieve such savings in light of the recently settled contract with the Corrections Officers.

VI. Other Items

FY 2002 – FY 2005 CASH FLOW PROJECTIONS

The NIFA statute requires the County to submit a four year Cash Flow Forecast together with the financial Plan. The cash flows NIFA received, while labeled "2002 – 2005 Cash Flow Forecasts," in fact contained cash flows for 2001-2004. In addition, the cash flows are dated July 30, 2001 and do not reflect the final 2002 Budget and Plan initiatives.

NIFA recognizes that substantial work has been performed to create a cash flow forecasting model for the County. However, the materials submitted on September 17th do not meet the requirements of the NIFA Act. NIFA has identified many areas of concern with the Budget and Plan, and the County needs to have a model ready to analyze impacts on cash flows as the Budget and Plan evolve so that cash flow borrowings can be properly estimated and other potential problems identified.

CERTIORARI

As required by the NIFA statute, the County has reported on its progress in streamlining the tax certiorari process and eliminating the backlog. NIFA agrees that the County has made progress in this area, but not nearly enough.

As of this date, the County is still unable to quantify the extent of the problem. It has not significantly upgraded its computer capability, co-located all certiorari departments in a central location, hired an administrative attorney to coordinate the certiorari process in the County Attorney's Office, filled vacancies on the Assessment Review Commission, or made progress in passing its legislative agenda in Albany. In NIFA's opinion the failure of the County to make sufficient progress in these areas results from the County's unwillingness to commit its own financial resources and make this problem the priority that it deserves.

In regard to the disposition of transitional State aid to the County, NIFA has repeatedly stated its position: NIFA is willing to pay for some start-up costs, but the preponderance of aid will be released based upon evidence that the backlog of certiorari claims has been reduced. The County has continued to incorrectly assume that the $5 million of transitional State aid provided by the State Legislature was meant to replace, rather than leverage and enhance County investments in personnel and infrastructure.

Since the creation of NIFA in June of 2000 and the availability of the $5,000,000 of transitional State aid, $103,242.01 of County expenses has been approved for payment. This disbursement was for overtime payments in the Treasurer's Office and was based upon concrete evidence of a decrease in the time required to pay pending certiorari claims. The only other request received to date is from the County Attorney's office, but the request was not supported by an adequate accounting and the necessary evidence of an improvement in the disposition of cases.

The County has planned for $776,000 for reimbursement of certiorari related expenses in 2001, $4,000,000 in 2002 and $224,000 in 2003. This scenario would require that in 2002 substantially all of backlog be addressed since the preponderance of aid will only be distributed based upon results. NIFA believes that these results, although they would be welcomed, are unlikely and have not been substantiated.

Notwithstanding the foregoing, NIFA is willing to assume that additional progress has been made and that in 2002 the County will give this problem the attention that it deserves. Consequently, NIFA will not put any of the monies that the County has requested at risk; however, it remains for the County to prove to NIFA's satisfaction that the County is committing its resources to solve this problem and that sufficient progress has been made to warrant the release of all remaining funds.

VII. Covered Organizations

NASSAU HEALTH CARE CORPORATION

Chapter 9 of the Laws of 1997 added Article 10-C to the Public Authorities Law creating a new public benefit corporation to be known as the Nassau Health Care Corporation (NHCC). On September 29, 1999 the acquisition “Agreement” between the NHCC and Nassau County was signed. In the Agreement the Nassau Health Care Corporation paid $82 million to the County. In exchange, the NHCC took over possession and operation of the County’s principle health care facilities. The main components transferred were the Nassau County Medical Center, the A. Holly Patterson Geriatric Center and the Community Health Centers.

The Agreement also provided that the County would supply various subsidies to NHCC. Among them were payments to subsidize the cost of uncompensated care and payments in consideration of NHCC providing certain contractual services (for some of which the County can receive State reimbursement). Services to be provided include tuberculosis clinical evaluation, family planning, and sexually transmitted disease testing and treatment.

To finance the acquisition and operation of the health care system NHCC issued 30-year revenue bonds in the amount of $259 million. These bonds were used to provide working capital, make payment to the County for the purchase of the health care assets, fund reserve accounts, and cover the costs of issuance. As part of the Agreement the County is also responsible for providing credit support for NHCC’s bonds in the following manner:

> The Corporation shall maintain an Operating Reserve Account containing an amount at least equal to 10% of the aggregate principal amount of all bonds and notes issued under the General Resolution (approximately $26 million). Included within this account is the Debt Service Reserve Account, which is required to contain an amount equal to the current year's principal and interest due on all bonds and notes outstanding under the General Resolution (averaging approximately $19.8 million). If by August 5th of each year the amount on deposit in the Debt Service Reserve Account is less than required, the Corporation shall issue a Notice of Deficiency to the County Executive, which shall set forth the amount necessary to make up the deficiency.
>
> Upon receipt of such notice, the County Executive shall include in the County budget for the next fiscal year an amount at least equal to the Deficiency Amount. Upon approval of the budget by the legislature, the County agrees to transfer to the Corporation, from the funds appropriated therefore, no later than January 15th of such fiscal year, monies equal to the Deficiency Amount. These funds shall be a general obligation of the

Corporation and shall be subject to repayment in accordance with one or more unsecured promissory note(s) bearing an interest rate of zero percent (0%), and be payable only after all Corporation bonds issued under the General Resolution have been fully paid or provided for.

In addition, the County guarantees the full and prompt payment of any principal or interest due on the Bonds of the Corporation when and to the extent monies on deposit in the Debt Service Reserve Account are insufficient, therefore, there has been a payment made by the Bond Insurer under the municipal bond insurance policy guaranteeing payment of principal and interest on the bonds. Provisions shall be made annually by appropriation by the County for the payment of its obligations under this Guaranty. If at any time the governing body of the County shall fail to make such appropriations, a sufficient sum shall be set apart from the first revenues thereafter received and shall be applied to such purpose.

Since no notice of deficiency has been filed with the County Executive, the County is not technically at risk for providing any credit support in FY 2002. However, financial operations at NHCC have worsened since the transfer. Headcount has increased by approximately 400 positions since the transfer and revenues have not kept pace with this increased expense. In FY 2000 NHCC had losses totaling $20 million and year-to-date actuals for FY 2001 are on pace to have losses of $40.4 million, which is $5.7 million worse than NHCC had budgeted.

NHCC has taken steps to attempt to stop this downward spiral. Primary among them has been the retention of Cap Gemini Ernst & Young, a leading consulting firm, to develop strategies to improve the operations. Forecasts from Cap Gemini indicated that without operational improvements NHCC would run out of funding in FY 2003.

To address this issue NHCC has undertaken several initiatives including the elimination of 24 physicians (projected to save $3.9 million annually), outsourcing laundry services (yielding annual savings of $1.5 million), and reductions in overtime (slated to save $6.9 million annually). NHCC is also seeking State assistance on several major issues such as capital reimbursement, bed decertification and a rebasing appeal. A sufficient amount of time has not passed to see a significant improvement in operations from these efforts and their success is uncertain.

Within the past month NHCC has raised with the County the potentially serious threat of mandatory Medicaid managed care. NHCC represents that a loss of $20 to $30 million could result from the lower payments received under a mandatory Medicaid managed care scenario and the potential loss of patients. The County has responded that mandatory Medicaid managed care has been scheduled to commence for several years and is mandated by the State. The County and NHCC will logically be on opposite sides of this planned implementation. For every dollar the County saves on it local share of Medicaid expenditures, NHCC will lose a multiple of these savings since service providers capture State and Federal matching revenue as well.

The County needs to evaluate its exposure to the potential need of providing credit support. The issuance of $259 million of revenue bonds at the inception of NHCC results in $568 million in total debt service payments through 2029, for which the County is ultimately responsible. The County does not generally believe it to be prudent to dedicate specific contingency reserves to specific risks when active efforts are underway to mitigate potential County obligations associated with such matters. Given this philosophy of not setting aside reserves, the County should, at minimum, provide a contingency plan describing what actions would be taken should the remedial actions not be successful.

NASSAU COMMUNITY COLLEGE

The FY 2002 budget for Nassau Community College ("the College") increased by 4.3% from the FY 2001 plan. Out-year increases are projected to grow at similar rates. Revenue for the College comes from three major sources: tuition, state aid, and funding from the County through property taxes. Property taxes in the out-years for the College, FY 2003 – FY 2005, are projected to grow by 5% annually, which mirrors the overall financial Plan. Tuition rates and State Aid are also projected to increase in the 4% to 5% range in the out-years.

In recent years the College has not experienced the same fiscal stress as the County. Tuition rates have remained among the lowest in the State for community colleges and the College has drawn significant enrollments from neighboring counties.

The recently adopted FY 2002 Budget for Nassau Community College contains some areas of concerns that could flow into the out-years of the financial Plan. The areas are state aid, the lack of a labor settlement with the adjunct faculty, and deferred maintenance of infrastructure.

The FY 2002 budget for the College anticipated an increase in State aid of $125 for each full-time equivalent (FTE) student. The recently passed budget kept State aid to community colleges at the same level as 2001 ($2,250 per FTE). While there is the possibility that the State will add funding during the year, there is no guarantee that the $125 increase will be implemented. This is particularly true in light of the events of September 11, 2001, which will negatively impact State revenues for FY 2002 and beyond. The exposure to the College on this item is $2 million.

The adjunct faculty at the College has been without a contract since 1995. This creates a potential liability depending upon the structure of the settlement. At the time of this writing it is NIFA's understanding that a settlement has been proposed but has not yet received legislative approval.

The infrastructure of the College, a majority of which is approaching 25 years of age, has suffered from a lack of operating budget funds and capital plans that have not materialized. Further deferral of this necessary maintenance could lead to operational difficulties and significantly higher out-year costs.