NIFA Nassau County Interim Finance Authority

October 8, 2003

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

Dear County Executive Suozzi:

Pursuant to the Nassau County Interim Finance Authority ("NIFA") Act, we have completed our review of the proposed Multi-Year Financial Plan For Fiscal Years 2004-2007 ("Plan"). Our review is transmitted to you in the attached report entitled, "Nassau County Interim Finance Authority Review of Proposed Financial Plan – Fiscal Years 2004-2007" ("Report").

The Report has been reviewed and adopted by the NIFA Directors. Since there has been confusion in the past, I want to emphasize that NIFA's acceptance of the proposed Plan does not mean that NIFA agrees with all of the numbers in the Plan or endorses all of the policy choices. Acceptance means that the proposed Plan is in substantial compliance with the requirements laid out in the NIFA Act.

It is now up to the County Legislators to review NIFA's Report and either adopt, reject, or modify the proposed Plan. After they take action, it should be returned to NIFA for final action.

Briefly summarized, the Report finds that:

FY 2003 – The County projects that it will end FY 2003 with an operating surplus of $1.5 million even after having funded approximately $100 million in expenditures that will positively impact the Out-Years. NIFA believes that the final number is higher.

FY 2004 – The Budget for FY 2004 appears to be balanced in accordance with the Act; however, this is the last year that the County will receive State aid and budget relief through restructuring. NIFA has identified a number of risks that the County must consider when adopting the FY 2004 Budget and the Proposed Financial Plan.

FY 2005 - FY 2007 – The County continues to have large Out-Year gaps, which remain largely unchanged despite substantial additional revenues and cost cutting measures the County has put in place. NIFA hoped these gaps would be smaller at this point. We recognize that Nassau County is not alone in confronting this situation, but that does not mitigate the problem or relieve the County of its obligations. The County should consider accelerating some initiatives as a way to reduce the Out-Year gaps.

Tom, the County has made important headway in reducing near-term gaps, but it still faces significant Out-Year deficits even after $85 million of state aid, $227 million of NIFA debt restructuring for budgetary relief, property tax increases and other gap-closing measures. To some extent, conditions outside the control of the County have contributed to the future risks.

However, new initiatives to redefine the architecture which governs how the County does its business are still required to manage the risks of the Out-Years. Working with the County, NIFA will continue to maintain a high level of oversight.

In the past two years, the County has submitted an update of the financial plan. NIFA believes that these updates have been useful for both NIFA and the County. Therefore, NIFA is again requesting that the County submit a financial plan update no later than June 1, 2004.

Please let me know if there is anything further we can do to be helpful.

Very truly yours,

Frank G. Zarb
Chairman

Attachment

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

Nassau County Interim Finance Authority

NIFA

REVIEW OF PROPOSED

MULTI-YEAR FINANCIAL PLAN FOR FISCAL YEARS 2004 – 2007

October 8, 2003

NASSAU COUNTY
INTERIM FINANCE AUTHORITY

DIRECTORS

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Corporate Secretary

Timothy P. Sullivan
Deputy Director

Jeremy A. Wise
General Counsel

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I. Executive Summary

In response to a deterioration in the financial condition of Nassau County, in June of 2000 Governor George Pataki and the New York State Legislature created the Nassau County Interim Finance Authority ("NIFA") or ("Authority").

A combination of significant County actions and substantial State assistance has led to a stronger current financial position and outlook for the County; however, much work remains to be done. NIFA staff has reviewed the County's Proposed FY 2004 Budget and Proposed FY 2004 – FY 2007 Financial Plan. We find that the Budget is reasonably balanced and that the Plan has a mix of strengths and weaknesses, but is acceptable under our statute. This Report will discuss all these items in depth.

NIFA'S MISSION

- Administering transitional State aid to the County. *By the end of calendar year 2003, this aid will have totaled in excess of $85 million and will total $105 million over five years;*

- Providing budgetary relief through the restructuring of County debt and, when requested, by issuing low cost debt on behalf of the County. *To date, NIFA has issued approximately $227 million in bonds to provide budgetary relief and $949 million for other County financing and refinancing needs, including payment of certiorari claims. NIFA borrowing is estimated to have saved the County in excess of $73.6 million in debt service expense over the life of NIFA's bonds;*

- Overseeing County finances through new financial reporting requirements, which included reviewing and commenting on the County's four-year financial plans. *To date, NIFA has commented on and approved the financial plans for FY 2001-FY 2004; FY 2002-FY 2005; and FY 2003-FY 2006. These reviews have brought about a better budget process with improved forecasts of revenues and expenditures, fewer "one-shots" and improved provision for contingencies.*

Without the $312 million of budget assistance and the fiscal discipline provided through NIFA, Nassau County would probably have fiscal problems similar to other troubled counties in New York State.

The County is being further aided by State legislation that has: (1) amended the NIFA Act to increase the amount of time available to bond certain activities of the County through NIFA; and (2) by lengthening NIFA's active oversight period. We see these changes as an indication of the State's commitment to Nassau County and recognition of NIFA's continuing value in bringing about the fiscal recovery of the County.

NIFA'S RESPONSIBILITY REGARDING THE FOUR YEAR PLAN

This report is written in fulfillment of the statutory requirement that the County present its four-year plan to the Authority for comment. It will review and comment upon the FY 2004-FY 2007 financial plan of the County Executive (the "Proposed Plan") that was submitted to NIFA on September 15, 2003. Last year, NIFA accepted the County's four-year plan on October 30 (the "Adopted Plan"), but because of a large number of uncertainties contained in the plan, requested an update of the Adopted Plan. The update was received by NIFA on May 1, 2003 (the "May Update") and was subsequently accepted by NIFA.

NIFA's statutory responsibility is to determine if the Proposed Plan is complete and complies with the requirements of the Nassau County Interim Finance Authority Act (the "Act"). Among other requirements, the Proposed Plan must:

- "contain projections of revenues and expenditures that are based on reasonable and appropriate assumptions and methods of estimation;" and
- "provide that operations of the county and covered organizations will be conducted within the cash resources available according to the authority's estimates."

As long as they are not inconsistent with the Act, policy decisions about the allocation of resources remain the responsibility and prerogative of those individuals elected by the voters of Nassau County.

DISCUSSION

In the midst of a sluggish economy, we recognize significant accomplishments over the past year including: reductions in workforce, although the Administration has retreated from its original goal; rating agency upgrades; resolution of certain union negotiations; diminished cash flow borrowing; the probable creation of a sewer and storm water financing authority ("SSWFA"); completion of a County-wide property reassessment; and limited certiorari settlement activity. Together with the 20% tax increase imposed in the prior year, these will aid in the recovery of the County.

The Proposed Plan continues to be presented in a professional, comprehensive and well thought out fashion. Overall, we agree with its upbeat assessment, acknowledgment of the need to increase revenues, and candid projection of a large structural gap as evidenced by continuing budget deficits in FYs 2005-2007 (the "Out-Years"). To manage the deficits, the Administration has proposed smart government initiatives, workforce reductions, labor concessions, and tax increases.

Much work remains to be done. The County recognizes that it has relied on State aid, restructuring of its debt and NIFA borrowings to balance its budget and fill its structural budget gap. However, FY 2004 is the last year for much of that assistance.

The major challenges to the Proposed Plan are:

- Closing the Out-Year gaps, which the County acknowledges are growing.
- Resolving the financial and health care issues arising from the financial stress at the Nassau Health Care Corporation ("NHCC").
- Meeting budget targets or filling shortfalls after negotiating away the right to lay off employees from the County's largest union.
- Managing properly to realize the savings that are projected from the Civil Service Employees Association ("CSEA") and Police Benevolent Association ("PBA") settlements; for example, the minimum manning changes in the PBA contract or the CSEA agreement to work an extra fifteen minutes per day.
- Meeting pension and salary increases that are higher than the rate of inflation while sales tax receipts and other areas of the economy remain weak.
- Downsizing while maintaining critical and/or revenue generating County services, without excessive overtime spending.
- Permanent elimination of the certiorari backlog and maintenance of up-to-date assessment roles.
- Replacement of aging infrastructure within a limited capital budget.
- Judicious use of accumulated fund balance.
- Improvement of information technology systems.

FINDINGS

NIFA is making the following general findings.

FY 2003 – The County projects that it will end FY 2003 with an operating surplus of $1.5 million even after having funded approximately $100 million in expenditures that will positively impact the Out-Years. NIFA believes that the final number will be higher.

FY 2004 – The Budget for FY 2004 appears to be balanced in accordance with the Act; however, this is the last year that the County will receive State aid and budget relief through restructuring**.** NIFA has identified a number of risks that the County must consider when adopting the FY 2004 Budget and the Proposed Financial Plan.

FY 2005 – **FY 2007** – The County continues to have large Out-Year gaps, which remain largely unchanged despite substantial additional revenues and cost cutting measures the County has put in place. NIFA hoped these gaps would be smaller at this point. We recognize that Nassau County is not alone in confronting this situation, but that does not mitigate the problem or relieve the County of its obligations. The County should consider accelerating some initiatives as a way to reduce the Out-Year gaps.

Acceptance of a plan by NIFA does not imply that NIFA agrees with all numbers in the plan, or endorses all the policy choices. Acceptance means that the plan in total is reasonably likely to lead to balanced operating results in the first year (the budget year) and adequately recognizes and addresses out-year revenues, expenses and gaps.

CONCLUSION

Nassau County has made headway in reducing near-term gaps. However, it still has a significant and largely unchanged structural deficit even after four years of State aid, NIFA assistance, substantial property tax increases and other major gap-closing measures. Had the County not received the State and NIFA aid, it would have been required to implement much more drastic budget measures and would likely still be lagging behind many other counties.

Although we credit the County with having implemented many effective strategies, such as workforce and debt reduction, other strategies remain in the nascent stages. These include elimination of the cert backlog, building consolidation, improved technology, and medical care for the indigent to name a few. In addition, we continue to believe that there are still special interest groups that have been spared and the savings contained in the recent labor agreements will only be achieved through continuing vigilance on the part of management.

Consequently, as a result of the foregoing concerns and the findings in the report that follows, NIFA will continue to maintain a high level of oversight and be ready to act when appropriate.

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The balance of this report provides background information and presents, in more detail, the findings of staff. The report is separated into the following major sections:

- FY 2003 recap.
- The proposed FY 2004 Budget.
- FYs 2005-2007 Financial Plan.
- Other items.
- Covered organizations.

The discussion that follows constitutes the NIFA staff's review and findings regarding the County Executive's proposed FY 2004 Budget and Plan. It is proposed that this document, together with the findings contained herein, be adopted by NIFA as the Report of the Authority 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. FY 2003 Recap

CURRENT STATUS

The Administration submitted a FY 2003 Budget that was reviewed by NIFA and thought to be reasonable and, if certain risks were resolved in the County's favor, expected to produce surpluses in 2003. The County was fortunate that several of the risks, and other events, turned in the County's favor. Favorable elements include conservative nature of the budget, the benefit yielded in the State's revised calculation of pension payments, workforce reductions, labor savings achieved from contract settlements, and lower debt costs. NIFA currently estimates that favorable events will lead to approximately $100 million of revenues in excess of expenses. This includes the impact of $15 million of State aid, $40 million of restructuring assistance, and $17 million of restructuring assistance that is still in question. The County plans to deploy most of these excess funds before the end of the year. Specifically, the Administration is planning to use these resources to:

- Defease the 1993 retirement debt service in 2004 – 2005 ($19.5 million);
- Pre-pay the County's 2002 early retirement incentive obligations ($23 million);
- Establish a reserve for greater-than-average sworn officer separations resulting from the recent PBA arbitration award ($18 million to $26 million);
- Eliminate the need for the County to draw down the previously budgeted tobacco securitization proceeds ($18 million);
- Provide additional funds for technology improvements ($12.2 million); and
- Purchase replacement police vehicles ($4.6 million).

The County is projecting only a modest year-end surplus of $1.5 million for FY 2003 after the effect of the items listed above. NIFA believes that the County is likely to end the year with a surplus in excess of $1.5 million because of positive variances that are not included in the County's projections. These include unneeded police termination costs and the savings from any reductions in headcount between the September 4, 2003 staffing levels and the end of the fiscal year.

CONCLUSION

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

- The County should end FY 2003 with a budget surplus since in virtually every case the County has adopted either an appropriately conservative or worst case scenario assumption.

- The County's current sales tax estimate of $878.2 million should be met, unless there is a significant negative variance to the October quarterly adjustment check.

- For the first time since the creation of NIFA, the County would have had an operating surplus without the NIFA and State aid assistance, if these one-time payments were not made.

III. Proposed FY 2004 Budget

This section presents NIFA's analysis and detailed conclusions regarding the proposed FY 2004 Budget and the major underlying initiatives designed to ensure year-end budgetary balance. The County's ability to achieve its fiscal objectives for FY 2004 is directly dependent on the actions that the County takes in the remainder of FY 2003 and its ability to fully implement FY 2004 gap-closing actions.

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

The County is facing a number of significant external risks. These risks include the effect of a sluggish economy, maintenance of essential services with a smaller workforce, increased contributions to certain mandated programs or negotiated benefits, NHCC, and progress toward solving the cert problem. Rigorous and timely monitoring can reduce the possibility that these and other enumerated risks break disproportionately against the County and require significant gap-closing actions near the end of FY 2004. Likewise, if these events produce positive budget variances, these variances should be used in a way that provides benefits in the Out-Years.

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 the quantifiable risks that affect the Proposed FY 2004 Budget and include items that may be:

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

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

FY 2004 Budget Risks

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

For example, if NIFA believes that a particular expense is incorrect, the amount of understatement will be identified. In those cases where NIFA believes that the full amount of a savings initiative will not be realized, NIFA will identify the amount that it believes will not be realized. In both cases, the County Legislature must weigh the risks and have substitute initiatives ready for enactment.

FY 2004 – FY 2007 Financial Plan Risks

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

(Table 1)
BUDGET RISKS AND OFFSETS

		Estimated Risk ($ in millions)	**Page**
FY 2004 Budget Risks	**Risks**		
	Overtime	8.0	14
	NIFA Restructuring	7.0	21
	Property Tax Adjustment	4.2	11
	Certiorari Reimbursement	3.6	52
	Eliminate Employee Transfer	3.0	24
	Technology Fund Transfer	1.8	26
	Subtotal	**27.6**	
	Offset of Attrition Savings	(Up to 10.2)	14
	Total	**$17.4**	
FY 2004 – FY 2007 Financial Plan Risks	Nassau Health Care Corporation – See discussion on page 55		
	Tax Certiorari – See discussion on page 49		
	Implementation of Police Management Initiatives for PBA Settlement – See discussion on page 30		
	Savings from CSEA Productivity Improvements – See discussion on page 32		
	Out-Year Labor Concessions – See discussion on page 40		
	Workforce Reduction Sustainability – See discussion on page 16		
	Unmet Infrastructure Needs – See discussion on page 21		
	Out-Year Pension Costs – See discussion on page 38		

While NIFA has identified these risks, we believe that they are manageable within the context of a budget that exceeds $2 billion. In order to minimize these risks, it is important that the County insure prompt implementation and monitoring of all proposed initiatives, particularly savings from recent labor settlements.

REVENUES

The Proposed Budget consists of four major revenue sources that total $2.3 billion. As shown in the chart to the right the two primary revenues are sales taxes and property taxes, comprising 72% of total revenues. The other major revenue sources include federal and state aid (14%), and other revenues (14%).

Composition of Revenues		
($ in millions)		
Sales taxes	$901.9	39%
Property taxes	$742.9	33%
Federal and State aid	$319.6	14%
Other revenues	$325.8	14%
Total	**$2,290.2**	**100%**

Sales Tax

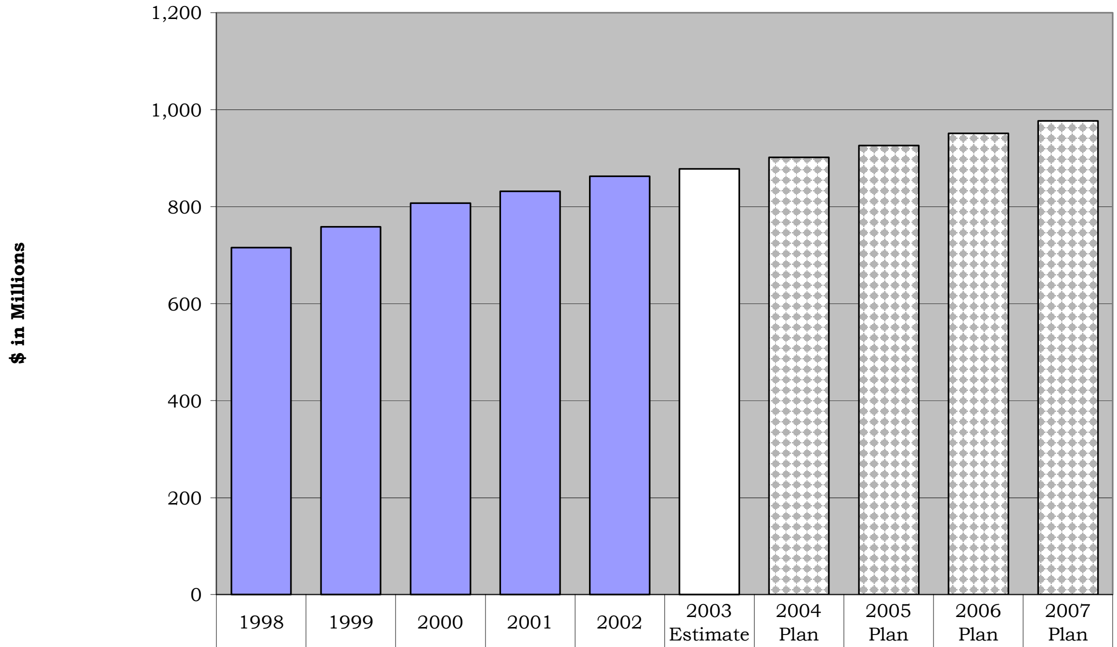
Sales tax is the largest revenue source for the County, comprising 39% of all revenues covered in this analysis, and is budgeted at $901.9 million for FY 2004. The current sales tax rate in Nassau County is 8.75%, of which 4.25% is the State's share, 4% is the County's share, 0.25% is allocated to the Metropolitan Transportation Authority, and the remaining 0.25% is distributed to the towns and cities in the County.

Sales tax receipts through October 3, 2003 total $582.8 million. This is $12.5 million, or 2.2%, ahead of last year's pace. The quarterly adjustment check to be received in mid-October will provide an important indication of year-end results.

From a projection of $878.2 million for the current fiscal year, the Proposed FY 2004 Budget projects a growth of 2.7%. Subsequent years in the Proposed Plan are also projected to grow by 2.7%.

Chart 1 illustrates historical sales tax growth for the County.

(Chart 1)
SALES TAX
FY 1998 – FY 2007



	1998	1999	2000	2001	2002	2003 Estimate	2004 Plan	2005 Plan	2006 Plan	2007 Plan
Sales Tax Revenue	715.5	758.2	807.0	831.7	862.6	878.2	901.9	926.2	951.2	976.9
Growth Rate	3.1%	6.0%	6.4%	3.1%	3.7%	1.8%	2.7%	2.7%	2.7%	2.7%

Years

Weakening from the strong growth rates experienced through most of the 1990's, sales tax revenues are recently growing at more modest levels. The current slow, but positive growth in Nassau's economy is a testament to its evolution from an economy dependent upon the defense industry to a more varied economic engine. Current conditions contrast greatly with the experience of a decade ago when Nassau was struggling to overcome a recession on the back of a drastic downsizing in the defense industry. 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 averaged 4.4% for the eight-year period 1995 through 2002. In projecting future sales tax growth the County assumes the continuation of a sluggish economy, with sales tax growth under performing historical averages.

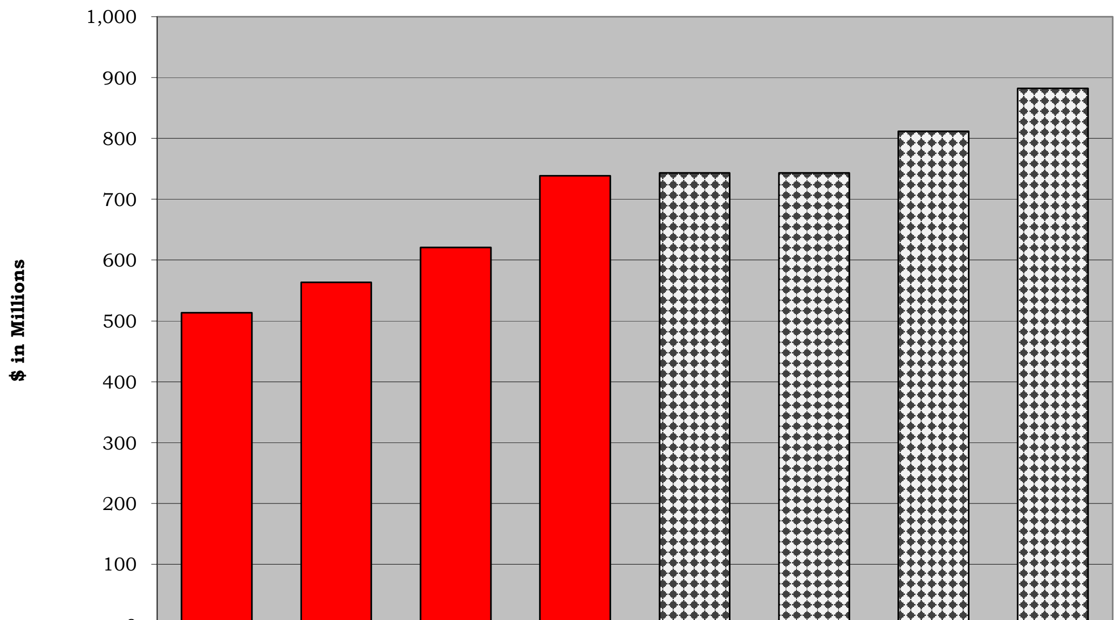
As one of its gap-closing measures the County proposes that sales tax growth may exceed their projections. While the County's projections are fairly conservative and may be surpassed, it is difficult to classify greater than anticipated growth as a gap-closing action. The County projects that growth closer to historical averages would yield an additional $6.6 million in FY 2004, $14.9 million in FY 2005, $23.7 million in FY 2006, and $33.1 million in FY 2007.

Property Taxes

Property taxes are the second largest revenue source for the County. They comprise nearly 33% of total revenues and are budgeted at $742.9 million in FY 2004. This represents an increase of 0.56% from a tax levy of $738.7 million in FY 2003.

The Administration has previously stated its intent to freeze property taxes in FY 2004. After consulting with officials within the Administration, they have indicated that this was a technical error. On September 29, 2003 the Administration submitted a tax levy ordinance to the County Legislature that kept property taxes frozen at the FY 2003 level of $738.7 million. This creates a gap of $4.2 million that must be closed during the budget adoption process.

(Chart 2)
PROPERTY TAXES
FY 2000 – FY 2007



	00 Actual	01 Actual	02 Actual	03 Budget	04 Plan	05 Plan	06 plan	07 plan
Annualized	513.3	563.6	620.7	738.7	742.9	742.9	811.7	882.5
Growth Rate	9.9%	9.8%	10.1%	19.0%	0.6%	0.0%	9.3%	8.7%

Years

As illustrated in the Chart 2 above, the Plan contemplates significant increases in property tax collections of $68.8 million in FY 2006, and $139.6 million in FY 2007. The County plans to realize increased property tax revenues through two mechanisms: an increase from the projected growth in property values, and increased property tax rates.

The Administration has funded a contract to annually update the newly revalued property tax roll. The County seeks to insure that increases in property values will be captured by concomitant increases in assessed valuation. Holding the tax rate constant, the County plans to increase property tax revenue by $32.9 million in FY 2006 and $58.5 million in FY 2007 due to the projected rise in assessed valuation.

The County also plans to increase the property tax rate in FY 2006 and FY 2007 if the State does not agree to cap Medicaid costs at the FY 2005 level. The County acknowledges in its report that there is a strong possibility that these costs will not be capped. To redress these increased costs the County is projecting property tax rate increases of $35.9 million in FY 2006, and $81.1 million in FY 2007.

State and Federal Aid

State and Federal aid is budgeted at $319.6 million in FY 2004. This is 14% of all revenues and represents an increase of 3.3% from the FY 2003 budget. A major reason for the increase is the County's plan to draw down $3.6 million of NIFA transitional aid that was made available in FY 2000 for tax certiorari reform.

The Proposed Plan for FY 2005 shows State and Federal aid declining by nearly 2%, due to the loss of NIFA assistance. FY 2004 is the final year of NIFA assistance, and is budgeted at $18.6 million ($15 million for transitional aid and $3.6 million for tax certiorari reform). The Plan contains annual increases of 4.1% to State and Federal aid for FY 2006 and FY 2007.

State and Federal aid projections are developed on a program basis in conjunction with the County's operating departments and generally parallel anticipated reimbursable expenditures. The 4.1% growth rates in State and Federal aid are attributable to the County's baseline assumption of salary increases at current staffing levels. State and Federal aid will be reduced to the extent that the County realizes any savings from workforce reductions in reimbursable programs. This potential loss of revenue will be more than offset by expense reductions in salaries as the workforce declines, yielding net savings to the County.

Other Revenue

The remaining revenues make up approximately 14% of the Proposed Plan. A major component is departmental revenue, which is budgeted at $133.1 million in FY 2004. This represents a decline of $18.5 million from anticipated departmental revenues in FY 2003. The decline stems from a phasing out of the Intergovernmental Transfer Program, to be completed by FY 2007, which was the funding method utilized to provide enhanced Federal aid for public hospitals and nursing facilities. This will not directly impact the finances of the County as the County transferred these Medicaid reimbursements to the State.

The County is projecting to realize an additional $4.2 million of departmental revenue through increased ambulance billings. The County has done well in this area, as they expect to surpass FY 2003 budget targets by over $3 million. Since the County is currently exceeding industry standards on collection rates, it is questionable as to whether they can continue to achieve the planned growth in this area.

Recent State legislation has given authorization to Nassau County to increase motor vehicle registration fees. The surcharge will increase the registration fee for passenger cars from between five to ten dollars, depending upon weight of the vehicle. The fee for commercial vehicles will be raised to $30. The County is projecting that this will generate an additional $9.9 in additional revenue.

EXPENDITURES

The Proposed Budget consists of $2.3 billion of expenditures.[1] As shown in the chart to the right, personal services ("PS") expenditures comprise 46% of the Proposed Budget and include the cost of salaries and wages as well as fringe benefits for employees and retirees. Other-than-Personal-Services ("OTPS") expenditures account for 20% of the Proposed Budget and include charges for contractual services, pre-school special education, early intervention, utility costs, local government assistance, mass transportation, and payments to the Nassau Health Care Corporation. Direct Assistance comprises 20% of the Proposed Budget and includes payments for public assistance, Medicaid, day care programs, and institutional expenses. Debt Service, which represents 14% of the Proposed Budget, refers to both principal and interest costs for County and NIFA issued debt, including 10.3 million that will be reimbursed by the Sewer Fund, but net of $15.5 million in relief provided by NIFA restructuring assistance.

Composition of Expenditures ($ in millions)		
PS	$1,043.7	46%
OTPS	$470.6	20%
Direct Assistance	$459.1	20%
Debt Service	$316.8	14%
Total	**$2,290.2**	**100%**

Personal Services

Personal services expenditures, which the County projects will exceed $1 billion, are driven by changes in the size of the workforce, changes in contractual salaries and benefits levels, and changes in the underlying cost of providing employee benefits. As shown in the chart to the right, projected expenditures for fringe benefits comprise 32% of the County's proposed PS budget, a ratio which has been growing as fringe benefits command a growing share of the cost of employing County workers due to the rapidly rising costs of pension and health insurance benefits.

Elements of PS Spending ($ in millions)	
Salaries and Wages	$711.3
Fringe Benefits:	
Health Insurance	$156.2
Pension Contributions	$87.8
Social Security	$49.8
Workers' Compensation	$11.0
All Other	$27.6
Subtotal Fringe Benefits	$332.4
Total	**$1,043.7**

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

Salaries and Wages

Salaries and wages, the largest component of PS expenditures, are projected to total $711.3 million in FY 2004. The County's estimate reflects the additional costs resulting from a new collective bargaining agreement and arbitration settlement with the CSEA and PBA, respectively, which have been mitigated by recurring salary savings resulting from the County's FY 2003 workforce reduction program, a projection of significantly reduced terminal leave costs, and anticipated control of overtime expenditures.

While the administration's public commitment to reducing further the size of the County's workforce remains unchanged, the Proposed Budget provides sufficient resources to fund headcount at current levels. These contradictory policies result in an inherent surplus, which the County can use to offset unexpected negative variances that may develop during the fiscal year. The County estimates that natural attrition, combined with limited replacement hiring, could yield unbudgeted savings of $10.2 million in FY 2004, and has chosen to reflect these potential gap-closing resources "below the line" in the Proposed Plan.

NIFA's analysis indicates that these unbudgeted savings may already be needed to fund overtime costs that are likely to exceed the County's assumptions by up to $8 million in FY 2004. The County has made some aggressive assumptions regarding its ability to constrain overtime spending in FY 2004. While the County has budgeted $48.2 million for overtime needs in FY 2004, an increase of $2.1 million above the County's FY 2003 Budget, NIFA projects that overtime expenditures will significantly exceed budgeted levels in the current fiscal year, particularly in the Correctional Center and the Police Department. Therefore, continued attrition in these traditionally overtime-intensive operations in FY 2004, combined with collectively bargained increases, will put upward pressure on this spending category. While the PBA arbitration settlement provides the County with increased staffing flexibility designed to mitigate the need for overtime usage in the Police Department, the full complement of savings can be realized only if the County mandates that police supervisors strictly enforce the settlement's terms, a task that NIFA believes may prove to be too difficult in practice. This is discussed further in "Labor Settlements" beginning on page 30.

In addition, since the Proposed Budget funds police termination expenses at a level lower than the County has expended annually in recent years, NIFA is concerned that these costs may exceed budgeted assumptions. In fact, the County acknowledges that it may experience a surge in police retirements in FY 2004 due to a contractual provision that becomes effective in FY 2005.[2] However, rather than funding this anticipated need in the Proposed Budget, the County proposes to utilize resources drawn from a new "off-budget" police termination pay reserve that it plans to create with at least $18 million in unused FY 2003 resources. NIFA notes that the creation and use of this reserve, while legally permissible under general municipal law, effectively converts what

[2] The PBA arbitration award revises downward by 6.5 percent the formula for calculating the value of termination payments effective January 1, 2005.

would otherwise have become undesignated fund balance into an FY 2004 operating revenue to cover FY 2004 operating costs. This is a dangerous practice that, if repeated, could seriously undermine the County's ability to attain long-term structural balance. NIFA expects the County to return all unexpended resources placed in the termination pay reserve to undesignated fund balance during the close of FY 2004. The County should not attempt to roll these resources into future years.

Fringe Benefits

Fringe benefits costs, which are projected to reach $332.4 million, continue to exert upward pressure on the Proposed Budget and Proposed Plan. Specifically, escalating expenditures for health insurance benefits combined with rapidly growing pension contribution requirements, resulted in approximately $39 million in new needs being funded in FY 2004 compared with the FY 2003 Budget. The County emphasizes that these costs are projected to grow by almost $78 million when compared to the County's current estimates for these costs in FY 2003. While employee pension benefits are not subject to collective bargaining, health insurance benefits can be modified during labor negotiations. Although the County had indicated that it would seek changes in this costly area, it negotiated new contracts with ShOA, CSEA, and the PBA without realizing any concrete financial relief.

Health Insurance

The County assumes that health insurance costs will grow by 15% annually for active employees and by 18% for retirees in FY 2004 followed by 15% annual increases thereafter. The Proposed Budget contains $156.2 million in FY 2004 for these expenditures, including $80.8 million for current employees and $75.4 million for retirees. Based on discussions with the New York State Department of Civil Service, it is clear that the County's assumptions are based on the optimistic end of a range of Civil Service expectations. However, since Civil Service "advance" guidance has traditionally proven to be more conservative than final rate increases have been, NIFA believes that these funding levels and assumptions are not unreasonable. The County must be prepared to deal with the consequences of higher-than-assumed rate increases since the Proposed Budget and Proposed Plan will be adversely affected by concomitantly higher costs. Conversely, the County may realize savings to the extent that premiums do not rise as rapidly as assumed, replacement hiring is delayed, and/or greater attrition occurs for non-retirement reasons. Savings accrue under this last scenario since there are no ongoing County obligations for health insurance coverage for former employees who have not retired from County service.

Pension Contributions

The County's contribution rates to both the Employees' Retirement System ("ERS") and the Police and Fire Retirement System ("PFRS") have risen dramatically over the last few years as the impact of weak investment performance caused by declines in the stock market impacted upon State actuarial calculations.[3] NIFA's analysis indicates that the County has appropriately budgeted these expenditures, which have grown by $26.4 million compared to the FY 2003 Budget and $55.5 million compared to FY 2003 estimates. Additionally, it appears that the County's projection of FY 2005 pension costs is reasonably estimated based on final rates recently provided to the County by the State Comptroller's office.

The State Legislature adopted a number of pension reforms this year that will make budgeting for these costs much more predictable than it has been in recent years. These reforms include the imposition of a minimum contribution requirement that will provide additional resources to the Common Retirement Fund in years following better-than-assumed investment returns to help mitigate the contribution rate volatility otherwise experienced by participating employers in years following worse-than-assumed investment returns. More importantly, the retirement systems' billing cycle was changed to base the required pension contributions on the retirement systems' prior-year investment experience, which allows more accurate budgeting.

Despite these favorable retirement system enhancements, the eventual direction and magnitude of changes in the County's required contribution rates will be influenced by the investment performance of assets held in the Common Retirement Fund, a situation that rests entirely beyond the County's control. The County's Out-Year projections in FY 2006 and FY 2007 will almost certainly change as future investment results are measured. While there is no near-term threat to budgetary balance, the County must continue to be mindful of this significant expenditure that could potentially undermine the County's efforts to attain long-term structural balance.

Workforce Reduction

The County's ability to attain long-term structural balance depends on its capacity for bringing its recurring expenditures in line with its recurring revenues. Since 46% of the County's projected expenditures are for personal services, headcount reduction remains a critical tool within the County's control through which expenditure cuts can be made. However, while the County has made swift workforce reduction a major cornerstone of previous gap-closing programs (headcount is down by approximately 1,100 positions from January 2002), the Proposed Plan delays the elimination of the remaining 300 positions originally scheduled for completion by September 2003 until FY 2007. The County plans to reduce its full-time headcount to 8,042 positions through attrition over the next four years, after negotiating away its right to lay off employees from the County's largest union.[4] The County estimates these phased reductions could

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[3] 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.

[4] The County's workforce reduction targets are based on headcount changes relative to its January 1, 2002, staffing level baseline of 9,442 full-time positions. This total includes 283 employees associated with the Federation Employment and Guidance Services (FEGS), Family Children's Association (FCA), and Mental Health Association (MHA).

yield savings of $10.2 million in FY 2004, $15.1 million in FY 2005, $21.2 million in FY 2006, and $28.1 million in FY 2007.

Despite the slower pace of future reductions, NIFA remains cautious in our assessment of the County's ability to maintain its headcount reduction objectives and its capacity to realize its modest additional out-year savings targets without impacting services in undesired ways and/or incurring significant unbudgeted overtime expenditures to sustain the delivery of desired services. For example, the Department of Social Services recently formulated a remedial plan to address a growing and costly backlog of pending Medicaid applications caused, in large part, by the loss of key personnel through attrition during FY 2002. The remedial plan includes the hiring back of a number of full-time and part-time employees as well as the use of employees on overtime to work down the backlog expeditiously. This is costly for a number of reasons beyond the obvious unplanned headcount related expenses. First, service providers, including the County's own fiscally distressed NHCC, must absorb the unreimbursed service delivery costs while awaiting extraordinary delays in receiving Medicaid payments. This additional burden is one reason why the NHCC began to deplete its working capital faster than anticipated, a worrisome trend recently flagged in reports issued by the State Comptroller and County Comptroller. Secondly, the County risks missing a temporary window of opportunity that ends in June 2004, which currently entitles the County to a higher Federal reimbursement rate for processed Medicaid claims. It is imperative to process these applications in a timely manner to avoid losing precious Federal assistance since the County's Medicaid obligation begins with the date of application, but the Federal reimbursement rate is based on the date a claim is processed.

NIFA encourages the County to develop department-level four-year headcount plans that reflect explicitly the County Executive's decisions concerning which services he wants continued, scaled back, and/or eliminated immediately and in the future rather than leaving the outcome of workforce reductions subject to the randomness of a broad County-wide attrition program The plans should ensure that revenue generating and State and Federal aid maximizing functions are protected. The level of authorized staffing and resources provided in each year of the Plan should then be made consistent with these decisions.

Other Than Personal Services

The County projects that it will spend $470.6 million on OTPS costs in FY 2004. 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, early intervention services, payments to the Nassau Health Care Corporation, mass transportation, and utility costs. The County stated that a freeze on non-essential and non-emergency purchases it imposed this fiscal year will be continued into

Elements of OTPS ($ in millions)	
Pre-School Special Education	$79.3
Local Government Assistance	$53.6
Early Intervention Services	$45.9
Payments to NHCC	$40.3
Mass Transportation	$37.5
Utility Costs	$26.4
All Other	$187.6
Total	**$470.6**

FY 2004. In general, the County has reasonably estimated these costs, although even in a low inflationary environment, limited nominal growth translates into real cuts. The County should closely monitor spending during FY 2004 to ensure that resources are not being depleted more rapidly than assumed and/or that operations are not being impaired by a failure to procure necessary goods and services.

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 Proposed Budget includes an additional $5.5 million for Pre-School Special Education and $2.1 million for Early Intervention Services compared with FY 2003. The County indicated these additional program costs are driven by caseload and rate increases.

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 $53.6 million in FY 2004, are an expenditure offset to the sales tax revenue collected by the County from its aggregate 8.75% sales tax rate.

The County estimates that its FY 2004 payments to the NHCC will be $40.3 million, approximately equal to the amount included in the FY 2003 Budget. These expenditures include $13 million in historic mission payments as well as the cost of retiree health insurance, longevity payments, and termination pay for certain employees of the NHCC.

The County projects that it will spend $37.5 million on mass transportation in FY 2004, or $3.9 million lower than included in the FY 2003 Budget. These expenditures are composed of $3.6 million in subsidies to the MTA Long Island Bus, which reflects a $4.8 million reduction from FY 2003, including a $3.9 million reduction for Able Ride, its handicap transportation service. In addition, the County is providing $22.3 million in payments for Long Island Railroad station maintenance, which includes a $0.9 million increase, and $11.6 million for MTA operating assistance, which remains unchanged. While Long Island Bus absorbed previous subsidy reductions, in part, by finding alternative funding sources, it is unclear if it can mitigate this round of cuts in a similar fashion. Some members of the County Legislature have expressed concern with this initiative and the impact it would have on residents that rely on fixed bus routes and paratransit services for transportation. Since commenting on policy choices like this one are not within NIFA's purview, the County Legislature must choose to either implement this initiative or substitute an alternative one with equivalent savings.

The County has budgeted $26.4 million for utility costs in FY 2004, or approximately the same level included in the FY 2003 Budget. NIFA believes these costs are reasonably projected although portions of the County's utility costs are subject to volatility of world energy prices. These costs must be monitored closely.

The County projects that all other OTPS expenditures will reach $187.6 million, including expenditures for contractual services in areas such as legal, medical and psychiatric services in the Correctional Center, the Assessment Review Commission, and program agencies such as Senior Citizens Affairs and the Youth Board.

Direct Assistance

Elements of Direct Assistance	
($ in millions)	
Medicaid	$318.3
Title XX	$44.4
TANF	$28.3
Safety Net Assistance	$15.5
All Other	$52.7
Total	**$459.2**

The County projects that it will spend $459.2 million on direct assistance in FY 2004, or one out of every five dollars appropriated in the Proposed Budget. These costs cover social service entitlement benefits for clients enrolled in a variety of support programs within the County. As shown in the chart to the right, these expenditures are made within four major categories: Medicaid, Title XX, Temporary Assistance to Needy Families ("TANF"), and Safety Net Assistance ("SNA"). The remaining expenditures, grouped in All Other, consist of spending on the County's other major social service program areas, including foster care, children in institutions, education for handicapped children, and juvenile delinquents. NIFA's analysis indicates that the County has conservatively estimated these costs, but that each program should be monitored closely should the impact of the weakened local economy result in a greater than assumed demand for social service programs and direct assistance spending.

Medical Assistance

Medical Assistance ("MA") expenditures, which account for 70% of direct assistance spending, cover a wide range of services, including payments for nursing homes, hospitals, home health care, and pharmaceuticals. The County assumes that these costs will grow by 13.5 percent annually, before the application of mitigating savings that are presented separately in the gap-closing program. While NIFA believes that the underlying growth rate is conservative, NIFA remains cautious in its assessment of the County's Medicaid utilization initiative, which is anticipated to generate $5 million in savings in FY 2004 and $10 million in annual savings beginning in FY 2005.

The County must monitor these costs closely in the Out-Years to determine if the twin dynamics of economy-driven caseload growth and eligibility-driven program expansion are likely to create budgetary variances. It is unclear if the County has provided sufficient funding in the Out-Years to cover these twin dynamics, as discussed in "Other Than Personal Services Costs" on page 39.

The Proposed Plan also includes an ambitious County proposal that calls for a State cap on Medicaid expenditures in FY 2006, which limits spending to FY 2005 levels, potentially saving the County $35.9 million in FY 2006 and $81.1 million in FY 2007. NIFA has previously noted that this initiative is highly speculative, however, in the Proposed Plan, the County Executive now states that he is prepared to impose a new, dedicated property tax to raise an equivalent amount of revenue beginning in FY 2006 to ensure financial plan savings are achieved should this initiative fail, as discussed in "Property Taxes" beginning on page 11.

Debt of the County and NIFA

This section of the Report discusses debt service costs contained in the Proposed Budget and recent events regarding the Sewer and Storm Water Finance Authority.

Debt Service

In the debt area, the Proposed Plan is essentially a continuation of the program initially laid out in the County's April 1, 2002 Plan, with subsequent modifications from later County Plans. There are no new gap-closing initiatives in the Proposed Plan but projected debt service is within the parameters previously established by the County. Debt service in 2004 is reduced somewhat from last year's projection due to lower NIFA issuance in 2003 (largely attributable to slower spending on capital and tax cert backlog payments). However, total debt issuance over the FY 2003 – FY 2007 period is consistent with levels in the Adopted Plan.

Projected Total NIFA and County Debt Service ($ millions)

FY 2004	FY 2005	FY 2006	FY 2007
$322 before any NIFA restructuring $306.5 after requested $15.5M NIFA restructuring*	$316.4	$309.2	$308.4

* Debt service fund Budget shows an expense of $316.8 million, but there is $10.3 million of revenue for debt service provided by the sewer fund, for a net cost of $306.5 million.

The County and NIFA are well positioned for continued debt issuance. The County benefited from positive market conditions in 2003, which enabled NIFA to refund $240 million of high coupon County debt for present value savings of $13.1 million. NIFA's notes and variable rate bonds have also carried exceptionally low interest rates in the past year, and because of conservative budgeting required by NIFA, the County should save about $4.5 million in FY 2003. This positive rate environment is generally forecast to continue in 2004 and the County has used reasonable assumptions in projecting interest expense.

In addition, 2003 brought ratings upgrades to both NIFA and the County, further reducing the cost of NIFA issuance and positioning the County for a return to the capital markets under its own credit – one of NIFA's principal goals. The County plans to issue its annual Tax Anticipation Notes (TANs) directly to the public markets in December 2003, for the first time since 1999 (NIFA financed this borrowing in 2000-2002). NIFA believes that with the proper structural security features, the County should be able to secure TAN ratings in the MIG1/SP-1/F-1 range and achieve a reasonable cost of funds.

Several aspects of the County's Proposed Plan do raise issues:

Additional NIFA Restructuring Assistance in 2003. NIFA debt restructuring provides one-time budgetary relief but increased expense for the subsequent 20 years, as the debt incurred is paid off. For this reason, NIFA's legislative mandate and policy is to minimize the use of restructuring. As part of our May 2003 bond issue, NIFA provided $40 million of such short term budgetary relief for FY 2003. As detailed on page 5 of this report, NIFA expects the County to have a gross positive budget variance in 2003 of $100 million and a net positive variance, after funding the cost of several prior early retirement programs, a reserve for police termination, and other one-time expenses, of $1.5 million, exclusive of additional NIFA restructuring. This net positive variance will flow to the County's fund balance.

The County has requested NIFA to provide an additional $17 million of restructuring in 2003. Given the County's financial performance in 2003 and our concern about taking actions that burden the Out Years, NIFA continues to evaluate the need for the additional $17 million of FY 2003 restructuring.

NIFA Restructuring in 2004. The County proposes $15.5 million of NIFA restructuring for budgetary relief in FY 2004. Together with State Transitional Assistance of $15 million, this $30.5 million of NIFA Assistance (as defined in the NIFA statute) must be matched with at least $122 million of recurring County gap closing measures under the 80/20 split set forth in the statute. Information provided by the County to date does not evidence this level of gap-closing measures. At most, giving credit where information is still incomplete, the maximum amount of County recurring gap closing measures is $93.8 million. This permits total NIFA assistance of $23.44 million, of which $15 million is State aid. Therefore approximately $7 million of FY 2004 restructuring must be considered "at risk."

Capital Needs. The County divides its capital program into two parts: County Building Consolidation (discussed below), and all other capital needs. It continues to reduce its projected capital borrowing outside of the building consolidation program, even as the adopted County Capital Plan calls for higher levels of funding. In addition, the County has continued to be unable to spend even the available capital funds on a timely basis. Recent steps to address this problem have not yet borne fruit.

Capital Borrowing and Spending ($ millions)

	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
2003-6 Adopted Financial Plan	94.72	70.36	70	70	100
2004-7 Proposed Financial Plan	60.9	74.4	68.6	61	61
County Capital Plan, 2004-2007:					
-- Authorization Amount	na	70.8	87.3	77.4	83.7
-- Draw Schedule (debt)	49.1	70.8	87.3	77.4	83.7
2003 Estimated Spending*	41.3				

*NIFA estimate based on draw down of NIFA bond proceeds January through September 2003. An internal County report shows a higher spending target but lower actual expenditure during this period.

The County Charter, as revised by voter referendum in 2001, requires the County to prepare a four year capital plan, of which the first year is the capital budget. The

County is using this process to identify and prioritize projects for funding within spending caps it has set based on debt burden targets. NIFA remains concerned that however good the capital planning process, if sufficient funds are not made available for County infrastructure needs, a backlog of deferred infrastructure projects poses a long term financial risk.

County Forecasting of Debt Needs. NIFA and the County have previously recognized that the County's ability to track bond proceeds expenditures and forecast debt issuance needs is an area needing County attention. In the past year, the County and its legal and finance advisors have taken major steps to improve record keeping and ensure compliance with Federal tax law. However, NIFA is concerned that the County is still unable to accurately estimate its spending needs in the critical areas of tax certs and capital needs. The Proposed Plan calls for NIFA borrowing in November 2003 of $13.5 million for tax certs and $17 million for capital. However, as of this date, NIFA has bond proceeds on hand from the May 2003 debt issue of $105.4 million for certs and $31 million for capital. At the average monthly rate these categories of funds have been drawn down in 2003, this is enough funding for 12.6 months of tax certs and 9 months of capital. We have asked the County to substantiate its stated new money needs but information received to date has not been complete or compelling. Under Federal tax law, NIFA cannot issue debt unless it has a reasonable expectation that the funds will be spent in an appropriate time period. In addition, the County must submit to NIFA a Declaration of Need, approved by the County legislature, at least 60 days before a NIFA financing is sought. No such Declaration has been received by NIFA or, to our knowledge, submitted to the County legislature. A decision on the timing and amount of the next NIFA borrowing will be made when further and better County information is available to NIFA.

County Building Consolidation Program. The Proposed Plan provides skeletal information on the County's ambitious program to reconfigure and upgrade County offices and court facilities. NIFA is requested to fund the gross cost of the program through bond anticipation notes (BANs), with the final cost, net of property sales proceeds and any other applicable funds, being financed through long-term NIFA debt in 2006. The first note sale is requested for November 2003, but despite numerous requests the Authority has not received sufficient information to evaluate the consolidation program plan of finance. We have most recently been advised that the plan will not be available until the end of the year.

In addition, NIFA's ability to issue debt expires at the end of 2005 (other than limited amounts of NIFA tax cert debt in 2006-2007 that would be authorized in the pending SSWFA legislation). The Authority cannot issue BANs unless it has the ability to issue bonds to retire the BANs, so the proposed BAN maturing in 2006 will not be feasible unless NIFA's statute is amended. In conversations subsequent to submitting the Proposed Plan, County staff has stated that the change in NIFA legislation will be sought in January 2004, so that no building consolidation notes will be requested in 2003. NIFA will have to consider the effect on its own credit ratings of an extension of substantial debt issuance into 2006.

Continued Borrowing for Settlements and Judgments. The County continues to borrow heavily to pay for the costs of routine legal settlements and judgments. To date, NIFA has provided over $127 million for this purpose, and the Proposed Plan calls for an additional $17.5 million in 2003 and $35 million/year of borrowing from 2004-2006, with $5 million/year reduction each year after. The County has started funding the smallest claims from the annual operating budget. In 2001, it paid settlements under $5,000 out of operating funds; in 2002, under $10,000; and in 2003, under $20,000. The FY 2004 Budget proposes an increase in such funding from $1.66 million in FY 2003 to $2.5 million in FY 2004. The County should move more quickly to fund more of this routine, predictable expense in the operating budget. NIFA may scrutinize this category of borrowing more closely in future debt issuances.

Sewer and Storm Water Finance Authority (SSWFA)

The Proposed Plan accurately describes the pending bipartisan SSWFA legislative package that resulted from lengthy negotiations with state and local elected officials. However, the County has substantially revised its SSWFA plan of finance since the legislative compromise was reached, dropping the "acquisition financing" plan to refund all outstanding County sewer debt through the State Environmental Facilities Corporation (EFC), significantly reducing savings to the ratepayers. The Proposed Plan does not explain why the County has abandoned the EFC debt refinancing it pursued with such tenacity over the past year, and appears willing to forego the EFC interest rate subsidy.

Planned restructuring debt issuance has dropped by almost 60%, from about $277 million to $115 million, and is now slated for issue by the new SSWFA, not the EFC. In addition, the County now asks NIFA to refund about $55 million of County sewer debt in 2003, strictly for present value savings. NIFA would urge the County to continue pursue EFC financing for any restructuring or refunding in addition to new money needs, with unsubsidized issuance channels, such as NIFA or the SSWFA, used only as a back-up if EFC cannot fund the issue in a reasonable time frame.

The Proposed Plan did not include a detailed SSWFA plan of finance that would enable NIFA to fully evaluate this new structure. Pending further information, we find:

- The new SSWFA plan of finance is a complete change of course from the plan the County previously advanced and greatly reduces the upfront cash flow benefit to the sewer funds that was expected from the larger EFC refunding. The actual impact of this change on the sewer fund is small, because in the County's initial, unsuccessful, SSWFA plan, the bulk of the upfront cash flow savings were to have transferred to the General Fund. However, the smaller plan still creates budget savings in the sewer fund to provide the agreed-upon rate stabilization program and to absorb the cost of water-related County General Obligation Bond debt service. The Proposed Plan covers only the initial rate period through 2007, but the County has separately affirmed that it can fulfill the entire 2004-2013 rate stabilization commitment.

- The County's SSWFA debt issuance plan calls for a series of small SSWFA note and bond issues each year, 2004 through 2008, sized to provide just enough sewer fund budget relief each year to fund the rate stabilization program. The issues would be similar to the NIFA restructuring of County debt in providing current year budget relief but stretching the cost out over 20 years. Without EFC's interest subsidy, these restructurings will have a negative present value. In addition, the plan to have at least 3 small issues a year (two probably less than $10 million and a third in the $19-25 million range) seems inefficient. Finally, with the SSWFA appearing to be further reduced in scope and importance, it may be harder to achieve the "A" ratings level the County seeks. Once NIFA is provided with the County's full plan of finance, we would like to work with the County to see if there is a better way to achieve its goals.

- By asking NIFA rather than the EFC to refund high coupon County sewer debt, the County avoids using more of the limited $350 million SSWFA debt issuance capacity negotiated in the legislation, and can plan the debt issue with greater certainty. However, it forgoes the 33% or 50% interest subsidy EFC debt provides – and the associated savings to the ratepayers – and the extended debt maturity schedule EFC provides. The proposed NIFA refunding also places extra NIFA debt service in the 2007-2010 period when NIFA's debt service coverage is already lowered due to the large refunding of County debt that took place earlier in 2003. NIFA will review this refunding proposal in detail, including a comparison of the relative merits of a NIFA or EFC refinancing, the likelihood of EFC funding, and the potential impact on NIFA's credit as part of our review of the full SSWFA financing plan.

- The 2004 – 2007 financial pro forma on page 146 of the Proposed Plan differs significantly from the similar schedules provided by the County as the SSWFA was being negotiated. Some changes are obviously the result of changes in the SSWFA plan, such as the removal of water employee costs, but the basis for other changes is not yet clear. Also, the pro forma needs restatement to correct a $1 million understatement of projected refunding debt service and to remove the approximate $3 million expense of transferring the salaries of 49 County public works employees to the sewer fund, a County plan that was withdrawn subsequent to submission of the Proposed Plan.

The SSWFA legislative package, which has not yet been passed by the State Assembly, includes revenues and other benefits to the County's general fund of $15 million, in addition to $3 million revenue anticipated from a County OTB teletheatre authorized by State legislation earlier this year. NIFA's statute is also amended to allow a small amount of NIFA bonding for tax certiorari refunds in 2006 and 2007. If the package does not pass, the County's budget during the Plan Period will be negatively impacted by $15 million in 2004, $15 million in 2005, $30 million in 2006 (including the loss of cert borrowing) and $25 million in 2007 (including certs).

INITIATIVES

The FY 2004 Proposed Budget contains "Smart Government Initiatives" totaling $34.8 million. Of these initiatives, NIFA believes that several are at risk. We are providing detailed explanations of only those FY 2004 initiatives that will impact the 2004 Budget by $500,000 or more. The Smart Government initiatives are as follows:

Medicaid Utilization HSSS01

The County is in the process of developing access to the state warehouse of Medicaid records, hiring a consultant, and purchasing computers and software. All of these tools will allow the County to determine if third party liability exists for the Medicaid costs that can be recovered. In addition other areas to be closely analyzed and evaluated are: fraud/abuse identification, investigation, and recovery; disproportionate share Medicaid optimization; indigent care medical cost conversions; provider billing; Medicare Part A and B maximization; 3rd party billing and recovery; Title XVI (SSI) eligibility; and payment computation and accuracy. This system will allow the County to look back two years and perform matching going forward. The third party liability contractor will be contracted on a contingency basis and will receive 12% of recoveries. The County schedule for implementation of the third party contracts and purchase of computer hardware is aggressive for FY 2004. The achievement of targeted savings of $5 million in FY 2004 may be questionable.

Audit Recoveries SSAC01

The FY 2004 objective of this initiative is primarily attributable to a $3 million refund from Verizon. Clearly, this initiative does not provide recurring revenue. Through the establishment of a Department of Investigations and coordination with the Comptroller's office, the County anticipates taking advantage of the provision requiring a 5% retainage, pending completion of an audit within six months after completion of service delivery from vendors. The recovery efforts projected for FY 2004 is $3.2 million. The Authority finds this amount to be reasonable.

Parks Revenue Enhancement Plan GSPK01

The FY 2004 objectives of this initiative encompass increased program income from the Aquatics Center, golf scheduling system revisions to require reservations for a tee time, the sale of excess museum collections at auction and increased rent revenue from Landmark Preservation units. For the out years the County has evaluated the park system and identified 12 facilities where utilization can be improved through marketing to a wider audience, or establishing partnerships with civic groups, municipalities and corporations. The County has issued Requests for Expressions of Interest some of which will be converted to Requests for Proposals (RFPs). Based on the milestones currently established, the RFP proposals are to be awarded in December 2003. The County has been enthusiastic and creative in the development of this initiative. The Authority believes the projected FY 2004 savings of $1.4 million may be overstated.

Night Simulcasting of Racing BFRV01

This initiative will generate increased revenues from Off-Track Betting ("OTB") parlors that have received Legislative approval in May 2003 to simulcast thoroughbred racing in the evening. The County receives 10% of the total handle and a surcharge of 1.9% of exotic bets placed. The legislation also imposes a State regulatory fee of 0.39% of the handle.

This initiative was implemented in FY 2003 and should be incorporated in baseline calculations of increased revenue to the County from OTB operations for the out years of the plan. The revenue projection of $1.5 million for FY 2004 is achievable.

Utilization Part-time Security Guards PSCC01

This initiative proposes the use of retired police officers in a part-time capacity at the Correctional Center. They will be assigned to less sensitive areas that do not need full-time correction officers. The County estimates that the presence of this part-time staff will reduce overtime paid to correction officers by $1.2 million. The review of qualified candidates is underway. This initiative has been scaled down from the alternative-staffing proposal in the May Update in the number of positions from 20 to 14 and the proposed savings has doubled. Savings may be achievable with an initiative of this type, however the projections of saving $1 million in FY 2004 from this initiative is questionable. NIFA is concerned that Correctional Center overtime may exceed budgeted assumptions, as discussed on page 14.

Increase Federal Reimbursement PSCC02

The Correctional Center houses an average of 200 Federal government inmates. The Correctional Center asked the Federal government for an increase in the rate paid for housing federal inmates. The current rate is $142.32 per day, and the request was for an increase to $165 per inmate per day. The County's request was approved in September 2003. There is a question of whether the County will receive the increase from the time of approval or from the date of signature. This initiative has been completed in FY 2003 and should be included in the baseline calculations.

Technology Fund/Capital Fund Charge Back SSIT02

This initiative proposes that $2 million, or approximately 20%, of departmental salaries and fringe costs for technical staff could be charged to the Technology and Capital Funds. This is composed of $1.8 million to the Technology Fund and $0.2 million to the Capital Fund. NIFA believes that the salary and fringe expenses associated with the development of technology in the County are an operating expense and therefore inconsistent with the purpose of the Technology Fund. As a result we consider $1.8 million for the transfer to the Technology Fund to be at risk.

College Reimbursement BFBU01

This initiative proposes that the County allocate to the town of residence the cost of tuition paid for Nassau residents who attend out-of-county community colleges. It had been the County's policy to absorb this expense in prior years. This initiative was developed in the May Update. County research indicates that the NYS Education Law permits the counties to charge back these costs to the town or city of the student's residence. This action represents a shifting of the $2 million in costs between levels of government, a task NIFA believes may be difficult to achieve.

OTPS Freeze BFBU03

The Administration instituted an OTPS freeze during the second half of FY 2003. This freeze was approved by the Legislature in July. The Office of Management and Budget ("OMB") then transferred 50 percent of all unencumbered funds out of most County departments into the Miscellaneous Budget. It is the Administration's plan to restrict OTPS spending in FY 2004 and save $4.4 million while holding growth to 1.25% annually. The Proposed Budget does not appear to reflect the decrease in spending contemplated in this initiative.

Collection of Unpaid Tax Liens BFTR02

In this initiative the County tax liens are being collected by two contractors Xspand and JER Receiver Services, whose fees are based on a percentage of collected liens. Legislative approval was received in October 2002 and the collections process began in December of the same year. The savings in this initiative represents the interest that accumulated on the tax liens and which has not been recorded by the County as income. In FY 2003 the companies have collected in excess of $1.2 million. This initiative appears to be underway and the FY 2004 savings of $1.9 million should be included in the baseline calculations.

Reduce MTA LI Bus Subsidy EDPL02

This initiative proposes to reduce the County's subsidy for LI Bus by $4.7 million in order to bring it down to its minimum level required by Section 18-b of the New York State transportation law and existing language in the Operating Agreement. The initiative is part of the County Executive's proposal to restructure the relationship between the County and MTA. The Administration has been carving away at the subsidy for LI Bus since FY 2002, saving the County $4 million. While implementation of this initiative is within the control of the County Executive and the Legislature, it has been a politically sensitive issue and it is unclear if these savings will be included in the adopted budget.

Improved Ticket Collection PSTV02

This initiative provides additional resources to the Traffic Parking Violations Agency ("TPVA") that are necessary to collect outstanding traffic ticket revenues. The projected income from yet unprocessed tickets is estimated at $0.9 million for FY 2004.

The Administration has authorized additional resources for computers, information technology, and additional staff at an estimated cost of $0.24 million. The unprocessed tickets have an estimated value of $75 million and the department is taking aggressive steps toward processing the backlog. NIFA believes the projected income is achievable.

Courts Initiative HSDR01

This initiative is projected to produce savings by expanding the use of specialized courts where first time, non-violent offenders are offered treatment in lieu of incarceration. The County has indicated that studies have shown that these courts produce nearly $5 in medical, criminal and social service savings for every dollar spent. While the actual savings resulting from this type of program are not immediate, the County has included this initiative in the May Update. Although the County has revised the projected savings downward in the Proposed Plan, NIFA remains concerned about the remaining target since the County seems to be stuck at the same implementation milestone as they were a year ago. The County's projected savings for FY 2004 of $0.85 million would appear to be in jeopardy.

Capital Project Charge backs GSPW02

The Department of Public Works manages the capital planning and project implementation process involving County-owned roads, buildings, etc. Most capital projects create an asset value with a useful life beyond one year. As such, departmental costs related to this process are re-allocated and charged back to the various funding sources in order to match the useful lives of the assets with cost (debt) on an ongoing, long-term basis. The department, in the past, incurred between $4 million and $5 million for this purpose on an annual basis. This initiative anticipates enhancing tracking of department costs and services. While the County was on course to meet the initiative from an implementation standpoint in FY 2002, there has been no visible progress in FY 2003. We put this initiative at risk for the FY 2004 revenue of $0.5 million.

Risk Mitigation SSAT02

This initiative involves the implementation of a comprehensive proactive system for risk management that will include policies and procedures, controls, reports, rapid response, education, training, compliance and third party oversight. The major tool for the implementation of this program is a case management system in the County Attorney's office. The County is still in the process of procuring that system for this and other purposes. The Administration has authorized a Risk Management Committee to develop a written plan. Their report is expected in January 2004. This initiative has been reduced from the Adopted Plan projections of $1.5 million to savings of $0.75 million for FY 2004. The County may be taking a more realistic look at the progress they expect to make in 2004.

Affirmative Litigation SSAT04

The County plans to initiate recoveries from litigation brought by the County for fees and legal services. The County Attorney has identified affirmative litigation such as collecting unpaid rent, collecting unpaid contract fees, and collecting unpaid franchise taxes. In addition, it is expected that the County will be receiving damage recoveries from vendors, employees and others who have damaged or stolen county property or taken advantage of commercial and social service contracts. This initiative requires the hiring of three attorneys and two support staff personnel. This initiative is essentially unchanged from the submission in the Adopted Plan, except the magnitude of revenues has been scaled back. Since the hiring has not yet occurred it is unlikely that the $0.75 million in recoveries for FY 2004 will occur.

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 Proposed 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 now understands that it cannot borrow every time it has to address shortfalls caused by unforeseen events, but must create reasonable reserves and contingency plans.

Good public policy demands reasonable reserves. We were disappointed last year in this area, but the County is beginning to understand its responsibility.

Through good fortune and conservative budgeting, the County currently expects approximately $100 million in excess resources that will be used for various non-recurring expenditures and pre-payments. Coincidentally, this is approximately the same amount as unrestricted aid provided to the County by New York State.

The County began the year with an accumulated fund balance of $75 million. Additional surpluses will increase this amount.

Unfortunately, as previously noted there remain significant risks, especially in the Out-Years when baseline revenues are growing more slowly than expenses and NIFA aid has been completed. Some of the risks are severe, but common to all counties. These include increases in pensions, Medicaid and health insurance. Other risks, such as NHCC and certs, are anomalous to the County.

NHCC - The County has identified a number of risks associated with NHCC, however, no funds have been provided in the Out-Years of the Proposed Plan. The County has commissioned a study to evaluate its options if the financial condition of NHCC does not improve. The study is a good idea and although we can't predict all of its conclusions, we do know that part of the solution will most likely require additional resources from the County. While the specific amounts to address these risks may not be known, the County should begin to allocate resources to meet the needs of the indigent in Nassau County.

CERTS – In the section entitled, "Tax Certiorari and Assessment Review," we express concern that the County is continuing to retreat from its productivity schedules and we are skeptical of many assumptions. Frankly, we understand that reducing this problem cannot be calculated with mathematical accuracy and that there is pressure to show progress. Without retreating from their goals, we urge the County to keep assuming the worst, but hoping for the best. Under this scenario, we suggest that the baseline assumptions be more conservative so that when the County doesn't have the ability to bond for certs, it will be able to absorb the potential liability.

In the end, the Proposed Plan recognizes that it may be necessary to raise taxes. Although this is not a popular position, we respect the County for recognizing that there are limits to its ability to "reduce the size of the workforce, re-engineer government, extract labor concessions, and curtail debt issuance."

LABOR SETTLEMENTS

This section of the report discusses the County's recent labor agreements negotiated with the PBA and CSEA.

PBA

Just prior to the release of the County's Plan, the panel for the PBA interest arbitration issued their award. NIFA estimates that scheduled wage increases and other contract provisions total 23.5% over the life of the agreement. The agreement also provides for certain changes in the deployment of personnel, which, if realized, would reduce the cost to the County. The award itself centers around only economic terms. Non-economic items will be the subject of an additional award that the County anticipates will be released by the end of FY 2003.

The new contract between the County and the Police Benevolent Association has a term of six years, beginning retroactively from January 1, 2001, and expiring on December 31, 2006. The scheduled wage increases for the agreement are listed below:

Base Wages	
1/1/02	3.9%
1/1/03	3.9%
1/1/04	3.9%
7/1/05	3.9%
7/1/06	3.9%
	19.5% *(Compounded equals 21.1%)*

The County's baseline contained annual increases of 4.1%, compounding to a planned increase in excess of 27% over the life of the contract. By securing a retroactive wage freeze for FY 2001, a six-month wage freeze in FY 2005, and increases slightly less than anticipated for the other fiscal years, the County estimates cumulative base wage savings exceeding $15 million over the life of the agreement.

Other key savings initiatives include:

- Altering the schedule for shift differential saving over 11%
- The elimination of Flag Day as a paid holiday
- The reduction of the hourly rate of pay used to calculate holiday pay, overtime, shift differential and termination pay by 6.5%
- New hires start at $23,000 (increases by nearly 50% to $34,000 at the expiration of this agreement)
- The elimination of travel time

Certain provisions contained in the contract will add costs. Primary among them are:

- A change in the longevity schedule that increases the average officer's base pay by over $900
- The institution of an education stipend that immediately increases an officer's pay by $600 (escalating to $650 in FY 2005, and $695 in FY 2006)

Another component of the new agreement relates to the addition of 48 hours of work per year for each member of the PBA. These additional hours will result in each officer doing an additional twelve hour tour per quarter. The extra hours will be paid at straight time in addition to current base salaries. This will increase an officer's annual salary by an additional 2.5%, for an estimated annual cost of $5 million.

The County estimates that it will achieve overtime savings of over $5 million by the scheduling of these additional hours. However, there are certain restrictions on the scheduling of these additional tours that may reduce the potential savings. The requirement of scheduling one tour per quarter prevents the County from a full utilization of the 48 hours during the peak summer season, when overtime is at its highest levels. An officer must also receive at least 14 days notice before assignment of the additional tour, thereby mitigating the benefit for covering a post when an officer is sick. The success of management in effectively scheduling the additional 48 hours of duty will ultimately determine its success. As a result of the restrictions placed on the scheduling of the additional tours, NIFA questions whether the County will achieve its projected level of savings.

Taking all of the components of the agreement previously discussed into account, NIFA's analysis of the new contract shows that, including the additional 48 hours of duty, a police officer's compensation will increase on average 3.6% annually. The total compounded increase over the six year life of the agreement totals 23.5%. These numbers could be lower if savings from civilianization, minimum manning, and the additional tours to be worked are realized.

The agreement gives the County the right to civilianize 50 police officer positions in FY 2004 and an additional 50 positions in FY 2005. In its analysis of the contract, the County anticipates generating savings of $5.4 million by FY 2006 through civilianization. The process of civilianization entails moving police officers from desk jobs onto patrol and replacing them with lower cost civilians. The County has not had much success in past attempts to civilianize as implementation was slow, often occurring as a result of attrition rather than through redeployment. The previous Memorandum of Agreement (MOA) identified specific areas for civilianization and prevented officers from being transferred from these duties without consent. While civilianization under the previous MOA was restricted, the new contract also indicates that both parties shall meet and confer as to which posts are to be civilianized. Should they be unable to do so, the arbitrators retain jurisdiction. The effectiveness of this process remains to be seen.

It also should be noted that over two years ago the County, in its labor agreement with the Sheriff Officers Association (ShOA), gained the right to civilianize 55 correction officers. To date this initiative has had virtually no success.

The County is also hoping to achieve personnel and overtime savings through a reduction in minimum manning. The agreement provides for the reduction of 417 tours per precinct and the County has indicated that this would save $3.2 million by FY 2006. A reduction of 417 tours per precinct would result in the reduction of over 3,000 tours that would generate savings as the Department would no longer need to fill those tours with overtime when vacant.

Conclusion

The County has estimated that the PBA arbitration award will yield $35 million in savings to the County baseline. While NIFA generally concurs with most of the hard savings factored into the Plan (e.g., changing the hours for shift differential, and the elimination of Flag Day as a paid holiday, etc.) other savings initiatives are less certain. An example of this is extending the work year by an additional 48 hours. The County is indicating that the $5 million in additional salary costs will be offset by savings in overtime. Similarly the County is projecting savings of $8.6 million from civilianization and changes to minimum manning requirements. Together these items total over $13 million of the projected $35 million (nearly 40%) in savings. Representing such a large percentage of the projected total savings, the County must develop the proper systems to closely monitor these initiatives. NIFA requests that the County report on the status of their implementation and success.

CSEA

In August 2003 the County approved a Memorandum of Agreement with the Civil Service Employees Association (CSEA), extending the expired 1998-2002 Collective Bargaining Agreement for 5 years through December 31, 2007. Salary increases are 2.5%, effective July 1, 2003, with subsequent increases on January 1st of each year, 2004 through 2007. The increases for the period 2004 through 2007 are pegged to the New York Metropolitan Area All Urban Consumer Price Index as of the preceding June for each year. Recent CPI data indicates that the increase for FY 2004 will be 2.8%. Increases for the 2005 through 2007 period will have a minimum rate of 2.5% and a maximum increase of 3.5%. In addition, CSEA employees will also receive Step increases each year, estimated at 1.5% by OMB, bringing the total salary increases for each year to a range of 4% to 5%.

The County projects savings of $23.5 million from this agreement. NIFA believes that this level of savings is overstated and agrees with the Office of Legislative Budget Review that the savings will range between $9 million to $18 million depending on CPI results. NIFA is also concerned that the agreement contains a no layoff provision. Such a provision could hamper the County's ability to achieve its targeted workforce reduction of 1,400 employees, or to take other personnel related actions that may be necessary to maintain budgetary balance throughout the period of the financial plan.

The CSEA agreement also extends the workweek from 33.75 to 35 hours. The County believes that this additional 15 minutes per day will yield productivity benefits of $7.3 million. Since the agreement also stipulates that the start and end of the work day not be altered, NIFA assumes that this will require adjustment of the lunch time or elimination of a break. This is an unclear and questionable assumption. While NIFA believes that the additional hours will yield some level of productivity, true savings can be realized only if additional staff reductions are made above the 1,400 positions, or if the amount of paid overtime is reduced.

Other Unions

The County is currently in binding interest arbitration with its two other police unions, the Detectives Association and the Superior Officers Association. The contract with its correction officers union, the Sheriff Officers Association, expires on December 31, 2004. The County states in the Plan that it is seeking savings proportionate to the PBA agreement that would total $34.5 million. NIFA views these increased saving levels as unsupported and overly optimistic.

First, when the County released its FY 2003 – 2006 Plan it indicated that the savings from these unions would total $15 million (ShOA $6.5 million, SOA $6 million, and DAI $2.5 million) by FY 2006. With the addition of another year, FY 2007, the County has more than doubled the projected savings without offering any rationale. Second, a significant portion of the projected PBA savings comes from provisions which are unique to that union, such as minimum manning and civilianization.

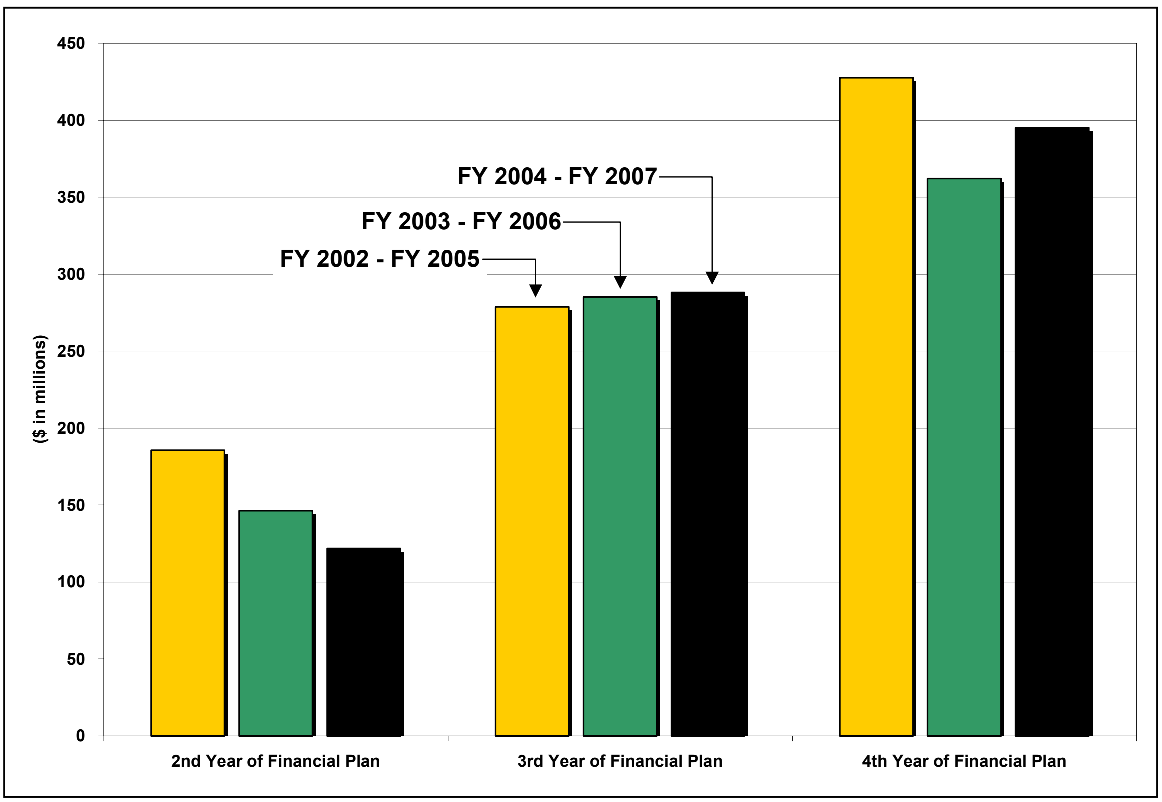
IV. Plan to Close the Out Year Gaps: FY 2005 – FY 2007

This section discusses the growth rates that were used by the County for revenues and expenditures in the Proposed Plan as well as the Out-Year gap-closing actions proposed by the County.

We credit the County with acknowledging that "the County's out-year structural budget gaps continue to grow over time." The County has identified Out-Year gaps of $121.8 million in FY 2005, $288.2 million in FY 2006, and $395.1 million in FY 2007. These projections are reasonable, but their size is troubling.

The County attributes the gaps to a sluggish economy, increases in pension costs, health insurance premiums, and mandated human service costs. To this list we add salary increases beyond the rate of inflation. There are also other risk factors, such as NHCC, that may significantly widen the gaps.

(Chart 3)
OUT-YEAR STRUCTURAL DEFICITS REMAIN LARGELY UNCHANGED



After examining the County's most recent baseline projections included in the Proposed Plan and comparing them side by side with previous plan submissions, NIFA concludes that the County has made little progress toward achieving long-term structural balance. As illustrated in Chart 3, since the time of the Administration's first financial plan submission in April 2002 (FY 2002 – FY 2005), the projected size of the County's out-year gaps have not materially changed. The projected structural deficit in the second year of each successive multi-year plan shows measurable progress, improving from \$185.5 million in April 2002 to \$121.8 million in the Proposed Plan (FY 2004 – FY 2007). However, in the third year of each financial plan submission, the County's projected deficits have actually grown from \$278.9 million to \$288.2 million. Finally, the Proposed Plan indicates that after revising downward the County's projected fourth year gap from \$427.6 million to \$362.1 million last year (FY 2003 – FY 2006), the Administration currently estimates that the structural deficit has increased to \$395.1 million, or only \$32.5 million smaller than when it took control of the County's finances in 2002.

The County's task of eliminating its baseline structural deficit has been made more difficult by several outside forces and has been exacerbated by a national recession. Clearly, projected sales tax growth is being limited by the lasting effects of a protracted slowdown in the local economy, which has also led to an associated increase in medical assistance and public assistance caseloads. The County is also confronted by rapidly rising pension costs, which are directly linked to the State retirement systems' under-performing investments, which have been dragged down by the falling stock market in recent years. The rapidly rising cost of providing health insurance coverage to County employees and retirees, of which the County has limited control, represents another drain on County finances. While the nature of the structural gap may have evolved over the years, it remains the County's responsibility to develop and implement the permanent, structural changes that are required to eliminate this persistent deficit.

In defense of the current Administration, many of these same factors are confronting other municipalities as they also grapple with growing deficits. The County acknowledges that it must still address many serious challenges, but points to their track record of developing and implementing workable solutions to ensure annual budgetary balance. NIFA commends the County's short-term budget balancing accomplishments, but must point out that long-term expenditure growth, and its resultant impact on out-year baseline deficits, is being driven by some of the unique choices the County has made regarding the size of its municipal workforce and the terms and conditions of recently negotiated collective bargaining agreements, which have provided wage increases above the rate of inflation. The County must work harder to align its recurring baseline expenditures and revenues in a way that matches their growth rates over the entire financial plan period if it truly seeks to achieve structural balance.

OUT-YEAR REVENUE GROWTH

For purposes of projecting baseline revenues in the Out-Years of the Plan (FY 2005 – FY 2007), the County used the following growth rates:

- Property taxes are projected to remain flat throughout the period of the plan.

- Sales taxes are projected to grow 2.7% in FY 2005, FY 2006 and FY 2007.

- State Aid and Federal Aid are projected to grow each year by 2.45% from FY 2004 levels, with some variance by entitlement program.

- All other revenues are projected to remain flat from FY 2004 levels.

OUT-YEAR EXPENDITURE GROWTH

The following is a discussion of the growth rates used in the Out-Years of the Plan for the more significant expenditure categories.

Personal Services Costs

Personal Services ("PS") expenditures comprise 46% of the budget and include the cost of salaries and wages as well as fringe benefits for employees and retirees.

Salaries and Wages

Salaries and wages represent the single largest expenditure category, representing approximately 30% of spending in the Plan. The baseline assumes that full-time headcount is maintained in the Out-Years at the same level the County had on September 4, 2003. The County projects that baseline salaries and wages will grow consistent with existing labor agreements, and reflect the savings from several provisions contained in the PBA settlement. The plan contemplates reducing this rate of growth through a number of major gap-closing actions, including workforce reductions obtained through attrition, labor concessions from currently expired contracts with the DAI, and SOA, and other contractual reductions, as discussed elsewhere in this report.

Fringe Benefits

The County projects that baseline fringe benefit costs will grow by an average of 11.7% annually during the Plan, slowing from 15.3% growth in FY 2005 to 9.8% growth in FY 2006 before slightly increasing to 10.0% growth in FY 2007. These projections translate into $130.4 million in additional fringe benefit expenditures that are included in the Plan by FY 2007, as shown in Table 2.

(Table 2)
GROWTH IN FRINGE BENEFITS
FY 2004- FY 2007

($ in millions)	FY 2004	FY 2007	Change
Health Insurance	$156.2	$237.5	$81.3
Pension Contributions	87.8	121.9	34.1
Social Security	48.8	55.9	7.1
Workers' Compensation	11.4	13.9	2.5
Other Fringe Benefits	28.1	33.5	5.4
Total Fringe Benefits	**$332.3**	**$462.7**	**$130.4**

Health Insurance

The largest element of fringe benefits is spending on health insurance. The County projects that health insurance costs will grow by 15% annually, on average, for employees and retirees, adding $81.3 million in new fringe benefit costs by FY 2007. As discussed earlier in "Health Insurance" on page 15, we find these assumptions to be reasonable based on discussions with the State Department of Civil Service. The County may realize financial plan relief to the extent that premiums do not rise as rapidly as assumed, replacement hiring is delayed, and/or greater attrition occurs for non-retirement reasons. Savings accrue to the County under this last scenario since there are no ongoing health insurance costs for former employees who have not retired from County service. In addition, the County has stated that it will seek to reduce its exposure to this rapidly rising expense as part of its labor concession gap-closing initiative, as discussed in "Labor Concessions" on page 40.

Pensions

The County assumes in the Plan that, after FY 2004, its required pension contributions to the retirement systems (New York State Employees' Retirement System and New York State and Local Police and Fire Retirement System) will begin to stabilize. In fact, the Plan provides only $11 million more for these expenditures in FY 2007 than the County currently projects it will spend in FY 2005. This moderate growth is driven solely by the projected increases in employee salaries and wages consistent with the negotiated terms specified in the County's collective bargaining agreements. This contrasts sharply with the County's recent experience of having to fund rapidly rising costs caused by escalating contribution rates, which were driven by the investment losses sustained by the Common Retirement Fund in recent years. NIFA remains concerned that, despite the County's recognition of these growing costs, the County has no control on how high and how fast these contribution rates can move in the Out-Years. Despite the exponential growth in these contribution rates, they still remain below historical highs. The County must monitor these costs carefully and make appropriate adjustments to the Plan as its pension projections change.

Social Security

The County assumes that growth in Social Security costs will closely track growth in employee wages. The County has no control over the level or growth in these expenditures outside of its ability to limit collective bargaining increases and manage workforce levels, as discussed in "Workforce Reduction" on page 40 and "Labor Concessions" on page 40.

Workers' Compensation

Workers' Compensation is projected to grow by 6.8% annually over the term of the financial plan. The County believes that it can reduce these costs by implementing a series of reforms in its Workers' Compensation program, as discussed on page 46.

Other Than Personal Services Costs

The County projects that baseline other-than-personal services (OTPS) expenditures, including spending on direct assistance, but excluding debt service, will grow by an average of 6.1% annually during the Plan, as shown in Table 3. These costs are driven by spending on Medicaid, which is projected to grow by 13.5% each year, resulting in $120.2 million of the additional $179.7 million in OTPS expenditures projected in FY 2007. As discussed in "Medical Assistance," beginning on page 19, NIFA considers the County's baseline assumptions to be conservative, since it exceeds the County's recent experience. However, the County based its out-year projections on FY 2004, a year that "benefits" from certain non-recurring adjustments, such as prior-year accruals and FMAP enhancements that expire in FY 2004. Therefore, should the County's assumed growth rates materialize, these costs will exceed Proposed Plan levels. NIFA is continuing to discuss these projections with the County.

(Table 3)
GROWTH IN OTPS
FY 2004- FY 2007

($ in millions)	FY 2004	FY 2007	Change
Medicaid (local share)	$260.1	$380.3	$120.2
All Other	669.6	729.1	59.5
Total OTPS	**$929.7**	**$1,109.4**	**$179.7**

Since the County lacks the authority to unilaterally limit Medicaid coverage provisions and associated costs, it must continue to aggressively pursue all measures designed to increase efficiencies and curb growth in these expenditures. The County proposed in its gap-closing program, an initiative designed to reduce Medicaid utilization and associated costs by $5 million in FY 2004 and $10 million annually thereafter, beginning in FY 2005. In addition, the Plan includes an ambitious County proposal that calls for a State cap on Medicaid expenditures in FY 2006, which limits spending to FY 2005 levels, potentially saving the County $35.9 million in FY 2006 and $81.1 million in

FY 2007. While we find this initiative to be highly speculative, the County has stated that it is prepared to raise property taxes by an equivalent amount, in the form of a dedicated Medicaid-based property tax levy, to ensure budgetary balance in the Out-Years.

The Other OTPS costs are projected to grow by 2.9% annually, or approximately equal to inflation. These expenditures are driven, in part, by expected spending growth in the County's public assistance programs, including TANF and Safety Net Assistance.

OUT-YEAR GAP CLOSING ACTIONS

Based upon the growth rates we discussed above, the County has identified Out-Year gaps of $121.8 million in FY 2005, $288.2 million in FY 2006 and $395.1 million in FY 2007 before implementation of County actions to close these gaps. The County has identified the following categories of gap-closing measures.

- Workforce reductions;
- Continued labor concessions;
- Reduction in cert liability;
- Growth in the property tax base;
- Other tax increases; and
- Smart government initiatives.

Workforce Reduction

The Proposed Plan calls for continued workforce reductions during the Out-Years. The Administration remains committed to reducing the size of its headcount by 300 full-time positions over the next four years in order to bring its cumulative workforce reduction program to 1,400 positions, as discussed on page 16. The County estimates that its attrition-based program will generate savings of $10.2 million in FY 2004, $15.1 million in FY 2005, $21.2 million in FY 2006, and $28.1 million in FY 2007 as its full-time headcount declines from it current level of 8,338 to 8,042 in FY 2007. NIFA remains cautious in its assessment of the County's ability to maintain its headcount reduction objectives and its capacity to realize its modest additional out-year savings targets without impacting services in undesired ways and/or incurring significant unbudgeted overtime expenditures to sustain the delivery of desired services.

Labor Concessions

The County states in the Plan that it is seeking savings proportionate to the PBA agreement, for its remaining unions (DAI, SOA and ShOA) that would total $22.5 million in FY 2006, and $34.5 million by FY 2007. When the County released its FY 2003 – 2006 Plan in September 2003, it indicated that the savings from these unions would total $15 million (ShOA $6.5 million, SOA $6 million, and DAI $2.5 million) by FY 2006. With the addition of another year, FY 2007, the County has more than doubled the projected savings without offering any rationale. Second, a significant portion of the projected PBA savings comes from provisions which are unique to that union, such as minimum manning and civilianization. NIFA views these increased saving levels as unsupported and overly optimistic.

Reduction in Cert Liability

The County estimates that ARC liability will be reduced by $18.4 million in FY 2006 and $28.6 million in FY 2007 from an estimated liability of $57 million in FY 2006 and FY 2007.

For the reasons outlined in section five of this report entitled, "Tax Certiorari and Assessment Review," we believe that this estimate of savings may be possible, but that the original estimate of remaining liability may be too low.

Property Taxes

The County plans to realize increased property tax revenues through two mechanisms: an increase from the projected growth in property values, and increased property tax rates. The Administration has funded a contract to annually update the newly revalued property tax roll. The County seeks to insure that increases in property values will be captured by concomitant increases in assessed valuation. Holding the tax rate constant, the County plans to increase property tax revenue by $32.9 million in FY 2006 and $58.5 million in FY 2007 due to the projected rise in assessed valuation.

The County also plans to increase the property tax rate in FY 2006 and FY 2007 if the State does not agree to cap Medicaid costs at the FY 2005 level. The County acknowledges in its report that there is a strong possibility that these costs will not be capped. To redress these increased costs, the County is projecting property tax rate increases of $35.9 million in FY 2006, and $81.1 million in FY 2007.

Other Taxes

In FY 2005 the Plan calls for the imposition of a 3.5% tax on residential energy costs. Items impacted by this sales tax would include fuel, oil, coal, wood (used for the purpose of heating), propane, natural gas, electricity, steam and gas used for residential purposes. Since New York State Tax law allows local governments to impose this tax, the only approval necessary is that of the County legislature. The County estimates that this would generate $47.6 million in FY 2005, $49.0 million in FY 2006, and $50.5 million in FY 2007.

As an alternative funding source to the residential energy tax, the County proposes a ¼% increase in the County's sales tax rate. The County would need to secure State authorization to effectuate this change. Increasing the sales tax rate by ¼% would raise the aggregate sales tax rate in the County from 8.75% to 9.0%, generating approximately $54.5 million in FY 2005, $56 million in FY 2006, and $57.5 million in FY 2007.

The County has indicated that these two gap-closing initiatives, raising the sales tax rate by ¼% and imposing a sales tax on residential energy, are both measures of last resort. Other savings (e.g., attrition) that the County has not factored into the Plan may develop, making these taxes unnecessary. It is important that the County outline the specific economic conditions that would necessitate their need.

Smart Government Initiatives

The Smart Government initiatives as stated on the Summary of Gap-Closing Measures are valued at $33.9 million in FY 2005, $69.7 million in FY 2006, and $90.2 million in FY 2007. Many of these initiatives are well intentioned, but the County does not provide sufficient detail to enable us to properly evaluate the projected results. We have not put these initiatives at risk because the fiscal impact affects the Out-Years of the Plan.

The County will need to ensure that proper planning and implementation takes place so that these initiatives achieve their stated amounts.

OUT-YEAR INITIATIVES

Medicaid Utilization HSSS01

The County is in the process of developing access to the state warehouse of Medicaid records, hiring a consultant, and purchasing computers and software. All of these tools will allow the County to determine if third party liability exists for the Medicaid costs that can be recovered. In addition other areas to be closely analyzed and evaluated are: fraud/abuse identification, investigation, and recovery; disproportionate share Medicaid optimization; indigent care medical cost conversions; provider billing; Medicare Part A and B maximization; 3rd party billing and recovery; Title XVI (SSI) eligibility; and payment computation and accuracy. This system will allow the County to look back two years and perform matching going forward. The third party liability contractor will be contracted on a contingency basis and will receive 12% of recoveries. The County schedule for implementation of the third party contracts and purchase of computer hardware is aggressive. The achievement of targeted savings may be questionable.

2005 $5,000,000
2006 $5,000,000
2007 $5,000,000

Audit Recoveries SSAC01

In the out-years of this initiative the County has identified a risk of billing errors on $400 million in contracts with outside vendors. There is industry information that indicates there can be as much as a 2% error rate. Through the establishment of the Department of Investigations and coordination with the Comptroller's office, the County anticipates taking advantage of the provision requiring a 5% retainage, pending completion of an audit within six months after completion of service delivery from vendors. The Proposed Plan assumes an average disallowance rate of 0.05% for a projected savings of $2.0 million. The County has reduced its discount factor from 75% to 25% in the Proposed Plan. Until these recovery efforts show some results, NIFA questions the feasibility of the recovery amounts.

2005 $1,5000,000
2006 $1,5000,000
2007 $1,5000,000

<u>Parks Revenue Enhancement Plan GSPK01</u>

For the out-years, the County has evaluated the park system and identified 12 facilities where utilization can be improved through marketing to a wider audience, or establishing partnerships with civic groups, municipalities and corporations. The County has issued Requests for Expressions of Interest some of which will be converted to Requests for Proposals (RFPs). Based on the milestones currently established, the RFP proposals are to be awarded in December 2003. The County has been enthusiastic and creative in the development of this initiative. The Authority believes the projected savings to be overstated.

2005 $4,000,000
2006 $8,600,000
2007 $8,600,000

<u>Night Simulcasting of Racing BFRV01</u>

This initiative will generate increased revenues from Off-Track Betting parlors that have received Legislative approval in May 2003 to simulcast thoroughbred racing in the evening. The County receives 10% of the total handle and a surcharge of 1.9% of exotic bets placed. The legislation also imposes a state regulatory fee of 0.39% of the handle.

This initiative was implemented in 2003 and should be incorporated in baseline calculations of increased revenue to the County from OTB operations for the out-years of the plan.

2005 $1,200,000
2006 $1,200,000
2007 $1,200,000

<u>Utilization of Part-time Security Guards PSCC01</u>

This initiative proposes the use of retired police officers in a part-time capacity at the Correctional Center. They will be assigned to less sensitive areas that do not need full-time correction officers. The County estimates that the presence of this part-time staff will reduce overtime paid to correction officers by $1.2 million. The review of qualified candidates is underway. This initiative has been scaled down from the alternative-staffing proposal in the May Update in the number of positions from 20 to 14 and the proposed savings have doubled. Savings may be achievable with an initiative of this type, however the projections for this initiative are questionable. NIFA is concerned that Correctional Center overtime may exceed budgeted assumptions, as discussed on page 14.

2005 $1,000,000
2006 $1,000,000
2007 $1,000,000

Increase Federal Reimbursement PSCC02

The Correctional Center houses an average of 200 Federal government inmates. The Correctional Center has asked the Federal government for an increase in the rate paid for housing federal inmates. The current rate is $142.32 per day, and the request was for an increase to $165 per inmate per day. The County's request was approved in September 2003. There is a question of whether the County will receive the increase from the time of approval or from the date of signature. This initiative has been completed and should be included in the baseline calculations.

2005 $1,600,000
2006 $1,600,000
2007 $1,600,000

Technology Fund/Capital Fund Charge Back SSIT02

This initiative proposes that $2 million, or approximately 20%, of departmental salaries and fringe costs for technical staff, could be charged to the Technology and Capital Funds. This is composed of $1.8 million to the Technology Fund and $0.2 million to the Capital Fund. NIFA believes that the salary and fringe expenses associated with the development of technology in the County are an operating expense and therefore inconsistent with the purpose of the Technology Fund. This should not be included as a savings initiative for the budget and Proposed Plan. As a result we consider $1.8 million for the transfer to the Technology Fund to be at risk.

2005 $2,000,000
2006 $2,000,000
2007 $2,000,000

College Reimbursement BFBU01

This initiative proposes that the County allocate to the town or city of residence the cost of tuition paid for Nassau residents who attend out-of-county community colleges. It had been the County's policy to absorb this expense in prior years. This initiative was developed in the May Update. County research indicates that the NYS

Education Law permits the counties to charge back these costs to the town or city of the student's residence. This action represents a shifting of costs between levels of government, a task NIFA believes may be difficult to achieve.

2005 $2,000,000
2006 $2,000,000
2007 $2,000,000

OTPS Freeze BFBU03

The Administration instituted an OTPS freeze during the second half of FY 2003. This freeze was approved by the Legislature in July. OMB then transferred 50 percent of all unencumbered funds out of most County departments into the Miscellaneous Budget. It is the Administration's plan to restrict OTPS spending growth to 1.25% annually. The Proposed Plan does not appear to reflect the decrease in spending contemplated in this initiative.

2005 $4,400,000
2006 $4,400,000
2007 $4,400,000

Collection of Unpaid Tax Liens BFTR02

In this initiative the County tax liens are being collected by two contractors Xspand and JER Receiver Services, whose fees are based on a percentage of collected liens. Legislative approval was received in October 2002; the collections process began in December of the same year. The savings in this initiative represents the interest that accumulated on the tax liens and which has not been recorded by the County as income. In FY 2003 the companies have collected in excess of $1.2 million. This initiative appears to be underway and should be included in the baseline calculations.

2005 $1,300,000
2006 $700,000
2007 $700,000

Reduce MTA LI Bus Subsidy EDPL02

This initiative is scheduled to be implemented in 2004 and should be incorporated in the baseline thereafter.

Program Reductions HSHS02

This initiative intends to save funds by reducing the contract expenses in the Senior Citizen Affairs and Social Services departments. This initiative was part of the Countywide reduction mandate savings that were included in the May Update. The County has determined that the previously planned cuts will not be necessary until FY 2005-2007, and that there will be smaller than previously anticipated cuts from three specific social services programs.

2005 $1,000,000
2006 $1,000,000
2007 $1,000,000

Energy Conservation GSPW04

The County expends over $25 million annually on public utilities with no emphasis on energy conservation. This initiative anticipates a savings yield of 20% over the next two years. The current year savings will be achieved through a Countywide energy conservation awareness program and energy audits conducted throughout the County offices. Out-year cost reductions will be part of the County building consolidations initiative and will involve building green light smart design programs, installing energy economizing technology and the purchase of energy from alternative sources at discounted rates.

This initiative was introduced in the Multi Year Plans for FY 2003-2005 and FY 2004-2006; it has not yet begun to provide measurable savings. The Authority believes that the County is ambitious and it is unlikely that the County will achieve the projected savings.

2005 $2,000,000
2006 $2,000,000
2007 $2,000,000

Workers' Compensation SSAT03

This initiative began in FY 2002 and has been dedicated to the overhauling of the operations in the Workers' Compensation Bureau. The County has been successful in claiming reimbursement from special funds owed to the County and clearing up the backlog of payables. The next step to this initiative is to appoint a Third Party Administrator (TPA) to manage current and future claims administration and payments. The RFP has been completed and the contract negotiations are ongoing with Triad. Completion of the contract and confirmation from the Legislature is expected in early FY 2004. Based on the success of Workers' Compensation initiatives taken to date by the County, the out-year revenue projection for this initiative is reasonable.

2005 $1,500,000
2006 $1,500,000
2007 $1,500,000

eGovernment Revenues SSIT03

This initiative proposes the enhancement of customer services with 13 applications via a newly designed web portal. The premise is that Nassau County residents will use the web to pay parking tickets, filing fees, and apply for various permits. This initiative is contingent on the Information Technology Fund being funded, which needs legislative approval that has not been forthcoming. NIFA agrees with the County that this initiative will improve customer service for those individuals who prefer to access and pay fees via the internet. However is doubtful this initiative will generate new revenue, therefore jeopardizing the income projections.

2005 $1,000,000
2006 $5,100,000
2007 $5,100,000

<u>Automated Time and Leave System SSPE01</u>

This initiative identifies an area of payroll processing that the County believes can be streamlined through the implementation of an automated system to allow for more accurate recording of labor data. Industry consultants believe a system of this type has potential areas for savings including a reduction of payroll errors, dedicated staff reductions, elimination of the manual time sheets retention and retrieval costs, and improved accuracy of hours paid to staff. The County expects the system to enable cost allocation of labor cost to departments. The County's projected savings will be achieved with staffing savings, payroll running time decreased and elimination of unauthorized leave. We question the County's ability to reach the targeted savings levels.

2005 $1,700,000
2006 $1,700,000
2007 $1,700,000

<u>Fee Increases BFBU04</u>

The County has indicated that they are going to revisit the fee structure for all County services in a formal way and on a regular basis. OMB and the County Legislature are in the process of collaboratively developing a revenue manual. The revenue manual will give guidance on when and how much fees should be modified. The County's fee-based income estimated at $98 million would have an across the board increase of 2.5% in FY 2005 and another 2.5% increase in FY 2007 to achieve this initiative. With the Legislature and OMB working together on this initiative, the annual review of fee-based revenues could generate increases in selected departments. However, NIFA questions whether the political will exists to raise all fees by this magnitude.

2005 $2,500,000
2006 $2,500,000
2007 $5,000,000

<u>Cash and Receivables Management BFTR01</u>

This initiative proposes to coordinate the collection of all receivables. There will be an RFP issued and awarded for collection services. The Treasurer will monitor the performance of the selected agencies and award additional work based on prior performance. Estimates using historical data indicate there is an unbooked receivable of at least $1.5 million. This initiative was proposed in the Adopted FY 2003 – FY 2006 Plan for implementation in 2003. Based on the information upon which this initiative was developed, there is a significant amount of duplication focused on ambulance billing.

The Authority feels that this initiative overstates the possible savings. There may be areas where the county can improve collections, but further review is needed to determine an appropriate value.

2005 $1,500,000
2006 $2,000,000
2007 $2,000,000

Ambulance Billing PSPD01

This initiative projects a 2.95% CPI increase in rates and as stated in the Adopted Plan, the County anticipates an improved collection rate rising from 40% to 60% from Med Bill Ltd. The CPI rate increase will generate an increase in revenue, however the projected 20% increase in collections was achieved in FY 2003. The collection rate is currently 67% and the industry standard is 50-60%. The County's anticipated continued growth of collection rates would be marginal as they are already ahead of industry standards. Since the lion's share of this revenue target has already been achieved in FY 2003, the revenue from this initiative should be rolled into the baseline. The anticipated additional revenue is overstated.

2005 $2,600,000
2006 $2,600,000
2007 $2,600,000

Coliseum Services Surcharge

This initiative proposes to charge ticket purchasers at the Nassau Coliseum a surcharge of $0.75 per ticket for security and traffic control at coliseum events. The requirement of State Legislative approval may hinder the initiative. The police also provide traffic control at other venues where entertainment and sporting events are held and the County has not included this surcharge for those arenas. If the County plan is to aggressively pursue this legislation the increased revenue is achievable.

2005 $1,500,000
2006 $1,500,000
2007 $1,500,000

Ticket Processing Surcharge

This initiative proposes to increase the surcharge fees assessed on parking and traffic tickets, which number 91,000 and 99,000, respectively. The County plans to use the funds to reinvest in TPVA for staff training and to improve workflow. There is a requirement for State and local legislative approval before this can be implemented. If the County plan is to aggressively pursue this legislation, the increased revenue is achievable.

2005 $1,500,000
2006 $1,500,000
2007 $1,500,000

V. Other Items

CASH FLOWS

Accurate cash flow modeling permits the County to plan for spending and investment and to better manage its cash flow borrowings. Since 2000, cash flow modeling and forecasting has been handled by the County's outside financial advisor. Over this period, the County has developed a greater understanding of factors affecting the timing of disbursements and receipts, and has better information about actual cash balances. This knowledge has, in turn, contributed to a reduction in annual cash flow borrowings and elimination in 2003 of the usual June/July Revenue Anticipation Note issue.

The County has been working to assume internal responsibility for cash flow monitoring. Due to staff turnover, the transition is not yet complete, but the County hopes to be fully responsible for its cash flow forecasts by December 2003. This is when, with NIFA's encouragement, it expects to enter the debt markets under its own credit with a short-term Tax Anticipation Note issue. (See Debt Service)

Nassau County will revise its cash flow forecast and submit it to NIFA once the FY 2004 budget is adopted.

TAX CERTIORARI AND ASSESSMENT REVIEW

INTRODUCTION

As required by the NIFA Act, the County has reported on its progress in streamlining the tax certiorari process and eliminating the backlog. NIFA finds that the County has made progress in this area, but whether it is sufficient depends upon expectations.

STATE COMMITMENT

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

On two occasions, the State Legislature has extended the County's ability to borrow for tax cert liability through NIFA and include the proceeds as revenue in balancing its budget. In the first instance, the County's right to borrow was extended from 2004 to 2005. In the second instance, the County was permitted to borrow $15 million for certs in 2006 and $10 million in 2007 (legislation pending).

COUNTY SUCCESSES

FY 2003 County progress toward resolving the cert problem includes: (1) continued employment and retention of experienced personnel; (2) completion of a stratified sample that was intended to accurately measure the extent of the cert backlog; (3) proposal of State legislation to charge fees for cert challenges and for the escheatment of money that was improperly held by landlords; (4) speedy settlement of $17 million in commercial claims at the commencement of 2003; (5) acceptance by the Office of Real Property Services of the 1% ratio for class two and class four property on the current assessment roll, as well as agreement with the County's ratio for class one property, and finally (6) the completion of a Countywide reassessment of its commercial and residential properties.

NIFA ASSISTANCE

NIFA has cooperated in these efforts by (1) continuing to meet with County personnel to review and comment constructively on their implementation plans; (2) supporting State legislation to extend the County's ability to borrow for certs, as well as charge fees for applications and institute an escheatment program; (3) providing $426.6 million of bond proceeds to the County to pay cert refunds; (4) having available $4.8 million, of the original $5 million in State aid, to help with the disposition of the cert backlog, and (5) facilitating exchange of information among the Assessor, County Clerk, County Executive and Legislature.

DISCUSSION

NIFA's remains concerned with the bottom line - will the cert backlog be eliminated in a timely manner and can the entire process of cert appeals be streamlined? We remain less skeptical than we were last year, but more skeptical than we should be at this point in our tenure. The following are some of the reasons for our concern:

a) **ASSUMPTIONS –**

- The April 2002 multi-year financial plan, the first submitted by the Suozzi Administration, said:

  "The tax certiorari reform plan will materially resolve the backlog of claims by December 31, 2003."

- The September 2002 multi-year financial plan (the Adopted Plan) said:

  "The Multi-Year Plan assumes that material resolution of the backlog will take place by December 31, 2004." This sentiment was repeated in the May Update.

- The September 2003 multi year financial plan (the Proposed Plan) says:

> "The *pre-revaluation backlog* (emphasis added) will be substantially eliminated by the end of 2004 although payment of claims will continue through 2005."

As illustrated by the foregoing, although the County continues to move the ball down the field, it also continues to shift the goal line and find reasons why its original estimates were flawed. Having seen the County fail to meet its previous targets for the ultimate disposition of cases, we are skeptical of the County's current productivity assumptions.

One of the reasons for the most recent shift is that the County now blames the reassessment for an increase in the number of legal challenges. This should not come as a surprise as NIFA warned in our Report last October:

> "The Plan also makes certain assumptions about the number of reassessment challenges that it will receive after the completion of the initial Cole Layer Trumble reassessment. We do not feel comfortable with the assumptions, as they are not based upon data from similar entities or other kinds of data that NIFA can confirm."

Without the benefit of a control group, we are not in a position to assign fault to the reassessment for the increase in the number of challenges. An increase in challenges may be normal and the County's figures may have been unrealistically low. In addition, Cole Layer Trumble's methodology was sufficiently good for the County to give them a six-year contract to do the updates.

Finally, although NIFA was given a summary of the data used in the much-referenced "stratified sample," it was not "reviewed" by NIFA. We are not equipped to do a review of the backlog methodology, but for lack of any other empirical evidence, we are willing to use the County's conclusion as a benchmark.

Notwithstanding our acceptance of the backlog as measured by this stratified sample, we are still having trouble reconciling the County's numbers regarding the cert liability going forward. We believe that the County is having a similar problem.

For example, after speaking with the County and reviewing numbers in the Proposed Plan, we understand that they are maintaining their estimate of $57 million in new cert liability for 2005, 2006 and 2007, offset by certain efficiencies in ARC. However, on page 141 of the Proposed Plan under "Tax Certiorari Liability Analysis Assumptions," the liability for 2005 is estimated to be $50.75 million. In the future, we suggest that baseline liability for FY 2005, FY 2006 and FY 2007 be stated as a single number and not as a seemingly unreliable higher baseline with offsets.

b) **PAY OUTS –**

Based upon the limited amounts of bond money that the County has drawn-down from NIFA to pay cert claims, the County has not paid out a large percent of the claims for which it has offered settlements. In fact, the County rate of cert payments is approximately the same as last year. Furthermore, NIFA currently holds approximately $100 million of the $141.5 million that was borrowed in May at the request of the County for cert payments.

Delaying payment on resolved cases costs the County in two ways: (1) the interest earned on unspent bond proceeds, which are invested short-term, is much lower than the long-term borrowing cost, and (2) settlements, which have been offered but not consummated, are languishing while the County accrues 4½% interest liability.

The Assessment Review Commission ("ARC") has given NIFA a list of nine critical steps in the cert process, which can account for delays in payments. Some of these steps are not under the sole control of ARC; however, the vast majority of those critical steps are within the control of the County. Our sense is that there could be considerable savings in interest and carrying costs if this process were streamlined and given the attention it deserves.

c) **INTERNAL CONTROLS AND AUDIT –**

In FY 2004 ARC had requested a budget of "$2.4 million in salary related expenses for 32 full time employees and $1.7 million in other than personal service expenditures." It has already made settlements in excess of $100 million and conservatively has over $200 million of settlements in the pipeline.

Regrettably, despite repeated urgings by NIFA and its Chairman, there are still few internal controls and no audits of the settlement process. We remain very concerned that after almost two years the County admits that it does not yet have "written procedures…an appraisal database, (or)…a modern technical information system." Our concerns are not diminished by their assertion that they are "now working with the Comptroller's office to establish on a pre-audit basis a program of controls…(and) a program of ongoing audits of the review process."

d) **STATE AID –**

Approximately $4.8 million of the funds given by the State to help the County streamline its cert process and eliminate the backlog are still in NIFA's possession. Although the County intends to ask for $3.6 million in 2004, this money was clearly not used to jump start the process as it was originally intended. Before releasing any additional monies, the onus is on the County to prove to NIFA that the backlog has been significantly reduced.

e) **ASSESSOR –**

The contentious relationship continues to exist between the County Executive and the County Assessor, as evidenced by a series of public pronouncements and actions. We are particularly disappointed that despite our urgings last year, the Assessor was still not given an opportunity to comment about sections of the Proposed Pan that impact his Department. We could site other examples of this disconnect, but that might deepen the rift. In the end, common sense dictates that minimizing the role of the Assessor, an elected County official, is inconsistent with the best interests of the County or the wishes of its citizenry.

Cooperation could greatly benefit the County in several areas, including personnel. In our October 2003 report, we noted that "The foremost impediment to solving the cert backlog is still the need to hire, train, mobilize and retain qualified personnel."

- *Training* - We note that the Assessor's request for $2 million in funds for training has once again been denied. This seems short-sighted and will result in CLT continuing to do functions that should be brought in-house. (See also PERSONNEL discussion below.)

- *Hiring* – Although there has been hiring in ARC, there has not been any significant hiring in the Assessor's Office, which is an integral part of the overall resolution of the cert problem. Regardless of why this condition exists, it is unacceptable. For the greater good of Nassau County, ARC and the Assessor should be working together to correct this deficiency. As part of NIFA's monitoring role, we intend to keep this issue in the forefront until we see progress. (See also PERSONNEL discussion below.)

f) **PERSONNEL –**

We question the County's statement that "in-house valuation staff consists of carefully selected civil service appointees" since most of the professional hires in ARC are provisional. We are concerned that the Civil Service System is not providing the permanent employees that are needed to staff the system.

We commend ARC for significantly lowering its FY 04 Budget estimate for outside consultants in small claims cases; however, we note that in the FY 04 Budget, ARC still has over $1.51 million for consultants and the Assessor over $1.38 million, not including the reassessment contract.

g) **COMPUTERIZATION –**

Last year the Plan referred to a $4.4 million computer system "to allow annual updates and link(s) to the operations of other agencies performing assessment and property tax functions." This purchase was scheduled for 2003, but the Fiscal 2003

Performance Summary for ARC merely says that a Request for Proposals was issued. Last year our Report indicated support for computerization, but we are concerned at the County's lack of implementation progress.

h) **LEGISLATION –**

We commend the County for presenting legislation that would have required filing fees and escheatment of monies that were deemed to be illegally held. Furthermore, we support the County's intention to resubmit this legislation and hope to see it in their legislative package for the new year.

In the interim, we urge them to do the following to assist the tenants in privately owned buildings throughout the County:

- Create a website that will list all properties and if there are any cert claims pending.
- Include on the website, a list of all refunds paid to landlords and for which properties for the past ten years.
- Make public service announcements on radio, television and in the press that inform tenants of their rights to refunds from landlords that receive reductions.
- Discuss with District Attorney the criminal liability of individuals who knowingly withhold refunds from their tenants.
- Discuss with State and Federal taxing authorities conducting audits of landlords to see that they are properly accounting for cert refunds.

CONCLUSION

Time to resolve the County's cert problem is running out. Failure to substantially eliminate cert claims by the end of FY 2005 would put an additional large annual burden on the general fund and hobble the County's financial progress.

Everyone recognized that resolving the "cert problem" was a big job, and that is why the County was given a myriad of resources. We are still not convinced by the County's claim that it has "turned the corner." Consequently, we urge the County to give the cert backlog and cert reform the high level of attention that they warrant.

VI. Covered Organizations

When NIFA reviews the Proposed Plan and the Budget, its efforts are primarily concentrated on the major funds in the County which are the general fund, police headquarters fund, police district fund, fire prevention fund, parks and recreation fund and debt service fund. NIFA has the authority, absent a few exceptions, to look at any other entity that receives monies directly, indirectly or contingently from the County. These other funds are called "covered organizations."

To date, the only covered organizations that NIFA felt merited attention were the Nassau Health Care Corporation and the Nassau Community College. This is because of the large infusion of County money to these entities and their potential effect on the overall budget.

In the future, NIFA reserves the right to classify the aforementioned or other entities as covered organizations and commence a more detailed review. Currently, the only entity that is likely to become a covered organization by the time of our next review is the proposed Sewer and Storm Water Financing Authority.

The balance of this section discusses the financial plans for the Nassau Health Care Corporation and the Nassau Community College.

NASSAU HEALTH CARE CORPORATION

The Nassau Health Care Corporation (NHCC) is a "covered organization" under the NIFA Act. Since its creation the Nassau Health Care Corporation has incurred annual operating deficits. In January 2001 NHCC retained a leading health care consulting firm, Cap Gemini, to assist in developing a plan to eliminate current and projected operating losses. It was envisioned in this plan that the Corporation would eliminate annual operating deficits by FY 2003. While many of the initiatives in the plan have been successful, in essence buying the Corporation some time, NHCC will not achieve budgetary balance in FY 2003. Given current trends, and absent major changes, the Corporation will deplete its working capital and run out of money.

NIFA, since its inception, has repeatedly called on the County to monitor and take an active role in the operations of the Corporation. As the ultimate guarantor of NHCC's debt service, the County needs to evaluate its exposure to the potential need of providing credit support. The County recognizes NHCC as a major threat to its progress towards financial recovery. However, it has failed to identify and dedicate specific reserves to address this risk. As discussed in the "Reserves" section of this Report, this "risk" is approaching certainty and specific financial provisions should be made.

The Administration has recently engaged George Kalkines, a leading health care expert, to examine the delivery of health services to Nassau residents, consistent with the County's financial capacity. While NIFA is heartened by this step, it agrees with State Comptroller Hevesi and County Comptroller Weitzman that NHCC could run out of cash in late FY 2004 or early FY 2005. Ultimately the County's financial health may be negatively affected by NHCC and the County needs to devote immediate attention to this area.

The health facilities, mainly consisting of the Nassau University Medical Center, A. Holly Patterson Geriatric Center and the Community Health Centers, were transferred by the County to the Corporation on September 29, 1999. In consideration for the transfer of the health facilities to the Corporation, the County was paid $82 million. This money came from the proceeds of the Corporation's issuance of Series 1999 Bonds ($259 million total issuance). Of the remaining funds, $135 million was kept by NHCC for working capital, $20 million was used to establish a debt service reserve account, $6 million was dedicated to an operating reserve account, and the remaining funding was used for cost of issuance and other miscellaneous items. It is the working capital component that has been subsidizing the Corporation's losses. In addition to the purchase of services, such as health care for correctional center inmates, the County also makes annual payments to NHCC of approximately $18 million per year (historical mission and various public health payments) to subsidize the cost of uncompensated care, and ultimately guarantees the payment of bonds.

Table 4 outlines the recent financial performance of the Nassau Health Care Corporation.

(Table 4)
Nassau Health Care Corporation

($'s in thousands)	**2000 Actual**	**2001 Actual**	**2002 Actual**	**2003 Budget**
Net Patient Service Revenue	382,924	373,413	373,804	401,099
Total Operating Revenue	**442,773**	**439,167**	**452,393**	**476,595**
Salaries	236,357	241,280	234,421	232,864
Total Operating Expenses	**471,765**	**487,433**	**472,138**	**489,051**
Gain (Loss) From Operations	(28,992)	(48,266)	(19,745)	(12,456)
Non-Operating Gain (Loss)	9,036	6,373	2,752	3,637
Net Income/(Loss)	**(19,956)**	**(41,893)**	**(16,993)**	**(8,819)**

NHCC incurred losses of $20 million in FY 2000, $41.9 million in FY 2001, and $17 million in FY 2002. The Corporation improved its operating results by $25 million from FY 2001 to FY 2002, mainly by the layoff of approximately 350 full-time employees. Even with this reduction in the workforce it has not been able to achieve break-even results. The budget for the current year, FY 2003, anticipates a loss of $8.8 million and they are unfavorable to Budget by $2.6 million for the first eight months. At this current rate, losses at NHCC could exceed $15 million, approximately double the budgeted shortfall.

As part of the Multi-Year Financial Plan, the County is required to include a plan from the Corporation. The plan submitted by NHCC is unchanged from the May 1st Update, projecting net losses through FY 2006. It fails to include FY 2007, the 4th year of the Plan, and also does not provide any specifics on gap-closing initiatives.

Subsequent to the release of the Proposed Plan, officials at NHCC announced plans to lay off 40 employees this year and possibly up to 300 through FY 2004. The Corporation estimated that this would save $5.65 million in FY 2003 and $25 million through FY 2004. Going forward, NHCC has not submitted a comprehensive plan demonstrating that they will be able to control costs without negatively impacting revenues. NIFA views the Plan of the Corporation as overly optimistic and questions their ability to attract new business and grow its revenue in an extremely competitive environment.

The main component of NHCC is the Nassau University Medical Center (NUMC). A quick look at the operations of this facility demonstrates the depth of the problem. The hospital has approximately 500 beds available to be filled, but as of August 2003 had an average daily census of 407. Over the past three years discharges, patient days and the average daily census have all shown favorable results. At the same time staffing levels have been reduced by approximately 10%. In spite of these seemingly positive indicators NUMC has already lost $8 million through the first eight months of FY 2003.

The other major entity of the Corporation is the A. Holly Patterson Geriatric Center (AHOP). The nursing home has recently had disappointing results and has been the subject of much unfavorable press. The average daily census data indicates a decline from 836 beds in FY 2000 to 668 beds (a decline of 20%) as of August 2003. A major problem for AHOP is that it is an antiquated facility that is unable to compete in the current market. NIFA anticipates that the County's consultant study, scheduled to be released by the end of FY 2003, will assess the viability and size of a proposed new nursing home in the current environment.

Going forward there are numerous threats to the Corporation including escalating pension contributions, the impact of managed care, State budget cuts, a rapidly declining census at the nursing home, and a labor force that is working without a contract. The Corporation has put forward an aggressive financial plan that will be difficult to achieve. Certain initiatives, such as the construction of a new nursing home, collective bargaining settlements, and refinancing of debt, require the approval of parties outside their immediate control. The County has noted its concern with the operations of NHCC and realizes that time is of the essence. The County has stated that an appropriate plan of action will be implemented once its consultant's study is completed.

NASSAU COMMUNITY COLLEGE

Nassau Community College has not experienced the same fiscal stress as the County. Largely this is due to the College maintaining a structurally balanced budget whereby recurring revenues and expenses are matched. This theme is likely to continue as the Plan for the College increases its revenues to account for contractual salary increases and escalating fringe benefit costs.

Salary and fringe benefit costs account for 86% of total expenses. The two teaching unions, the Nassau Community College Federation of Teachers ("NCCFT"), and the Adjunct Faculty Association ("AFA") are both settled into contracts through the fall of FY 2005 and CSEA employees are in a long term contract that covers the life of the Plan. This provides relative cost certainty for the Plan. While fringe benefit inflators for major items such as health insurance and pension contributions are slightly less than what the County has budgeted, the estimates are reasonable.

Revenue for the College comes from three major sources: tuition, state aid, and funding from the County through property taxes. These three funding sources account for over 86% of total revenues for the College. Property taxes in each year of the Plan increase by 3.9%. While this increase is always subject to County Legislative approval, recent history indicates a commitment to this funding source.

The College projects State Aid at $2,280 per full-time equivalent student (FTE), for FY 2004 and at $2,300 for FY 2005 to FY 2007. Overall State Aid grows 2% from FY 2005 to FY 2007 as the College is projecting annual 1% increases in student enrollment.

Tuition in each year of the Plan is scheduled to increase by $125 from a current FY 2003 rate of $2,525. When coupled with the anticipated yearly 1% increase in enrollment, growth in aggregate tuition exceeds 5% annually.

The projected 1% increase in enrollment presents a potential risk to the College. Recent indications are that the 2003 Fall semester shows a slight decrease in enrollment. Should enrollment stay flat or decline over the course of the Plan, tuition and State Aid projections will be negatively impacted. Enrollment also factors into chargeback revenues the College receives from students attending the College who reside outside Nassau County. While NIFA sees the projected enrollment increases as a risk, it recognizes the prior track record and financial management ability of the College to deal with this risk.

Two other areas of potential concern are maintaining and upgrading technology, and the infrastructure of the College. Recent County approvals for capital improvement, which will be substantially matched by the State, forms a basis for redressing these concerns.