



CITIZENS BUDGET COMMISSION

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Testimony before the Select Committee on Budget and Tax Reform on Improving Transparency, Forecasting and Flexibility in New York State's Budgetary Process

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Good afternoon. I am Elizabeth Lynam, Deputy Research Director at the Citizens Budget Commission (CBC). Thank you for the opportunity to testify today. As you know, the Citizens Budget Commission is a nonprofit, nonpartisan watchdog organization dedicated to influencing constructive change in the finances and services of the New York City and State governments.

The CBC has been an active advocate of state fiscal reform for many years, and supported the Budget Reform Act of 2007, which made changes in the budget process to improve transparency and accountability in the State's fiscal decision-making. Unfortunately, the impact of the reforms has been limited. Some of the changes, such as the financial impact reports for legislators and mandatory conference committees, have been only sporadically implemented. Others that have been fully implemented, such as the changes to the budget timeline, the enhanced revenue forecast process, and the line item requirement, have proven too narrow to have a significant positive impact. What follows is a brief assessment of the effectiveness of each provision.

1. Timing changes

Established a "Quick Start" Process and Enhanced Revenue Forecast Process for Budget Deliberations. Each house of the Legislature and the Governor are required to prepare forecasts of receipts and disbursements before November 5, to hold negotiations over these estimates, and to publish a joint report on the negotiations by November 15. In the event of no consensus, the State Comptroller is authorized to set a revenue estimate. This process was adhered to in all three years since the passage of the Act and a consensus revenue estimate has been reached. Nonetheless final revenue figures and one-house budget bills have deviated from the initial consensus forecast. The difference between the general fund and other state funds has sometimes been used to justify a larger spending envelope. Although the new milestone has created an earlier point to begin dialogue on budget adoption, serious deliberation continues to take place only at the last minute, just before the April 1 start of the new fiscal year.

Accelerated Amendment Submission. The Governor is now required to propose any amendments to the Executive Budget within 21 days of its submission to allow the Legislature sufficient time to enact a budget. The new deadline was met in 2008, but not in

2009. In December 2008 the Governor submitted the 2009-2010 Executive Budget early voluntarily, which altered and lengthened the timeline for deliberations.

2. Reporting, transparency, and accountability measures

Conference Committees. The Act requires the use of conference committees to advise the majority leaders. The committees were used in 2007 and 2008, but not in 2009. The tendency to negotiate budget items at the last minute has pressured the conference committee calendar so that in years when the process was used, they were rushed and not meaningfully utilized.

Mandated Impact Reports for Legislators Prior to Voting. The Act requires that appropriation bills be accompanied by a budget summary document showing the impact of the appropriations on the Governor's General Fund budget, the additional revenue sources available, and the impact on local governments and the state workforce. This summary is to be distributed to legislators before a vote takes place so that legislators can assess the impact of the bills on which they are voting. For the first time the summary reports were used in both chambers in 2009, and they were also made available to the public, but they were only issued very late in the process without sufficient time for legislators or the public to seriously review them and public release was not mandatory. In addition, the narrow focus on the General Fund only partially illuminates the activities encompassed in the State budget.

Prohibition on the Use of Certain Lump Sum Appropriations. The Act prohibits the use of lump sum appropriations for certain types of programs, including those often associated with member items. This procedure has largely been followed in the fiscal year 2007-2008, 2008-2009, and 2009-2010 budgets. However, it is still very difficult to identify and track the line item appropriations added as member items.

New Budget Balance and Reporting Requirements. The Act established a statutory requirement that the budget for the General Fund be balanced on a cash basis. It also enhanced multi-year financial planning by lengthening the required financial plan from three years to four. In addition, certain previously "off budget" spending by public authorities was required to be identified in budget documents. These requirements were met in all three years since the passage of the Act. The longer financial planning horizon and the improved presentation of off budget spending have been helpful. The budget balance requirement, on the other hand, based only on the General Fund, has had no visible impact.

3. Fiscal stability

Expanded Rainy Day Fund. To help promote fiscal stability, a new "Rainy Day" fund was authorized at up to 3 percent of General Fund spending to be used in the event of future economic downturns, natural disasters, or other catastrophic events. Together with the pre-existing TSRF, this permits the State to increase its rainy day reserves from 2 percent to 5 percent of General Fund disbursements. The fiscal year 2007-2008 budget included a \$175 million deposit in the new fund. Since fiscal conditions have begun to deteriorate no additional deposits have been made. The added reserve authority has brought the State limit more in line with other states. However, the reserve has not been funded and a 5 percent total

is likely inadequate for New York, which is highly dependent on the personal income tax and as a result will experience great volatility in revenues.

Now let me turn to possible points of improvement as your Committee moves forward.

Broader and More Accurate Measures of State Spending Commitments. One of the weaknesses of 2007 Budget Reform Act that has become more apparent is its focus on the General Fund as a basis for budget balance, revenue forecasting, and financial reporting. Simply put, the General Fund is an outdated and artificial construct that is not serving the public's interest. The General Fund represents a small subset of the State's spending and revenue base. Last year, for example, the All Funds cash total was \$121.6 billion while the General Funds portion was only \$54.6 billion, or about 45 percent the total. The original argument for the emphasis on the General Fund was that spending from that Fund is mainly supported from tax revenues, and therefore, General Fund spending actions most accurately reflect the true impact of the budget on taxpayers. That argument no longer holds true. State Funds also include taxes and other revenues that affect taxpayers. Perhaps the largest of these, the School Tax Relief program (STAR), is now supported by more than \$3 billion in personal income tax revenues transferred out of the General Fund every year.

Therefore, the basis for reporting and budget reform should be broadened to encompass all of the activities of state government. The Governmental Accounting Standards Board (GASB) has adopted a unified presentation that includes all funds used to support governmental activities. The unified approach also requires a fuller accounting of the cost of using capital assets in the provision of services (depreciation) and of long-term retirement liabilities that were previously uncounted (Other Post Employment Benefits, or OPEB). The State Comptroller has moved in this direction to ensure that the financial statements comply with new GASB standards and now the budget documents should follow. Until this approach can be phased in, all documents and budget reform requirements should be based on the newly denominated "State Operating Funds" currently used by the Division of Budget, which includes everything except federal aid and capital spending supported by borrowing.

As part of moving to a "State Operating Funds" budget, the State's capital budget should be separated from its annual operating budget plan, and it should cover the activities of public authorities as well as State agencies. Additional information is needed on the condition of State assets and programmatic plans for capital investments. Plans should identify key goals and align funding with specific projects.

The State currently budgets on a cash basis, instead of an accrual (GAAP) basis, which means bills are recorded as paid when the funds are expended, rather than when the liability is actually incurred. Cash accounting, although common among states, provides a great deal of flexibility from year to year that can be exploited to hide deficits. Last year, for example, the Annual Financial Report of the State Comptroller showed that the State ran a \$13.5 billion deficit on a GAAP basis, while the State's cash report showed a positive year-end balance of \$1.9 billion. This difference resulted in part from the postponement of cash payments at the end of year. As receipts expected from tax settlements last April fell well short of the mark, the Division of

Budget reduced the cash outflows, dropping cash spending totals. On a GAAP basis, however, certain liabilities had already been incurred. The spending obligations within that year were established and the revenue targets were not met resulting in a large imbalance. The GAAP presentation, not the cash basis, was a truer picture of State obligations in that fiscal year. In the same fashion, the true annual deficit this year and next can be obscured with rolling cash management tactics.

Currently the State is required to report GAAP results for the General Fund only and only for out-years, and it provides a cash-to-GAAP reconciliation that is virtually unintelligible. More detailed GAAP reporting requirements should be adopted. The 'cross walk' prepared by the Division of the Budget should be accompanied by a detailed explanation of the differences so that postponed commitments and revenue shortfalls are easily identified. In addition, reporting of year-end results on a GAAP basis should be required on State Funds, State Operating Funds, and All Funds for each of the out-years included in the financial plan.

In addition, the relationship between cash disbursements shown in the Executive Budget and the appropriations contained in the budget bills the Legislature enacts is virtually indecipherable. Re-appropriations are even more puzzling. A simpler, more transparent budget format that tracks cash disbursements should be developed. The public, and individual legislators, should be able to easily move from the Governor's language to the Legislature's.

Performance Measurement and Reporting. The public needs to know more about how its government performs with the money entrusted to it. The CBC's work in this area shows that New York lags in systematically assessing its efforts. States like Florida, Texas, and North Carolina have been involved in comprehensive performance management since the early 1990s, and are already into their third and fourth generations of programming. New York City put requirements for a Mayor's Management Report into its Charter decades ago.

New York State needs to catch up. A few years ago at the end of the Pataki Administration an executive-led effort was launched that was intended to move key agencies toward using performance management techniques. The effort was marred by too much of a "thousand flowers bloom" approach. Each agency had its own strategic plan; some were up on the web, some were not. Discussion of the issue resumed under Governor Spitzer but leadership change and higher priority budget problems have stalled any movement.

The Legislature can and should play a key role in this area. Metrics that are well developed, regularly reported to the public, and discussed with agency heads in public hearings help improve accountability. In New York City the Mayor's Office of Operations collects the metrics but they are required to publish them twice per year and the City Council has full oversight powers and typically holds a hearing on the report itself.

These are the additional reforms that CBC believes are the most important and that would have the greatest impact. There are other reform proposals being discussed today, and the CBC has reviewed and testified on prior occasions on many of them.

Thank you for your time. I am happy to answer any questions.