OPTIONS FOR BUDGETARY SAVINGS IN NEW YORK STATE

A Background Paper Prepared by the

Citizens Budget Commission

For

A Forum on Making More Effective Use of State Resources
October 17, 2007

New York's Nonpartisan Voice for Effective Government

FOREWORD

Founded in 1932, the Citizens Budget Commission (CBC) is a nonprofit, nonpartisan civic organization devoted to influencing constructive change in the finances and services of New York State and New York City governments. A major activity of the Commission is conducting research on the financial and management practices of the State and City.

All research by the CBC is overseen by a committee of its Trustees. This report was completed under auspices of the Budget Policy Research Committee. We serve as co-chairs of that Committee. The other members of the Committee are Lawrence D. Ackman, Stephen Berger, Seth Bernstein, Larry Bettino, Lawrence B. Buttenwieser, Karen Daly, Evan A. Davis, Stephen DeGroat, Cheryl Cohen Effron, Roger Einiger, David Elliman, Laurel FitzPatrick, Bud H. Gibbs, Kenneth D. Gibbs, James F. Haddon, Jeffrey Halis, Walter Harris, Patricia Hassett, H. Dale Hemmerdinger, Fred P. Hochberg, Brian T. Horey, Eugene J. Keilin, Peter Kiernan, Peter C. Kornman, Robert Kurtter, Stephen F. Langowski, Richard A. Levine, Jeffrey Lynford, Norman N. Mintz, Lester Pollack, Carol Raphael, Heather Ruth, Edward L. Sadowsky, Teddy Selinger, Andrew Sidamon-Eristoff, Adam Solomon, Joan Steinberg, Merryl H. Tisch, Cynthia King Vance, Mark Wager, Kevin Willens, Nancy Winkler, James L. Lipscomb, ex-officio.

This paper is the second in a series of three being prepared for three public forums during the Fall of 2007 on the upcoming State budget for fiscal year 2008-09. These forums are a continuation of the CBC's commitment to promote reforms in the content and process of the New York State budget. Previous research reports were prepared for conferences held in Palisdes, New York in November 2003 and in Armonk, New York in April 2006.

Elizabeth Lynam, Deputy Research Director, prepared this report with support from Selma Mustovic, Senior Research Associate; Tammy Pels, Research Associate, Darcie Harvey, Research Associate, and Sheila Spiezio, Research Consultant. The authors and the Committee are grateful to Paul Francis, Director of the New York State Division of the Budget, and members of the Division staff for their cooperation in research for the paper and for their helpful comments on a preliminary draft of this paper. Corey Kunz, Communications and Public Affairs Associate at CBC, formatted the document for publication.

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INTRODUCTION

The months between September 2007 and adoption of New York State's next annual budget in March 2008 are a critical juncture in the efforts to "fix Albany." The process by which that budget is prepared and debated, as well as the substantive decisions it embodies, are critical to the movement for political and fiscal reform in New York State. In order to promote fiscal reform, the Citizens Budget Commission (CBC) is convening three agenda-setting conferences for key stakeholders in the state budget process. Each session will focus on one aspect of fiscal reform with a goal of identifying specific changes that are assigned high priority for the coming budget cycle by a wide range of interested parties. The expectation is that the priority measures can begin to be implemented in the course of adopting the fiscal year 2008-09 budget. The first session was held on September 20 at the Rockefeller Institute in Albany: the second will be held on October 17 at Milano The New School for Management and Urban Policy in New York City, and the third is planned for December 6 in Albany.

The three dimensions of fiscal reform to be considered are:
1. Greater accountability and transparency in fiscal decision making.
2. More effective use of State fiscal resources.
3. More equitable and affordable local tax burdens.

This background paper focuses on the second issue. It has been prepared to inform discussion among the participants at the second CBC agenda setting conference on October 17.

The paper is organized into two sections. The first describes the nature of the looming fiscal problem confronting the State of New York. In all but three of the past 11 years, State spending growth exceeded inflation; the current fiscal year 2007-08 budget makes financial commitments for education aid, local property tax rebates, capital investments, and social services that help create large projected future year budget gaps. The second section identifies $5.4 billion in saving initiatives that could be enacted in 2008 and beyond to reduce future budget gaps. Conference participants are asked to review the options, which will form the basis for discussion at the forum.

THE PROBLEM - STATE SPENDING THAT EXCEEDS EXPECTED REVENUE GROWTH

The State of New York both provides services directly to the public and provides financial aid to local governments. Its budget is the third largest in the nation, below the federal government and California. In fiscal year 2007-08 New York's cash spending will reach $78.7 billion, not including federal aid or capital outlays. This represents a per capita bill for every New Yorker of about $4,000.

Not only is New York's budget big, it is expected to grow significantly over the next four years. Based on the commitments made this year, operating spending is projected to grow an average of 6.9 percent per year through fiscal year 2011. During the same period receipts are expected to grow only 4.5 percent annually. The difference leaves the State facing budget gaps rising from $4.3 billion in the most immediate year to $7.6 billion in 2011. With recent economic events the gaps may be even worse. (See Table 1.)

Table 1
New York State Cash Financial Plan, Fiscal Years 2008-09 to 2010-11
Projected State Funds Budget Gaps
(dollars in millions)

	2007-08	2008-09	2009-10	2010-11	Total Change in dollars	Total Change percentage	Average Annual Rate of Growth
Operating Receipts	$76,697	$79,592	$83,232	$87,582	$10,885	14.2%	4.5%
Operating Disbursements	$78,658	$84,641	$90,531	$96,173	$17,515	22.3%	6.9%
Capital Receipts	$5,450	$5,569	$5,457	$5,305	-($145)	-2.7%	-0.9%
Capital Disbursements	$5,014	$5,620	$5,582	$5,424	$410	8.2%	2.7%
Net Transfers	$639	$808	$1,022	$1,095	-$456	71.4%	19.7%
Planned Use of Prior Year Reserves*	$886	$468	$467	$556	NAP	NAP	NAP
Surplus/(Gap) With Reserves	$0	($3,824)	($5,935)	($7,059)	NAP	NAP	NAP
Surplus/(Gap) Without Reserves	($886)	($4,292)	($6,402)	($7,615)	NAP	NAP	NAP

Source: State of New York, Division of Budget, *First Quarterly Update to the 2007-08 Financial Plan* , July 2007.
Notes: *The 2007-08 budget was balanced this year by relying on $886 million in reserves accumulated in 2005-06 that were rolled forward. At the close of fiscal year 2007-08 the State expects to retain $1,491 in cash reserves that it plans to portion out to help close budget gaps in each year of the financial plan in the schedule shown in the table above, $468 million, $467 million, and $556 million.
NAP indicates not applicable.

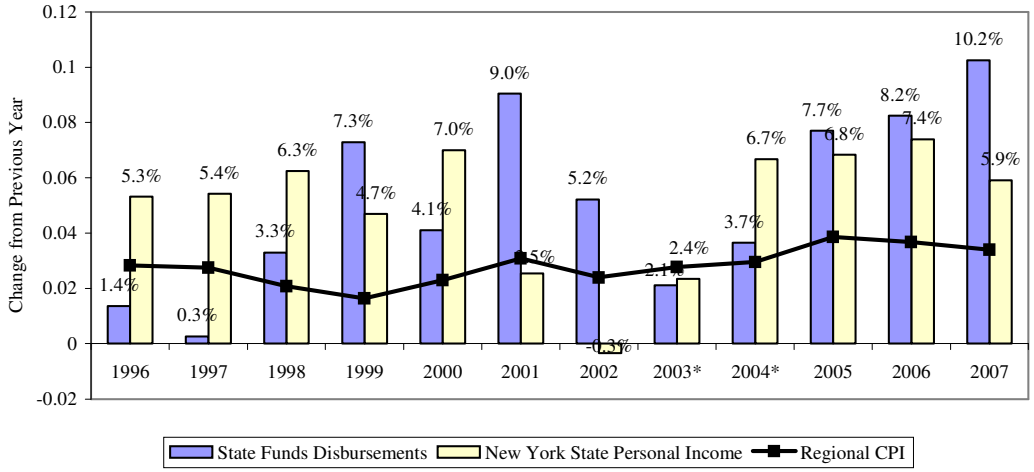
Although the spending commitments are in areas that are arguably priority needs for the State, future budgets still need to be balanced. The key challenge facing State leaders is how to maintain the commitments already made, leave capacity for future needs that may arise, and identify and adopt measures to make spending more cost effective in other areas to yield much needed savings. This challenge will be made more difficult by the prospect of lower-than-expected receipts. If the recession some economists are predicting becomes a reality, State leaders will be hard pressed to honor the promises already made.

A History of Significant Spending Growth

In fiscal year 1994-95, State spending, not including federal aid and capital disbursements, was $42.2 billion. By fiscal year 2006-07 it reached $77.2 billion, a $35 billion increase. This change amounted to an 83 percent increase over a 12-year period, and an average annual growth of 5.2 percent or just under twice the rate of inflation. However, the trend was not level. In five fiscal years spending growth was markedly higher—fiscal years 1998-99, 2000-01, 2004-05, 2005-06 and 2006-07 were all years in which spending growth at least doubled (and in three years at least tripled) the rate of inflation. (See Figure 1.)

Spending not only outpaced inflation, it also grew more rapidly than the underlying economic base. Compared to personal income growth, in fully half of the years covered State spending exceeded the mark, and in three years quite significantly. During the difficult economic times of fiscal years 2001 and 2002, State spending grew at a rate more than three times higher than personal income growth. In fiscal year 2006-07 spending growth was nearly twice personal income growth. For the upcoming fiscal year 2008-09, Governor Eliot Spitzer and Budget Director Paul Francis have recommended that spending growth be held to personal income growth, an expected 5.3 percent.[1]

Figure 1
State of New York Spending Growth Trends Compared to Inflation
State Funds Cash Basis, Excluding Capital Disbursements
Fiscal Years 1995-96 to 2006-07



Sources: Office of the New York State, *Annual Cash Report to the State Legislature* , fiscal year 1995-95 to 2006-07 editions; inflation data from Bureau of Labor Statistics, *Consumer Price Index for New York-Northern New Jersey-Long Island, NY-NJ-CT-PA* , available at http://data.bls.gov.
Note: *Fiscal years 2003 and 2004 adjusted for $1.9 billion in deferred tobacco securitization proceeds.

[1] Speech delivered by Paul Francis to the Citizens Budget Commission on September 20, 2007 available at http://www.budget.state.ny.us/pubs/press/2007/finDownturn092007.html.

The State spending shown in the tables and figures of this paper includes funds allocated to State agencies to perform direct services, such as operating State parks, and funds granted to local governments, such as State aid for local school districts. It also includes debt service paid to public authorities that have issued debt to support the State and paid to the holders of general obligation bonds issued directly by the State. Subsidies to public authorities the State partially supports, such as the Metropolitan Transportation Authority, are included in the total, but total authority spending is not.

Large Increases in Education and Health Spending Outstrip Others.

Spending growth is driven by a few functions performed by a key set of agencies. The ten largest agencies/functions in the State capture about 80 percent of the spending total. (See Table 2.) Education and health and welfare spending account for 57 percent of the total.

Table 2
State of New York State Funds Disbursements by Department/Division
Fiscal Years 1995 and 2007
(dollars in millions)

				Percent of Total Spending			Average Annual Percent Change	
	1995	1998	2007	1995	1998	2007	1995 to 2007	1998 to 2007
Total, Excluding Capital Disbursements	**42,204**	**44,300**	**77,227**	**93.1%**	**93.4%**	**94.1%**	**5.2%**	**6.4%**
10 Largest Departments/Divisions	**22,579**	**34,984**	**61,951**	**49.8%**	**73.8%**	**75.5%**	**8.8%**	**6.6%**
Education	10,920	12,458	23,357	24.1%	26.3%	28.5%	6.5%	7.2%
Health and Welfare	11,632	11,348	20,911	25.6%	23.9%	25.5%	5.0%	7.0%
Health	NA	8,016	17,486	NA	16.9%	21.3%	NA	9.1%
Welfare	NA	3,331	3,425	NA	7.0%	4.2%	NA	0.3%
State University of New York	2,907	2,947	5,099	6.4%	6.2%	6.2%	4.8%	6.3%
Transportation	2,027	1,811	2,740	4.5%	3.8%	3.3%	2.5%	4.7%
Correctional Services	1,442	1,590	2,498	3.2%	3.4%	3.0%	4.7%	5.1%
Office of Court Administration	1,065	1,159	2,162	2.3%	2.4%	2.6%	6.1%	7.2%
Mental Retardation	1,349	1,411	1,907	3.0%	3.0%	2.3%	2.9%	3.4%
Mental Health	1,624	1,385	1,859	3.6%	2.9%	2.3%	1.1%	3.3%
City University of New York	880	657	1,065	1.9%	1.4%	1.3%	1.6%	5.5%
Environmental Conservation	365	218	352	0.8%	0.5%	0.4%	-0.3%	5.5%
All Others	5,790	6,230	10,781	12.8%	13.1%	13.1%	5.3%	6.3%
Debt Service	2,203	3,085	4,495	4.9%	6.5%	5.5%	6.1%	4.3%
Capital Spending*	3,149	3,130	4,838	6.9%	6.6%	5.9%	3.6%	5.0%

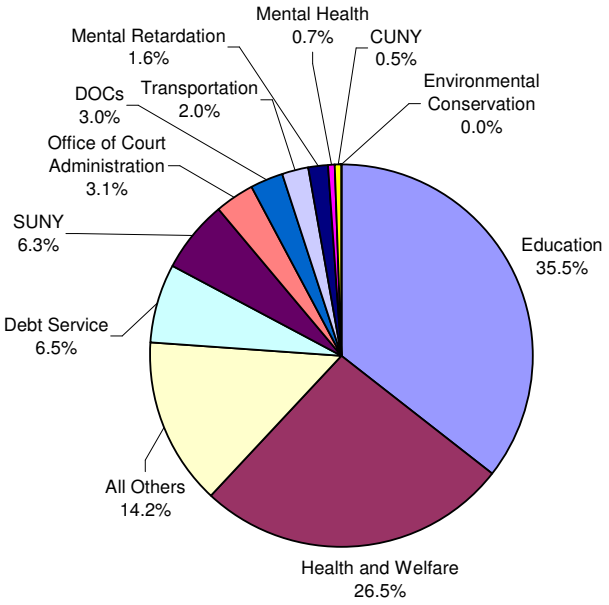
Source: State of New York, Office of the Comptroller, *Annual Cash Report to the State Legislature*, fiscal year 1995-95 to 2006-07 editions.
Note:*Capital spending shown here includes federal grants.

Over the period fiscal year 1994-95 to 2006-07 two of the ten largest departments experienced growth above the average annual rate for the period of 5.2 percent - education (6.5 percent) and the Office of Court Administration (6.1 percent). The next highest growth rate was health and welfare (5.0 percent). Within this category health spending grew much more rapidly than welfare. For example, from fiscal year 1997-98 to fiscal year 2006-07, when available data allow health spending to be separated from welfare spending, health grew at an average rate of 9.1 percent compared to welfare's 0.3 percent. If the earlier fiscal years could be disaggregated and added to the trend, the health growth rate would be somewhat dampened by the Pataki Administration's marked emphasis on Medicaid cost reduction during those years.

Also growing rapidly during the period, but outside the ten agencies/functions, was debt service (6.1 percent). A host of smaller agencies, representing about 13 percent of State spending, grew at a rate that slightly exceeded the average of 5.3 percent.

Because some areas, such as education and health and welfare, are much larger than others, their growth drives the overall total. Changes in education and health and welfare spending accounted for about for about 62 percent of the $35.0 billion increase or $21.7 billion. (See Figure 2.) Of the remainder, about 63 percent ($8.3 billion) is changes in SUNY, Correctional Services, Court Administration, Mental Health, environmental conservation, and debt service, and 37 percent ($5.0 billion) is spending for a host of smaller agencies.

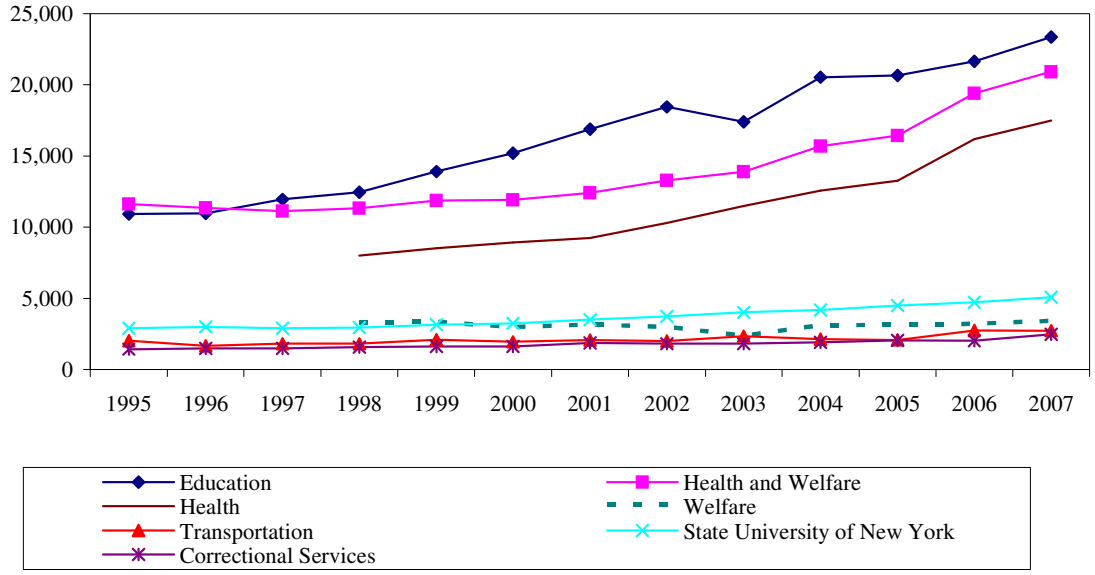
Figure 2
State of New York Changes in State Funds Disbursements by Department/Division , Excluding Capital
Fiscal Years 1994-95 to 2006-07



Source: State of New York, Office of the Comptroller, A*nnual Cash Report to the State Legislature* , fiscal year 1995-95 to 2006-07 editions.

The spending trends reflect policy decisions made during the Pataki Administration. They include an early Administration focus on containing Medicaid spending that loosened over the second and third terms, and a sharp upturn in education spending from the start of the second term to the end. (See Figure 3.) The SUNY system grew in part due to a rise in the Tuition Assistance Program (TAP) grants. Department of Correctional Services (DOCS) spending rose with inflation despite a significant decline in the number of inmates.

Figure 3
State of New York State Funds Disbursements, Five Biggest Departments, Excluding Capital
Fiscal Years 1994-95 to 2006-07
(dollars in millions)



Source: State of New York, Office of the Comptroller, *Annual Cash Report to the State Legislature* , fiscal year 1995-95 to 2006-07 editions.

Education, the largest item in the budget, grew most between 1998 and 2002, at an average annual rate of 10.3 percent. That period marks the phase-in of the new School Tax Relief program, or STAR. Intended to provide relief to local taxpayers, STAR reimburses school districts for property tax revenue they would, in theory, otherwise have raised from local taxpayers. While STAR was expanding, school aid for other programs also increased. The average annual growth in school aid without STAR over the four-year period was 6 percent. In addition to STAR, the State began a multi-year expansion of a group of programs—known together as LADDER—that included pre-kindergarten, full-day kindergarten, reduced class size in the early grades, minor maintenance and repair, instructional technology, and shared services for the five largest city schools districts. The total committed to these programs grew from $133 million in fiscal year 1998-99 to $496 million in fiscal year 2000-01.

In the other large category of State spending, health and welfare, health increases outstripped increases in welfare. With welfare caseloads diminishing over the period, New York enjoyed budget relief from federal welfare reform. While making the federally required maintenance of effort payments, State leaders were able to support programs formerly charged to the general fund with federal welfare funds. From fiscal year 1997-98 forward welfare spending remained essentially flat, while health spending increased about 9 percent annually.

Health and welfare spending grew most rapidly in the last five years. In fiscal year 2005-06 the growth was 18.1 percent, which is partly explained by the addition of spending in "off-budget" accounts authorized by the Health Care Reform Act (HCRA) to the budget. After

adjusting for this transfer, the growth rate is 8.7 percent, still the highest in the years since 1995. The average annual growth between fiscal years 2001-02 and 2004-05 was a substantial 7.3 percent.

A major factor contributing to the high growth since fiscal year 2005-06 is the cap on local Medicaid spending. This measure became effective in January 2006, capping local Medicaid spending at calendar year 2005 levels plus 3.5 percent in 2006, 3.25 percent in 2007, and 3.0 percent in 2008 and each year thereafter. The State also accelerated the takeover of local Family Health Plus costs in fiscal year 2005-06; the assumption of local costs was phased in over two years, beginning in January 2005. The combined cost to the State of these two actions is $756 million in fiscal year 2007-08.[2]

No single factor explains the relatively high growth rate in the years prior to fiscal year 2005-06. Actions related to responding to the terrorist attacks of September 11, 2001, including a special temporary relaxation of Medicaid eligibility regulations through the Disaster Relief Medicaid program,[3] and tighter controls in other areas resulted in disproportionate growth in health spending. During these years Executive Budget proposals included billions in cost-cutting measures to balance the budget, mostly in health, which were rejected by the Legislature.

Tax Cuts Were a High Priority

Despite a couple of years of fiscal difficulty after September 11, 2001, the State's revenues grew significantly during the fiscal year 1994-95 to 2006-07 period. This permitted not only the spending growth described above, but also made possible significant tax cuts.

Across all funds, including federal grants and capital spending and as reflected in financial statements prepared in accord with generally accepted accounting principles, total expenditures in fiscal year 2006-07 reached $110 billion. Over the fiscal year 1994-95 to 2006-07 period revenues grew $49.8 billion, while spending grew $50.1 billion. In fiscal years 1994-95, 2001-02, 2002-03, and 2003-04 the State ran deficits. (See Figure 4.) In addition, spending growth was supported by borrowed funds after September 11, 2001, when State leaders authorized the securitization of tobacco settlement funds to finance the operating budget. Revenues were also increased during this period with a temporary surcharge on the personal income tax, which expired in 2006.

During the earlier years revenues were decreased by a series of significant tax cuts. The current annual value of tax cuts enacted in the early years is about $13 billion, and the decreases helped bring New York's state taxes more in line with national norms. (See Figure 5.) In fiscal year 2004-05 New York State taxes per $1,000 in personal income were $67.62, ranking 30th among States. Last year, as the economy remained strong, State leaders returned to tax cutting mode enacting about $200 million in business tax reductions.

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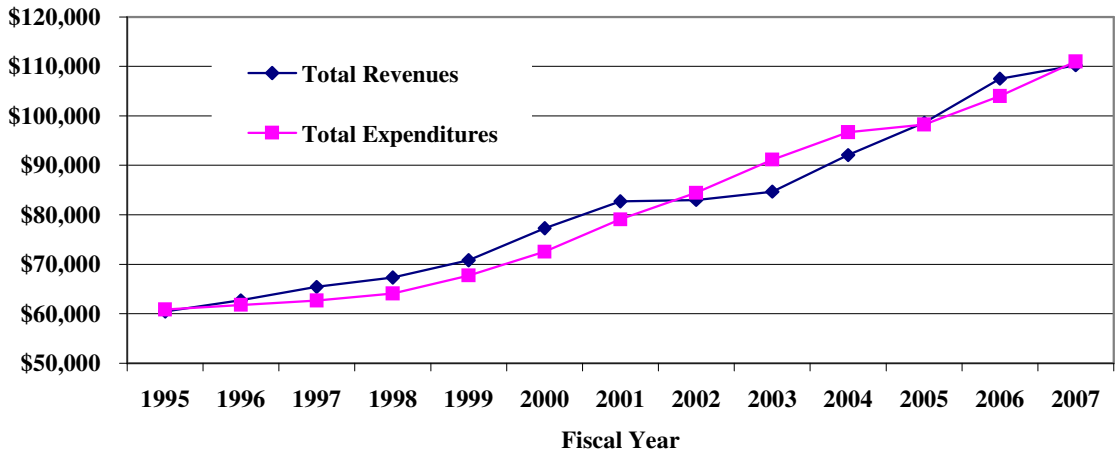
[2] State of New York, Division of Budget, First Quarterly Update to the 2007-08 Financial Plan, July 2007, p. 35.

[3] New York State Department of Health and Cornell University School of Industrial and Labor Relations, *Disaster Relief Medicaid Evaluation Project,* December 2005, available at http://www.nyhealth.gov/health_care_/Medicaid /related/docs/drm_report.pdf.

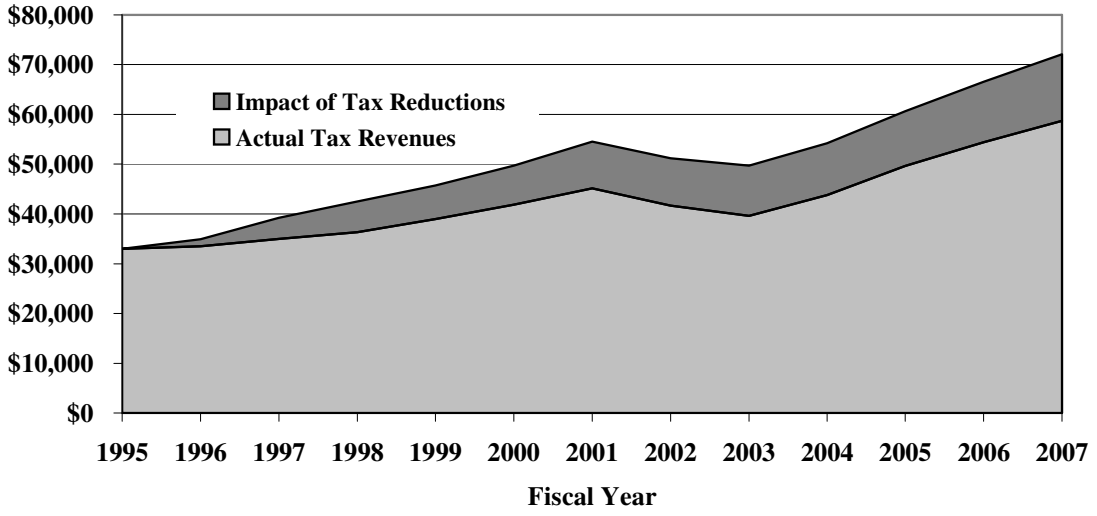
Figure 4
State of New York All Funds Revenue and Expenditure Trends, Fiscal Years 1994-95 to 2006-07
Audited Results Prepared According to Generally Accepted Accounting Principles (GAAP)



Source: State of New York, Office of the Comptroller, *Comprehensive Annual Financial Report*, fiscal year 1994-95 to 2006-07 editions.

Left undone on the State's to-do list were full fixes for the problem of high local taxes, the high State debt burden, and the insufficiency of the State's rainy day funds. Although State leaders capped local Medicaid growth to 3 percent, they did not address the basic mandate that causes local governments to bear a $7 billion burden for the program. During the period the State reduced its outstanding debt by only $1 billion, using surplus funds accumulated in the Debt Reduction Reserve Fund. This represents a 2 percent reduction in the outstanding long-term burden. At the end of fiscal year 2006-07 the State's rainy day funds had reached their statutory maximum, just over $1 billion or 2 percent of general fund spending; this is widely recognized as not enough to withstand a major downturn without radical action.

Figure 5
Impact of State Tax Reductions on Total Tax Revenues
Fiscal Years 1995 to 2007
(dollars in millions)



Sources: Tax revenue data are from State of New York, Office of the Comptroller, *Comprehensive Annual Financial Report*, fiscal year 1994-95 to 2006-07 editions; tax reduction data are from State of New York, Division of Budget, *Fiscal Year 2007-08 Executive Budget, Explanation of Receipt Estimates,* January 2007.

Major Spending Commitments Create Large Future Budget Gaps

The fiscal year 2007-08 budget, enacted in April 2007 and modified at the end of the legislative session in June, increases State funds spending 8.2 percent. This total includes capital spending, the majority of which is paid for with borrowed funds. By subtracting capital spending, it is possible to calculate the "operating" budget for the State. This budget increased 7.0 percent. The operating increases are driven in part by major new commitments for education aid and local tax relief. These commitments continue over the four-year financial plan, increasing spending until fiscal year 2010-11 at an average annual rate of 6.9 percent. Operating receipts growth over the period is projected to be about 4.5 percent per year, and with recent economic events actual growth may be less. Thus, the already sizeable budget gaps—projected at $4.3 billion, $6.4 billion, and $7.6 billion in fiscal years 2008-09, 2009-10, and 2010-11, respectively—are likely to grow even larger. (See Table 3.)

Table 3
New York State Cash Financial Plan, Fiscal Years 2008-09 to 2010-11
Projected State Funds Budget Gaps
(dollars in millions)

	2007-08	2008-09	2009-10	2010-11	Total Change in dollars	Total Change percentage	Average Annual Rate of Growth
Operating Receipts	**$76,697**	**$79,592**	**$83,232**	**$87,582**	**$10,885**	**14.2%**	**4.5%**
Taxes	62,028	65,401	69,073	72,530	10,502	16.9%	5.4%
Miscellaneous*	20,119	19,760	19,616	20,357	238	1.2%	0.4%
Operating Disbursements	**$78,658**	**$84,641**	**$90,531**	**$96,173**	**$17,515**	**22.3%**	**6.9%**
Grants to local governments	53,924	58,374	63,144	67,503	13,579	25.2%	7.8%
State operations	15,460	15,935	16,273	16,634	1,174	7.6%	2.5%
General state charges	5,146	5,593	5,921	6,233	1,087	21.1%	6.6%
Debt service	4,128	4,739	5,193	5,803	1,675	40.6%	12.0%
Capital Receipts	**$5,450**	**$5,569**	**$5,457**	**$5,305**	**($145)**	**-2.7%**	**-0.9%**
Capital Disbursements	**$5,014**	**$5,620**	**$5,582**	**$5,424**	**$410**	**8.2%**	**2.7%**
Net Transfers	**$639**	**$808**	**$1,022**	**$1,095**	**$456**	**71.4%**	**19.7%**
Planned Use of Prior Year Reserves**	**$886**	**$468**	**$467**	**$556**	**NAP**	**NAP**	**NAP**
Surplus/(Gap) With Reserves	**$0**	**($3,824)**	**($5,935)**	**($7,059)**	**NAP**	**NAP**	**NAP**
Surplus/(Gap) Without Reserves	**($886)**	**($4,292)**	**($6,402)**	**($7,615)**	**NAP**	**NAP**	**NAP**

Notes: *Miscellaneous receipts include $60 million in unrestricted federal grants.
**The 2007-08 budget was balanced this year by relying on $886 million in reserves accumulated in 2005-06 that were rolled forward. At the close of fiscal year 2007-08 the State expects to retain $1,491 in cash reserves that it plans to portion out to help close budget gaps in each year of the financial plan in the schedule shown in the table above, $468 million, $467 million, and $556 million.
NAP indicates not applicable.

Source: State of New York, Division of Budget, *First Quarterly Update to the 2007-08 Financial Plan* , July 2007.

To prepare for a possible constriction in the State's ability to finance these spending increases the budget call letter this year asked agencies to prepare plans to make more effective use of State resources. In the letter Budget Director Paul Francis warns that "…it will be necessary to reduce spending below the current services level in most agencies in order to achieve a balanced budget that still invests in the Governor's core priorities."[4]

The two most significant drivers of future spending are grants to local governments and debt service. Grants to local governments are expected to increase $13.6 billion or 25 percent, growing from $53.9 billion in fiscal year 2007-08 to $67.5 billion in fiscal year 2010-11. Of the total planned growth of $17.5 billion, grants to local governments account for fully three-quarters. These grants encompass a variety of programs; the most fiscally significant are school aid, Medicaid, and local property tax relief initiatives. State leaders recently enacted major policy changes in these areas.

With the long-awaited resolution of the Campaign for Fiscal Equity lawsuit came a costly expansion of school aid. Nearly half the increase in grants to local governments took the form of baseline additions to school aid. The baseline additions were for enacted as a multi-year funding plan. The new "foundation aid" approach—although modified in the final days of budget negotiations—was based on proposals by the New York State Board of Regents,

[4] See *2008-09 Executive Budget Call Letter*, August 16, 2007, available at http://www.budget.state.ny.us/brm/callLetter0809.pdf.

and it vastly simplified and made more rational what was a process largely driven by politics not need.

Over the school years covered by the financial plan school aid increases $5.9 billion, the lion's share of which will be foundation aid. (See Table 4.) Certain types of spending, such as aid for buildings and transportation, were exempted from the foundation aid grants. These other items are expected to add $1.1 billion to the original baseline. Smaller amounts were added to expand pre-kindergarten and other programs.

Table 4
State of New York
Projected School Aid Increases, School Years 2007-08 to 2010-11
(dollars in millions)

Category	2007-08	2008-09	2009-10	2010-11	Total Change in dollars
Foundation Aid	**$1,110**	**$2,343**	**$3,858**	**$5,512**	**$4,402**
Universal Pre-kindergarten	104	200	300	350	246
Additional Pre-kindergarten	43	-	-	-	(43)
High Tax Aid	100	-	-	-	(100)
Supplemental Public Excess Cost	17	-	-	-	(17)
NYC Academic Achievement Grant	89	-	-	-	(89)
EXCEL Building Aid	112	184	197	197	85
Expense-Based Aids (Transportation, Building, High-Cost, BOCES, private excess cost)	141	332	785	1,280	-1,139
Other Categorical/miscellaneous	51	63	200	300	249
Total School Aid Additions	**$1,767**	**$3,122**	**$5,340**	**$7,639**	**$5,872**

Source: State of New York, Division of Budget, *First Quarterly Update to the 2007-08 Financial Plan* , July 2007.

About $2 billion of the growth in the grants to local governments is the expansion of local property tax relief initiatives. Fulfilling a promise made during his campaign, Governor Spitzer proposed expanding the STAR program to provide larger property tax exemptions. The enacted budget included a new property tax rebate program based on the proposal. Accordingly, taxpayers will receive rebate checks from the State that increase over the term of the financial plan at rates that vary by income level. The program starts this year at $1.3 billion and grows to $2.7 billion in fiscal year 2010-11.[5]

Medicaid disbursements also account—as they typically do—for much of the growth in this category. Enrollment increases and inflation account for some of the growth, as does the cost of cap on local Medicaid spending. The number of Medicaid recipients is expected to grow 4 percent in fiscal year 2008-09 to four million. By fiscal year 2010-11 the State expects enrollment of 4.3 million. Costs associated with the Medicaid cap and the full takeover of the local costs of the Family Health Plus program add $1.3 billion, $1.9 billion, and $2.3 billion to spending in fiscal years 2008-09, 2009-10, and 2010-11, respectively.[6]

[5] State of New York, *Division of Budget, 2007-08 Enacted Budget Report*, May 2007.
[6] State of New York, *First Quarterly Update to the 2007-08 Financial Plan*, July 2007, p 35.

The enacted budget included about $1 billion in actions to contain and restructure Medicaid spending. State leaders moved toward a long-held CBC goal of restructuring State funds that subsidize graduate medical education, with more money going to institutions with higher percentages of Medicaid patients. Restructuring of the prescription drug program will yield savings totaling $112 million. Also, some modest rate reductions were made for hospitals and nursing homes.

The next largest category of spending, State operations, comprises $15.5 billion or about 20 percent of the total. Its growth is a more moderate 2.5 percent per year on average. However, this growth estimate is unrealistic because future costs of new labor contracts are not included. Contracts with most of the State workforce expired on March 31, 2007, and negotiations are underway with the major unions. Historically the State has faced contractual increases of about 4 percent annually. If these costs were in the financial plan, then the increase in State operations costs would be more substantial. In addition, the number of full time equivalent employees budgeted for the Executive branch climbs from 195,529 to 199,384, an increase of 3,859 positions.

General state charges, which include the costs of fringe benefits for the State workforce, is expected to grow at an annual rate of 6.6 percent to reach $6.2 billion in fiscal year 2010-11. Health insurance premiums are projected to increase at an annual rate of 10 percent. At this rate health insurance costs will jump nearly $1 billion to $3.5 billion in fiscal year 2010-11. Pension costs remain relatively level over the period at about $1.3 billion. The cost of pension contributions in fiscal year 2007-08 is 9.5 percent of payroll.

Debt service accounts for a smaller share of the budget, about $4.1 billion or 5 percent, but it is expected to grow rapidly, an average annual rate of 12.0 percent. This reflects the addition of significant capital spending both on and "off" the budget. In fiscal year 2007-08 capital spending for which the State pays debt service more than doubled to reach $10 billion from $4.9 billion in fiscal year 2004-05. (See Table 5.) The rapid expansion of capital spending will continue. During the final days of the legislative session this year $436 million in capital spending was added, mostly for transportation and economic development programs.[7] In addition, the EXCEL program for school capital will double again next year to reach its full authorization of $2.4 billion. These actions drive the double-digit growth in debt service.

[7] State of New York, Division of Budget, *First Quarterly Update to the 2007-08 Financial Plan*, July 2007, p. 28.

Table 5
Total Capital Spending Fiscal Years 2005 through 2008
All Funds
(millions of dollars)

Program areas	2005	2006	2007	2008*
Capital Projects Fund				
Transportation	1,756	3,425	3,365	3,795
Parks and Environment*	510	500	548	601
Economic Dev. And Gov't oversight**	408	501	243	939
Health and Social Welfare	103	154	120	351
Education total	667	725	631	689
Public Protection	206	285	274	343
Mental Hygine	297	355	228	269
General Government	90	116	104	115
Other	-	(929)	45	249
Total Capital Projects Fund (on-budget)	**$4,036**	**$5,131**	**$5,558**	**$7,351**
Off-budget				
Transportation	N/A	317	349	367
Economic Dev. And Gov't oversight	N/A	214	129	298
Health and Social Welfare	N/A	2	18	9
Education (not including EXCEL)	N/A	289	318	457
EXCEL	-	-	297	1,450
Mental Hygine	N/A	145	139	138
Other	N/A	50	41	-
Total Off-budget	**$881**	**$1,017**	**$1,712**	**$2,719**
Total Capital Spending (on and off budget)				
Transportation	1,756	3,742	3,714	4,162
Parks and Environment*	510	500	548	601
Economic Dev. And Gov't oversight**	408	715	372	1,238
Health and Social Welfare	103	156	138	359
Education total	667	1,014	1,246	2,595
Public Protection	206	285	274	343
Mental Hygine	297	500	368	407
General Government	90	116	104	115
Other	-	(879)	86	249
Total Capital Spending (on and off-budget)	**$4,917**	**$6,148**	**$7,270**	**$10,070**

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Sources: State of New York, Division of Budget, 2007-08 New York State Executve Budget, Five-Year Financial Plan, January 2007; and State of New York, Division of Budget, New York State 2007-08 Enacted Budget Financial Plan, April 2007.
Note: * Totals for 2007-08 are projected for year-end.

Other Needs May Add to Future Budget Gaps

In the budget and multi-year commitments adopted this year, the State made major commitments in some areas and not others. Needs in other areas are likely to be addressed when the interests of advocates and State leaders align. Potential additional pressures on the financial plan include: expanding health insurance programs to cover more people; funding the significant future liabilities for other post employment benefits, mainly health insurance for retirees; and additional expansions of pre-kindergarten programs.

Broader Health Insurance Coverage

About 2.8 million or 15 percent of New Yorkers are uninsured. Of these fully 1.2 million, including 288,000 children, are eligible for, but not enrolled in, the Medicaid program.[8] Another 3.6 million residents (19 percent) have coverage through the State subsidized Medicaid, Child Health Plus or Family Health Plus programs for the poor and working poor, while about 2.5 million have coverage from the federal Medicare program.

To address this problem Governor Spitzer proposed and the Legislature enacted a plan to increase the eligibility cut-off for the federally supported Child Health Plus program to 400 percent of the Federal Poverty Level, a level that would include residents with household income up to nearly $83,000 for a family of four. The change was expected to insure an additional 70,000 children. However, federal officials have rejected this plan. New York has joined with other states in a lawsuit over the denial of the program's expansion. In the meantime plans for the expansion of the program are in limbo.

State leaders including Governor Spitzer are committed to expanding health insurance coverage. Indeed, broader coverage is not only a humane policy, but is also fiscally prudent. Currently a complicated patchwork of federal, state and local programs reimburse primarily hospitals for their care to the uninsured. This system creates a bias for the uninsured to seek care in the most expensive settings—hospital emergency rooms and clinics. Equally important, the current system prevents the uninsured from gaining care for chronic or non-emergency conditions until they become emergencies or require intensive, expensive treatments.

In 1999 a CBC report, *Financing Medical Care for the Uninsured in New York State*, estimated that $3.9 billion in public funds were spent reimbursing health care institutions for the too little care, provided too late, to the uninsured in New York State. The CBC found the money would be better spent if redirected toward subsidizing the purchase of health insurance for the group. In addition to the CBC, the United Hospital Fund and the Urban Institute have taken the position that some portion of the significant public resources expended on care to the uninsured could and should be redirected toward subsidizing health insurance. If State leaders are willing to redirect these funds for the purchase of health insurance there need be no additional demand on the financial plan.

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[8] Danielle Holahan et.al, *A Blueprint for Universal Health Insurance Coverage in New York*, United Hospital Fund and the Commonwealth Fund, (New York), 2006.

Governor Spitzer has requested that the State Health Commissioner and State Insurance Superintendent hold hearings throughout the State over the next year to develop options for providing universal coverage. The estimated costs of the various proposals under consideration range from $3 billion to $6.2 billion depending on how generously subsidies and benefits are structured.

Health Insurance and Other Post Employment Benefits for Retirees

Until recently governments were not required to estimate or disclose their future liabilities for health insurance and other post employment benefits promised to retirees and current employees. Taxpayers could not evaluate the impact of long-term commitments their elected officials made with public employees. These costs were handled as pay-as-you-go expenses rather than as debt. In 2004 the Governmental Accounting Standards Board (GASB) changed this practice with its Statement 45. To comply with GASB 45, governments must disclose, but not necessarily fund, the future liability attributable to the cost of health insurance and other post employment benefits.

The deadline for compliance is next year, and the New York State Comptroller will include a note that estimates the value of this liability in the fiscal year 2008 Comprehensive Annual Financial Report. Based on preliminary estimates, the future cost of health insurance and other post employment benefits for New York State was $49.7 billion as of April 1, 2006. If the liability were converted to an actuarially-funded system like pension benefits, the estimated required annual contribution would be $3.8 billion for fiscal year 2007-08.[9] The State is currently paying about $1 billion per year.

There is no legal requirement to fund the newly disclosed liabilities. However, other factors are relevant. Bond rating firms and banks that lend money to public entities are monitoring disclosures closely and may expect governments to put plans in place to address the liabilities, whether by funding them or reducing them as the private sector did when their debts for post-employment benefits became public.

New York City has begun to address its $53.5 billion liability with a new Retiree Health Insurance Trust Fund. Over the last two years City leaders deposited $2.5 billion in this fund. Although a good start, City leaders still need a plan that addresses the problem more comprehensively. New York State has yet to respond in any way.

If New York State were to fund fully currently promised benefits, the added cost above the $1 billion the State is now paying would be $2.8 billion.[10] If New York were to reduce the cost of benefits by negotiating more favorable conditions of purchase or increasing the share of the premium paid by retirees, then the annual cost could be reduced. Options for restructuring benefits described in subsequent sections of this paper have the potential to significantly reduce the liability.

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[9] Uses a level payroll approach under the Frozen Entry Age method, with actuarial accrued liability calculated using a 4.1 percent annual discount rate. See State of New York, *Update to Annual Information Statement* (AIS), August 3, 2007, page 51.

[10] State of New York, *Update to Annual Information Statement* (AIS), August 3, 2007, page 51.

More or More Expensive Pre-Kindergarten Enrollment

In fiscal year 2005-06 about 38 percent of the State's four-year olds were enrolled in a preschool program funded by the federal government (Head Start) or by New York State's two programs—Targeted PreK (TPK) and Universal PreK (UPK). Among 3 year-olds, 8 percent were attending these publicly funded programs. New York State spent about $255 million on preschool, covering 8 percent of state program students. New York spent slightly more per student, $3,512, than the national average of $3,482.

TPK provided means-tested, half-day preschool along with some social services in about 14 percent of the state's public schools. In order to qualify, students' families met income standards generally in line with other public income-tested programs such as Food Stamps. The program was opened to 3 year-olds only if all eligible 4 year-olds in the district were served. Total State spending on TPK in fiscal year 2005-06 was $54 million or about $3,700 per child.[11]

UPK was begun in 1997 with the intention of serving all 4-year olds in the State, regardless of income. The program has never met its goal due to a lack of sufficient funding. Last year it was available in about 25 percent of the State's school districts. Localities determined whether full or half-day services are available. In fiscal year 2005-06, State UPK spending was $201 million or about $3,500 per child.

Until this year Head Start, TPK and UPK were fixed amount or "flat" grants to school districts in the State. The fiscal year 2007-08 budget combined the funding for these programs and increased the amount $147 million, an increase of 50 percent from $295 million in 2006-07, for a total of $442 million. The financial plan for fiscal years 2008-09 to 2010-11 provides significant new funding in order to offer an average grant of $3,500 for the enrollment of every 4 year-old.

Although the benefits of high quality early education programs are widely recognized—including higher math and reading scores, less need for remediation, and a greater likelihood to attend college[12]—many children in New York State go without any formal instruction prior to kindergarten. From the perspective of advocates the flat grant approach limited availability in two respects. First, although in some areas the amount was sufficient to provide full-day programming, in most it supported only a half-day program that working parents typically found difficult to accommodate. Second, the flat grant amounts did not keep pace with provider costs.

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[11] National Institute for Early Education Research, *The State of Pre School, 2006 State Yearbook*, available at www.nieer.org.

[12] See The National Academies of Science, 2000; http://www.nap.edu/books/030906*9882/html; Dale Purvis, *Body and Brain*, Harvard University Press, 1988, adapted from D.W. Thompson, *On Growth and Form*, Cambridge University Press; New York State Department of Education, *Experimental PreK Evaluation*, 1982, New York State Board of Regents Study on Cost Effectiveness in Education; US Department of Health and Human Services, 2001,. http://www.mathmatica-mpr.com/PDFs/buildsumm.pdf; Centers for Disease Control, 2002 http;//www.the communityguide.org/GUIDE/SCE/ECD/PAGER/htm#1; Scweinhardt, High Scope/Perry Pre-School Study 1993; http://www.highscope.org/Research/Perry Project/perryfact.htm.

To respond to these concerns, this year the funding approach was changed from a flat grant to a formula. The formula is based on the one used for school-age school aid, although the grants were limited to half the per pupil amount that the school age formula provides. The Council of School Superintendents reports that most districts receive more aid per pupil under the new approach.[13] Advocates would extend the program to cover all 3 year-olds, in effect doubling the scale of the current program.

If pressure mounted to address more fully the limitations of New York State's public pre-school options, then the amounts in the financial plan would be inadequate. Providing foundation aid for full-day options for 4 year-olds, increasing the grant amounts by the projected inflation rate to address cost increases, and offering half-day grants for 3 year-olds across the State would cost an additional $900 million in fiscal year 2010-11.[14]

[13] The Council of School Superintendents, *Last Best Hope: 2007-08 Enacted State Education Budget Analysis*, May 2007.

[14] Grants to fund half-day programs for all four year-olds are projected to cost $400 million in the *2007-08 Enacted Budget*. Doubling that to do a full-day grant adds $400 million, plus $400 million for a half-day program for 3 year-olds plus, an inflationary increase amounts to the estimated $900 million new need.

RECOMMENDED OPTIONS FOR CLOSING BUDGET GAPS

In order to honor the commitments State leaders made in the 2007-08 budget and to allow for meeting other priority needs, spending reductions are needed in other areas. This will be especially true if economic growth slows and revenue shortfalls emerge. The progress achieved in the school aid and Medicaid programs in 2007 can serve as a starting point for further restructuring. In other programs, State leaders should consider how to make the most effective use of limited resources. Pursuing any of the options for more targeted State spending will be difficult in a State not known for its spending discipline. Real leadership is needed to make hard choices.

To start the necessary and inevitable policy dialogue, the CBC offers nine options. They are not mutually exclusive and provide opportunities for variations. All are heavy lifts politically and could be implemented in stages.

1. Phase Out School Aid for the Wealthiest School Districts

A key goal of State school aid is to "equalize" the tax burden among school districts by providing State aid in inverse proportion to a district's ability to raise local revenues. With the exception STAR, New York's aid programs accomplish this goal to some degree. Aid provided to the wealthiest districts is about 14 percent of what is provided to the poorest. However, the system of equalization is far from perfect, and the wealthiest districts still get significant State aid that contributes to spending inequities.

The disparities in revenue-raising capacity among schools districts are striking. For example, the poorest 10 percent of school districts have a per pupil property valuation of $129,694; the per pupil valuation in the wealthiest 10 percent of districts is about thirty times greater or is $3,143,121. The disparities in local wealth lead to significant per pupil spending inequities. In the same poorest districts average per pupil spending is $10,778; in the same wealthiest it is $20,356. Within this high-spending group are extremely high spenders with some spending as much as $64,000 per pupil.[15] Wealthy districts are able to raise these revenues at tax rates considerably below the statewide median, while their counterparts in poor communities must tax at higher rates to raise much lower sums. Despite their relative wealth and high spending, the wealthiest 10 percent of districts receive a base grant in State aid of about $1,200 per pupil.

The foundation aid approach enacted this year was designed to allocate aid through a formula more tailored to need and ability to pay. The improvements include movement away from the "shares" method that divvied up aid predicated more on politics than rationality, the consolidation of many arcane categorical aid categories, and a special education component that allows greater flexibility of services. While these improvements are noteworthy and significant, they involved other compromises that created problems in need of fixing. Two features in particular should be addressed: a) more stringent application of requirements that districts raise revenues at the median tax rate; and b) removal of the base

[15] Fishers Island based on school year 2006-07 data- state aid plus tax levy per total weighted pupil unit.

grant amount and hold harmless provisions that guarantee wealthier districts increased State aid.

a. More stringent application of local tax levy provisions

The school aid "foundation" approach recommended by the New York State Regents and by the Governor requires local school districts to raise local revenues for education by applying the median tax rate to their taxable resources. As enacted, the foundation approach allows local districts to avoid this requirement. They were permitted alternative methods for calculating the amount required from their own sources. Districts could select the method most favorable to them. This approach dilutes the intended tax equalizing effects of the foundation approach.

Under a "pure equalization" policy, some districts would not qualify for State aid. For example, a CBC analysis of school year 2004-05 data that applied a uniform tax effort set to the statewide median to raise local revenues against a target for per pupil spending set at the statewide median identified 97 districts that would not qualify for State aid. By removing the aid allocation for these districts, all of whom were capable of reaching adequate spending per pupil on their own, the State would have saved $334 million.

b. Phase out aid for the wealthiest top 10% of districts

In addition to allowing districts to choose the most favorable revenue requirement option, the compromise approach increased the aid amounts for the wealthiest districts. The Governor proposed that districts that would otherwise not qualify for State aid increases under the foundation formula receive a minimum grant increase of 3 percent. During enactment the formula was changed; as a result, the State aid for districts receiving the minimum amounts was upped from $149 million to $329 million.[16]

Base grants and hold harmless provisions for the wealthiest districts work against equity, exacerbating disparities in per pupil spending. In the 2007-08 enacted budget, aid to the 68 (top ten percent) wealthiest school districts is $229 million.[17] Eliminating this unnecessary and ineffective aid would allow these funds to be used for other needs.

2. Continue To Restructure Medicaid To Target Benefits To The Neediest New Yorkers

As noted earlier, the Department of Health, and specifically the Medicaid program, accounts for about one-quarter of all State spending and is expected to remain the second largest source of spending (after education) through fiscal year 2010-11. The case for further, extensive Medicaid reform, beyond the progress made in this year's Enacted Budget, is clear and convincing, New York spends far beyond national norms for its Medicaid program in

[16] Calculation based on data from State of New York, State Education Department, *2007-08 Enacted Budget State Aid*, July 2007.
[17] Calculation based on data provided by the New York State Education Department, Fiscal Analysis and Research Unit.

total and per beneficiary. New York accounts for over 14 percent of Medicaid spending nationally while covering 8.6 percent of all beneficiaries. New York's spending per beneficiary, $7,910, is nearly 69 percent above the national average.

Unfortunately, New York does not have exemplary outcomes to show for its generous spending. High spending does not automatically result in high quality, and actually may hinder good care. Two recent national studies of the federal Medicare program show that high spending has no correlation to high quality; in fact, states with the highest spending tend to have the highest rate of avoidable hospitalizations, actually increasing patients' mortality rates due to risks related to "unnecessary and counterproductive" treatments. New York is among the highest health care spending states in both studies, and is also noted for a high rate of avoidable hospital admissions, with poor quality rankings relative to other states.[18]

New York's Medicaid program is the nation's most expensive because it differs from other states' programs in three fundamental ways: a) It pays some institutional providers, specifically hospitals and nursing homes, at rates above competitive costs, b) It extends Medicaid eligibility to the non-poor or middle class for long-term care services, c) It allows excessive use of personal care services and inpatient hospital care.

Initiatives directed at addressing these differences would bring the cost of the program to more affordable and effective levels. Because Medicaid has a federal and local funding match, the savings described below would actually be much larger. For the purposes of this paper—to identify budgetary savings for New York State government—only the State share is quantified in the recommendations.

a. Reduce non-competitive institutional rates.

Rates paid to hospitals and nursing homes in New York State are about 15 percent higher than national norms, adjusting for differences in the cost of living and health of patients. The 2007-08 budget reduced the expected hospital rate increase from 2.5 percent to 1.875 percent and continued "assessments" or taxes on hospital charges to recover $44.3 million from the hospitals. New York's Medicaid hospital rates pay for the training of physicians or graduate medical education (GME). Governor Spitzer proposed cutting and re-programming this money to institutions that care for the greatest number of Medicaid patients. The 2007-08 budget cut only a small portion of the GME program, about $20 million. Medicaid rate adjustments to hospitals totaled $87.1 million. Reducing rates by the full 15 percent would produce an additional $125 million in savings.[19]

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[18] See Joel C. Cantor et. al, *Aiming Higher, Results from a State Scorecard on Health System Performance*, The Commonwealth Fund Commission on a High Performance Health System, (New York: NY) June 2007, www. commonwealthfund.org, downloaded June 13, 2007, and John E. Wennberg, *Variation in Use of Medicare Services Among Regions and Selected Academic Medical Centers: Is More Better?* The Commonwealth Fund, December 2005.

[19] Hospital savings based on 15 percent of total hospital inpatient expenditures of $5,679,307,696, for total savings of $852 million. The State share at 25 percent equals $213 million less $87 million in hospital rate reductions enacted in 2007-2008 for net State savings of $125 million. Medicaid expenditure data from United States Department of Health and Human Services, Centers for Medicare and Medicaid, 2004 MSIS Data, available at http://www.cms.hhs.gov.

Medicaid nursing homes rates are about 29 percent higher than the national norm, after adjusting for the cost of living. The 2007-08 budget cut the expected annual increase for nursing home rates to 1.875 percent, resulting in savings of $18.2 million. Reducing nursing home rates by 29 percent would yield additional savings of about $735 million.[20]

b. Close eligibility loopholes for the non-poor

Generous long-term care eligibility contributes significantly to New York's unusually high Medicaid costs. New York State has nearly 28 percent of the national share of medically-needy beneficiaries (15 states don't allow this type of eligibility that permits those with income beyond federal guidelines to "spend-down" to Medicaid eligibility). Because long-term care is so expensive—Medicaid nursing home costs average over $32,000 per beneficiary—recipients can "spend-down" relatively quickly. Medically-needy expenditures accounted for $12.8 billion or over one-third of total Statewide Medicaid expenditures in 2004.

The State is relying on federal changes from the Deficit Reduction Act of 2005 to limit spending on these services in New York, but the new federal rules are unlikely to prevent eligibility abuses and, in fact, may increase the number of non-poor accessing Medicaid. Two practices are in question: spousal refusal and asset transfers.

Take Over Estate Recovery for Spousal Refusal by the State. New York is one of only three (Connecticut and Florida are the others) states that have extensive use of spousal refusal—the process by which individuals refuse to contribute to the cost of care for their spouse in need of long-term care, thereby enabling the spouse to access Medicaid services by appearing poor, or abandoned. States must provide Medicaid to an abandoned spouse. This federal regulation was recently upheld in 2005 by the 2nd Circuit Court of Appeals in reference to a Connecticut spousal refusal case. The use of the spousal refusal provision varies by county, but Nassau County found that 95 percent of "community spouses" (those remaining in the house, not requiring nursing home care) had signed spousal refusals at the time of their spouse's Medicaid application.[21]

States, however, have the option to recover Medicaid payments from the abandoning spouse through legal action. Most states not currently allowing spousal refusal make it clear to their residents that they will vigorously pursue spousal refusal recoveries in an effort to keep this practice from spreading. New York State relies on counties to recover the funds, but counties have very little financial incentive to do so—they receive only 10 percent of the

[20] The Division of Budget is currently conducting a study of nursing home rates to ascertain why New York's costs are so much higher when half of the home operators in the State report that they running their facilities at a loss. Nursing home savings based on 29 percent of total nursing home expenditures of $6,502,691,543 for total savings of $1,885,780,547. The State share at 40% equals $754 less the $18 million in nursing home rate reductions enacted in 2007-2008 for net State savings of $735 million. Medicaid expenditure data from United States Department of Health and Human Services, Centers for Medicare and Medicaid, 2004 MSIS Data, available at http://www.cms.hhs.gov.

[21] Brian Burwell and William H. Crown, Medicaid Estate Planning in the Aftermath of OBRA "93 (Cambridge, MA: The Medstat Group, August 1995), p. D-6.

proceeds (because the local share for long-term care is 10 percent); the State and federal governments receive 90 percent of the proceeds.

A 2003 report on Nassau County's Medicaid program details the difficulties counties encounter in pursuing recovery: a) Families do not notify the county when the recipient dies. b) The county cannot run a financial check on the living spouse. c) The State Medicaid computer system and nursing home billing practices prevent the county from getting needed information quickly. (d) The county does not have enough legal expertise to take on private practice, experienced eldercare lawyers.[22] Thus, New York State counties have not done as well as other states in recovering funds. New York ranks 34th in a national study of Medicaid estate recovery programs, with a recovery rate of 0.2 percent of Medicaid long-term care spending compared to a national average of 0.61 percent.[23] If New York State assumed responsibility for recovery at the State level and recovered at the national average rate of 0.61 percent, New York State would recover $45 million.

Apply Asset Look-back to Home Care and Decrease the Home Value Exemption to the Lower Federal Standard. Federal regulations address asset transfers prior to applying for Medicaid and were updated in the Deficit Reduction Act (DRA) of 2005. The updates include: (a) The "look-back" period for asset transfers was extended from three to five years (meaning any assets transferred in the five years prior to Medicaid application for *nursing home services* will have to be "spent-down" before Medicaid is approved) with the penalty for transfers beginning at the time of nursing home care rather than at the time of the asset transfer. (b) An individual applying for Medicaid cannot have home equity greater than *$500,000 or at state option greater than $750,000;* however, the home is exempt from consideration if the community spouse is living in the house.

The DRA continues to allow states the option of whether or not to apply the look-back period to those applying for home care services. New York State continues **not to apply the look-back period to home care.** This is significant because of New York State's unique medically-needy eligibility. For someone seeking Medicaid home care, assets may be transferred without penalty and result in immediate Medicaid eligibility for home care services. In the 15 states without a medically-needy program, the individual would actually have to spend their assets in excess of Medicaid eligibility levels on their care before they could gain access to Medicaid.

The new DRA regulations will possibly result in greater use of Medicaid-financed home care, and greater use of the spousal refusal option in New York State, requiring greater State-level attention to these issues. The $4 million in savings in the 2007-2008 enacted budget related to "encouraging counties to pursue spousal refusal recoveries" is not a serious effort to address this issue. The State has chosen the most lenient and highest level allowed by federal regulation—home value of $750,000. This exceeds the lower end of the federally allowed range by fully $250,000 (about the cost of a two-year nursing home stay on Long Island). The State could decrease the home value limit to the lower level allowed by the federal

[22] Office of the Nassau County Comptroller, Field Audit Bureau, *Nassau County Department of Social Service Medical Assistance Unit*, April 8, 2003.
[23] Erica F. Wood and Ellen M. Klem, *Protections in Medicaid Estate Recovery: Findings, Promising Practices, and Model Notices,* ABA Commission on Law and Aging, May 2007.

government of $500,000, and extend the look back period to home care applicants. If one percent or 4,089 or the current 408,908 personal care recipients were required to contribute $250,000 toward their care prior to Medicaid eligibility, total State savings would be $409 million.[24]

c. Reduce excessive utilization of some services

In addition to lenient access to Medicaid for personal care services, the hours of care provided are far above national standards. New York's $3.5 billion expenditure for personal care is nearly 19 percent of the national total, with expenditures per beneficiary reaching $8,442 compared to $2,957 nationally. This difference is due to the higher average number of hours of care in New York, 30 hours per week versus the national average of 11 hours per week. If the average hours of care were reduced to 17 hours per week, still 50 percent higher than the national norm, and applying the change to a smaller pool of eligibles to assume that the recommendations above were implemented, estimated State savings would be $433 million annually.[25]

Improved management of high-cost elderly and disabled beneficiaries through a managed care system would reduce the number of unnecessary hospital admissions for this population. One of the previously mentioned national Medicare studies estimates that if New York were to reduce unnecessary hospital admissions for the elderly, the Medicare program would save $686 million. If New York could reduce unnecessary Medicaid admissions by 20 percent, or less than half the 47 percent difference in admission rates noted in the Medicare study, the State would save $241 million after reductions in Medicaid hospital payment rates as recommended earlier. This savings estimate assumes that the remainder of savings from reducing hospital admission rates to the national level would be invested in managed care systems for these patients.

3. Restructure Fringe Benefits For Employees

State costs for its employee and retiree health insurance and pensions can be addressed by bringing the State's practices more in line with those of private sector and other public sector employers. As CBC reported in previous studies, most government workers are now paid more than their private sector counterparts—the generous health insurance and retirement packages developed to attract public sector workers are no longer justified.[26]

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[24] Requiring 4,089 individuals to contribute $250,000 would create total savings of $1,023 million and 40 percent of this amount would accrue to the State.

[25] Assuming the home care eligibility reduction savings above reduces total personal care spending of $3,452 billion by $1,022 billion, to $2,520 billion and applying a 43 percent reduction in hours (from 30 to 17 hours) results in total savings of $1,083 billion. Applying the 40 percent State apportionment, State savings equal $433 million. Medicaid expenditure data from United States Department of Health and Human Services, Centers for Medicare and Medicaid, 2004 MSIS Data, available at http://www.cms.hhs.gov.

[26] See: CBC, *The Case for Redesigning Retirement Benefits for New York's Public Employees*, 2005, and *Old Assumptions, New Realities: The Truth About Wages and Retirement Benefits for Government Employees*, 2006, available on the CBC website at www.cbcny.org.

a. Health Insurance Restructuring

In 2007 New York State will spend approximately $2.6 billion to provide health insurance to over 1 million employees, retirees and their dependents. New York State offers its employees and retirees a choice of health plans and pegs its contribution to the cost of a comprehensive plan. For employees and retirees hired prior to 1983, the State pays the full premium for individual coverage—$5,553 in 2007. For family coverage, the State pays 86 percent of the $12,675 premium; the enrollee contributes $1,774 for 2007. For those hired after 1983, the State requires employees and retirees to pay 10 percent toward individual coverage and 25 percent of the difference in costs between an individual and family coverage, or 18 percent of family coverage costs. For these employees and retirees, individual premium contributions are $583 annually and family plan contributions are $2,440.

However, upon retirement, State employees receive a credit equal to half the value of their unused sick leave that is applied toward the retiree's share of the premium costs. For many retirees this significantly reduces or eliminates the required premium contribution.

Retirees who are over age 65 are eligible for the federal Medicare program. The Medicare program provides a significant foundation for health care coverage of retirees, but it leaves two significant gaps. It does not cover those under age 65 (many state workers retire before age 65—"early retirees") and it only covers a portion of health care costs for those over age 65 so that "supplemental" coverage is required. In addition to providing its retirees with supplemental Medicare insurance, the State reimburses retirees for the Medicare Part B premium charged by the federal government.

New York State's employee health insurance benefits are generally comparable to benefits provided by other state and local government employers, although they are vastly more generous than benefits provided to most private sector employees. For retirees, New York State's plan is exceptionally generous when compared to both other public and private sector retiree benefits.

A survey conducted by The Segal Company finds that on average in 2003 most public employers paid 90 percent of the cost of employee individual health insurance coverage and 78 percent of the cost family coverage. For retirees, states paid 57 percent of individual premiums on average for both early and Medicare retirees. However, for retirees and their spouse, state employers paid only 47 and 44 percent of premium costs for early and Medicare retirees, respectively.[27] A Commonwealth Fund study of retiree health benefits shows that on average in 2005, public sector Medicare-age retirees paid an average of $116 per month for individual coverage or $1,392 annually.[28] Notably, only six states pay any portion of Medicare Part B premiums.

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[27] The Segal Company, *2003 Segal State Health Benefits Survey: Medical Benefits for Employees and Retirees:* New York, 2006.
http://www.segalco.com/publications/surveysandstudies/2003statesurvey_medicalbenefits.pdf. Accessed 6-26-07.

[28] Heidi Whitmore, Jeremy Pickreign, and Jon. R. Gabel, The Commonwealth Fund/Center for Studying Health System Change Survey of Retiree Health Benefits, 2005, New York: July 2007.
http://www.commonwealthfund.org. Accessed on 6-27-07.

Among private sector employers health insurance costs are typically shared more with employees and retirees. A Kaiser/Hewitt survey of very large (1000 plus employees) private sector firms shows that in 2006 workers contributed $627 on average toward individual coverage (about 15 percent of premium costs), and $2,973 toward family coverage—about 26 percent of the total premium.[29] For retirees, the Commonwealth Fund study shows that in the private sector, only 9 percent of small firms (3 to 199 workers) offer any retiree health benefits compared to 35 percent of firms with more than 200 workers.[30] Another survey by Kaiser/Hewitt of retiree health benefits at very large firms shows that fully 55 percent of employers pay 40 percent or less of retiree premium costs for both Medicare-age and early retirees. On average, early retirees contribute $2,724 toward their coverage while Medicare-age retirees contribute $1,320 on average.[31] Moreover, only 9 percent of large private sector employers pay any share of Medicare Part B premiums.

If the State were to bring its practices more in line with other public sector employers, then it would require an additional 4 percent contribution toward family plan premiums for post-1983 hires. This would bring the share of the total premium borne by employees to 22 percent and the share borne by New York State to 78 percent, comparable to the 78 percent paid by most states. The savings to the State under this proposal would be an estimated $75 million.[32] For retirees New York could require a 50 percent contribution toward premiums and save $432 million.[33] It could also eliminate payment for Medicare Part B premium contributions for savings of $207 million.[34]

b. Pension Restructuring

In addition to generous health insurance benefits, New York State employees and retirees have unusually generous pension benefits compared to other public and private sector workers. New York's unusual pension benefits are a large and rapidly growing expense.

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[29] The Kaiser Family Foundation and HRET, *Survey of Employer Health Benefits 2006,* September 26, 2006. http://www.kff.org. Accessed, 8-3-07.

[30] Heidi Whitmore, Jeremy Pickreign, and Jon. R. Gabel, The Commonwealth Fund/Center for Studying Health System Change Survey of Retiree Health Benefits, 2005, New York: July 2007. http://www.commonwealthfund.org. Accessed on 6-27-07.

[31] The Kaiser Family Foundation and Hewitt, *Retiree Health Benefits Examined, Findings from the Kaiser/Hewitt 2006 Survey on Retiree Health Benefits*, December 2006. http://www.kff.org. Accessed, 6-26-07.

[32] Savings estimates based on data from the New York State Department of Budget. The number of employee family contracts in 2007--146,967 times an additional 4 percent of the family premium, or $507, equals calculated savings of $74.5 million. The total family premium in 2007 is $12,674.76. Assumes all employee contracts are for post-1983 hires.

[33] Savings estimates based on 84,024 retirees contributing an additional 40 percent toward individual coverage, or $2,221, equals $186.6 million, and 60,423 retirees contributing an additional 32 percent toward family coverage, or $4,056, equals $245 million, for total estimated savings of $431.7 million. Employee and retiree health insurance program and cost data were provided by the New York State Division of the Budget.

[34] Savings estimate based on the 2007 Medicare premium of $1,122 times two 2 (for family/ a couple) times 54,567 Medicare retirees with family coverage equals calculated savings of $122,448,887, plus $1,122 times the 75,355 retirees with individual coverage for calculated savings $84,548,041; total savings from the two measures added to $206,996,927. These calculations assume that the split between family and individual contracts for Medicare retirees is the same as for all retirees.

State required pension contributions more than quadrupled from $274 million in fiscal year 2001-02 to $1.1 billion in 2005-06; pension costs are expected to reach $1.3 billion in fiscal year 2010-11.

Efforts to change pension benefits must recognize their protected status under the New York State Constitution. Absent a constitutional amendment, it is not able to change benefits of current employees and retirees. In contrast, pension benefits of newly hired workers are not protected and can be changed legislatively. Changes to pension benefits have been accomplished by creating new "tiers" within the system according to hiring date: Tier 1 (before 1973); Tier 2 (1973-1976); Tier 3 (1976-1983) and Tier 4 (since 1983). A new tier could address the aspects of the system that make it more costly. Four features of New York system are unusually generous.

Exclude Overtime from Pensionable Base and Lengthen Period for Final Average Salary Calculation. All New York State retirees are allowed to include overtime earnings in their pension payment calculations. Nationally fully 94 percent of full-time employees of state and local governments are *not* allowed to include overtime in their salary base for pension purposes. Moreover, most public pension benefit payments are based on a three to five year, final average salary (FAS), rather than one year, as is allowed for retirees in Tier 1 and for police and fire system retirees in New York. One-year FAS is optional for localities for police and fire. Some State fire retirees have one-year FAS; State troopers and State park police do not, they have three-year FAS.

Define Eligibility for Disability Pensions More Narrowly. If a worker becomes accidentally disabled prior to otherwise becoming eligible for retirement benefits, the State pension plans permit the worker to receive benefits without meeting age and service requirements. Disability benefits usually equal what the regular retirement benefit would have been based on the worker's FAS. However, for State uniformed workers, the disability benefit is greater than the regular retirement benefit. For example, at 20 years of service the disability payment for employees accidentally disabled while undertaking their duties is 75 percent of the FAS versus a regular retirement benefit of 50 percent of FAS. This differs from most state and local government workers nationally who do not receive enhanced disability pensions. Moreover, New York defines disabilities in ways that allow an unusually large percentage of uniformed workers to qualify for added disability benefits. The State legislature controls how disabilities are defined and it has become common that they approve pension benefit enhancements at the request of specific public employee organizations as an "end run" around collective bargaining agreements. For example, in the last legislative session, 20 different bills were introduced to enhance benefits for City and State retirees, including an effort to create the "presumption" of injury during service so that more workers can claim a disability pension.

Apply Minimum Age Requirements to All Employees. The minimum age and service requirements for most state workers are generally comparable to other state and local government systems: State teachers are eligible at age 55 with 20 years of service with no benefit reduction; Tier 1 at age 55, and all others at age 55 with 30 years of service and at age 62 with 25 years of service. Tiers II, III, and IV have benefit reductions if age 55 with less than 30 years of service and age 62 with less than 25 years of service. However, uniformed service workers, such as State police officers, have no minimum age requirement, and the minimum

for all other workers is significantly below that of the federal Social Security System, of federally-tax deferred private 401(k) plans, and even most European public-sector retirement systems.

Increase Required Contributions. The required contributions from State workers are low compared to what is required of other public employees—including those required by New York City workers. Contributions are not required for retirees in Tiers 1and 2 and for members of the State's Police and Fire Retirement System. Members of Tiers 3 and 4 are required to make contributions of only 3 percent of salary for the first ten years of service. Required contributions vary by date of hire, years of service and other factors, but few workers contribute more than 3 percent. In contrast, among public sector defined benefit plans nationally, about 74 percent of those required to contribute must contribute more than 3 percent.

Five changes could be made to make the public pension system more affordable for New York State taxpayers. Four are doable by creating a new defined benefit Tier V. They are: 1) Pension benefits could be based on a more standard definition of final average salary (FAS). That is, on the average salary over five years experience and should include base salary only—excluding overtime and other supplements subject to manipulation. 2) Work-related disability could be defined more rigorously, and the State legislature's role in pension benefit expansions curtailed. 3) The minimum retirement age could be raised to more closely align with that of other employers, perhaps with a lower minimum age for uniformed workers. 4) Required employee contributions could be increased and expanded beyond 10 years.

Another option is to move to a defined contribution Tier V where employees would participate in a 401k-type fund and rely more on the accumulation of their own contributions and abilities to manage their investments. The option is very common in the private sector and is offered by a few public sector employers.

Possible savings from a new tier are difficult to estimate, because they can only be applied prospectively to new workers and are likely to have their greatest impact over time horizons that extend well beyond the present financial plan. However, if the State were able to reduce its 9.3 percent of payroll contribution to 7.0 percent, future savings when the change was fully implemented would total $424 million.[35]

4. Increasing the State Employee Work Week

A 40-hour work week is the norm for the majority of workers in public sector jobs. According to Bureau of Labor Statistics Data, among all state and local public sector employees fully 63 percent work a 40-hour week. For government workers in blue-collar and service occupations, fully 85 percent have a work schedule that is 40 hours or more.[36]

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[35] The State reports that its annual pension bill at 9.2 percent of payroll in fiscal years 2008-09 will be $1.3 billion. Reducing the contribution rate to 7.0 percent would require that the State pay $989 million instead for an estimated future savings of $424 million.

[36] United States Department of Labor, Bureau of Labor Statistics, Employee Benefits in State and Local Government, 1998, available at www.bls.gov.

Although some employees of New York State work a 40-hour week, the more typical schedule for non-managerial, civilian employees is 37.5 hours.[37] Increasing their weekly hours to 40 would allow for productivity gains through reduction of the workforce. With more work accomplished in a longer work week fewer employees are needed to perform the same functions.

To achieve this change the State would need to put this demand on the table during collective bargaining. Contracts with most of State workforce are being negotiated now as they expired on March 31, 2007. Savings from the productivity gain could be shared with workers or retained in their entirety by the State depending on what was negotiated.

Other issues of specification of work title and disparate locations would need to be resolved to maximize savings. These issues might also require collective bargaining with employee unions and have implications for civil service rules and regulations.

In an options paper considering a 40-hour work week for New York City's non-managerial employees, the CBC estimated possible savings for New York City. The same model, modified to reflect the average cost of a New York State employee, produces estimated savings for the State of $227 million. The model also includes the typical costs of fringe benefits because cost savings are not limited to wages and salaries. Fewer employees also mean lower costs for fringe benefits. These costs for the State are substantial and add an estimated $24,000 per employee to the total personal services budget.[38]

5. Streamline Purchasing and Other Back Office Functions

With state operations spending expected to grow more than 5 percent, other productivity options to reduce costs could be explored. Government procurement processes have typically been cumbersome and costly. State guidelines could be reviewed and revamped to aid agencies in purchasing necessary goods and services more efficiently. Printing and other back office administrative functions could be consolidated to eliminate duplicative functions. For example, collections and cash management of various state funds now performed by more than one State agency could be brought together in one agency. Human resources support performed by internal offices in State agencies could be centralized. To cut payroll expenses State employees and firms that have contracts with State governments could be required to have direct deposit to minimize the costs associated with processing paper checks. If the State were able to reduce State operations costs 2 percent by year three of the financial plan, for example, total savings would be $333 million.[39]

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[37] The New York State Division of the Budget reports that on average about 63 percent of State employees are on a 37.5 hour schedule.

[38] Calculation assumes that the employees who would be reduced by attrition are employed at an average non-managerial non-uniform salary of $51,900 with fringe benefit costs of $23,993, as reported by the New York State Division of Budget.

[39] In fiscal year 2010-11 State operations spending is expected to total $16,634 million. See Table 3 for sources. Two percent of this total equals $332.7 million.

6. Reduce And Restructure Ineffective Economic Development Programs

In recent years New York State has expanded its economic development programs considerably. Some of these programs have not been used effectively. Empire Zones and the Centers for Excellence programs have failed to deliver the desired result. These programs could be eliminated or scaled back for an estimated maximum savings of $800 million.

a. End the Empire Zones Program

Empire Zones were formed out of an earlier economic development zone program created in 1986. It offers tax breaks to firms for locating and expanding in economically distressed communities. At the end of the program's first year there were 10 zones. In 1993 the legislation was amended to allow counties to create a zone if they faced "sudden and severe" job loss. This caused a rapid expansion of the program; by 1995 there were 40 zones. In 2000 legislation formally changed it to the Empire Zone program effective on January 1, 2001. The 2000 criteria for site selection eliminated the required threat of job loss, opening the floodgates for the proliferation of zones. In 2007 there were 87 Empire Zones throughout the State. The program has grown at an average annual rate of 11 percent.[40]

According to the 2007-08 Tax Expenditure Report, the program will forego $558 million in tax revenue in calendar year 2007. This includes tax credits for personal income, corporate franchise, bank, insurance, and sales taxes.

The program suffers from multiple flaws revealed in audits by the State Comptroller's Office numerous times. A lack of accountability has led to shoddy practices. Among them is a phenomenon known as "shirt changing," where businesses reincorporate under new names to claim they are creating new jobs when in fact the jobs already existed. A 2004 audit by the State Comptroller found that 23 percent of businesses receiving empire zone tax credits reduced employment, while only 30 percent of recipients met or exceeded their employment targets. In addition, the audit determined that Empire Zone Boards are not aware of the total cost of the program or the total benefits provided to the community.[41]

Multiple reforms have been attempted. In 2002 the Legislature enacted new criteria that attempted to tie eligibility determinations to job losses. Counties then exploited another loophole by adding past jobs lost to their "expected future" job losses. Calculating job loss that way enabled almost any county to qualify, and three counties that would not have qualified under the older rules became eligible.

In 2005 the Legislature again tried to improve reporting and enforcement provisions. The provisions required businesses that maximized their Empire Zone tax breaks by changing their names and claiming they were a new business to prove to the tax department that they

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[40] A.T. Kearney, *Delivering on the Promise of New York State: A Strategy for Economic Growth and Revitalization*, Prepared for the New York State Empire Development Corporation, 2007.
[41] Office of the State Comptroller, Division of Local Government Services and Economic Development, *The Effectiveness of Empire Zones*, 2004.

had a "valid business purpose" for reincorporating. If the business did it only to get bigger Empire Zone tax credits, tax officials can deny them the credits. However, the tax department has not yet denied any businesses tax credits as a result of the 2005 reforms. In the process of enacting these measures the Legislature expanded the program again by allowing Empire Zone tax abatements to apply to individual businesses under the "Regionally Significant Project" designation.

There have been calls to shut down the program entirely. In the meantime talk of further "reform" continues. In June 2007 the Assembly conducted a public hearing on the Empire Zone program. In July 2007 the Empire State Development Corporation issued letters to 3,000 companies that were recipients of Empire Zone tax breaks that did not create at least 60 percent of the jobs or investment that they predicted when they applied for the benefit.

b. Scale back the Centers of Excellence program.

The Centers of Excellence (CoE) program was established in 2001 with the goal of leveraging the intellectual capacity of the State universities for economic development. High tech centers situated around the State were to draw in private and public investment and create jobs. The Pataki Administration established the first five: Nanoelectronics and Nanotechnology (Albany); Bioinformatics and Life Sciences (Buffalo); Photonics and Optoelectronic (Rochester); Wireless and Information Technology (Stony Brook); and Environmental and Energy Systems (Syracuse). Two others were added by Legislative action in 2006: Small Scale and Systems Integration at Binghamton and Bioscience in New York City. From 1997 to 2005 these Centers received $529 million.[42] Almost all of these funds were allocated through memorandums of understanding shielded from public review.

Before 2007 the CoEs had no job creation requirements. The Empire State Development Corporation has recently taken over their management and has instituted procedures for estimating job creation, but as of yet there is no way to ascertain their impact on job creation. A recent assessment by AT Kearney for the Empire State Development Corporation concluded that only one CoE, The Center for Excellence in Nanoelectronics and Nanoscience at UAlbany, had been effective in drawing significant private capital.[43] The center in Albany has attracted $1.2 billion in private investment; the other six centers have attracted a combined $135 million. It is not clear if the conditions that made for Albany's success can be replicated at the other locations.

The State made funding commitments for the CoE program through fiscal year 2005-06 of $586 million. Of the total, $342 million goes to the center at UAlbany and the remainder will

[42] Kent Gardner and Erika Rosenberg, *Capital Pork: How State Politicians Divvy Up Billions of Dollars for Favored Capital Projects*, Center for Governmental Research: Institute for Competitive State Government, March 2006.

[43] A.T. Kearney, *Delivering on the Promise of New York State: A Strategy for Economic Growth and Revitalization*, Prepared for the New York State Empire Development Corporation, 2007.

be spread among the other centers.[44] The State could scale back the size of the program to fund only the successful UAlbany center for a savings of $244 million.

7. Develop A Comprehensive Capital Plan

The State, directly and through its public authorities, owns capital assets and infrastructure valued at approximately $138.8 billion.[45] Most of these assets - $78.3 billion - are owned and operated directly by the State. The State owns another $7.3 billion in higher education and other facilities used for the operations of the State and City Universities of New York (SUNY and CUNY). The remainder – approximately $53 billion – are assets operated by State public authorities, predominately the Metropolitan Transportation Authority (MTA).

Despite the enormous value of these assets, no one agency is responsible for centralized capital planning or strategic capital asset management in the State. Transportation has a long-term master plan, but no other agency does. The State has a rolling five-year capital program, and agencies submit their capital budget requests to the Division of the Budget, where they are assessed independently of each other and without an eye toward an overall capital agenda. The lack of a coordinated process and a comprehensive plan fuels spending. Because there is no overall envelope for total capital spending over a certain period and agency budgets are handled on an ad hoc basis, there are no explicit tradeoffs. Agency needs are not evaluated based on a total available amount or their relative priority in the overall picture. The State's experience with the SUNY/CUNY capital plan over the past decade illustrates the problem.

In 1998 the Legislature and Governor Pataki instituted a five-year planning process with SUNY. The five-year plans were supposed to detail expenses. However, after a few years the capital appropriation process began to drift. Eventually, no time frame, total amount, or pressure from other needs bound the process. SUNY was routinely requesting and receiving supplemental appropriations outside the planning framework. Consequently, although the original amount appropriated for the five-year plan for SUNY was $3.25 billion, the total amount appropriated in those years was $4.15 billion.[46] During the same period, the

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[44] *Ibid.*; p.30 based on "New York State Center of Excellence Progress Review;" Public Financial Management, 2006.

[45] This number may not be comparable to the ones reported by other state governments because it does not account for the depreciation of transportation infrastructure. New York City, for example, depreciates its transportation assets, and reports on all its capital assets (except land and construction) net of depreciation; the State has adopted an approach which does not depreciate transportation assets, and therefore, produces a larger value for infrastructure assets on its statements than if these assets had been depreciated yearly.

[46] The SUNY multi-year plan equaled $1.6 billion, the CUNY multiyear plan equaled $1.1 billion for senior colleges and $55 million for community colleges. $3.2 billion in appropriations has been added to the SUNY budget and $950 million has been added to the CUNY budget. State University Construction Fund, *SUNY Master Capital Plan Report*, http://www.sucf.suny.edu/project/mcp.shtml, accessed on September 24, 2007. State of New York, Division of the Budget, *2007-08 Executive Budget Capital Plan*, page 78. State of New York, *Education Labor and Family Assistance Budget Bill 2007-08*, SUNY and CUNY sections, (S 2103-D/A 4303-D), 2007.

Legislature flagged the fact that nearly 85 percent of SUNY's approximately 3,000 buildings were at least 20 years old. They called for a viable plan to address maintenance needs and hold SUNY more accountable for its capital planning. As part of the budget this year, SUNY agreed to submit a new five-year capital plan. The goal is for them to live within the amount allocated for the five-year plan and to return the process to a meaningful one.

In the last four years a new problem has emerged in the form of capital spending classified as "off-budget," meaning that the outlays are not included in the State budget. Funds need not be appropriated in the budget, because the outlays are made by public authorities whose budgets are set independently. But the capital outlays are funded with debt that is repaid by State appropriations for the debt service. These commitments have significant ramifications for the debt service costs the State will face in future years and will create additional pressures on the operating budget. From fiscal years 2004-05 to 2007-08 off-budget capital spending grew from $881 million to $2.7 billion.

If the State were to develop a more coordinated capital planning process to better reconcile competing needs, it is reasonable to assume that savings would accrue. Because of the way the State budgets, any potential savings would be experienced in the form of a reduced capital project funds budget and in the debt service fund. For example, if the State were able to shave 10 percent off the capital budget, then it would save $1 billion per year in avoided capital outlays and about $100 million per year in avoided debt service.[47]

8. Close Unnecessary Correctional Facilities

The Department of Correctional Services (DOCS) has an annual budget of $2.7 billion. It is responsible for 63,000 inmates at 70 facilities throughout the State. In the past two decades its mandate has been affected by significant changes in sentencing policy. The movement to "get tough" on crime by lengthening sentences and limiting judicial discretion increased the number of felons in custody, peaking at 71,466 in 1999. (See Table 6.) To deal with the rapid increase, DOCS facilities were used beyond normal capacity. In 1999 and 2000 DOCS opened two new maximum security prisons—Upstate and Five Points, respectively—and crowding was significantly reduced.

Since 1999 the prisoner population has decreased considerably. In August 2007 DOCS had custody of 63,614 inmates. Changes in the number of people incarcerated for drug-related crimes and 2004 revisions to the State's notorious Rockefeller Drug Laws have reduced the number of prisoners. In addition, DOCS continues to explore expanding drug treatment and alternatives to incarceration for inmates who could benefit from these options and be safely released to the communities.

Despite the reduction in the number of inmates, DOCS staffing has remained nearly stable. During the peak year of 1999 DOCS employed 32,246 people, and since then the number

[47] In fiscal year 2007-08 total on- and off-budget capital outlays are expected to equal $10,070 million. See Table 5 for sources and notes. Reducing this amount by 10 percent results in $1 billion in lower capital outlays. At an interest rate of 5 percent over 30 years bonds debt service savings are estimated to total about $100 million annually.

dropped by just 311. This represents a reduction of less than 1 percent during a period when the inmate population fell 11 percent.

To achieve savings facilities must be closed and the ones that remain open must be used to full capacity. However, legislative provisions limit the ability of DOCS to close facilities. Two changes in the correctional law in 2005 affecting prison facilities. The first required that one-year notice be given before closing any correctional facility. The law further stipulated that before facilities are closed the Commissioner must meet with certain other state agencies and labor unions to ensure that the closure will minimize impact on the state workforce and the local economy.

A second provision modified the pre-existing requirement for an adaptive reuse plan. The law originally required the development of a plan after a facility was slated for closure. The 2005 language requires that a reuse plan be developed six months *prior to* prison closure. The adaptive reuse plan must include the potential to use the facility for some other state purpose, the potential to sell the facility, the condition of the facility, and the investment needed to keep the facility in a state of good repair or to make it viable for other use.

Table 6
New York State Department of Correctional Services
Changes in Inmate Population and Employment
Fiscal Years 1994 to 2007

	Inmate Population		DOCs Employee Total	
	Number	Annual Percent Change	FTEs	Annual Percent Change
1994	66,758	3.4%	29,804	
1995	68,486	2.6%	30,709	3.0%
1996	69,647	1.7%	30,526	-0.6%
1997	69,106	-0.8%	31,013	1.6%
1998	70,001	1.3%	31,711	2.3%
1999	71,466	2.1%	32,246	1.7%
2000	70,153	-1.8%	32,486	0.7%
2001	67,375	-4.0%	32,768	0.9%
2002	67,394	0.0%	32,018	-2.3%
2003	66,745	-1.0%	31,155	-2.7%
2004	65,197	-2.3%	30,721	-1.4%
2005	63,698	-2.3%	31,005	0.9%
2006	62,661	-1.6%	31,882	2.8%
2007*	63,614	1.5%	31,935	0.2%
Total Reduction from 1999 Peak	**(7,852)**	**-11.0%**	**(311)**	**-1.0%**

Sources: Inmate data from State of New York, Department of Correctional Services, *Men and Women Undercustody: 1987-2001* , Department of Correctional Services, *Annual Undercustody Reports 2002-2006* . For 2007 data were reported directly from Department of Correctional Services on August 27, 2007. The FTE data from the Office of the State Comptroller, *Workforce Changes by Function and Agencies* .
Note:*FTE from April 2007, inmate population from August 2007.

In 2006 Governor Pataki proposed exempting correctional facilities from both the one-year notice rule and the adaptive reuse plan requirement in order to close Camp Pharsalia, a medium security work camp, and turn it over to the Office of Mental Health for the civil confinement of sexually violent predators. The legislature rejected the proposal and appropriated $5.2 million to keep Camp Pharsalia as a correctional facility.

In 2007 Governor Spitzer proposed establishing a prison closing commission modeled on the successful approach used for hospital infrastructure by the Berger Commission. The legislation met with resistance, however, and the idea died during budget negotiations.

The concept could be revived this year and a commission formed to close unnecessary prison facilities. The unfortunate truth is that in many communities prisons serve as a form economic development. This is inappropriate and places an unnecessary burden on

taxpayers. The size of prison infrastructure should be fitted to the population that needs it. Likewise, the costs for operating the system should be no more than is required to provide for the safety of guards and inmates. At an average per prisoner cost of $39,000, the care of 7,852 fewer inmates could result in savings of about $310 million.[48]

Additional facilities could be closed if DOCS were able to reduce its census of incarcerated individuals by more than the recent trend. This would require developing alternatives to incarceration for a greater share of prisoners. Expanded research staff would be required for DOCS to carefully pursue the options. In a 2000 study the CBC made three recommendations for shortening inmate sentences based on programs that were shown to be cost-effective: 1) apply boot camps and residential drug treatment approaches more broadly; 2) develop less extensive prison term options (such as home confinement with high tech bracelets) for certain categories of inmates, including property offenders and older inmates; and 3) improve and redesign parole programs by implementing a kiosk check-in system to shift parole officer duties to aiding parolees in gaining access to counseling, work placement and drug treatment programs.[49] These were estimated at the time to save about $100 million.

9. Streamline The Judiciary

The judiciary has been and will continue to be a major source of growth in State spending. It is the third branch of government, and the division of powers in the State constitution prevents the Executive from interfering overtly in judicial budget requests to the Legislature. However, the judiciary is managed by the Chief Judge, who also serves as the chief fiscal officer for the court system.

The New York State court system is said to be one of the largest and busiest in the Western World. It consists of nearly 1,300 state-paid judges, 2,300 town and village justices and approximately 15,000 non-judicial employees. Pursuant to the Unified Court Budget Act, the cost of operating the Unified Court System, excluding town and village courts, is borne by the State.

The administrative structure of the Unified Court System is complex. The system is comprised of the Court of Appeals, the Appellate Division with four departments, and 11 separate but overlapping trial courts. Because of population growth trends the 2nd Appellate department now includes half of the State's population (this department covers areas adjacent to New York City including Long Island and Westchester County). Trial courts include the Supreme Court (with branches in all 62 counties), County Courts, City Courts, District Courts, Family Courts and Town and Village Justice Courts among others.

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[48] See Citizens Budget Commission, *Making More Effective Use of New York State's Prison System*, June 2000, p. 15. In 1999 the CBC calculated that the per inmate cost, including debt service, was $32,232. Cumulative regional inflation for 1999 through 2005 period was 22.4 percent. Increasing $32,232 by inflation results in a current estimated per inmate cost of $39,451.

[49] See Citizens Budget Commission, *Making More Effective Use of New York State's Prison System*, June 2000, available at www.cbcny.org.

Because of the complex nature of the judicial system related cases often have to be heard by one or more court. The classic example is that of the couple going through a divorce (Supreme Court), battling over child custody (Family Court), where one spouse is also pressing criminal charges for domestic violence (Criminal Court). Each case must be brought before a different court, and the judge from one case is unlikely to have information about the person's other pending judicial matters.

Fulfilling her duties as chief fiscal officer and manager, Chief Judge Kaye prepared a comprehensive reform package in 1997. She proposed reconfiguring the state's major trial courts into a two-tiered structure, consisting of a Supreme Court and a statewide system of District Courts with limited jurisdiction. The reconfigured Supreme Court would have at least five divisions – family, commercial, probate, state claims and criminal – and more divisions could be established by the Chief Administrative Judge. The Supreme Court would have general jurisdiction over all civil, criminal and family matters. The District Court would have jurisdiction over misdemeanor criminal cases, housing cases, and civil cases involving claims of $50,000 or less. She also proposed the creation of a Fifth Judicial Department to relieve the caseload burden on the state's appellate court system and the elimination of the limitation on legislative authority to increase the number of Supreme Court Justices.

The Legislature made several changes to the 1997 package, but then it failed to approve the revised plan. In 2002 Judge Kaye modified the plan, but again no legislative action was taken. She was, however, able to make some changes in Family Court operations to streamline services. Family Courts were authorized to deal with housing and child support issues along with divorces to create a kind of one-stop shopping for families experiencing difficulty.

To gain traction for court modernization (and address the need for judicial pay increases) Judge Kaye appointed the *Special Commission on the Future of the New York State Courts* in 2006. The final recommendations of the Commission were submitted to State leaders this year .and they became legislation introduced by Governor Spitzer in May 2007. Many of the major components of the 2007 reforms are the same as those first proposed in 1997. After its submission the legislation was referred to the Attorney General for opinion where it remains today.

The special commission estimated that the restructuring proposal would save $59 million annually through reductions in administrative costs at the Office of Court Administration.[50] If used for other needs, such as helping offset the recently added costs of improving town and village courts, this would replace funds the State would otherwise need to spend on the judiciary.

[50] Special Commission on the Future of New York State Courts, *A Court System for the Future: The Promise of Court Restructuring in New York State*, February 2007, Appendix II, page 111-124, available at http://www.nycourts.gov/reports/courtsys-4future_append2007.pdf. This net savings figure includes a $1.9 million cost for judicial salary equalization.

SUMMARY OF OPTIONS

If the State were to implement all these options, then $5.4 billion could be saved in annual State spending. (See Table 7.)

Table 7
Summary of Savings Options for New York State
(dollars in millions)

Option	Estimated Annual Savings
Eliminate School Aid to the Wealthiest Districts	**$334**
Continue to Restructure Medicaid Programs	**$1,988**
Pay more competitive institutional rates	*860*
Hospitals	125
Nursing Homes	735
Close eligibility loop-holes in long-term care	*454*
State recovery on spousal refusal	45
Look-back on home care and lower home value exemption	409
Reduce excessive utilization of home care	*433*
Expand Managed Care to High-Cost Populations	*241*
Employee and Retiree Fringe Benefit Restructuring	**$1,138**
Health insurance changes	*714*
Higher premium for employees with family coverage	75
Higher premium for retirees and elimination of Part B reimbursement	639
New Tier on the pension system when fully implemented	*424*
Increase Employee Work Week to 40 Hours	**$227**
Streamline purchasing, back office functions, human resources, and payroll processing	**$333**
Eliminate or Restructure Ineffective Economic Development Programs	**$802**
Empire Zones	*558*
Centers of Excellence	*244*
Develop a Comprehensive Capital Plan to Help Provide Spending Discipline	**$100**
"Rightsize" Operations at the Department of Correctional Services	**$410**
Close unneeded facilities	*310*
Implement additional successful alternatives to incarceration	*100*
Streamline the Judiciary	**$59**
TOTAL	**$5,391**

Source: Citizens Budget Commission staff analysis