Review of the New York State Fiscal Year 2009-10 Budget

The New York State Legislature completed its work on the New York State fiscal year 2009-10 budget on April 3, 2009. The nine bills that comprise the budget were delivered to Governor David Paterson, who signed them on April 7. The State Division of the Budget (DOB) reported on the enacted budget on April 28. The CBC staff reviewed the budget bills and DOB report, and prepared this assessment.

The key points are:

- Spending remains high and few cuts were achieved.
- No concessions were agreed to by public employee unions.
- Large tax and fee increases help support the enlarged spending.
- Temporary federal stimulus aid is relied upon to sustain recurring spending commitments, creating a risk of large future budget gaps.
- A few positive steps were taken to reduce wasteful or poorly targeted programs.

The fiscal year 2009-10 budget was adopted in the midst of the nation's worst economic conditions since the Great Depression of the 1930s. The combination of existing budget gaps and severe revenue losses created a budget gap of unprecedented size – fully $17.9 billion. The budget crafted in response to these difficult circumstances can be characterized in terms of five key features.

1. High spending. All Funds spending in fiscal year 2009-10 is expected to total $131.9 billion, an increase of $10.3 billion or 8.5 percent over last fiscal year. (See Table 1.) This is a greater rate of increase than in many previous years when times were better. Although the federal stimulus package mandates significant spending increases for some items, State leaders failed to lower spending in General and State Operating funds to respond to the crisis. These spending levels will ultimately be unsustainable, and the failure to take action this year will necessitate more precipitous and potentially damaging spending cuts in the future.

Table 1
New York State Spending Changes, Fiscal Year 2009-10
(dollars in billions)

	Fiscal Year		Change	
Fund	2008-09	2009-10	Amount	Percent
General Fund	$54.6	$54.9	$0.3	0.5%
State Operating Funds	78.2	78.7	0.5	0.6%
All Funds	121.6	131.9	10.3	8.5%

Source: State of New York, Division of the Budget, *2009-10 Enacted Budget Financial Plan*, April 28, 2009. All figures are on a cash basis.

Spending reductions in the budget lowered the total from baseline estimates by $3.2 billion – just 18 percent of the overall gap-closing package. (See Table 2.) Of this amount, about $1 billion is

from initiatives that lower recurring Medicaid spending, and $2.2 billion is from all other areas of spending.

Table 2
Closing the Budget Gap
New York State Fiscal Year 2009-10 Enacted Budget
(dollars in billions)

	State's Classification 2009-10 Gap-Closing Actions	CBC Classification 2009-10 Gap-Closing Actions	Difference
Budget Gap Before	**($17.9)**	**($17.9)**	**$0.0**
Recurring Revenues	5.3	8.1	2.8 *
Spending Reductions	6.0	3.2	(2.8) *
Medicaid	2.0	1.0	(1.0)
Other	4.0	2.2	(1.8)
One-shots	1.0	1.0	-
Use of federal aid	5.6	5.6	-
Budget Gap After	**-**	**-**	**-**

Notes:
* Measures recategorized from the revenue to the spending total include $1.5 billion in cancelled STAR tax rebates, $850 millionin taxes on health insurance, and $400 million in tuition and motor vehicle fee hikes.
Source: State of New York, Division of the Budget, *2009-10 Enacted Budget Financial Plan* , April 28, 2009.

Many spending restraint measures proposed by the Governor in the Executive Budget were not enacted. For example, legislative actions halved the Governor's original Medicaid cost-containment proposals. (See Table 3.) For hospitals the Legislature rejected 56 percent of the Governor's proposed cuts, enacting $306 million in rate reductions. Nursing homes will experience $225 million in rate reductions with the Legislature rejecting 43 percent of the Governor's proposed cuts. In personal care the Legislature rejected 64 percent of Governor's proposed cuts, enacting $28 million in reductions. The remaining $448 million in Medicaid savings came from a $175 million fraud reduction initiative, $165 million from increased utilization of managed care, and about $108 million in pharmacy cost controls and small cuts to multiple public health programs.

Table 3
Medicaid Spending Changes
New York State Fiscal Year 2009-10 Enacted Budget
(dollars in millions)

Initiative	Executive Budget Proposal	Enacted Budget Action	Difference Amount	Difference Percent
Hospital Rate Reductions	$700	$306	($394)	-56.3%
Nursing Home Rate Reductions	398	225	(173)	-43.5%
Home Care Rate Reductions	189	68	(121)	-64.0%
Pharmaceutical Savings	99	28	(71)	-71.7%
Fraud Reduction	125	175	50	40.0%
Utilization & Managed Care	108	165	57	52.8%
Miscellaneous	110	80	(30)	-27.3%
Total	**$1,729**	**$1,047**	**($682)**	**-39.4%**

Source: State of New York, Divison of the Budget, *Governor Paterson Announces Enacted Budget Agreement Includes Major Reforms to New York's Health Care System, Record Savings for Taxpayers*, March 29, 2009.

Other Medicaid items—notably the ones less likely actually to produce the targeted savings—were significantly increased. Fraud reduction was increased 40 percent or $50 million; utilization and managed care, problem areas for the State, were increased 53 percent or $57 million.

The actual $3.2 billion in spending restraint contrasts with the claim from State leaders that they reduced spending by $6.0 billion. While budget actions totaling $2.8 billion lower general fund outlays, they represent real cost increases for New Yorkers and should be counted as revenue raisers. The largest of these measures are the cancellation of the School Tax Reduction (STAR) payments valued at $1.5 billion, and $850 million in new or increased taxes on health insurance companies. Tuition increases for the public universities generating $122 million also are revenue increases that are officially reported as reductions in general fund spending.

2. No concessions from public employee unions. In his Executive Budget Governor Paterson proposed adding a new tier to the public employee pension system with less generous benefits for future hires, dropping the final 3 percent raise in the granted in the multi-year contracts under which most State employees work, requiring an additional sliding scale contribution for retirees for health insurance coverage based on years of service, and reducing the reimbursement for retirees for Medicare Part B premiums. Together these items were expected to save $209 million in fiscal year 2009-10 and more in future years. The Governor also proposed reducing the size of the State workforce by 3,108 positions by consolidating some agencies. All these measures were rejected by the labor unions and the Legislature.

To achieve savings in lieu of the savings from the rejected proposals, the Governor has announced that he plans to layoff 8,700 employees beginning in July. This will reduce the workforce to 190,700. To put these reductions in perspective, during the last brief downturn in

2003-04 the workforce was 187,365, fully 3,335 positions smaller than it will be after this round of reductions. The personnel actions are expected to save $170 million in fiscal year 2009-10.

3. A heavy reliance on new taxes and fees. Given their limited effort to reduce spending, State leaders were obliged to rely heavily on revenue raising measures. As shown earlier in Table 2, such measures totaled $8.1 billion.

Largest among the recurring revenues is the increase in rates for higher income brackets under the personal income tax; this is estimated to raise $3.9 billion. (See Table 4.) Two new brackets were created; single filers with incomes of $200,000 and $500,000 have their tax rate rise from 6.85 percent to 7.85 percent and 8.97 percent, respectively. For joint filers the thresholds are $300,000 and $500,000. The new rates expire in three years. Because the new rates affect only the highest income levels, they will increase New York's already heavy reliance on a small group of earners at the high end of the income scale, and exacerbate the overall volatility of the New York tax system. In addition, the earnings of these high earners are not assured, and the amount of revenue anticipated from the tax may be too high.

Table 4
Revenue Increases
New York State Fiscal Year 2009-10 Enacted Budget
(dollars in millions)

Personal Income Tax rate increases	$3,948
Middle Class School Tax Relief (STAR) rebate cancellation	1,539
Health insurance company assessments	857
Utility tax	547
Tax compliance program	273
Limit deductions for taxpayers with income above $1m	140
Tuition increases	122
Bottle Bill	115
Empire Zones	90
Vehicle registration fees	61
Fees on partnerships	50
Auto insurance fee	48
Captive insurance companies	31
Sales tax on transportation	26
Increase bond issuance charge	20
Application fee for retailers of cigarettes and increased fines for non-compliance	19
Miscellaneous fee and tax increases below $15 million each*	201
Total	**$8,087**

Notes:
* There are 36 such measures.

Source: State of New York, Division of the Budget, *2009-10 Enacted Budget Financial Plan*, April 28, 2009.

4. Too much reliance on short-term federal aid. To help address the severe national economic downturn, the President and Congress authorized a major new program in February that provides aid to states. The total federal stimulus package for New York is expected to be $24.6 billion over 27 months, about $14.0 billion of which is for fiscal stabilization and $10.6 billion for infrastructure investments. The purpose of this aid is to prevent states from having to take actions harmful to regional economies. Since New York is the epicenter of the financial services meltdown and bears much downside risk in its revenue forecast, the intent was that State leaders use the federal funds to create a path to a more sustainable long-term spending level.

The fiscal year 2009-10 budget relies on $13.3 billion of these funds. About $6.1 billion is used to close the budget gap, largely by supporting general fund spending; $7.2 billion was added to the all funds budget for infrastructure projects, food stamps, unemployment assistance, and welfare grants. An additional $1.3 billion in federal funds were spent from the fiscal relief component of the stimulus package during the final three months of fiscal 2008-09. This means that State leaders have already spent $14.6 billion in federal stimulus funds, more than half of the total slated for New York.

While the capital funds were intended to be incremental spending for infrastructure, the $7.4 billion in federal stabilization aid should have been used primarily as a substitute tax and fee increases, not as a substitute for the kinds of spending changes that will be needed when the funds run out. State leaders have only postponed the inevitable. The disappearing federal aid and the expiration of the personal income tax surcharge help to create a budget gap of $13.7 billion to address in just three years.

A similar problem arises from the use of federal funds specifically provided for school aid. While the Governor's Executive Budget proposed school aid reductions of $700 million, these actions were reversed and $1.4 billion was added in the adopted budget, supported by $2.1 billion in federal funds. Aid for school year 2009-10 will reach $22.8 billion. After the federal funds expire it is likely that school districts will be forced to make harsh cuts, as annual increases of this magnitude are likely unsustainable.

5. A few positive notes. Although largely unresponsive to the dire fiscal circumstances New York faces, the budget did contain a few positive initiatives. The Legislature dropped the Middle Class STAR rebate program which was poorly conceived, expensive, and inadequately targeted to provide property tax relief where it is most needed. The Empire Zones program was reformed. Firms abusing the program will be removed, and remaining firms will be required to generate a return at least equal to the tax benefits they receive through the program. Most significantly, the sunset date on the program was accelerated from 2011 to 2010 providing an earlier opportunity to close it down to new entrants.

In addition, some of the State's underutilized correctional infrastructure will be closed. Three of the four prisons the Governor proposed closing will be closed at dates certain and without the elaborate community review process that had been required in the past. Also, several juvenile detention facilities that were running at 20 percent occupancy or less will be closed. Rockefeller drug law reform, contained in the budget this year, will cause further decline in the incarcerated population; this will permit more downsizing of correctional facilities in the near future.