CITIZENS BUDGET COMMISSION

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Dear Legislator:

I write to convey the Citizens Budget Commission's (CBC's) recommendations for legislative action on the New York State Executive Budget for Fiscal Year 2021.

This year's budget is notable because it must close sizable budget gaps even though New York continues to benefit from a ten-year economic expansion. These gaps totaled $4.0 billion in the current year and $7.1 billion in fiscal year 2021. Over five years, the gaps totaled $38.6 billion, of which more than $18.0 billion was due to previously unbudgeted Medicaid spending.

The Executive Budget rightly eschews tax increases and primarily relies on spending restraint and higher-than-expected revenues to close the gaps. With the strong exception of permanently delaying $1.9 billion in Medicaid payments, the Executive Budget approach is appropriate since the gaps are driven by unsustainable spending growth rather than revenue losses.

It also is a strategy that helps maintain New York's competitiveness, given New York's already high taxes and the ongoing risk presented by the 2017 federal cap on the deduction of state and local taxes. Furthermore, raising taxes during an economic expansion makes it even more challenging to consider such a strategy when New York inevitably endures a recession. In this way, the Executive Budget's approach helps preserve the State's ability to protect New Yorkers in bad times, as well as good ones.

The largest component of spending restraint is in Medicaid, which is reasonable since Medicaid spending is responsible for a significant portion of the gap; however, there is considerable risk in relying on $2.5 billion

in Medicaid savings that are yet to be determined. Medicaid reductions need not compensate for the entire Medicaid-related gap if other options would minimize negative impacts on New Yorkers. The best strategy to pursue in enacting a budget prioritizes:

- Medicaid spending control that does not shift costs to local government;
- Education aid increases that are limited only to districts that currently lack revenues to fund a sound basic education;
- Building rainy day reserves to the extent possible to prepare for economic uncertainty; and
- Maintaining competitiveness by not increasing taxes.

Restrain State Medicaid spending without shifting costs onto local governments

Support appropriately targeted, prudent, and publicly vetted spending controls recommended by the Medicaid Redesign Team (MRT). Developing the required magnitude of savings in a short time will be challenging, but it is imperative for the MRT to be successful. The MRT should examine high growth areas and spending where New York historically is an outlier. This includes, but is not limited to, long-term care, personal care, and home care, which may benefit from tightened eligibility as well as other reforms. The MRT should identify ways to improve efficiency and minimize reductions in services, including savings from care redesign and labor productivity from work rule and benefit changes. Previous CBC work also has identified potential savings from better targeting the Health Home program and Medicaid supplemental payments.

During its first meeting, the MRT announced final recommendations would be voted on at the mid-March meeting. The MRT should abide by this timeline and provide ample details on proposals to allow the public and Legislature to vet the proposed recommendations prior to including them in the Enacted Fiscal Year 2021 Budget.

Reject increase in local Medicaid share. New York historically has been a national outlier in the significant amount it requires local governments to contribute to Medicaid. One of this Administration's great achievements was to cap the growth in the local share of Medicaid. This should not be reversed. Counties and New York City have very limited control over the program and should not be saddled with absorbing program growth: the federal government and the State set reimbursement rates and eligibility standards, which are the main drivers of spending. Local governments should manage their responsibilities well, work with the State to root out waste, fraud and abuse, and contribute ideas to curtail spending growth. Implementing this will require data sharing, cooperation, and communication.

Eliminate the annual Medicaid payment deferral. The State should make efforts to eliminate the Medicaid deferral that was initially implemented at the end of fiscal year 2019. By deferring March bills into the next fiscal year in perpetuity, the State not only papers over a problem but sets a precedent of fiscal irresponsibility.

Limit increases in education aid to those needed to fund a sound basic education and improve the Foundation Aid formula

Target school aid to underfunded districts. Limiting increases in school aid, which comprises 27 percent of the State operating budget, would restrain budget growth. CBC analysis shows the State could support a sound basic education in ***every*** district by increasing school aid by approximately $75 million— if targeted only to underfunded districts. Limiting school aid increases to only these high-need districts would save more than $750 million from the Governor's proposed $826 million increase.

Do not undermine Foundation Aid progressivity by layering on less progressive forms of aid. The Executive Budget permanently folds ten education aid streams totaling $1.8 billion into Foundation Aid, but preserves their previous allocation methods rather than targeting them based on need. Several of these funding streams disproportionally benefit wealthier districts, and adding them without reforming them will

reduce the progressivity of Foundation Aid. These ten aids should instead be folded fully into an improved Foundation Aid formula that distributes all aid based on need, and appropriately accounts for student need and district ability to provide local resources.

Avoid tax increases

Avoid tax increases, including health care taxes. Revenue collections are strong, projected to yield $1.0 billion more to help close the fiscal year 2020 deficit and $2.1 billion more in fiscal year 2021. The millionaire's personal income tax surcharge that was initially implemented during the last recession continues in effect, and last year the State increased taxes on real estate transfers in New York City for the benefit of the Metropolitan Transportation Authority. New York's share of the very wealthy is already declining, and the State relies heavily on high earners; the top 1 percent of personal income tax filers pay 37 percent of the personal income tax revenues—1 out of every 5 dollars of State operating spending.[1] In addition to personal income taxes, New Yorkers are also burdened by high taxes on health insurance with various surcharges increasing costs for family coverage by more than $1,000 annually.[2] The State should not increase taxes on health care which would make health insurance less affordable.

Prepare for the next recession by building reserves

Increase deposits to rainy day funds. Despite a thriving economy, New York State's rainy day funds are still woefully inadequate. In contrast, other states have bolstered significantly their reserves; for example, California has set aside reserves equal to 12.4 percent of annual general fund expenditures, far greater than New York's 2.8 percent.[3] If the State makes the planned $428 million deposit at the end of this fiscal year, rainy day reserves will have grown by $678 million since fiscal year 2018. This is a positive step, but it is insufficient: The $34 billion three-year revenue shortfall experienced during the average recession would dwarf the State's reserves. Greater reserves are critical if the State is to weather an eventual economic downturn without harmful spending cuts or counterproductive tax increases.

In addition, CBC makes the following recommendations:

Enact Executive Budget proposals to:

Rationalize retiree health insurance contributions. New York State's other postemployment benefits (OPEB) liability, the cost to provide health insurance benefits to State retirees, was $65.1 billion in fiscal year 2019—about $3,345 per resident.[4] The Executive Budget proposes to reduce this liability by prospectively implementing a tiered retiree health benefit based on years of service for future employees; eliminating the reimbursement of the Medicare Part B surcharge for high-income retirees; and capping Medicare Part B premium-sharing. Implementing these reforms would reduce OPEB liability by $8 billion and reduce budget costs by $48 million annually by fiscal year 2023.[5]

Expand Design-Build authorization. One way to reduce the high cost of some public construction projects is to expand the use of design-build, which allows for consolidating the design and construction bidding

process. New York already has successfully utilized this process, and the State should adopt the Governor's proposal to expand it to other state agencies and to information technology systems.

Extend rational tuition policy at the State University of New York (SUNY) and the City University of New York (CUNY). In 2011 New York implemented a new tuition policy for SUNY and CUNY. This policy introduced a rational and predictable tuition plan and a commitment to maintain State financial support to public universities. SUNY and CUNY tuition rates remain lower than other states' public institutions; incremental tuition increases will not endanger New York's ability to attract students. The Executive Budget would re-authorize increases of up to $200 per year for four years.

Modify Executive Budget proposals in order to:

Further reduce the film tax credit. Since the enactment of the State film tax credit in 2004, the State has authorized $7.3 billion in subsidies to the film and television industry. The Executive Budget proposes to decrease the share of expenses that may be granted as a refundable tax credit from 30 percent to 25 percent in most instances, while increasing the total allocation by another $420 million. This small step in the right direction should be a first step that begins the credit's full elimination by decreasing the share of eligible expenses in 5 percentage point increments until it is completely phased-out.

Evaluate the cost-effectiveness of Excelsior Jobs program before granting long-term expansion. The Executive Budget proposes to extend the Excelsior Jobs Tax Credit program by 15 years and expand benefits for certain "Green Projects." CBC has previously praised Excelsior as a model of pay-for-performance economic development programs, but before granting a long-term extension and expanding the program, the program should be evaluated, preferably by an independent firm whose work would include, at a minimum, a comparison to other New York programs and similar programs in other states.

Adopt a five-year Department of Transportation (DOT) capital program based on a comprehensive statewide capital planning process. The Executive Budget proposes a two-year DOT capital program, a reduction from the typical five-year capital program. Rather than decreasing planning horizons, the State should enact provisions similar to those passed by the Legislature in 2019 (but vetoed by the Governor) to implement a rigorous capital planning process for DOT.[6] Enacting best practices for capital planning and programming will support more effective investments in the State's transportation infrastructure based on best practices.

Reject Executive Budget proposals that would:

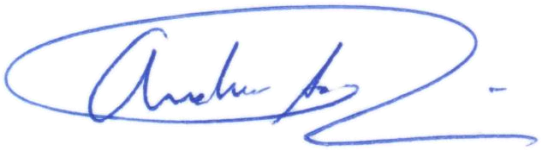
Expand Executive authority. The Executive Budget proposes to expand Executive authority by allowing the Division of the Budget to unilaterally increase spending on specific programs, while limiting the ability of the Office of the State Comptroller to exercise its constitutional duty to report on State spending. These changes should be rejected.

Shift costs onto local governments. In addition to rejecting the Medicaid cost shift, the Legislature should reject shifting costs for Temporary Assistance for Needy Families onto New York City and special education out-of-district placement costs onto school districts outside of New York City.

Discourage the purchase of long-term care insurance: Given Medicaid's rising long-term care costs the State should not remove incentives for New Yorkers to acquire long-term care insurance.

Thank you for considering CBC's recommendations. As always, my staff and I are happy to answer questions or discuss these issues.

Sincerely,



Andrew S. Rein
President
Citizens Budget Commission

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[1] United States Census Bureau, "Individual Income and Tax Data, by State and Size of Adjusted Gross Income, 2017"(SOI Tax Stats, January 16, 2020), https://www.irs.gov/statistics/soi-tax-stats-historic-table-2#main-content, and 2010 edition.

[2] This value represents the estimated statewide average impact of the Health Care Reform Act (HCRA) Surcharge and HCRA Covered Lives Assessment on average employer-sponsored family plan premiums and gold-rated premiums sold on the New York State of Health marketplace. Estimates are based on rate filings of commercial plans for 2020. Surcharge impacts are calculated by applying the HCRA Surcharge commercial rate of 9.63 percent to the portion of rates associated with hospital costs reported in the unified rate review exhibits. Covered Lives Assessment impacts are estimated by applying region-specific rates to approved rates approved by the Department of Financial Services for each plan. Increased health insurance premiums and taxes are generally passed to employees in the form of reduced wages or are paid directly by those purchasing coverage. These estimates will be presented as part of forthcoming research by CBC on the impacts of HCRA. See: New York State Department of Financial Services, "Rate Applications by Company" (accessed January 26, 2020), https://myportal.dfs.ny.gov/web/prior-approval/rate-applications-by-company; New York State Department of Health, "2020 Covered Lives/Assessments/Surcharges" (December 2019), www.health.ny.gov/regulations/hcra/gme/2020_surcharges_and_assessments.htm; Section 2807-j of the Public Health Law; and Katherina Baciker and Amitabh Chandra, *The Labor Market Effects of Rising Health Insurance Premiums* Working Paper 11160 (National bureau of Economic research, February 2005) www.nber.org/papers/w11160.pdf.

[3] Office of the New York State Comptroller, *The Case for Building New York State's Rainy Day Reserves* (December 2019), p. 10, https://osc.state.ny.us/reports/budget/2019/rainy-day-reserves-2019.pdf.

[4] Office of the New York State Comptroller, *Comprehensive Annual Financial Report Fiscal Year 2019* (September 1, 2019), https://www.osc.state.ny.us/finance/finreports/cafr/2019-cafr.pdf.
[5] New York State Division of the Budget, *FY 2021 New York State Executive Budget Public Protection And General Government Article VII Legislation Memorandum In Support* (January 21, 2020), p. 21-24, www.budget.ny.gov/pubs/archive/fy21/exec/artvii/ppgg-memo.pdf.
[6] CBC supported these changes. See: Andrew S. Rein, Citizens Budget Commission, letter to The Honorable Andrew M. Cuomo, (November 11, 2019), https://cbcny.org/advocacy/cbc-urges-governor-sign-a4880s1673-improve-capital-planning.