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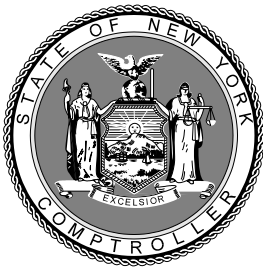
# 2002-03 Budget Analysis

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## Review of the Enacted Budget

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June 2002



**H. Carl McCall**  
**State Comptroller**

State of New York  
Office of the State Comptroller  
Office of Fiscal Research & Policy Analysis  
Albany, New York 12236

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H. CARL McCALL  
STATE COMPTROLLER



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STATE OF NEW YORK  
**OFFICE OF THE STATE COMPTROLLER**

June 2002

*To the People of the State of New York:*

The State began the 2002-03 fiscal year without an enacted budget for the 18<sup>th</sup> consecutive year. The final plan was created with minimal involvement from the public and from rank-and-file legislators. The conference committee process that was created in 1995 was a positive step toward meaningful reform, but was not used or even considered in this year's process.

The enacted budget spends \$89.6 billion, an increase of 6 percent over last year and 1 percent over the Executive's proposal. The increase comes after an additional \$1.4 billion receipt shortfall, as reported in April, on top of the Executive's January estimated revenue shortfall of \$6.8 billion for fiscal years 2001-02 and 2002-03. The increased spending relies on over \$4 billion in nonrecurring revenues and fund raids. In addition all available reserves were tapped.

The State should have more aggressively seized opportunities during the economic strength of recent years to prepare for fiscal downturns by creating meaningful reserves, reforming the budget process, and paying down the highest debt load in the country. The over-reliance on one-shots and lack of reserves makes future budgets particularly challenging.

Clearly, much remains to be done. The problems ignored in the past have taken on increased urgency. Now more than ever before, New York needs to end its short-sighted approach to governing and develop a long-range plan to address those challenges—current and future—so that New Yorkers of all ages can prosper and enjoy the vast opportunity this State has the potential to offer.

Sincerely,

A handwritten signature in black ink, appearing to read "Carl McCall".

H. Carl McCall  
State Comptroller

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## ***EXECUTIVE SUMMARY***

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### **Overview**

All Funds spending increases by 6 percent, or \$5.1 billion, to \$89.6 billion. General Fund spending decreases 2.4 percent to \$40.2 billion. However, General Fund spending is understated by more than \$1.5 billion due to the shift of certain spending needs to non-general funds.

### **Multiyear Impact of the Budget**

While the budget as presented by the Division of the Budget is balanced, it relies on fiscal gimmickry and dubious funding streams that may not materialize. As such, out-year gaps reported in the proposed budget of \$2.8 billion and \$3.3 billion for 2003-04 and 2004-05, respectively, will likely be significantly higher. The budget utilizes over \$1.7 billion in reserves, leaving only \$716 million for future needs. Furthermore, the enacted budget includes over \$4 billion in non-recurring actions – 10 percent of total General Fund spending – resources that will not be available next year.

### **Reserves**

The budget uses over \$1.7 billion in reserves, including \$185 million set aside for previously enacted tax cuts, leaving only \$710 million in the Tax Stabilization Reserve Fund and \$6 million in the Contingency Reserve Fund for future needs. The Tax Stabilization Reserve Fund, the State's only true "rainy day" fund, contains only 1.8 percent of General Fund receipts, compared with a national average of over 5 percent.<sup>1</sup> Recent events, including the attacks on the World Trade Center and the national recession, enforce the need for considerable reserves. While the State is able to utilize a significant amount of reserves for current year needs, the vast majority of those funds are not restricted reserves but revenues resulting from Wall Street surpluses rolled over from prior years.

### **Education**

A \$420 million, 3 percent increase in school aid is provided, produced by small increases in operating aids, restoration of reimbursement formulas for BOCES and special education services, and other changes. The universal pre-kindergarten and class size reduction programs are once again frozen. While the budget's increase will help ameliorate property tax increases in some districts, no attempt is made to reform school aid or address issues raised in the Campaign for Fiscal Equity (CFE) lawsuit. In fact, the budget provides greater increases to rich districts (6.5%) than to poor ones (2.75%).

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<sup>1</sup> According to the National Association of State Budget Officers "Fiscal Survey of the States - May 2002," there are 43 states with budget stabilization reserve funds holding an average of approximately 5.5 percent of state General Fund revenues.

Although the Legislature rejected the Executive's proposal to withhold one third of students' TAP awards until graduation, the budget still delays approximately \$60 million in TAP payments to colleges. Both the State and City university systems are provided with virtually flat funding, forcing universities and colleges to again face the need to increase fees, or reduce services. While college opportunity programs that were cut in last year's "bare bones" budget are restored this year, they are still provided the same funding as 1994, a loss of 30 percent after considering inflation. Community colleges are provided a small increase of \$50 per student.

## **Health and Social Services**

The budget includes a 3 percent cost-of-living adjustment for certain health and human services workers that were left out of the January health legislation. The impact of the 6 percent tax on nursing home revenues that was enacted in January is partially mitigated by exempting Medicare receipts. However, many families will continue to face higher bills for their loved ones because the tax is still levied on private payments. Important funding like HCRA and TANF intended for health care and social services is increasingly being used for budget relief. This year budget relief from these programs exceeds \$3 billion. Unfortunately, the budget also fails to extend the Community Reinvestment program which dedicated savings realized from institutional closings to community-based mental health services.

## **Environment**

The enacted budget fails to provide Superfund authorization or funding to continue needed projects across the State, and also raids \$64 million in funds earmarked for Superfund. Furthermore, the budget relies on \$200 million in funding "loaned" from the Environmental Protection Fund (EPF). Last year, EPF funds went unused and Superfund went unchanged in light of dysfunctional budget negotiations. The enacted budget provides Superfund with \$11 million to cover existing staff costs only.

## **Revenue Actions**

The enacted budget includes approximately \$140 million in new fees, including \$38 million from an additional \$0.50 surcharge on cell phones with an option for counties to charge another \$0.30 for local needs. Bond issuance fees paid to the State by public benefit corporations will increase by \$115 million, thus increasing costs for borrowers, including schools and not-for-profit organizations. Additional taxes on non-cigarette tobacco products are projected to generate \$27 million. New York City was granted authorization to increase its cigarette tax by an additional \$1.42, bringing the tax to \$1.50, generating an expected \$250 million to be split between the City and State. Projected revenues also include \$175 million from a tax amnesty program and nearly \$4 billion in non-recurring revenue. All told, the budget relies on approximately \$4.5 billion in non-recurring resources, fees, and reserves - 11 percent of General Fund spending.

The budget provides a number of back-loaded tax cuts, with only \$59 million affecting the 2002-03 financial plan and \$24 million in 2004-05. Ten Empire Zones (four previously authorized and six new), an income tax waiver for families of the victims of the World Trade Center attacks, three sales tax free periods in lower Manhattan, and a STAR cost of living increase for seniors are included.

### **Local Governments**

The budget provides no additional funding for municipalities across the State, while cutting \$6.1 million in Supplemental Municipal Aid to towns and villages. While the budget continues to provide \$22 million in unrestricted aid to counties, it will not be enough to cover recent health policy changes that could potentially cost counties more than \$300 million over the next three years.

### **Debt and Capital**

Although there is minimal financial plan impact in 2002-03, the budget includes over \$3 billion in new debt authorization including over \$1 billion for local initiatives that will provide no appreciable State asset, thus continuing the trend that began with the Community Enhancement Facilities Assistance Program (CEFAP) and the Strategic Investment Program (SIP). While all of these programs are intended to provide targeted economic development to localities around the State, a more comprehensive way of promoting growth should be pursued.

The budget also provides a new tool for managing debt by authorizing the issuance of variable rate debt and interest rate exchange agreements for all entities authorized to issue State-supported debt. Variable rate debt and income tax-backed revenue bonds are expected to lower costs for State debt. Although income tax-backed revenue bonds have been rated the same as the State's General Obligation Debt, actual savings for such a structural change is still unclear. Nonetheless, these changes continue to pull new debt away from voters as backdoor, authority-issued debt becomes the norm.

## ***OVERVIEW OF THE ENACTED BUDGET***

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The budget process in New York continues to be dysfunctional. A recap of recent budget events demonstrates the need for meaningful budget reform:

- Last year the Governor walked away from budget negotiations completely. On August 3, 2001, the Legislature out of sheer frustration was forced to pass a “baseline budget” that was primarily based on the budget submitted by the Governor in January. Although the budget rejected some of the Governor’s reduced funding for Medicaid and education building aid, it failed to meet the funding needs of school districts, social services, local governments, and others. The hope was that this action would bring the Governor back to Albany to work out an improved plan. The Governor initiated a lawsuit against the Legislature charging that it lacked the authority to construct the baseline budget in the manner that it did. This litigation continues today.
- Budget paralysis and an already weak economy were further compounded by the September 11 terrorist attack on the World Trade Center that stunned the nation and resulted in an unfathomable human toll. On October 24, 2001, a supplemental budget was passed that provided some restorations of nonprofit funding, education, and economic development. These were funded by delaying payments to school districts, retroactively changing laws to avoid paying tax refunds to the Tennessee Gas Pipeline, and using federal welfare monies to pay for General Fund programs. The big news in the supplemental budget was the authorization of six casinos, multistate lottery games, and video lottery machines at racetracks. Instead of longer-term, thoughtful and meaningful fiscal leadership and an economic rejuvenation plan, this supplemental budget placed all bets on gambling.
- Before the Governor even submitted his proposed 2002-03 budget to the Legislature, he proposed a far-reaching, three-year health care proposal and insisted that it be acted upon without the context of the overall financial budget picture. A multibillion dollar package was passed in January that provided funding for health care workers’ salaries, Medicaid coverage for women diagnosed with breast cancer through the CDC, Medicaid coverage for the disabled, increased Medicaid funding for community health centers, and a foundation to improve health care and simplify the health insurance program enrollment process. However, funding for these laudable health purposes is shaky because the plan relies on non-recurring proceeds from the conversion of Empire to a for-profit insurer, an uncertain and unlikely multiyear increase in the federal share of Medicaid (FMAP), a new tax on nursing homes, and the use of dedicated health care funds for General Fund budget relief.
- When the Governor constructed his proposed budget in January, he estimated a multibillion-dollar revenue shortfall for fiscal year 2002-03 related to the WTC attack and the slowing economy. His proposed budget flatlined education funding for

schools, cut the Tuition Assistance Program (TAP), and relied on nonrecurring resources, uncertain revenues, dedicated fund raids, increased borrowing, and the use of all available reserves. The impacts of a shortfall in April tax collections and federal tax law changes were estimated by the Governor to result in an additional budget gap of \$1.4 billion. The enacted budget restored some of the Governor's cuts in programs like school aid, TAP, and AIDS/HIV spending.

- Unfortunately, the recently enacted budget continues to illustrate a lack of leadership in constructing long-term creative solutions to the challenges that face New York. Clearly, economic weakness and the repercussions of the terrorist attack justify resorting to some short-term fixes for the current year in order to fund priority areas such as education and health care. However, this budget is overly reliant on non-recurring revenue sources and debt, with no accompanying longer-term plan to address the fiscal imbalance that the State will face next year and beyond.

The remainder of this section will provide a summary description of the State budget, focusing on the financial plan and changes from the Executive Budget.

### Overall State Spending

According to the financial plan released by the Division of Budget (DOB), All Funds spending in the budget totals \$89.6 billion, an increase of \$5.1 billion or 6 percent. This total excludes an estimated \$2.76 billion in federal disaster aid funds that flows through the State directly to New York City.

State Funds spending for 2002-03 is \$59.4 billion, an increase of \$2.4 billion or 4.2 percent. DOB projects General Fund disbursements will total \$40.2 billion, a \$1 billion decrease or 2.4 percent. This decrease is achieved by moving approximately \$1.5 billion in spending that was previously supported by the General Fund to either federal TANF funding or other non-General Fund sources like dedicated health care funding (HCRA).

#### Spending by Fund Type 2002-03 Enacted Budget (Millions)

Comparison Basis	Spending	Change from 2001-02	Growth
All Funds	\$89,556	\$5,081	6.0%
State Funds	\$59,358	\$2,380	4.2%
General Funds	\$40,214	(\$1,008)	(2.4%)

## Changes from the Executive Budget

The enacted budget adds almost \$700 million in All Funds spending over and above that of the Executive's proposal, including General Fund increases of \$360 million in school funding for the fiscal year (the Executive had proposed no increase), \$149 million to restore the Tuition Assistance Program, \$91 million in health and human services, and \$30 million in member initiatives.<sup>2</sup>

### Comparison of 2002-03 Spending Levels Proposed by the Executive and Enacted

(Millions)

Comparison Basis	Executive	Enacted	Difference
All Funds	\$88,866	\$89,556	\$690
State Funds	\$58,882	\$59,358	\$476
General Funds	\$40,221	\$40,214	(\$7)

In April, before budget negotiations were complete, the Division of the Budget announced that the financial plan as proposed by the Executive in January (amended in February) was facing an additional shortfall of \$1.4 billion due to slower than anticipated tax receipts and effects of federal tax law changes. The revenue shortfall, coupled with additional spending, creates a total need of over \$2 billion from the Executive proposal, which is detailed below:

Uses	Amount
Education (fiscal year increase)	\$360
Tuition Assistance Program (restoration)	\$149
Health and Human Services	\$91
Legislative Spending Additions	\$30
Other (including tax cuts)	\$60
Revenue Shortfall	\$1,400
Total	\$2,090

Resources	Amount
Non-Recurring (above Executive Proposal)	\$1,186
Offsets (including additional TANF and HCRA)	\$198
Spending Reductions	\$200
New Fees	\$376
Building Aid Restructuring	\$88
Other	\$42
Total	\$2,090

<sup>2</sup> Legislative additions total \$200 million with \$170 million payable after April 1, 2003. There is a language provision that requires the State Comptroller to transfer funds if additional spending needs (over and above \$30 million) take place in fiscal year 2002-03.

The budget reduces General Fund needs by transferring spending to other non-General Fund categories. Federal TANF funds are used to supplement the Tuition Assistance Program and welfare needs, among others. HCRA funding supplements General Fund Medicaid needs. Almost \$1.4 billion is shifted out of the General Fund, thus decreasing General Fund needs and increasing All Funds spending. In total, All Funds spending increases by approximately \$700 million.

## ***STRUCTURAL BALANCE***

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### **Future Budget Gaps**

In the Executive Budget submission, the Governor is required to include a financial plan projection for the two years following the budget to allow an evaluation of the State's financial condition and to measure the impact of the Executive Budget. There is no similar requirement for the enacted budget. For many years, the Comptroller's budget reform agenda has advocated changing the law to require a full evaluation of the enacted budget on future years.

The Executive's proposed budget initially projected General Fund gaps of \$2.8 billion for 2003-04 and \$3.3 billion for 2004-05. However, these projections were completed in January (before the realization in April that the current-year gap was \$1.4 billion higher than initially projected), and assumed the Legislature would adopt all aspects of the Governor's proposal. Future budget gaps are likely to be significantly higher than these estimates, due to the portion of the shortfall in 2002-03 tax receipts (identified in April 2002) that is expected to be recurring, and the extent to which added spending for education and other program areas recurs in future years. These increases are only partially offset by new recurring revenues and spending reductions. The higher budget gaps are particularly serious since virtually all of the available reserves and fund balances will be depleted.

### **Reserves**

As proposed by the Governor, the 2002-03 enacted budget plan depletes all reserves except \$710 million in the Tax Stabilization Reserve Fund ("rainy day fund"), which is restricted to mid-year budget shortfalls, and \$6 million in the Contingency Reserve Fund. The budget utilizes a total of \$1.25 billion from the Personal Income Tax Refund Reserve, a General Fund account used to hold money for personal income tax refunds and move undesignated funds from one year to the next. Of this amount, \$185 million is from funds previously held to fund already enacted tax cuts and \$1.07 billion is unspent surplus funds remaining from past years.

#### **Reserves Tapped in 2002-03 Enacted Budget** (Millions)

<b>Description</b>	<b>Amount</b>	<b>Fund Type</b>
Unrestricted PIT Refund Reserve	\$1,065	General Fund
PIT Refund Reserve Set-Aside	\$185	General Fund
Contingency Reserve Fund	\$151	General Fund
Community Projects Fund	\$160	General Fund
Universal Pre-K Funds	\$5	General Fund
TANF surplus reserves	\$955	Federal Fund

## **REVENUE ACTIONS**

### **Non-Recurring Resources**

Over \$4 billion in non-recurring resources are utilized in the enacted budget, creating additional pressure on future budget needs. As such, the extensive use of non-recurring resources in this budget is open to scrutiny since out-year gaps will increase.

The Office of the State Comptroller estimated that the Executive budget proposal utilized over \$2.5 billion in non-recurring resources to balance the General Fund.<sup>3</sup> The enacted budget adds an additional \$1.4 billion bringing the total amount of non-recurring resources to over \$4 billion. The budget contains language that establishes certain revenues and savings the State will repay (e.g., EPF and HCRA) when funds become available to do so. However, historically these types of loans are not generally paid back.

### **Non-Recurring Resources – 2002-03 Enacted** (Millions)

<b>Description</b>	<b>Executive</b>	<b>Enacted</b>
State of New York Mortgage Agency	\$150.00	\$150.00
New York State Housing Finance Agency	\$50.00	\$50.00
Port Authority of New York/New Jersey	\$16.00	\$0.00
Environmental Protection Fund (loan)	\$100.00	\$200.00
Superfund	\$0.00	\$64.00
Various Health/Medicaid Special Revenue Funds	\$114.00	\$341.00
Personal Income Tax – EFT Threshold	\$25.00	\$25.00
Sales and Use – EFT Threshold	\$32.50	\$32.50
Abandoned Property Sale	\$0.00	\$300.00
Power Authority Transfer to Power for Jobs	\$0.00	\$42.00
Tax Amnesty	\$0.00	\$175.00
Additional HCRA	\$72.00	\$200.00
Prepaid Cigarette Sales Tax Index	\$5.80	\$5.80
TANF Reserve	\$885.00	\$955.00
Higher Education Services Transfer	\$0.00	\$39.00
Dormitory Authority Transfer	\$0.00	\$12.00
Other Transfers	\$0.00	\$75.00
Change in Tax Payment Date for Businesses	\$0.00	\$100.00
Recovery of School Aid and Welfare Recipient Overpayments	\$39.00	\$39.00
PIT Refund Reserve	\$1,133.00	\$1,065.00
Other Refund Reserve	\$0.00	\$185.00
<b>Total – Non-recurring Revenue</b>	<b>\$2,622.30</b>	<b>\$4006.30</b>

Source: OSC

<sup>3</sup> Office of the State Comptroller. 2002-03 Budget Analysis: Review of the Executive Budget. February 2002. Page 16.

## **Other Revenue Actions**

The Governor proposed \$68 million in fee actions and another \$570 million in revenue enhancements in January, including lottery and gambling revenues and tax enhancements. Some of these are included in the enacted budget, which raises \$140 million in new fees and \$440 million in other new revenues, including:

- \$38 million from a \$0.50 increase to the monthly surcharge on cell phones, supposedly to be used in establishing a cellular 911 system. This Office recently released an audit regarding the use of such funds as General Fund relief for the State Police.<sup>4</sup> The budget also authorizes counties and New York City to opt into an additional \$0.30 increase (bringing the total surcharge to \$1.50 per phone per month).
- \$8 million by increasing Alcoholic Beverage Control fees.
- An estimated \$250 million from the authorization of a \$1.42 increase in cigarette tax in New York City, bringing the total City tax to \$1.50 (on top of the State tax of \$1.50). The State is to share the proceeds with the City. All State funds from this tax are dedicated to HCRA.
- \$15 million by increasing the State's 20 percent tax (by weight) on non-cigarette tobacco products to 35 percent.
- \$115 million by increasing bond issuance fees.
- \$22.5 million surcharge for county clerk filings.

## **Tax Cuts**

The enacted budget continues all tax cuts already on the books and includes a number of new tax cuts that will cost \$59 million for fiscal year 2002-03 and \$24 million in 2004-05. Tax cuts include:

- 10 Empire Zones (four previously authorized and six new)
- Tax relief for families of 9/11 victims (State income tax waiver for next two years)
- Business tax relief for post-9/11 business investment (coupled with federal law)
- Low-income housing (included in Executive proposal)
- STAR COLA adjustment for seniors (included in Executive proposal)
- Three sales tax-free periods for lower Manhattan
- Investment tax credit extension for lower Manhattan
- Exclusion of Medicare payments from base for nursing home assessments.

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<sup>4</sup> The Office of the State Comptroller released an audit in March 2002 (2001-S-27) regarding the use of cell phone surcharges by the State Police and their role in providing cellular 911 service.

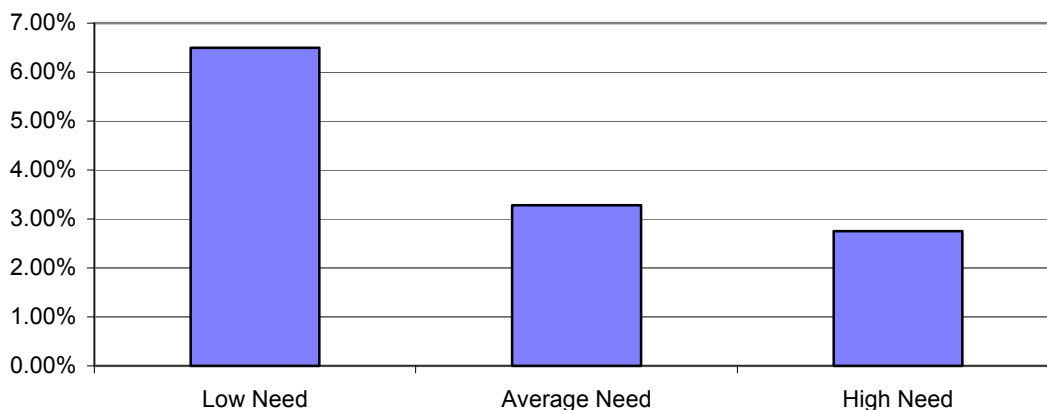
## School Finance

The enacted budget provides for a \$420 million, 3 percent increase in State aid for the 2002-03 school year, bringing total aid to almost \$14.6 billion. The funds allow for small increases in operating aids, restoration of reimbursement formulas for BOCES and special education services, and other changes. Two new grant programs are added for “academic services” and “stabilization,” with funds paid out as specified by the Legislature. The Governor’s building aid cut was enacted, although it will not impact aid until next year. Early education aids—universal pre-kindergarten and early-grade class size reduction—are once again frozen.

The enacted budget’s school aid increase is preferable to the Governor’s zero-increase approach, and will be of help in ameliorating property tax increases in some districts. The infusion of new funds will also provide some help to the financially strapped large city school districts that are struggling to close huge budget gaps. However, this is an inflationary aid increase that will not essentially change the big picture this year, which is that most school districts are cutting programs at the same time that they are raising taxes.

The budget also makes no attempt to reform school financing or to address issues raised in the Campaign for Fiscal Equity (CFE) lawsuit. This budget provides precisely the same shares of funding that are politically decided every year (e.g., New York City received its traditional 38.86 percent of the statewide increase).

**Neediest Districts Get the Lowest Aid Increases**  
2002-03 Average Percentage School Aid Increases



Far from providing reform, this budget actually delivers the greatest average percentage increases to the wealthiest districts: low-need (or relatively well-off) school districts received an average 6.5 percent increase in school aid, while the least wealthy

were given a 2.75 percent increase. In fact, new property tax–report card data show a growing gap in per-student spending among poor and wealthy districts, which the New York State Council of School Superintendents logically attributes to the cumulative impact of last year’s “baseline budget” and the Governor’s proposed freeze this year. The State’s continuing pattern of inaction and lack of reform will not only undercut the Statewide effort to raise educational performance, it may well lead to a court-ordered solution in the CFE case.

The aid distribution is accomplished through new manipulations of the State’s hodgepodge of school aid formulas. For example, Comprehensive Operating Aid is frozen at last year’s level but includes a new calculation that provides minimal (and identical) 1 percent increases in aid for most districts (those with a “combined wealth ratio” less than 1.0, or about 70 percent of districts). Similarly, Operating Standards Aid is provided through a modified formula that gives minimal increases to some districts.

Two new grant programs were added. Academic Services Aid provides \$25 million for the Big 5 City School Districts, and \$7.7 million in Stabilization Grants are allocated to 56 school districts (another \$16 million in legislative member items is unallocated, while some member items are being used for existing aid programs like national board certification for teachers and teacher centers). These new grant programs provide sorely needed aid to needy schools. However, it should be pointed out that the programs are paid as explicitly directed by the Legislature—much like a member item—and this method of approaching school aid cannot form the basis for permanent reform.

Much of the increase provided by the Legislature stems from rejection of the Executive’s proposal to merge BOCES and special education aids into the general operating aid apportionment (effectively freezing them). These changes alone increase aid by more than \$300 million. This budget also restores \$75 million in teacher recruitment, training, and retention programs the Executive had proposed cutting.

Building Aid is reduced by \$190 million due to changes made last year. The Legislature adopted the Governor’s proposal to extend assumed amortization requirements to “hard dollar projects”—smaller projects for which districts generally pay cash and are fully reimbursed the following year. Hard dollar projects undertaken in 2001-02 will be paid in full in 2002-03, but aid payments in future years will be based on the assumed amortization approach. The Comptroller and education organizations have been critical of applying an assumed amortization schedule to all projects, as these changes will drive up local costs.<sup>5</sup>

Once again, the State failed to exempt districts from the Wicks Law, thereby failing to help districts save significant sums of money in construction projects.

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<sup>5</sup> The Comptroller issued a report, “School Construction and Building Aid: An On-Again, Off-Again Priority,” in January 2002, which criticized building aid policies enacted in 2001-02, and detailed the negative impacts that the State’s approach to funding school building projects has had on local districts.

Nineteen school districts, including the Big 5, can now bond almost \$460 million in anticipated school aid due to them from prior years. Almost all of this borrowing authority—\$435 million—will be made available to New York City (although much of this amount has already been accrued by the City and will therefore not provide new spending authority). These funds are already owed to the school districts, but the State generally only pays a small proportion of these claims each year. This so-called “acceleration in payments” is actually only an authorization for districts to borrow against future school aid payments (they can borrow up to the amount of prior year adjustments already owed). The Municipal Bond Bank Agency (MBBA) will issue bonds, but districts pay off the bonds, with interest.

In New York City, much of this money will be used to help pay for teachers’ salary increases recently approved through long overdue contract negotiations. Regardless of how this money is spent, the stream of funding will not be available next year. This fiscal maneuver may cause big city governments to dig themselves into a hole with a large one-time resource. The big city school systems, like others around the State, are still reeling from the effects of last year’s extremely confusing and late State budget and, as a result, have had to deal with huge budget gaps through program and staff cuts.

No action was taken to help address future budget problems for school districts, such as allowing districts to carry a larger fund balance for unforeseen budget contingencies. As noted in a recent report from the Comptroller, in such uncertain financial times, school districts need to be able to carry a fund balance greater than 2 percent (which they are limited to by current statutes).

## ***HIGHER EDUCATION***

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Regrettably, the newly adopted State budget is only a small departure from the proposal set out earlier this year in the Executive Budget. Consequently, public higher education in New York State remains severely under funded in 2002-03. This continues an unfortunate trend: New York's spending on higher education over the past ten years has increased just 19.2 percent. Compared to a national spending increase of 59 percent, New York ranks 47<sup>th</sup> nationwide. Only Hawaii, Montana, and Alaska have fared worse.

With the State budget now in place, SUNY and CUNY still face virtually flatlined funding. Campuses will now have to prepare to cover millions in negotiated salary increases and inflationary increases on their own. In light of these funding realities, one fact is clear: Whether the remedy materializes in the form of fee increases, staffing reductions, or reduced services, it will exact a significant toll on the quality of public higher education in New York State.

By emphasizing the fact that SUNY and CUNY tuition rates have not increased since 1996, the impact of the flat spending plan has been downplayed. However, State-operated campuses will have to increase student fees or cut services to make up for budget shortfalls. Student fees at SUNY campuses have already more than tripled since 1991—soaring from an average of \$252 per academic year to just over \$800. Moreover, public tuition in New York State is now 16 percent above the national average and 14<sup>th</sup> highest in the nation.

### **Student Aid**

The Legislature rejected the Governor's plan to withhold one third of students' TAP awards until after graduation. However, this restoration was achieved in part by delaying some \$60 million in TAP payments to colleges.

The enacted budget restores last year's cut to college opportunity programs. By providing an additional \$13.7 million, HEOP, SEEK/CD, and EOP are restored to the levels they were at before last year's "bare bones" budget. However, this leaves funding at the same level it was in 1994—a net loss of 30 percent after inflation.<sup>6</sup>

### **Community Colleges**

The Legislature rejected the Executive's freeze in aid, and provided a small increase of \$50 per student for community colleges. While the increase is welcome, it does not approach the level needed to restore the State's share of funding to one third, as was originally provided. The State's share is even further below the 40 percent share promised in the 1970s when community colleges were asked to serve as full opportunity institutions, opening admissions to all students with a high school diploma or GED. Furthermore, at less than 2 percent, the increase may not cover inflation. New York's community college tuition is already nearly double the national average.

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<sup>6</sup> Measurement based on the Higher Education Price Index (HEPI), produced by the Research Associates of Washington.

## ***HEALTH AND SOCIAL SERVICES***

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### **Health and Mental Health**

Chapter 1 of the Laws of 2002, sometimes referred to as HCRA 2002, contained major programmatic and budget changes to the State's health care programs. This legislation was adopted prior to the introduction of the Executive budget and is described in a previous report.<sup>7</sup> However, the enacted budget includes the following changes from the Executive budget:

- **Cost Of Living Adjustment (COLA) for workers.** Chapter 1 of the Laws of 2002 provided Medicaid funding to support raises for direct care staff in hospitals, nursing homes, and home care agencies beginning April 1, 2002. However, certain other health and human services workers were excluded from HCRA 2002. The Legislature successfully added funding in the enacted budget to provide a 3 percent COLA for certain workers, including mental health workers, hospice workers, private duty nurses, and home care nurses and aides. However, these raises are set to take effect on December 1, 2002, eight months later than the HCRA 2002 increases. These increases are estimated to cost the State approximately \$23 million in 2002-03 and at least \$80 million when fully annualized. The funding increase is larger when the federal and local shares of the Medicaid funding are incorporated.
- **Nursing Home Tax.** As part of the HCRA 2002 package, the Governor proposed a 6 percent tax on nursing home receipts that would offset General Fund State Medicaid costs. The Medicaid-reimbursable nature of the tax mitigates the impact on homes that serve Medicaid patients. However, for years the State has encouraged homes to maximize Medicare revenue and other private pay patients in order to reduce reliance on Medicaid. For many of the nursing homes that have diversified their revenue base, the nursing home assessment would have a very detrimental effect on their bottom line. It is possible that instead of increasing worker recruitment and retention, the losses from this tax could result in staff layoffs and have an impact that is exactly opposite from what the legislation intended. The Legislature was successful in modifying the tax base to exclude Medicare receipts, which provides relief of \$22 million for nursing homes in 2002-03 and \$75 million annually thereafter. In total, the State estimates an additional \$267 million in 2002-03 (after changes in enacted budget). However, the 6 percent tax on private pay receipts remains intact, and either nursing homes will experience reduced revenues, or patients and their families will pay higher bills.
- **HCRA diversion.** The enacted budget diverts almost \$400 million in General Fund Medicaid spending to HCRA special revenue accounts. Approximately \$200 million is characterized as a loan intended to fund Medicaid costs related to the Disaster Relief Medicaid program. In addition, almost \$200 million in HCRA funding is used

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<sup>7</sup> Office of the State Comptroller. 2002-03 Budget Analysis: Review of the Executive Budget. February 2002. Pages 30-35.

to support \$73 million in Medicaid pharmacy costs and \$124 million in New York City related Medicaid expenditures formerly paid from the General Fund. These amounts are in addition to the Medicaid budget relief of \$78 million in Medicaid physician costs proposed in the Executive Budget. In the aggregate, HCRA provides budget relief totaling approximately \$1.2 billion in health-related program areas in the 2002-03 enacted budget. These actions serve to depress State General Fund spending for Medicaid and other programs, including the Elderly Pharmaceutical Insurance Coverage (EPIC) program, Roswell Park Cancer Institute, and many other public health programs.

- **Restoration of Program Cuts.** The enacted budget also restored some program cuts proposed by the Governor including: \$5 million for community health center transition funding related to the implementation of managed care, \$6.5 million in HIV/AIDS cuts, almost \$1 million for school-based health centers, and \$4 million for the adult home Quality Improvement Program (QUIP). In addition, new funding of over \$3 million is provided for an HIV/AIDS—communities of color initiative, which is targeted at prevention and services delivered by community-based providers who demonstrate an understanding of racial, ethnic, and cultural differences.
- **Community Reinvestment.** The enacted budget failed to extend Community Reinvestment. The reinvestment act was enacted in 1993 and provided that 85 percent of the savings generated from institutional closings would be reinvested in community-based mental health services. The remainder was to be used to enhance staffing at the remaining State institutions to reflect the increasingly more complex patient population. The Act has been extended several times and expired in September 2001. This year, the Governor’s budget did not propose a Community Reinvestment Act extension thus effectively shifting deinstitutionalization savings to General Fund relief instead of community mental health needs.
- **Infertility Mandate.** The enacted budget requires that group health insurance policies provide coverage for some types of infertility services. Insurance policies that cover prescription drugs must also cover pharmaceuticals approved by the FDA for diagnosis or treatment of infertility. The enacted budget includes \$10 million in grant funding from HCRA.

### **Public Assistance**

New York receives an annual block grant of \$2.4 billion from the federal government to help fund public assistance. This amount was based on the public assistance caseload in 1995. Since that time, caseloads have declined significantly and New York now receives a greater share of total program costs from the federal government. The additional amount of federal funding compared to the old program is generally called the “TANF surplus.” These monies are spent on a range of support services, including child care, job training, employment subsidies, and transportation, which are designed to assist families in attaining self-sufficiency. The enacted budget estimates the TANF surplus to be \$1.6 billion (approximately \$100 million higher than the Executive budget).

## TANF Surplus

In State fiscal year 2002-03, the enacted budget uses \$2.6 billion in TANF surplus spending. Total TANF spending is based on this year's TANF surplus (\$1.6 billion), complete depletion of TANF reserves accumulated over the past five years (\$955 million), and the use of unspent TANF funds (\$25 million). Unlike prior years, but consistent with budget practices this year, the enacted budget does not set aside funds for future needs.

The 2002-03 enacted budget uses \$1.8 billion in TANF funds to support programs that would otherwise be paid for by the general funds of the State and local governments. The largest components include the Earned Income Tax Credit (EITC), a Social Services Block Grant (Title XX) transfer, Tuition Assistance Program (TAP) funding, and Pre-Kindergarten funding.

### Allocation of Available Federal TANF Surplus Monies

(Millions)

Program	2002-03
Child Welfare (Title XX, local JD/PINS, NYC foster care tuition)	\$546
Tuition Assistance Program	\$380
Earned Income Tax Credit (EITC)	\$351
Child Care Block Grant	\$340
Earned Income Tax Credit (Prior year claims)	\$220
Prior Year MOE Reconciliation	\$187
Services/Education/Health	\$131
Employment/Transitional Initiatives	\$104
World Trade Center MOE Relief	\$100
Child and Dependent Care Credit (CDCC)	\$87
Child and Dependent Care Credit (Prior year claims)	\$62
Pre-Kindergarten Program	\$50
Audit recoveries	\$30
<b>TOTAL</b>	<b>\$2,588</b>

Source: Division of Budget

Highlights of legislative changes include:

- \$35 million in increased funding for the Tuition Assistance Program above the proposed Executive budget. The Legislature did not approve the Governor's proposal to hold back one third of the TAP scholarship until a student graduates.
- \$10 million in increased funding for employment and transitional initiatives, which are targeted to individuals with incomes below 200 percent of the federal poverty level. The block grants are reduced from \$60 million to \$34.5 million and funding is increased for specific purposes. For example, services targeted to those families with

children at risk for foster placement increases from \$7 million to \$18 million. Instruction in English as a second language is funded at \$5 million.

- \$46 million in increased funding for various health and services initiatives. Funding for advantaged schools, which is an after-school program, increases by \$15 million, to \$25 million. Funding for home visiting, which provides a range of preventive services to pregnant and parenting women, increases from \$5.6 million to \$16 million.

The federal TANF statute is up for renewal on September 30, 2002. The federal budget proposed by the President retains the TANF block grant and keeps overall funding at the same level. However, the relative share to states could change. If this were to happen, the amount provided to New York, as well as other aspects of the funding process, could be altered before a final budget agreement is reached.

### **Caseloads**

Between 1995 and November 2001, public assistance caseloads in New York fell by 58 percent. In 2002-03, caseloads are projected to decline a further 2 percent, to 1.2 million cases. The number of family assistance recipients is projected to fall by 8 percent to 519,694. This differs from the 1.4 percent decrease in the Executive budget. The number of safety net recipients is projected to increase by 5 percent to 116,838.

Beginning in 1997, the federal government began imposing a 60-month (five-year) lifetime limit on benefits for public assistance recipients. Once the limit is reached, family assistance benefits cease. Benefits provided after that point must come from State and local resources (i.e., federal funds cannot be used to pay for benefits). The Executive estimated that approximately 61,000 recipients, who have met the 60-month limit, would transition from family assistance to safety net programs in fiscal year 2002-03.<sup>8</sup>

### **Temporary Assistance Caseloads**

<b>Program</b>	<b>2001-02</b>	<b>2002-03</b>	<b>Change</b>	<b>Growth</b>
Family Assistance	562,820	519,694	(43,126)	(8%)
Safety Net	111,644	116,838	5,194	5%
Subtotal	674,464	636,532	(37,932)	(6%)
SSI	619,693	625,612	5,919	10%
<b>Total</b>	<b>1,294,157</b>	<b>1,262,144</b>	<b>(32,013)</b>	<b>2%</b>

Source: Division of Budget

Due to the projected increases in caseloads, General Fund spending for safety net programs is expected to increase 6.5 percent, to \$265 million. Although family assistance caseloads decline, the State must meet the required maintenance of effort (MOE), and therefore spending is not proportional to the projected decline in recipients. The State's

<sup>8</sup> In the short-term, the additional State and local expenditures would be effectively offset by a reduction in State and local funding for TANF using the available surplus funds, as long as they maintain a level of spending on social services programs set by the State.

share of Supplemental Security Income (SSI) is estimated to increase by \$10 million, to \$633 million.

**Temporary Assistance Programs: General Fund**  
(Millions)

<b>Program</b>	<b>2001-02</b>	<b>2002-03</b>	<b>Change</b>	<b>Growth</b>
Family Assistance	\$421	\$282	(\$139)	(33.0%)
Safety Net	\$248	\$265	\$17	6.9%
State Share of SSI	\$623	\$633	\$10	1.6%
<b>Total</b>	<b>\$1,292</b>	<b>\$1,180</b>	<b>(\$112)</b>	<b>(8.7%)</b>

Source: Division of Budget

On a cash basis, General Fund spending for public assistance is expected to decrease 8 percent, or \$112 million, to \$1.2 billion. Although caseloads continue to decline, the State must meet the required MOE, and therefore the reduction in spending is not proportional to the projected decline in recipients.

**Child Care**

The proposed 2002-03 budget increases total funding for the Child Care Block Grant by \$37 million, to \$877 million (TANF accounts for \$340 million, less than half of the amount). It supports an increase of 9,500 child care–subsidized slots to fund a total of 183,400. The block grant was created in 1997-98 and combines the public assistance, transitional, at-risk, and State low-income day care into one seamless funding system. In addition, the grant helps working families obtain affordable and high quality child care.

## ***LOCAL GOVERNMENTS***

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### **General Purpose State Aid & Supplemental Municipal Aid**

The adopted budget makes no changes to revenue sharing (General Purpose State Aid and Supplemental Municipal Aid) from the Executive Budget, which included a reduction of \$6.1 million in Supplemental Municipal aid, affecting 62 towns and villages and 3 counties.

The relatively new “county revenue sharing program” is also continued. However, the program’s original sunset date is not extended in the budget—a cause for concern for local county governments. This unrestricted aid program was introduced in the 2000-01 budget, and was loosely linked to HCRA and the increased costs that were passed on to counties when the Family Health Plus program was created.

The fiscal strain put on counties by the recently expanded HCRA legislation will also be compounded. In order to offset the costs of new provisions, the Executive Budget relied heavily on changes to the federal medical assistance percentage (FMAP). These changes, which require Congressional approval, have not yet materialized. NYSAC estimates that a failure to secure the FMAP change will result in a net loss of \$260 million for county governments over the next three years. Other enhancements to health care workforce provisions (that are in the adopted budget but were not originally part of the Executive Budget) threaten to push the total local impact to over \$300 million over the next three years.

This budget fails to restore Consolidated Highway Improvement Program (CHIPS) funding eliminated in last year’s “bare bones” budget. Towns, villages, and cities (outside NYC) had their operations and maintenance funding converted into the CHIPS capital program, but counties were not included in the conversion.

The budget also eliminates about \$35 million in funding for county-based employment and transitional services. The Executive budget included \$125 million for these services. The adopted budget cut funding to \$90 million. The decrease is tied to the Legislature’s move to provide \$2.6 billion in funding for the TANF program—\$95 million more than was offered in the Executive budget.

The adopted budget again fails to address a number of important mandate relief measures. These measures include an exemption to the multiple contracting requirements of the Wicks Law for school districts and BOCES, and revised binding arbitration guidelines that would give greater consideration to a municipality’s ability to pay.

## ***DEBT AND CAPITAL***

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### **Local Initiatives**

The enacted budget authorizes \$1.2 billion in additional debt for local initiatives and transportation capital projects, although the capital plan will not be formally updated until August 16. The new debt has little financial plan impact in 2002-03, as debt will be issued either late in the current fiscal year or in subsequent years.<sup>9</sup>

The majority of this additional debt is paid with State revenues but does not provide the State with additional physical assets, much like the Strategic Investment Fund and CEFAP, both criticized by this office in the past as being “bonded pork.” To date, the State has authorized over \$1.5 billion in debt for such initiatives, placing additional fiscal strain on the State as a whole, while providing little economic benefit for those localities fortunate enough to have a representative who can effectively garner significant funding from these programs.

- The Empire Opportunity Fund appropriates \$50 million in 2002-03, with plans for a total of \$100 million when fully implemented (the Governor had proposed \$750 million). The program provides 25 percent of required funding for economic development projects that range from waterfront development to brownfields cleanup.
- Centers for Excellence are designed to aid in the creation and upgrade of research facilities throughout the State (four have been announced thus far in Albany, Buffalo, Long Island, and Rochester). The budget appropriates \$250 million funded from State bonds (as does the Executive proposal – although the Executive only authorized \$62.5 million for fiscal year 2002-03), and it is hoped that enough private financing will be acquired to provide a 3-to-1 private/public investment.
- Gen\*NY\*sis, as initially proposed by the Senate, is funded by \$225 million in debt to maximize research and development capabilities throughout the State. The Governor’s Centers for Excellence program and the Senate’s Gen\*NY\*sis program are similar, with the key difference in administration as the Centers for Excellence program will be administered by the Urban Development Corporation.
- The budget also allows for increased debt for a new program originating in the Assembly—Rebuilding the Empire State Through Opportunities in Regional Economies (RESTORE NY). The program is funded at \$150 million and will provide project financing or assistance (such as grants or loans through the Dormitory Authority) for the development and/or improvement of community and civic facilities that offer training, economic development, and educational benefits. Priority will be given to high technology and biotechnology projects.

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<sup>9</sup> The budget provides a \$34 million appropriation in the Debt Service budget bill for economic development and “other” initiatives by the Urban Development Corporation, the authority responsible for funding and implementing these local initiatives.

- START (Security Through Advanced Research and Technology) is provided with \$5 million to assist colleges and universities with start-up funding to help secure additional federal funds for security needs.

### **Other Debt Actions**

The Executive proposal to expand the authority to issue variable rate debt and enter into interest rate exchange agreements with such instruments was enacted in the final budget. Previously, only the State with General Obligation debt, the Local Government Assistance Corporation, the Dormitory Authority and the Urban Development Corporation (doing business as the Empire State Development Corporation) had the authority to issue variable rate debt and/or enter into interest exchange agreements. The policy expands this authority to any other entity with the power to issue State-supported debt. It limits the amount of variable rate State-supported debt and interest rate exchange instruments to 15 percent of the total principal amount of State-supported debt outstanding.

In defining “interest rate exchange or similar agreement,” the policy includes the use of SWAPS as an instrument to mitigate possible shortfalls involved with variable rate debt. Any authority that is authorized to issue State-supported debt is authorized to enter into such agreements.

The enacted budget also contains language amending the Public Authorities law that increases bond issuance fees paid to the State by public benefit corporations (including Industrial Development Corporations, which were previously not included). Additional State revenue is estimated to be \$115 million for the 2002-03 fiscal year, due largely to a significant debt restructuring by the Metropolitan Transit Authority. The change will increase borrowing costs for all institutions, including schools, hospitals, nursing homes, and other not-for-profit organizations that utilize public authorities for easier and cheaper borrowing. The Division of the Budget has discretion over which institutions pay such fees.

### **Debt Condition**

New Yorkers face one of the highest debt burdens in the country. In the past ten years, debt service on State-supported debt has increased from 3.7 percent of All Governmental Funds Receipts to an estimated 5 percent in fiscal year 2001-02.

New York’s State-supported debt burden has increased from \$1,332 per person in fiscal year 1992-93 to an estimated \$2,070 per person in fiscal year 2002-03. This debt represents 5.7 percent of New York’s personal income, an increase from the 1992-93 level of 5.3 percent.

For years, New York has had one of the lowest credit ratings in the nation. Recently, Standard and Poor's upgraded the State's credit. However, Moody's continues to rate New York's credit as the lowest in the nation, along with Louisiana.

**Standard and Poor's Ratings of State General Obligation Bonds**  
(As of June 2002)

AAA	AA+	AA	AA-	A+	A	A-
Delaware	Florida	Alabama	Hawaii	California	Louisiana	
Georgia	Indiana	Arkansas	Massachusetts			
Maryland	Iowa	Connecticut	Montana			
Michigan	Kansas	Illinois	North Dakota			
Minnesota	Maine	Kentucky	Rhode Island			
Missouri	New Hampshire	Mississippi	West Virginia			
North Carolina	New Mexico	Nevada	Wisconsin			
South Carolina	Ohio	New Jersey				
Utah	Vermont	<b>New York</b>				
Virginia	Washington	Oklahoma				
		Oregon				
		Pennsylvania				
		Tennessee				
		Texas				
		Wyoming				

Source: Standard and Poor's Corporation.

**Moody's Ratings of State General Obligation Bonds**  
(As of March 31, 2002)

Aaa	Aa1	Aa2	Aa3	A1	A2	A3
Delaware	Indiana	Alaska	Alabama	California	Louisiana	
Georgia	Iowa	Arkansas	Hawaii		<b>New York</b>	
Maryland	Kansas	Connecticut	Idaho			
Michigan	New Mexico	Florida	Mississippi			
Minnesota	Ohio	Illinois	Montana			
Missouri	Texas	Kentucky	North Dakota			
North Carolina	Vermont	Maine	Oklahoma			
South Carolina	Washington	Massachusetts	Rhode Island			
Utah		Nevada	West Virginia			
Virginia		New Hampshire	Wisconsin			
		New Jersey				
		Oregon				
		Pennsylvania				
		Tennessee				

Source: Moody's Investors Services

## **New York Compared to Other States**

According to a Moody's Investors Service report, *2002 State Debt Medians*, New York ranks among the top five of all states in two measures of tax-supported debt burden:

- New York is fifth highest in tax-supported debt per capita, with Connecticut, Hawaii, New Jersey, and Massachusetts as the four states with heavier debt loads per person. New York's per capita debt of \$2,045 is nearly two and a half times the national average of \$810. This does not include local debt paid through local taxes.
- Per capita figures do not account for differences in ability to pay for debt among the states. A more precise measure relates debt to the total income of a state's residents. New York ranks fourth in tax-supported debt as a percentage of personal income, with only Connecticut, Hawaii, and Massachusetts having higher burdens. New York's highest debt burden of 5.9 percent of personal income was over two times the average level of all states.<sup>10</sup>

Despite the 2000 debt reform and the 2001 revenue bond enactment, New York still lacks meaningful debt reform. In fact, according to the latest data, New York still ranks 4<sup>th</sup> in the country in tax-supported debt as a percentage of personal income.

Even after six straight surpluses, the State increased its debt-load by 27 percent since 1995. Debt has more than doubled since 1990. Clearly the residents of this State deserve better and meaningful debt reform. This office has repeatedly advocated proposals to address the issue of rapidly escalating debt while considering the growing needs of the State. In light of the recent economic downturn, the State can and should act responsibly now to save in the future.

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<sup>10</sup> Moody's Investors Service, *2002 State Debt Medians*, April 2002.

**This report was prepared by the State Comptroller's  
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