NASSAU COUNTY
OFFICE OF THE COMPTROLLER

REPORT ON THE COUNTY'S FINANCIAL CONDITION FOR THE FIRST SIX MONTHS OF FISCAL YEAR 2004

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Nassau County Comptroller

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Executive Summary

This report is mandated by Article IV § 402.9 of the Nassau County Charter, as modified by Local Law 3-2003. It assesses the financial condition of the county for the first six months of the fiscal year 2004 (FY 04) and provides an opinion as to whether a surplus or deficit shall exist at year-end. It also presents comments on certain estimates included in the county's Multi-Year Financial Plan Update.

Because other entities (such as the Nassau Interim Finance Authority, the county Office of Management & Budget, and the Legislative Budget Office) also report on Nassau County's financial condition, we have chosen to highlight areas of potential significant variance from the county's adopted 2004 Budget, rather than present a line-by-line review of the budget in its entirety.

Pension relief legislation recently enacted in New York State could result in a significant FY 04 budgetary variance. This legislation changed the date by which municipalities are required to make their yearly New York State & Local Retirement System contributions from December 15th to February 1st of the following year. This change could save Nassau County $78 million in 2004, and between $6 million and $7 million in each of the years 2005 through 2007. The administration has indicated that it will reserve the total amount of the anticipated 2004 savings to fund future retirement system costs. Because the pension relief measure will create non-recurring budgetary savings, it is appropriate for the county to create the reserve and remove the expected FY 04 savings from its year-end surplus. The legislation also allows municipalities to borrow a portion of 2004 - 06 pension costs to provide transitional relief while municipalities adjust their finances to accommodate the projected increased levels of employee pension benefit costs. We understand State Comptroller Hevesi will be issuing a directive as to the recommended treatment of pension liability under this legislation.

Our analysis of expenses and revenues through the end of June, together with our forecast for the remaining six months of the year, projects that the county will experience FY 04 fiscal results of between break-even and a surplus of $38 million for its primary funds (General Fund, County Parks, Fire Safety, Debt Service, Police Headquarters and Police Districts). This estimated surplus is primarily the result of conservative budgeting by the Suozzi administration and a number of significant favorable budget variances that more than offset certain revenue shortfalls and cost overruns. Most notably, gross sales tax receipt growth is projected to generate a positive variance of $35 million over the adopted budget.

The $38 million range in the projected surplus represents the reserve established at the end of 2003, to fund termination pay associated with an extraordinary volume of Police Benevolent Association (PBA) retirements projected to take place during 2004. The ultimate number of PBA retirements will not be known until the end of this year. To the extent that the $38 million reserve is not used, the balance will increase the FY 04 surplus.

Our analysis does not include the receipt of $21 million of budgeted revenues from the Nassau County Tobacco Settlement Corporation (NCTSC). For the last two years, the county has deferred drawing down these revenues from the NCTSC. If the same strategy is employed this year, the money will be available to fund obligations in future fiscal periods.

The year-end surplus is projected despite a number of significant budgetary shortfalls, most notably in police and corrections overtime, Department of Mental Health early intervention educational services, automobile registration surcharges, parks revenues and utility costs. While sales tax revenues are projected to generate the most significant positive budgetary variance, other substantial favorable variances are projected for state and federal aid, employee fringe benefits and debt service costs.

At this time, members of two of the county's three police unions, the Detectives Association, Inc. (DAI) and Superior Officers Association (SOA), are currently working without labor contracts. The last DAI agreement expired on December 31, 2000 and the SOA agreement expired on December 31, 2001. The resolution of these contract disputes may impact this year's projected surplus.

As we have consistently reported, Nassau County's structural budgetary deficit is expected to increase dramatically over the next several years because the growth in county expenses is far outpacing revenue growth. The Updated Multi-Year Financial Plan presents a number of gap closing measures, which include smart government initiatives, labor concessions, and workforce reductions, in addition to new or increased taxes. We believe that some of these revenue generating / cost reduction initiatives may not be realized, and additional budget measures will have to be identified.

Revenue and Obligations Forecast for 2004*

($ millions)

	2004 Budget	2004 Projected Actual	Variance
Revenues:			
Sales Tax	$901.9	$936.9	$35.0
Property Tax	738.8	743.0	4.2
State and Federal Aid	319.8	336.2	16.4
Tobacco Settlement	20.9	-	(20.9)
Other Revenues	725.8	702.8	(23.0)
Total Revenues	2,707.2	2,719.0	11.8
Obligations:			
Payroll and Fringe Benefits	1,043.1	1,052.6	(9.5)
Debt Service	322.1	316.7	5.4
Social Services	459.1	461.2	(2.1)
Other Obligations	882.9	888.1	(5.2)
Total Obligations	2,707.2	2,718.6	(11.4)
Projected Surplus before Pension Relief and Police Reserve	**0.0**	**0.3**	**0.3**
Pension Legislation		78.4	
Pension Reserve		(78.4)	
Police Termination Pay Reserve		38.5	
Total Projected Surplus		**$38.8**	

* This forecast includes the following six county funds:
General, Parks and Recreation, Police Headquarters, Police District, Debt Service, and Fire Prevention, Safety, Communication and Education

SIGNIFICANT VARIANCES - Revenues

Tax Revenues

Sales Tax

Gross sales tax receipts are projected to total $936.9 million, which is $35 million over the $901.9 million adopted budget. Sales tax revenues collected in first half of FY 04 have been approximately 8% greater than those collected in the same period in FY 03. This favorable trend began in the last quarter of 2003, when quarterly results approached 9% over the same quarter of the prior year.

Recent economic data for Nassau County is positive. New jobs were added in each of the last 21 months, with 13,900 jobs added in the twelve months ended May 31, 2004. Above average increases in employment were reported in the construction, transportation, leisure and hospitality industries. Correspondingly, the unemployment rate is down. Consumer spending has also increased, especially in the areas of apparel, food, gasoline and housing.

The combination of inflation, economic growth and new jobs will positively impact sales tax receipts. Nassau County economist Dr. Irwin Kellner predicts that 2004 collections will be 6% to 8% higher than the prior year.

The Multi-Year Financial Plan Update includes revised growth of 3 percent on a revised 2004 base estimate of $921 million. The financial plan's budgetary gap-closing measures include a contingency for additional sales tax revenue growth, which brings total sales tax revenue growth to 3.5 percent in future years. The actual outcome of this assumption will have to be monitored.

	JULY 1 YTD Sales Tax Collected	**GROSS ANNUAL Sales Tax Collections**
	($'s in millions)	
2001	$ 351.9	$ 831.9
2002	358.0	865.5
2003	362.2	895.5
2004	392.0	936.9*
		*Projected

Special Taxes

A shortfall of $3.6 million is projected for Police Headquarters Fund special tax revenues. The legislation enacting the automobile registration surcharge was delayed until May 2004. The Comptroller's Office estimates that this delay will result in a $4.6 million unfavorable variance from the $16.1 million amount budgeted. Revenues for 911 surcharges are estimated to exceed budget by $1 million, and will partially offset the registration shortfall presented above. Through June 2004, 911 revenue collections for land-line and cell phone surcharges totaled $3.4 million of the $5.2 million budget.

Non-Tax Revenues

State Aid

In total, state aid is projected to be $12 million over the FY 04 adopted budget of $206.5 million. Contributing to this favorable variance is the $15 million under-budgeting of overburden aid for long-term care of the mentally ill. The budget was overly conservative; it was completed before final FY 03 data was available, and at the time, the county believed the State was going to cap overburden reimbursements. State aid for increased early intervention expenditures added to the overall favorable state aid variance. Partially offsetting these favorable variances in FY 04, is the unfavorable impact of the Governor's proposal to shift $7.5 million of NIFA transitional aid from FY 04 to FY 05 and the county's decision not to utilize $1.8 million in budgeted NIFA reimbursement for the effort to reduce the backlog in tax certiorari challenges.

STATE AID INCOME ($'s in millions)			
2003 Actual	**2004 Budget**	**YTD June 2004**	**Forecast 2004**
$ 213.8	$ 206.5	$ 17.3	$ 218.5

Federal Aid

We project a favorable federal aid variance of $4.4 million against an adopted budget of $113.3 million for 2004. The most significant factor contributing to this estimate relates to the Federal inmate population at the county's Correctional Center. The federal government has increased by 16% the daily reimbursement rate for federal inmate care at the Correctional Center. Additionally, the number of Federal inmates is higher than originally projected.

FEDERAL AID INCOME ($'s in millions)			
2003 Actual	2004 Budget	YTD June 2004	Forecast 2004
$ 107.6	$ 113.3	$ 32.1	$ 117.7

Tobacco Settlement Revenue

The Comptroller assumes that the county may opt not to take either the annual or residual portions of the Tobacco Settlement proceeds in 2004, a total of $20.9 million. The county has pledged, however, to use a minimum of $250,000 per year for tobacco education services for the youth in Nassau County.

Parks and Recreation Revenue

During the first six months of 2004, the county Department of Parks and Recreation collected $5.5 million in departmental revenue, 29.7 percent of the budgeted amount. The total budget for Parks departmental revenue for FY 04 is $18.5 million, an increase of 36 percent over last year's actual of $13.6 million. Based on the current level of revenues, a shortfall of $3.5 million is projected for FY 04. A portion of this shortfall is attributable to the negative impact of inclement weather on the department's ability to generate revenue. Our analysis concludes that Parks Department revenue levels will remain flat through 2007; however, we project the revenue to level off at $15 million, not the $16.6 million stated in the Financial Plan.

County Parks Fund Departmental Revenue ($'s in millions)				
YTD June 2003	Actual 2003	Budget 2004	YTD June 2004	Forecast 2004
$ 5.6	$ 13.6	$ 18.5	$ 5.5	$ 15.0

OTB Profits

We project a $3 million shortfall in Off-Track Betting revenue as a result of thoroughbred nighttime racing revenue not achieving expectations. In addition, in FY 04, the NYS Racing and Wagering Board imposed an unanticipated regulatory fee of .39 percent on total wagering. This fee will impact revenues negatively by approximately $1.2 million. These variances will be partially offset by the $2 million unbudgeted revenues generated from the new OTB Tele-theater.

SIGNIFICANT VARIANCES - Obligations

Labor Costs

Overtime

Overtime costs for the Police Department and the Correctional Center total $23.1 million through the end of June 2004. Overtime for these two departments is projected to exceed the $42.6 million adopted budget by $21.2 million. This unfavorable variance is comprised of $12.1 million in the Police District Fund, $2.8 million in the Police Headquarters Fund and $6.3 million at the Correctional Center.

Reduced sworn headcount coupled with contractually mandated minimum staffing requirements are contributing to the projected unfavorable variance in the police funds. Notably, there will be 635 sworn officers eligible for retirement by year-end, representing more than one-quarter of all officers currently on board. Headcount at the Correctional Center is under budget (budget 1,168 vs. actual 1,130) due to losses of officers by attrition.

Police and corrections overtime expense in 2005 through 2007 will continue to be dependent on staffing levels and the effectiveness of management actions to reduce the overtime incurred.

OVERTIME ($'s in millions)						
	YTD June 2003	**Actual 2003**	**Budget 2004**	**YTD June 2004***	**Forecast 2004**	**Variance**
Police District	$ 7.0	$ 24.7	$ 13.2	$ 7.1	$ 25.3	$ (12.1)
Police Headquarters	5.8	16.1	14.6	6.3	17.4	(2.8)
Correctional Center	8.6	20.1	14.8	9.7	21.1	(6.3)
Total	$ 21.4	$ 60.9	$ 42.6	$ 23.1	$ 63.8	$ (21.2)

***** Paid overtime through June is proportionately less than for the whole year since a significant portion of overtime earned is deferred until November and a certain amount of the overtime is seasonal.

Police Termination Pay

The Comptroller's Office estimates that 110 eligible police officers will retire during 2004. Based on this projection we expect FY 04 termination pay in the Police Headquarters and Police District Funds to finish close to the $25.1 million adopted budget.

There is, however, the possibility that additional members of the Police Benevolent Association could elect to retire before the close of the 2004 fiscal year. This potential for accelerated retirements results from a clause in the current PBA labor agreement that effectively reduces the termination pay of officers retiring after December 31, 2004 by 6.5%. Pursuant to the agreement, the hourly rate calculation of termination pay is based on 1,985 work hours per year rather than the current 1,856 hours.

The termination pay contingency was adequately provided for at the end of 2003, when a $38.5 million reserve was established to cover the potential for an extraordinarily high number of PBA retirements during FY 04. Based on average 2003 PBA termination pay of $225,000, the $38.5 million reserve is enough to cover 171 retiring officers. We are presently unable to reasonably project the expected number of police officers that will retire under this more favorable retirement climate. To the extent that this retirement reserve is not fully utilized, the unused reserved funds will increase this year's surplus.

Unresolved Police Labor Agreements

Currently, the Detectives Association (DAI) and Superior Officers Association (SOA) labor contracts are in binding interest arbitration. The county expects that arbitration awards for the DAI and SOA (due to be resolved and awarded in September 2004) will follow the pattern established for the PBA arbitration award. A successful arbitration settlement with the DAI and SOA will contribute to a positive variance relative to amounts included in the Financial Plan's baseline.

Fringe Benefits

Retirement System Contributions

The retirement system legislation recently enacted in New York State could provide Nassau County with pension relief in 2004 of $78.4 million. The legislation would enable Nassau County to defer payment of its 2004 pension bill until February 2005. As a result of the one-fiscal-year delay in required payments, the county will also obtain budget relief in each subsequent year through 2007, of $6 million, $7 million and $7.2 million, respectively. The county intends to place the $78.4 million from 2004 in a reserve to help transition to projected increased levels of pension benefit costs.

	FORECASTED PENSION EXPENSE								
	($'s in millions)								
	2004 Budget	2004 Forecast		2005 Forecast		2006 Forecast		2007 Forecast	
		Pension Expense	Savings	Pension Expense	Savings	Pension Expense	Savings	Pension Expense	Savings
Non police	$ 42.5	$ 4.6	$ 37.2	$ 49.9	$ 1.7	$ 52.6	$ 1.7	$ 55.5	$ 1.7
Police	45.3	4.7	41.2	53.6	4.3	55.8	5.3	58.1	5.5
Total	$ 87.8	$ 9.3	$ 78.4	$ 103.5	$ 6.0	$ 108.4	$ 7.0	$ 113.6	$ 7.2

Health Insurance

The FY 04 budget includes employee health insurance rate increases of 15 percent for active employees and 18 percent for retirees. Actual increases were 14 percent and 12.4 percent for actives and retirees, respectively. This difference accounts for an estimated favorable variance of $5.2 million. Notably, when the cost of health benefits for retirees from the county's health care facilities (which now comprise the Nassau Health Care Corporation) are included, the cost of retiree health insurance currently exceeds the cost for active workers. Expenses for past health care workers are budgeted as a cost of supporting the NHCC, not as a county fringe benefit.

The Comptroller's Office is projecting slight savings related to a reduction in estimated rate increases for health insurance costs in fiscal years 2005 to 2007; the Multi-Year Financial Plan Update factors rate increases of 13.8 percent for active employees and 15 percent for retirees. Based on the most current information available from the New York State Health Insurance Program (NYSHIP), the Comptroller's Office projects rate increases of 12 percent for active employees and 15 percent for retired employees.

HEALTH INSURANCE EXPENSE				
($'s in millions)				
	2003 Actual	2004 Budget	YTD June 2004	Forecast 2004
Active employees	$ 69.9	$ 78.8	$ 40.0	$ 80.4
Retired employees	63.8	75.4	35.8	71.6
NHCC retired employees	15.1	18.0	7.2	17.3
Total	$148.8	$172.2	$ 83.0	$169.3

Debt Service

In total, debt service is projected to be $5.4 million under the adopted budget. This year's budget for debt expense differs from the past. Traditionally, it has consisted of general obligation bond interest and principal expense, and NIFA set-asides, which are county sales tax revenue held and accumulated by NIFA used to pay debt service. This year, consistent with the newly created Sewer and Storm Water Finance Authority, costs related to borrowings for sewer and water projects will be reimbursed by the Authority. For FY 04, the expense that will be reimbursed is approximately $10 million, resulting in a negative variance of about $6 million. This amount, in addition to the negative variance generated by the pension bond payoff of $1.5 million, is more than offset by the positive variance generated by NIFA's Fall 2003 and Spring 2004 borrowings which contained both restructuring and refunding of county bonds. These borrowings occurred after the 2004 budget was prepared, and resulted in a total of $13 million positive variance.

Social Services

For 2004, the Comptroller's Office is projecting a negative variance of $2.1 million, primarily due to increased caseloads for recipient grants, which include subsidized adoptions, foster children, safety net and temporary assistance for needy families.

The Medicaid budget of $260.1 million for 2004 is projected to be sufficient. This calculation is based on current trends in Medicaid payments, including an additional $2 million for the processing of outstanding Medicaid applications for skilled nursing facilities, and taking into consideration a $6.5 million FY 03 accrual for the backlog of Medicaid applications that has been substantially reduced during 2004.

Our estimates agree with the Multi-Year Financial Plan Update forecast for Medicaid expense in 2005, but we project $8.3 million less expense than the Financial Plan for FY 06 and $20 million less in 2007. This difference is primarily due to savings generated from moving Medicaid clients to managed care, and the reduction in the rate of increase in caseloads for the Family Health Plus program. The Financial Plan presents annual increases in the cost of Medicaid local share in the amounts of $37.1 million in FY 06 and $77.4 million in FY 07. The Plan indicates these increases may require a dedicated property tax increase, in the absence of the cap on county Medicaid costs, which both the County Executive and the Comptroller have urged the State to approve. The New York Association of Counties (NYSAC) has advised that the New York State budget, when adopted, may include a three year takeover of Family Health Plus, which would impact this projection.

MEDICAID EXPENSE ($'s in millions)			
	2003 Actual	**2004 Budget**	**Forecast 2004**
Medicaid, net of IGT	$ 228.2	$ 260.1	$ 260.1

Education of Handicapped Children

We are projecting a negative variance of approximately $9.3 million in the adopted budget for the early intervention programs administered by the Department of Mental Health due to increased caseload and more significantly, costs per child. We anticipate actual FY 04 expense to be $88.6 million, against an adopted budget of $79.3 million. This projected variance will be partially offset by increased reimbursements from New York State, which will amount to approximately $5 million.

Delays in the billing of early intervention services by local school districts make it difficult for the department to accurately budget for these expenditures. Based on this year’s cost level, we anticipate significantly higher expenditures in comparison to the Multi-Year Fiscal Plan estimates for FY 05 through FY 07.

EARLY INTERVENTION EXPENSE ($’s in millions)				
YTD June 2003	**Actual 2003**	**Budget 2004**	**YTD June 2004**	**Forecast 2004**
$ 48.7	$ 86.7	$ 79.3	$ 62.4	$ 88.6

Utilities

Utility costs are projected to exceed the FY 04 adopted budget of $26.3 million by $2.5 million. The principal reason for this unfavorable variance is the volatility currently being experienced in the petroleum marketplace. Increases in world oil prices have resulted in significant increases in the county’s oil and electric utility costs.

UTILITY COSTS ($’s in millions)				
YTD June 2003	**Actual 2003**	**Budget 2004**	**YTD June 2004**	**Forecast 2004**
$ 13.1	$ 29.9	$ 26.3	$ 20.4	$ 28.8

Contractual Obligations

Contractual obligations are projected to be $1.7 million less than the $163.4 million adopted budget. The county established a reserve at the end of 2003 for the 2004 property assessment contract with Cole Layer Trumble Company originally budgeted in FY 04, resulting in a $4.5 million favorable variance. This variance was offset by a $1.6 million encumbrance for a contract with the Manatt, Phelps & Phillips law firm concerning the county’s relationship with the Nassau Health Care Corporation, and a supplemental budget increase of $1.2 million for the purchase of mass transit buses by the Planning Department.

Nassau Health Care Corporation

Financial Position

The financial condition of the Nassau Health Care Corporation (NHCC) continues to be a threat to the overall fiscal recovery of the county. The Comptroller's latest monthly review of NHCC cash found that, as of July 15, 2004, the balance had dwindled to $23 million. The corporation continues to spend more money than it takes in. Although a number of fiscal initiatives have been implemented, a cash crisis appears to be imminent. The Multi-Year Financial Plan Update indicates that county tobacco settlement revenue reserves may have to be used to avert a crisis. Sufficient additional short and long-term reforms in Corporation operations must be put into place as soon as possible, however, so that the Corporation's medical facilities can remain viable.

Ongoing County Support

Although the FY 04 estimate for NHCC support contained in the Multi-Year Financial Plan Update appears reasonable, the plan does not reflect any increase in these costs for future years. Our analysis concludes that by FY 07, these expenditures, comprised of the historic mission payment, termination pay and fringe benefit expenses for former NHCC employees, will generate a shortfall of $8.7 million. The mission payment is subject to renegotiation and, if not resolved by September 2004, will go to binding arbitration. The new payment amount will be effective in 2007. The largest component of the other expenses, health insurance for retirees, is forecasted to increase 15.3 percent each year.