Blueprint for a Better Budget

A Plan of Action for New York State

E.J. McMahon and Josh Barro

EMPIRE CENTER
FOR NEW YORK STATE POLICY
A project of the Manhattan Institute for Policy Research

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P.O. Box 7113
Albany, NY 12224
(518) 434-3100
info@empirecenter.org

www.empirecenter.org

Special Report SR1-10 January 2010
Revised

About the authors

E.J. McMAHON is director of the Empire Center for New York State Policy, a project of the Manhattan Institute for Policy Research. He also is the Manhattan Institute's senior fellow for tax and budgetary studies. His recent work for the Institute and its Empire Center has focused on state government reform, tax policy, public pension reform, competitive contracting of public services and the fiscal record of the Pataki administration. McMahon's professional background includes more than 25 years as a senior policy maker and analyst of New York government. He has served as Deputy Commissioner for Tax Policy Analysis and Counselor to the Commissioner in the state Department of Taxation and Finance; Director of Minority Staff for the state Assembly Ways and Means Committee; vice chancellor for external relations at the State University of New York; and Director of Research for The Business Council's research arm, the Public Policy Institute. His articles have appeared in the Wall Street Journal, Barron's, the Public Interest, The New York Times, the New York Post, the New York Daily News, Newsday and the New York Sun, among other publications.

JOSH BARRO is the Walter B. Wriston Fellow at the Manhattan Institute focusing on state and local fiscal policy. Prior to joining the Manhattan Institute, he served as a Staff Economist at the Tax Foundation, where he authored the 2009 State Business Tax Climate Index and the 2009 "Tax Freedom Day" report. At the Tax Foundation, he wrote several critical analyses of state tax and budget proposals and gave testimony on tax reform before officials in Arkansas, Louisiana, Maryland, New Jersey, Rhode Island, and South Carolina. Barro holds a Bachelor of Arts degree from Harvard College.

Blueprint Project Senior Research Analyst: **PETER DRAO**

Blueprint Project Research Analyst: **KEVIN BRONNER Jr.**

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INTRODUCTION

This document represents an effort to develop a fiscally practical, comprehensive approach to putting New York State's budgetary house in order.

It explains why and how the state developed such massive budget deficits.

It identifies programmatic changes to begin closing the gaps and to put the state's finances on a more stable footing.

It explains how privatization and competitive contracting can help produce more efficient and affordable public services.

It proposes structural reforms to improve the state budget process and to reduce costs at every level of government in New York.

Finally, it outlines tax policy goals to promote renewed economic growth.

OVERVIEW

New York State is broke. After decades of growing reliance on taxes generated by Wall Street, the revenue side of the state budget has collapsed to a level from which it will only slowly recover. Yet state spending has continued to rise, fed by old reserve funds, new gimmicks, tax and fee increases, and temporary federal aid. Like a runaway train, New York's budget is in danger of running completely off the rails. It needs to be brought under control—before it's too late.

New York's fiscal crisis is not confined to state government. Counties, municipalities and school districts all have been affected by the economic downturn and its aftermath. All levels of government will feel the impact of actions needed to close unprecedented state budget gaps over the next several years. New York State faces a comprehensive, multi-year challenge demanding comprehensive long-term solutions—including:

- structural reforms and mandate relief to help every level of government cope with the recession and its aftermath, and

- state budget-making reforms to promote better long-term financial planning and instill more transparency and accountability into the process of spending taxpayers' money.

New York has been out-spending and out-taxing most of the country for many years—and has also experienced a mass exodus of taxpayers[1] and slower than average economic growth.[2] Reversing those trends is the ultimate goal of the Blueprint for Better Budgeting. The plan is organized as follows:

I. The Collapse and Its Cause
How and why the state's budget gaps developed, and where the budget stood as of the end of 2009

II Rightsizing State Government
A 30-point budget savings and reduction plan worth almost $14 billion annually when fully implemented, plus privatization and outsourcing options potentially worth billions more

III A Framework for Reform
Strategies for making state and local government more efficient and affordable—starting with a public-sector pay freeze

IV Better Budget-Making
How to instill more discipline, transparency and accountability into the state budget process

V A Template for Tax Reform
Tax policy changes to promote a lasting economic recovery

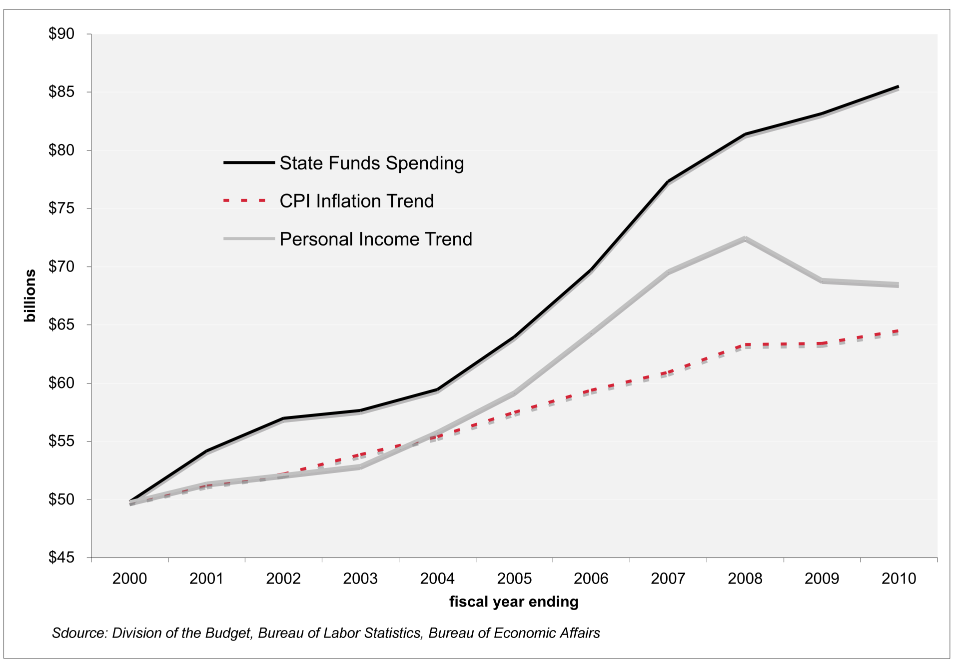
I. THE COLLAPSE AND ITS CAUSE

The size and scope of New York State's budget problem is primarily a result of excessive and unsustainable spending.

State spending—from all revenue sources other than federal aid—has risen by nearly 70 percent (roughly $35 billion) over the past decade. As depicted in Figure 1 (below), spending growth slowed only slightly during the sharp downturn of 2001-03, and it has continued to increase even during a financial crisis that Governor Paterson describes as the worst since the Great Depression.

The estimated State Funds budget total for 2009-10, including the General Fund,[3] does not include nearly $6.6 billion in normally state-financed spending temporarily offset by federal stimulus aid, which Lt. Governor Richard Ravitch has aptly described as "two years of one shots."[4] Counting expenditures supported by stimulus money, the 2009-10 rate of State Funds budget growth is about 8 percent. Inflation for the same fiscal year is estimated at zero.[5]

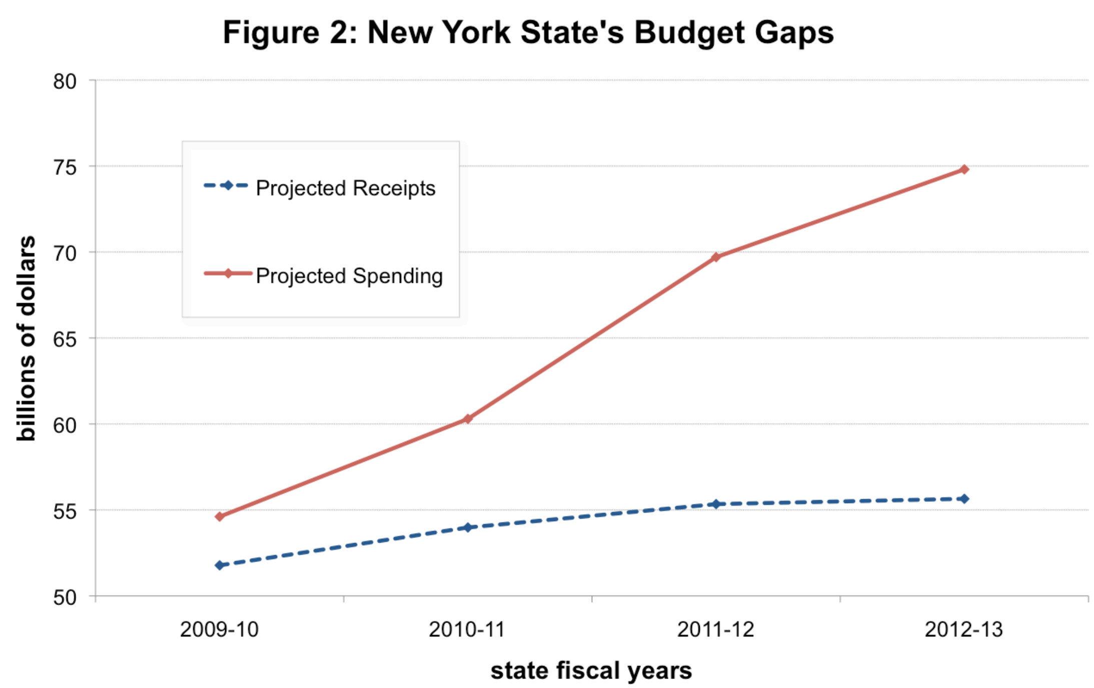
Figure 1: State Spending in New York, SFYs 1999-2000 to 2009-10



New York would be spending $21 billion less if its budget growth over the past decade had been held to inflation, and $17 billion less if budget increases had tracked New Yorkers' personal income.

Spending Rises As Revenue Drops

Most of the $3.2 billion deficit[6] projected at the halfway point in the 2009-10 fiscal year could be traced to shortfalls in tax collections. But rising spending will represent a growing share of the problem over the next three years. In Figure 2 (below), the solid line represents projected General Fund spending, and the dotted line represents projected revenues, both as of the Mid-Year Financial Plan issued at the end of October 2009.



Source: Division of the Budget, 2009-10 Mid-Year Financial Plan Update

After bottoming out in 2009-10, General Fund revenues are projected to increase slightly over the next three years. But spending is projected to surge by over $5 billion in 2010-11 alone—and by nearly twice as much between fiscal years 2010-11 and 2011-12, when federal stimulus aid is due to expire and spending temporarily supported by the stimulus will be reclassified back into the General Fund. Meanwhile, even after this year's temporary state income tax increase expires at the end of 2011, General Fund revenues are projected to hold their own between 2011-12 and 2012-13.

What spending categories are driving the spending trend in the year ahead? That question is answered in Table 1 on the following page, which shows projected trends in "baseline" expenditures—those that that would take place under current law if the budget were left on autopilot.

Table 1: General Fund Actual and Projected Baseline Spending				
(millions of dollars)				
			Change	
GENERAL FUND BASELINE:	2009-10	2010-11	Total	Rate
School Aid*	17,428	19,248	1,820	10%
Medicaid	11,599	13,851	2,524	30%
"FMAP" Medicaid Stimulus Aid	(3,155)	(2,883)	272	-9%
Mental Hygiene	2,167	2,283	116	5%
Children and Family Services	1,788	1,936	148	8%
Other Education Aid	1,634	1,689	55	3%
Temporary and Disability Assistance	1,310	1,506	196	15%
Public Health	708	826	117	17%
All Other	5,040	4,621	(419)	-8%
State Operations				
Personal Service	6,560	6,878	318	5%
Non-Personal Services	1,926	2,070	144	8%
Pension Contributions	1,179	1,653	474	40%
Health Insurance				
Active Employees	1,747	1,928	181	10%
Retired Employees	1,130	1,250	120	11%
Other General State Charges	(187)	(445)	(258)	138%
Transfers to Other Funds				
Debt Service	1,695	1,774	79	5%
Capital Projects	525	1,165	640	122%
Other Transfers	925	1,092	167	18%
TOTAL	54,019	60,442	6,423	12%
General Fund Base Including Federal Stimulus	58,680	64,049	5,369	9%

* Reflects shift of $391 million in stimulus funding and of $200 million VLT franchise fee from 2010-11 to 2009-10 under December 2009 Deficit Reduction Plan.

Source: Division of the Budget, Mid-Year Financial Plan Update; some Empire Center re-estimates

As shown above, General Fund baseline spending is set to rise by **12 percent** next year, including amounts necessary to offset reductions in available federal stimulus funds. Even after adjusting the totals to reflect the impact of federal stimulus aid on recurring spending, the underlying current-law baseline growth is **9 percent**.

This $6.4 billion of unadjusted baseline spending growth accounts for nearly all the projected 2010-11 budget gap. While the figures will be revised in the financial plan issued with the 2010-11 Executive Budget, the fundamental problem will remain. Two thirds of that problem is concentrated in two areas: school aid and Medicaid.

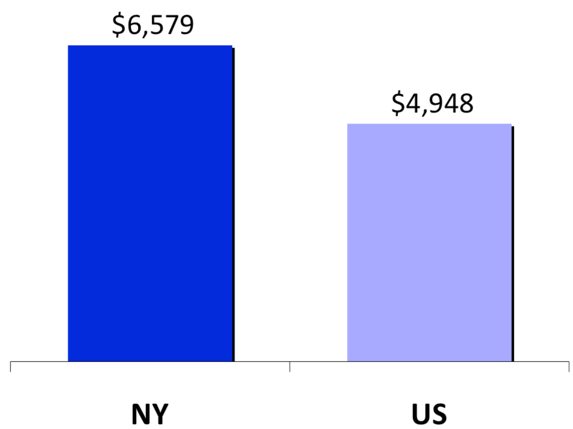
II. Rightsizing State Government

As illustrated on the previous pages, New York faces enormous state budget gaps over the next several years mainly because spending is projected to grow much faster than revenues. To close these gaps, New York does not need to *cut* total spending but to *control* its growth.

Controlling spending is not a simple matter of across-the-board restraint, however. Projected growth in debt service, for example, mainly reflects past borrowing. The costs of some large social programs, such as Medicaid, are driven in part by caseload growth and by complex rules dictated by the federal government. Local governments and school districts dependent on state aid must grapple with fixed costs, often state-mandated, which will continue rising unless the rules are reformed. Holding the line on total General Fund spending will require *real* cuts that actually result in *lower* spending in some other program categories. Those reductions need to produce permanent, recurring and growing savings in the years ahead.

BENCHMARK

State Spending Per Capita, 2008



New York had the 8th highest state spending per-capita, 33 percent above the national average.

Source: US Census Bureau

Can the state of New York provide essential services to taxpayers at a lower cost? The comparative statistics certainly suggest that it can—and should.

For example, although New York's local taxpayers shoulder an exceptionally heavy share of the burden for public services, New York's state government nonetheless spends considerably *more* than the national per-capita average. This includes significantly higher spending on such core state government functions as public education, transportation, prisons, public welfare, mental health, courts and the Legislature. If New York had budgeted at the national per-capita average in 2008, it would have spent *nearly $32 billion* less.

The recommendations that follow were inspired by three basic questions:

Do we really need this?
Can we afford this?
Is there a better way to do this?

“Priorities of Government”

A Performance-Based Approach to Balancing the State Budget

Conventional thinking says there are only two ways to balance a budget: raise taxes or cut important services. It says budgeting is all about maintaining the *status quo*. But when the state of Washington faced a budget crisis in 2003, then-Governor Gary Locke adopted a third approach: budgeting based on results, without raising taxes. He called this process a Priorities of Government (POG) review.

Used properly, the new budget model can help lay the foundation for responsible state spending—and in any state, including New York.

Instead of blindly struggling to maintain the state's existing budget by adjusting for inflation and caseload increases, and cutting or taxing to make up the difference, Locke (now U.S. Secretary of Commerce) wiped the chalkboard clean and started by answering four very basic questions:

1. How much money does the state have?
(What is the existing and forecasted revenue?)

2. What does the state want to accomplish?
(What are the essential services we must deliver to citizens?)

3. How will the state measure its progress in meeting those goals?

4. What is the most effective way to accomplish the state's goals with the money available?

- If a service/program is a core function, what level of government should provide it?
- How can services be provided efficiently and effectively?
- How can market forces and competition be introduced into core functions, assuring costs are controlled and quality enhanced?

After answering these questions, the governor prioritized agency activities (using ranks of high, medium and low) and purchased only the most important ones within existing revenue.[7] The result was a balanced budget—eliminating a $2.8 billion budget gap (the per-capita equivalent of the gap New York faces in 2010-11).

While the governor's model was good, he left out an important consideration: cutting important services isn't the only way to find cost savings. Necessary savings can also be found by providing services more efficiently and effectively (e.g. competitive bidding) and by instituting tough performance expectations.

Only by carefully considering the proper role of government can state officials protect individual rights while providing essential services to taxpayers in an efficient, cost-effective manner. This is not an “anti-government” philosophy; rather it is ensuring that what government is supposed to do, it will do well.

Source: Evergreen Freedom Foundation (www.effwa.org)

The proposals listed below are discussed in more detail on the following pages.[8] This 30-point plan does not represent an exhaustive list of potential budget-balancing actions; indeed, added savings will be needed to close future gaps. However, these ideas are offered as a starting point on the road to a more affordable and sustainable state budget for the future.

Table 2: Budget Actions and Savings from Projected General Fund Baseline (thousands of dollars)

		2010-11	2011-12	2012-13
1	Reform and restructure Medicaid	1,801,000	2,097,000	2,501,000
2	Medicaid fraud and abuse target	300,000	300,000	300,000
3	HCRA program reductions	173,000	173,000	173,000
4	Early Intervention means-testing		27,500	27,500
5	Refund NYSHIP premium overcharges	206,000		
6	Reduce health insurance mandates	80,000	80,000	80,000
7	Reduce and cap school aid	1,660,000	2,400,000	4,400,000
8	Cap STAR benefits	153,000	340,000	483,000
9	SUNY-CUNY flexibility reform	285,000	430,000	502,000
10	Extend Mental Hygiene DRP savings	112,000	112,000	112,000
11	Cap Municipal Aid	100,000	100,000	100,000
12	Freeze and cap non-personal service spending	144,000	252,000	312,000
13	Reduce and reorganize Judiciary	65,000	130,535	196,000
14	Reduce legislative budget by 50 percent	110,359	110,359	110,359
15	Eliminate "member item" funding	120,000		
16	Agency mergers and consolidations	54,555	54,532	54,553
	Division of Human Rights - Attorney General	*9,781*	*9,781*	*9,781*
	Council on the Arts - Education Department	*35,000*	*35,000*	*35,000*
	Consumer Protection Board - Attorney General	*3,266*	*3,231*	*3,231*
	Office of Real Property Services - Taxation and Finance	*2,500*	*2,500*	*2,500*
	Office for Prevention of Domestic Violence - Criminal Justice Services	*2,311*	*2,311*	*2,311*
	Governor's Office of Regulatory Reform - Division of the Budget	*697*	*697*	*697*
17	Welfare reforms	197,500	231,700	231,700
18	Eliminate low- and medium-priority housing programs	34,715	34,715	34,715
19	Eliminate stem cell and innovation fund	66,289	67,860	162,615
20	Adjust prison capacity to reflect population	57,000	200,000	310,000
21	Reduce spending on capital projects	140,000	100,000	100,000
22	Streamline purchasing and back office functions	50,000	166,000	333,000
23	Across-the-board cut in economic development agencies	36,000	36,000	36,000
24	Adjust State Police staffing	30,000	60,000	90,000
25	Eliminate public broadcasting subsidies	9,400	9,400	9,400
26	Eliminate Amtrak "Montrealer" subsidy	5,000	5,000	5,000
27	State workforce savings	669,000	1,574,173	1,603,173
	State Employee Wage Freeze	*328,000*	*796,000*	*882,000*
	State Employee 40 Hour Work Week		*227,000*	*227,000*
	Require early retirees to pay larger share of health premiums	*207,000*	*224,000*	*242,000*
	Modify state employee contributions for family health care	*75,000*	*75,000*	*75,000*
	Require state retirees to pay Part B Medicare premiums	*134,000*	*134,000*	*134,000*
28	Revenue actions	345,000	389,000	389,000
	Collect taxes on purchases from Indian reservations	*200,000*	*200,000*	*200,000*
	Repeal inefficient and inequitable tax credits	*64,000*	*108,000*	*108,000*
29	Moratorium on open-space land purchases	29,000	29,000	29,000
30	Pension reform and amortization		500,000	1,100,000
	GRAND TOTAL	7,032,818	10,009,774	13,785,015

1. Reform and Restructure Medicaid

New York's Medicaid program, the most costly in the nation, needs to be reconfigured to provide individual health care institutions and citizens with incentives to spend less. As of 2006, the latest year for which comparable statistics were available:

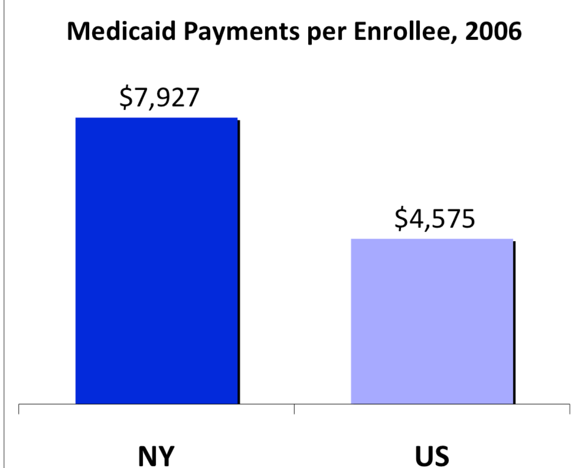
- With 6.4 percent of the nation's population and 8.7 percent of all Medicaid enrollment, New York accounted for 14 percent of all Medicaid spending.[9]

- New York's $44 billion Medicaid program, including the local government share, was larger than the total budgets of 42 states.

- New York spent 25 percent more than California, whose Medicaid program covered twice as many people.

- New York's federal, state and local Medicaid spending exceeded the Medicaid budgets of Florida, Texas and North Carolina *combined*.

BENCHMARK



New York State's Medicaid spending per enrollee is second highest in the nation, 73 percent above average.

Source: Kaiser Family Foundation

New York's massive Medicaid budget reflects deeply rooted patterns of health-care spending, regulation and utilization primarily designed to serve the needs of health care *providers* rather than patients. This yields especially extreme results when it comes to the elderly and disabled category of the Medicaid population—on whom New York spends roughly double the national average.[10]

Left unchecked, state-funded Medicaid spending in New York will grow by 37 percent over the next three years, according to projections in the 2009-10 state budget.[11] The increase will be driven largely by growing enrollment, a result in part of state policies deliberately designed to attract more New Yorkers to the Medicaid rolls. The number of New Yorkers on Medicaid was projected to rise from 3.7 million to 4 million in 2009-10 alone. By 2013, the caseload is projected to hit 4.8 million—one of every four New Yorkers. This does not include an estimated 425,000 current enrollees in Family Health Plus (FHP), a Medicaid offshoot program for families up to 150 percent of poverty, which was expected to add another 125,000 enrollees over the next three years even before the U.S. Senate passed its version of national health care legislation, which would further expand Medicaid FHP coverage.[12] State officials estimated the Senate measure would cost New York $1 billion.[13]

Closing just half the total gap in Medicaid per-enrollee costs between New York and the national average would save state and local taxpayers roughly $5 billion a year. The options outlined below would move the state a big step closer to that goal.

Managed Care Consumer Choice — Florida has pilot-tested a promising Medicaid reform that motivates health care consumers to get preventive and primary care. The pilots had two components: Choice Counseling, which helps managed care enrollees select the health maintenance organizations (HMOs) or provider service networks (PSNs) best-suited to their needs, and the Enhanced Benefit Reward (EBR) program, which creates an incentive for such enrollees to participate in routine preventive health activities.[14] An independent analysis of the Florida program found that expenditures in the demonstration counties were 22 percent lower for the disabled population and 4.6 percent lower for other managed care enrollees.[15] Based on those results, a similar pilot program in New York City could be expected to yield state-share Medicaid savings of at least $327 million a year when fully implemented.

Cap Personal Care Hours — The most costly of the optional Medicaid services financed by New York's state and local taxpayers is "personal care," a category of in-home assistance including personal hygiene, dressing and feeding. At $24,762 per recipient, personal care expenditures in New York were 234 percent of the national average in 2008.[16] By capping personal care hours at an average level that is still 150 percent of the national norm, we estimate New York could save $480 million a year. This change should be phased to minimize disruption of existing arrangements.

Adopt Competitive Institutional Rates — New York's Medicaid program pays cost-driven hospital and nursing home rates that are 15 percent above average after adjusting for differences in the cost of living and patient conditions, according to a 2007 CBC report.[17] Reducing institutional reimbursement rates to the national norm would save a total of $860 million, including $125 million in hospital payments and $735 million in nursing home payments, CBC has estimated.[18] Rate reductions proposed by Governor Paterson in his 2009-10 Deficit Reduction Plan (DRP) are incorporated in this proposal.[19]

Close Eligibility Loopholes for Certain Services — New York is one of 35 states that allow non-poor individuals to "spend down" their assets to become eligible for Medicaid care. It is even possible to do this by shifting assets away to family members. The state has a 60-month "look-back" period on patient assets to determine eligibility for skilled nursing care, but there is no look-back for home care services. New York also relies on poorly incentivized counties to recover long-term care costs from individuals of financial means who refuse to pay for care provided to their spouses under the Medicaid. The Citizens Budget Commission (CBC) has estimated that New York could save at least $454 million by instituting a look-back period for home care and by actively pursuing “spousal refusal” estate recoveries on the state level.[20]

Tighten Eligibility Screening — Asset tests, personal interviews and fingerprinting have all been eliminated as part of the eligibility screening process for Medicaid and welfare benefits. Senate Republicans have estimated that restoring these procedures would save at least $34 million a year.[21]

Postpone Family Health Plus Expansion — The Paterson Administration is seeking a federal Medicaid waiver that would allow a further expansion of the Family Health Plus (FHP) program to cover families with incomes up to 160 percent of the poverty level, compared to 150 percent under current law, and for the first time would allow FHP coverage of government employees. Based on a proposal by Senate Republicans during the DRP debate, we estimate postponement of the FHP expansion would save at least $80 million a year.[22]

Reduce Excessive Hospitalization of the Elderly — As of 2004, New York's Medicaid spending of $27,200 per elderly recipient was 242 percent of the average for other states. One reason for this was New York’s extraordinarily high rate of inpatient hospital treatment of elderly patients.[23] By reducing unnecessary hospital admissions 20 percent, after allowing some shift of funding to managed care, the state could save an additional $241 million in Medicaid payments, CBC has estimated.[24]

Evaluate and Prioritize Optional Services – New York offers most of the optional Medicaid services authorized by the federal government. In addition to personal care (see above), these include eyeglasses, and non-emergency transportation. Analysts of the system have pointed out that some optional services, especially prescription drugs and dental treatment, help prevent patients from neglecting conditions that would ultimately require more expensive mandatory Medicaid care. However, the entire array of optional Medicaid services is beyond the coverage offered under many employer-based health insurance plans. During the fall 2009 special session, Senate Republicans proposed eliminating up to $200 million in optional services, without further specifics.[25] The Governor and the rest of the Legislature should follow up by directing the state Health Department, in consultation with Medicaid administrators and health officials on the local level, to (a) report in detail on the cost and utilization of Medicaid optional services on a statewide and regional basis, (b) establish priorities among these services based solely on health care needs, and (c) to recommend at least $75 million in recurring annual savings starting on a pro-rated basis in the final quarter of 2010-11.

Table 3: Summary of Medicaid Reforms and Savings (thousands of dollars)			
	2010-11	2011-12	2012-13
More Competitive Hospital & Nursing Home Rates	860,000	860,000	860,000
Eligibility Loopholes Closure	454,000	454,000	454,000
Reduce Unnecessary Elderly Hospitalizations	241,000	241,000	241,000
Personal Care Cap	120,000	240,000	480,000
Family Health Plus Non-Expansion	80,000	80,000	80,000
Eligibility Screening Restoration	34,000	34,000	34,000
Optional programs target	18,500	75,000	75,000
Managed Care Consumer Choice and "Reward" Pilot	-	163,000	327,000
TOTAL SAVINGS	1,801,500	2,097,000	2,501,000

2. Medicaid Fraud and Abuse Target

Set Higher Targets for Fraud and Abuse Savings — A *New York Times* investigative series in 2005 quoted one authoritative source as estimating that at least 10 percent of New York Medicaid spending was based on fraudulent claims, and that another 20-30 percent was wasted on non-criminal "abuse" of the system.[26] The state's Office of Medicaid Inspector General has been ramping up to fuller effectiveness since it was established in 2006, and Governor Paterson recently raised the Medicaid fraud recovery target by $150 million for the last quarter of 2009-10 as part of his DRP.[27] In December 2009, the state comptroller called on the Health Department to increase scrutiny of Medicaid payments after auditors identified up to $92 million in overpayments, billing errors and other problems.[28] Under the circumstances, it is not unreasonable for the state's multi-year financial plan to include a hard target of at least $300 million a year in Medicaid fraud and abuse recoveries.[29]

3. HCRA Program Reductions

The $5 billion Health Care Reform Act (HCRA) budget—supported by targeted health care industry assessments, taxes and one-shot revenues from sources such as the conversion of non-profit health insurers—has mushroomed over the past decade into a vast financing pool for programs including indigent care, graduate medical education, the Elderly Pharmaceutical Insurance Coverage (EPIC) program, and Child Health Plus. It also pays for miscellaneous initiatives promoted by various health care providers and unions. The state could save about $173 million a year by eliminating various HCRA-funded "workforce" grants ($80 million) along with tobacco research grants (approximately $60 million) and smaller grants. The related taxes and assessments would be redirected into the General Fund over the next three years but slated for phase-out or steep reduction in the long term.

4. Early Intervention Means Testing

New York's Early Intervention (EI) program offers a variety of therapeutic and support services to eligible infants and toddlers with disabilities. The non-federal share of program costs historically had been split between the state and counties, although the local share was slightly increased in 2009-10 budget. However, the state has not instituted a system of means-testing for this program, which has a $183 million General Fund appropriation in 2009-10. In other states, means testing of EI "has discouraged frivolous use of services and takes into account parental ability to pay," the New York State Association of Counties says.[30] At a minimum, as first proposed by Governor Paterson in his 2009-10 budget, a system of co-pays for EI services should be instituted to save the state $28 million a year when fully implemented.

5. Refund NYSHIP premium overcharges

A recent audit by the state Comptroller's Office concurs with the findings of a 2008 Nassau County report finding that the state government and localities had paid $540 million in excessive premiums charged by the self-insured, government-run New York State Health Insurance Program (NYSHIP), which covers many public employees and retirees. A New York State Association of Counties study suggests that the state's health premiums could be reduced $206 million if NYSHIP's premium margins were reduced to the 2 percent in effect as of 2002.[31]

6. Reduce health insurance mandates

Inpatient and outpatient mental health treatment are the latest and costliest mandated benefits to be added to small group policies sold in New York. But in the case of "Timothy's Law"—as the mandate was named, after a mentally ill child who committed suicide—legislators took the unprecedented step of appropriating money to subsidize the added costs they knew they were imposing on small businesses. The $80 million subsidy should be repealed, and lawmakers should offset the cost to small firms by eliminating a sufficient number of the state's 44 insurance coverage mandates to generate equivalent savings in premiums.[32]

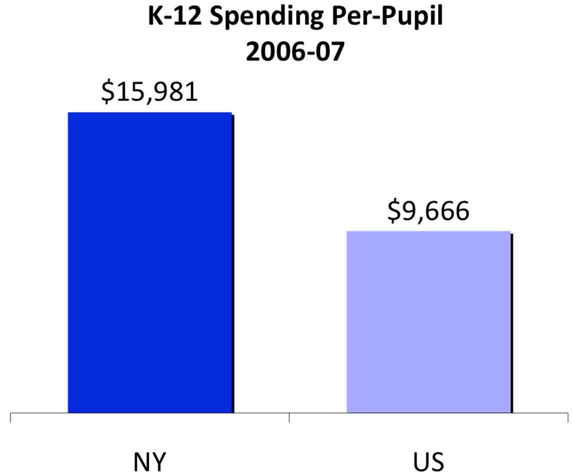
7. Reduce and Cap School Aid

Education in New York, like the state's Medicaid-subsidized health care system, costs far more the national average. Year in and year out, per-pupil spending in the Empire State is at or near the top of the charts. In the latest 50-state ranking of school spending, New York is once again number one.[33]

Aid to K-12 public schools is the largest state-funded category of New York's budget. It is also the largest single factor in the projected future growth of the state's budget shortfalls. School aid has increased 75 percent in the past 10 years—a time when enrollment was flat.

Under current law, the baseline budget for 2010-11 calls for a further increase of 11 percent (see Table 1), followed by 16 percent growth over the following two years. There is simply no way to balance New York's budget on a long-term basis without first halting and partially reversing the state's school spending binge. There are two sides to the Blueprint school aid proposal—financial restraint and essential reforms.

BENCHMARK



New York spends more on K-12 education than any other state, 65 percent above the national per-pupil average.

Source: US Census Bureau

Financial Restraint

These steps are necessary to return school aid appropriations to an affordable level for taxpayers:

- Reduce school aid by 7.5 percent on a school year basis, or about $1.6 billion below the 2009-10 level. Even after this reduction, school aid at the end of the current gubernatorial term would be about 14 percent ($2.5 billion) above the level provided by Governor Pataki's final budget in 2006-07.

- Hold school aid level in school years 2011-12 and 2012-13, allowing time for state revenues line to recover sufficiently to finance renewed increases on a sustainable basis.

Essential reforms

The pattern of state education spending in the late 1980s was strikingly similar to the trend of the past five years. After a very significant increase in state school aid, a severe fiscal crisis forced the governor and Legislature to take some of the money back. But in doing so without enacting mandate relief and other reforms, they also triggered a steep run-up in school property taxes.

This time around, taxpayers should be protected and school officials should be given tools to cope with austerity. To that end, school aid restraint should be statutorily hard-wired to the following reforms:

- Enact a school property tax cap like the one originally proposed by Governor Paterson and passed by the state Senate in 2008. The cap, modeled on Proposition 2½ in Massachusetts, would limit school property tax levy increases to inflation (currently near zero) while giving voters the opportunity to "override" the limit if they want to support larger locally funded spending increases for specific purposes.[34]

- Freeze teacher salaries for three years. For school districts outside New York City, the resulting estimated savings will offset 70 percent of the proposed state aid cut in 2010-11. A freeze would offset over half of New York City's aid reduction, compared to planned levels.

- Repeal Taylor Law provisions[35] that give teacher unions excessive financial leverage in dealings with school boards. These include the "Triborough amendment," which allows teachers to continue collecting longevity "step" increases in their salaries after expiration of contracts, and provisions restricting the ability of school districts to outsource services.[36]

- Repeal the provision in the recently enacted Tier 5 pension bill that prohibits school districts from making changes in health benefits for retirees without seeking the permission of active employees.[37]

- Ensure that schools faced with tough staff reduction choices can preserve jobs for teachers who meet the highest professional performance standards by reforming the "3020-a" statute, which makes it prohibitively expensive for districts to attempt to fire incompetent teachers, and by eliminating the statutory "firewall" between pupil performance measures and teacher evaluations. [38]

- Raise or eliminate the charter school cap to continue broadening educational choice and to ensure the state can effectively compete for its share of $4 billion in funding for educational improvement under the federal government's "Race to the Top" program, a move supported by both the Board of Regents and Governor Paterson.[39]

- Enact contracting reforms that can significantly reduce capital construction costs. As detailed in Section III (p. 44), these include repeal of the Wicks Law and of prevailing wage requirements that add hundreds of millions of dollars to school capital expenses.

8. Cap STAR Benefits

The School Tax Relief (STAR) program, enacted in 1997 and fully effective in 2000, sends money to school districts to pay for generous homestead exemptions on school property taxes. An "enhanced" STAR benefit is provided for income-qualified senior citizens. STAR effectively makes the state government a co-taxpayer with every homeowner outside New York City—which, in turn, means that the cost of STAR rises with taxes. By providing what amounts to a matching grant for school property tax increases, STAR also has had the perverse effect of encouraging *more* growth in school taxes and spending.[40] The state can save $153 million in 2010-11, growing to $483 million in 2012-13, by capping the STAR appropriation for homestead tax exemption at its current level and by raising the age threshold to effectively prevent any growth in the number of homeowners eligible for the enhanced STAR tax break.

9. Flexibility Reform for SUNY and CUNY

New York currently provides about $3.1 billion a year in General Fund support to two of the nation's largest systems of public higher education—the State University of New York, and the City University of New York.[41] However, while SUNY and CUNY have a significant degree of autonomy compared to most state agencies, they still lack control over important aspects of their operations.

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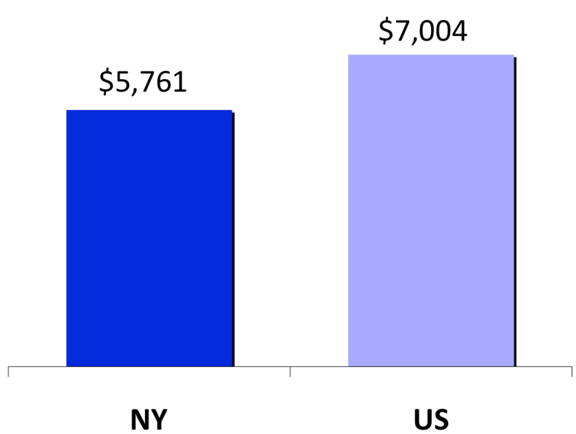
Average In-State Tuition and Fees
4-Year Public Colleges and Universities, 2009-10



Tuition and fees at 4-Year SUNY and CUNY campuses rank 36th among 50 states, 18 percent below the average.

Source: The College Board, Annual Survey of Colleges

Because almost all SUNY and CUNY revenue and expenditures flow through the state budget, tuition changes effectively require legislative approval, which inevitably leads to intense politicization of the issue. The average in-state tuition and fees charged by New York's four-year public colleges and universities was $1,243 below the national average for 2009-10. The difference between SUNY's "flagship" campuses and peers in the Northeast and New England states was even greater, as shown in Table 4 on page 16. New York also financed the nation's most generous higher education tuition assistance program, spending an average of $975 per student on need-based aid in both public and private colleges and universities.[42] Out of 50 public university systems, SUNY is one of 15 that does not control and retain its own tuition revenues, and one of only four whose contractual expenditures are pre-audited by the state comptroller.[43] University union contracts are negotiated by the governor's office, generally fitting the "pattern" of other state labor agreements.

The Blueprint proposal is:

- Grant SUNY and CUNY greater flexibility to set tuition, sell and lease assets, and collectively bargain with their employees. State General Fund support for these two systems would be converted to lump sums, eliminating all other budget appropriations for the two institutions.[44] Like the state's largest public authorities, SUNY and CUNY also would budget their own revenues; this will restrain the tendency that state officials have shown to milk university tuition and fees to close state budget gaps.

- Reduce general fund support for SUNY and CUNY by 4 percent in 2010-11 and freeze that support over the following two years. Compared to the budgetary baseline, this generates a savings of $285 million in 2010-11, growing to $502 million by 2012-13.

- Enact Tuition Assistance Program (TAP) reforms including an increase (from 12 to 15) in the semester credit-load defined as "full-time"; elimination of TAP for graduate students and students in default on federal loans; elimination of an added nursing scholarship and loan forgiveness program; and a requirement that non-remedial students meet higher academic standards to continue qualifying for TAP. Shift the resulting savings of $50 million to backfill General Fund support of SUNY and CUNY.

Table 4: Tuition and Fees at Flagship Public Institutions
Mid-Atlantic and New England, 2009-10

		In-State	Out-of-State
CT	University of Connecticut	$9,886	$25,486
DE	University of Delaware	$9,486	$23,186
ME	University of Maine	$9,626	$23,876
MD	University of Maryland: College Park	$8,053	$23,990
MA	University of Massachusetts Amherst	$11,917	$23,415
NH	University of New Hampshire	$12,743	$26,713
NJ	Rutgers, The State University of New Jersey*	$11,886	$22,518
NY	State University of New York at Buffalo	$7,013	$14,913
PA	Penn State University Park	$15,308	$25,946
RI	University of Rhode Island	$9,528	$26,026
VT	University of Vermont	$13,554	$31,410

* New Brunswick/Piscataway Campus

Source: The College Board, Annual Survey of Colleges

10. Cap Mental Hygiene Spending Growth

The General Fund share of local assistance spending on Mental Hygiene programs—including Mental Health, Mental Retardation and Development Disabilities, and Alcoholism and Substance Abuse—was reduced $112 million as part of the deficit reduction plan approved by Governor Paterson and the Legislature in December 2009. This same figure should be the minimum target for recurring annual savings in this area, whose General Fund budget otherwise is projected to grow by 18 percent ($384 million) over the next three years.

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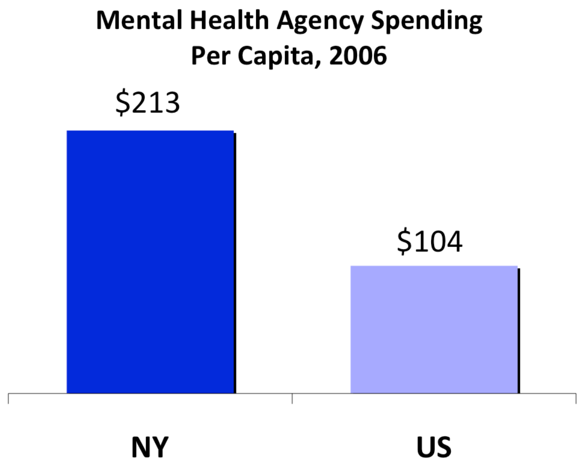

New York spends more than twice the national average on its mental health agency and ranks third overall.

Source: Kaiser Family Foundation

Budget reform in the Department of Mental Hygiene should focus primarily on the state's expensive system of mental hospitals and treatment centers, which are the major reason why New York's mental health spending is more than twice the national per-capita average. As of 2004, while only 10 percent of the 500,000 New Yorkers in mental health programs were housed in one of the state's inpatient psychiatric facilities, about one-third of the total mental health budget was spent on their case.[45] However, past gubernatorial proposals to close or merge facilities repeatedly have been rejected by the Legislature. The state's 2007 law authorizing civil commitment of sex offenders has only added to mental health institutional costs. A task force modeled on the Berger Commission, which recommended a restructuring of New York hospitals and nursing homes, should be created to recommend a comprehensive overhaul of the mental health system.

11. Cap State Aid to Municipalities

The establishment of Aid and Incentives to Municipalities (AIM) program in the 2005-06 budget marked a significant reform of the state's revenue sharing program for towns, cities and villages. Five categorical aid streams were merged into one and linked to a requirement that municipalities adopt long-term financial plans with the goal of reducing costs and property taxes. The program has since grown from $850 million to nearly $1.1 billion. In the December 2009 Deficit Reduction Plan (DRP), Governor Paterson and the Legislature agreed to cut $32 million in AIM payments, reserving the largest cuts for cities least reliant on aid. Following up on the DRP action, a $100 million annual reduction in AIM over the next several years would still leave the program about 18 percent above 2005-06 levels. The AIM distribution formula should be revised to limit the impact of the aid reduction on the most "distressed" municipalities. However, as with K-12 school aid, reductions in municipal aid should be accompanied by sweeping mandate relief that will produce recurring savings for local governments (see Section III). For example, a wage freeze would save cities and towns a combined total of $100 million, minimizing the impact of an AIM reduction.[46]

12. Freeze non-personal service spending

This part of the budget includes expenditures on supplies, travel and contractual services. Freezing it at 2009-10 levels would save $144 million in 2010-11, growing to $312 million by 2012-13.

13. Reduce Judiciary Staffing and Restructure Budget

Administrative control of New York courts is unified at the state level under the Office of Court Administration (OCA), which oversees everything from court operations to courthouse design. National filing statistics indicate New York courts handle one of the nation's heaviest per-capita caseloads.[47] However, New York State's combined judicial spending is also strikingly high, given the economies of scale that would be expected to result from a centralized system.[48]

The Judiciary has been one of the fastest growing areas of the budget over the past 10 years, adding 2,435 full-time equivalent employees since 1999-2000, a staff increase of 16 percent. Prior to her retirement in 2008, Chief Judge Judith Kaye and her special commission on modernization of the court system presented the Legislature with a court reorganization plan that they said would yield savings of $59 million a year.[49] That plan, which requires a constitutional amendment to fully implement, has not been approved by the Legislature, which also has not acted on a proposed judicial pay hike.

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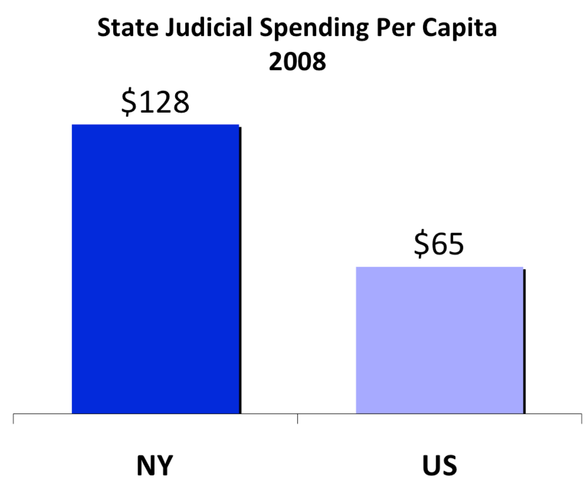

New York State ranks seventh in judicial spending, nearly double the national per-capita average.

Source: US Census Bureau

We estimate that a phased-in rollback of court staffing to 1999-2000 levels through attrition would save $65 million in 2010-11, growing to nearly $196 million in 2012-13, not counting further savings from a proposed pay freeze.[50]

14. Adjust Legislative Spending to National Average

At nearly $1 million per member, the budget for New York's 212-member state Legislature was more than two-and-a-half times the national average per member as of 2008. With 3,550 full-time equivalent employees as of July 2009, the combined Senate and Assembly staff was also among the largest. The New York State Legislature is rife with duplication, including separate TV studios and photography operations for each conference in each house.[51] Cutting this budget in half—to a level still well above the national norm, easily exceeding legislative budgets in most large states—would save $110 million a year compared to projected amounts.

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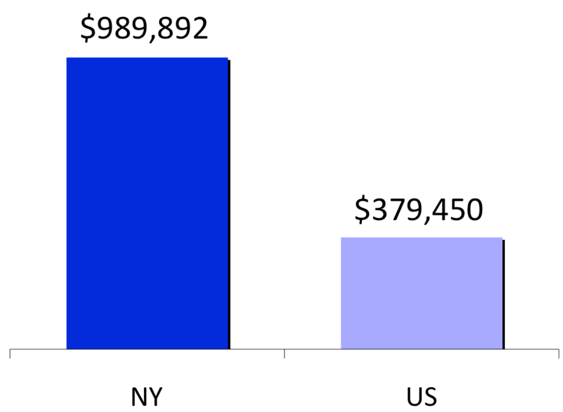
Legislative Spending Per Member 2008



New York ranks fourth in legislative spending, 161 percent above the national average.

Source: US Census Bureau, National Conference of State Legislatures

15. Permanently eliminate legislative "member items"

The Legislature this year once again refilled its principal pork barrel account with thousands of grants, mostly small, for a seemingly endless variety of purposes. Member items include dozens and dozens of grants to Little Leagues and other youth sports groups for everything from uniforms to field improvements—the kind of thing that, not too long ago, such groups paid for entirely through voluntary bake sales, raffles and 50-50 drawings.

Member items often service unobjectionable or even laudable community purposes—but why are the taxpayers throughout the state footing the bill? Not counting member items, the $133 billion state budget already includes hundreds of millions of dollars in funding for regular state agency programs with goals similar or even identical to that of member-item grants in areas such as services to senior citizens. The state could save $120 million in 2010-11 by immediately and permanently eliminating cash reserves being held for member items.

16. Agency mergers and consolidations

Division of Human Rights – Attorney General's Office

New York has a proud history of promoting civil rights and equality of opportunity, dating back to open-housing statutes passed a full two decades before the federal civil rights revolution of the 1960s. Given the hundreds of millions of dollars now spent on multiple layers of law enforcement, courts and prosecutors at the federal and state level, a separate state human rights agency with a 222-member staff (nearly 30 percent larger than in 1996) and a budget of nearly $13 million is difficult to justify. After shifting $3 million to the Office of the Attorney General to create a new Human Rights Unit, net annual savings from eliminating the Division would come to nearly $10 million.

Council on the Arts – Department of Education

New York's heavy spending on state grants to cultural institutions, arts groups and individual artists is especially striking given the fact that New York City separately is spending $160 million in local funds for essentially the same purposes—exceeding the budget of the National Endowment for the Arts.[52] Arts and cultural agencies, like other nonprofits, have been financially stressed during the recession. Nonetheless, it is difficult to defend continued high spending in this area during a fiscal crisis that threatens the financing of essential public services. Eliminating the Council of the Arts, moving grants administration to the Department of Education, and limiting arts spending to the national per-capita average in areas outside New York City would generate savings of $35 million.[53]

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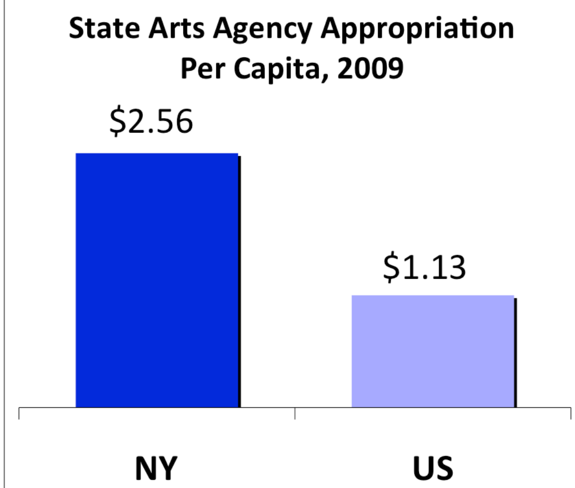

New York spends more on arts than any state, more than double the per-capita average.

Source: National Assembly of State Arts Agencies, US Census Bureau

Consumer Protection Board – Attorney General's Office

The state now supports both a Consumer Protection Board and an active Consumer Frauds Bureau in the Attorney General's office. Eliminating the CPB and shifting its function to the Attorney General would save $3.3 million a year.

Office of Real Property Services – Department of Taxation and Finance

The Office of Real Property Services (ORPS), a small agency that oversees local property tax administration, would fit neatly into the much larger state Department of Taxation and Finance (T&F), which administers all other state and local taxes. This was recognized in Governor Paterson's 2009-10 budget initiative to have T&F "host" human resources and procurement for ORPS. Assumed savings from a complete administrative merger of the two agencies are estimated at $2.5 million.

Office for Prevention of Domestic Violence – Criminal Justice Services

While domestic violence is a serious social and legal issue, there is scant justification for having a separate agency dedicated to its prevention. The functions of the Office, including a statewide hotline complementing local hotlines, should be shifted to the Office of Criminal Justice Services, for a net annual savings of $2 million.

Office for Regulatory Reform – Division of the Budget

The creation of this Office was meant to signal the Pataki administration's commitment to de-regulation, but its impact and significance has faded. Eliminating the agency and shifting responsibility for regulatory cost-benefit analysis to DOB would save about $700,000 a year.

17. Welfare reforms

The landmark federal welfare reform bill of 1995, keeping President Bill Clinton's promise to "end welfare as we know it," was a significant success in New York and across the country. The shift in emphasis from handouts to employment incentives, buttressed by increased subsidies for low-income workers, led to a 62 percent drop in the public assistance caseload between 1995 and 2005. In the first 10 years after the reforms were enacted, over one million New Yorkers left the welfare rolls, and the state's child poverty rate fell by 23 percent.[54] But New York's per-capita state spending on general welfare programs remains high by national standards, even though part of the cost is borne by New York City and county governments. The welfare reforms summarized in Table 5 on the following page would seek to reinforce the success of welfare reform and build on the principle of rewarding self-sufficiency and discouraging dependency. The resulting budget savings can be used to prevent deeper cuts in other social program areas.

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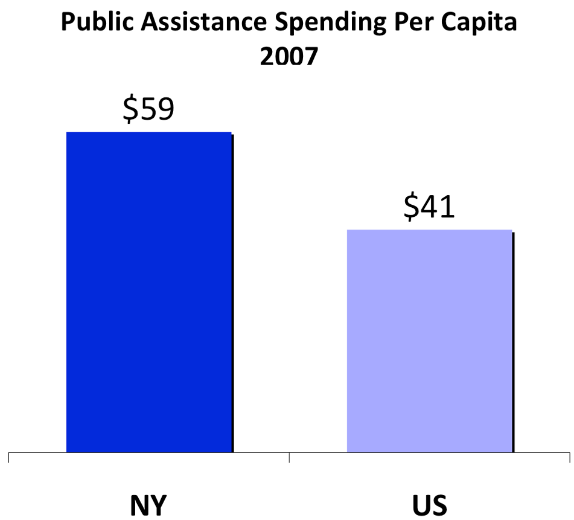


New York ranked seventh in per-capita state public assistance spending, 44 percent above average.

Source: Kaiser Family Foundation, Census Bureau

Table 5: Proposed Welfare Reforms (thousands of dollars)			
	2010-11	2011-12	2012-13
Authorize withholding of an individual's welfare grant for failure to fulfill an employment obligation	11,900	11,900	11,900
Realign earnings limits to reflect length of time an individual has been on welfare	2,100	2,100	2,100
Reduce the personal needs allowance for certain Safety Net recipients	2,200	2,200	2,200
Recognize the presence of SSI recipients when determining the grant level of a public assistance household	12,100	12,100	12,100
Establish penalties for local districts' non-compliance with minimum work requirements	11,400	45,600	45,600
Reduce the cash benefit of public assistance recipients in OASAS treatment facilities	4,400	4,400	4,400
Postpone welfare grant increase	72,000	72,000	72,000
Reduce state supplement for SSI recipients in the community	81,400	81,400	81,400
TOTAL	197,500	231,700	231,700

18. Repeal low- and medium-priority housing programs

In its 2008 core mission budgeting report, the Division of Housing and Community Renewal identified its periodic local subsidies program (which totaled $15.4 million in 2009-10) as a "low" priority.[55] The Neighborhood Preservation program ($11.6 million) and Rural Preservation program ($4.97 million) were identified as "medium" priorities. Repealing these programs, and requiring tenants (through landlord surcharges) to finance what is now a $2.7 million General Fund subsidy for administration of rent regulations in New York City and a handful of other localities, would save $34.7 million a year.

19. Eliminate Stem Cell and Innovation Fund

In 2007, New York created its own fund to subsidize stem cell research. While the Empire State had never committed so much direct support to any other form of medical research, the stem cell initiative served to highlight ideological differences between New York officials and the Bush administration on the restriction of federal funding for embryonic stem cell research. Those restrictions have now been loosened by the Obama administration, and a state-funded stem cell fund is a luxury New York taxpayers could not afford in any case. Cutting-edge medical and scientific innovation is best left to the traditionally effective mix of private venture capital and federal support. State officials can best strengthen the prospects of New York's own medical research sector by adopting comprehensive pro-growth economic policies. Eliminating the stem cell fund will save $66.2 million in 2010-11, growing to $163 million by 2012-13.

20. Adjust prison spending to reflect inmate decrease

The vast expansion of New York's prison system in the 1980s and early 1990s created the cell space needed to back up improved policing and tougher sentencing laws in the 1980s and 1990s. But New York's corrections system wasn't just more spacious; it was also more costly than the national norm as of 2001, the latest year for which comparable state data are available, as shown in the chart at right. New York's inmate population peaked at 71,472 at the end of 1999, and had dropped to 58,868 by December 2009. But prison capacity and staffing has not moved in line with population. The state now employs about 52 corrections staff per 100 inmates, compared to 46 per 100 a decade ago.

It's time to implement former Governor Spitzer's proposal, rejected by the Legislature in 2007, to establish a prison closing commission patterned after the Berger Commission. A 2007 Citizens Budget Commission study suggested that New York could save $310 million by fitting its prison structure to the population it houses.[56] Since then, the population has dropped by another 2,000 inmates, so potential savings may be even larger. Some steps in the right direction were taken by Governor Paterson and the Legislature in the 2009-10 budget with the closing of three minimum security correctional camps and of some prison annexes. The state could realize significant added savings by more aggressively pursuing alternatives to incarceration for nonviolent offenders and probation violators, as the state of Texas has recently done with some success.[57]

21. Reduce spending on capital projects

The state plans new debt issuances of $6.1 billion in 2010-11—about $130 million more than in 2009-10, and a full $1 billion more than in 2008-09. About 11 percent of the projected bonded capital consists of previously voter-approved general obligations for transportation and environmental projects, and another 17 percent would consist of transportation bonds supported mainly by dedicated taxes and fees. The remaining roughly two-thirds is distributed for other purposes, with education (both K-12 and higher education) and economic development dominating a list that also includes prisons and mental health facilities. One of the largest economic development borrowings is in support of a $4.2 billion semiconductor plant near Albany—the biggest state-subsidized project in New York's history, in which the taxpayers are effectively partnering with a subsidiary of the world's number-two semiconductor manufacturer, AMD. That project is well underway and irreversible at this point.[58] But borrowing is also authorized for a slew of other less essential purposes, including a variety of regional development projects of the sort that critics have labeled "capital pork."[59]

At least half of these non-transportation, non-voter authorized borrowings—including the final phase of the "EXCEL" school construction program—should be cancelled or postponed. The resulting $1.8 billion reduction in bonding would translate into debt service savings of about $100 million a year, although project scheduling probably means no more than half that figure could be saved in 2010-11. Another $90 million could be saved by cancelling the non-bonded portion of "state facilities equipment" purchases. We estimate total savings from this reduced capital spending would come to $140 million in 2010-11 and $100 million in subsequent years.

22. Streamline purchasing and back office functions

Governor Paterson's 2009-10 Executive Budget proposed some sharing of services by agencies, but the Legislature approved no significant changes in administrative operations. A 2007 paper by the Citizens Budget Commission (CBC) described the opportunity as follows:

> Government procurement processes have typically been cumbersome and costly. State guidelines could be reviewed and revamped to aid agencies in purchasing necessary goods and services more efficiently. Printing and other back office administrative functions could be consolidated to eliminate duplicative functions. For example, collections and cash management of various state funds now performed by more than one State agency could be brought together in one agency. Human resources support performed by internal offices in State agencies could be centralized. To cut payroll expenses, State employees and firms that have contracts with State governments could be required to have direct deposit to minimize the costs associated with processing paper checks.

CBC suggested the savings would come to 2 percent of state operations costs. After adjusting for other state operations reductions suggested in this report, that would come to about $324 million by 2012-13.

23. Across-the-board adjustment in economic development

Excluding capital projects, the state's General Fund spends about $183 million on the operations and local grants of New York's four major business service and economic development grant-making agencies: the Department of Agriculture and Markets, Department of Economic Development, the Empire

State Development Corp. and the Science and Technology Foundation. A strong case can be made that economic development grants and loans are a form of corporate welfare that has no place in the state budget even in good times. As argued in Section 5 of this report, the best economic development policy is one geared to producing low taxes and avoiding needless and costly regulations.

New York's much-criticized Empire Zone program is scheduled to expire in June 2010; in its place, the governor and Legislature should be focusing on comprehensively addressing obstacles to growth and investment throughout the state. However, the state also needs to live up to the economic development commitments it has already made; with other jurisdictions seeking to attract businesses from New York, the state cannot simply abandon the field. A cut of 20 percent in this area would yield a savings of $36 million a year.

24. Scale back State Police through attrition

The Division of State Police has added more than 1,000 employees, mostly uniformed troopers, since 1999-2000. Roughly 400 State Police employees have been assigned to the five-year-old Operation IMPACT program, which assigns state troopers and investigators to 17 high-crime urban areas outside New York City. However, the New York City Police Department has shown that crime prevention is not a mere matter of increased headcount; the city's crime rate has dropped more than 20 percent since 2002, a period in which the number of city cops was reduced by 3,400, or roughly 8 percent, despite the NYPD's added anti-terrorism responsibilities. Reducing the State Police force strength by attrition to the 1999-2000 headcount over the next three years—while making greater use of the latest digital technology to replace troopers monitoring reduced-speed zones, for example—would save $30 million in 2010-11, growing to $90 million by 2012-13.

25. Eliminate public broadcasting subsidies

The state's annual appropriation of $9.4 million in subsidies to public broadcasting is a vestige of a bygone era in communications. Government meetings increasingly are available on live webcasts, and the "educational" function that was an original justification for state support of public television has been overtaken by technology; instructional audio and video, for use by individuals or in classrooms, can now be shared online or through DVDs or other digital media. At this point, fans of commercial-free or limited-commercial public broadcasting should be expected to pay for it themselves.

26. Eliminate Amtrak subsidy

The state provides an annual subsidy of $5 million for Amtrak's *Adirondack Montrealer* train, or about $45 per rider as of 2008.[60] Meanwhile, private sector bus companies and airlines serve the same New York-Albany-Montreal corridor with no state subsidy. The subsidy should be repealed.

27. State Workforce Savings

Freeze state employee wages

Unlike most other fiscally troubled states, New York has yet to demand sacrifices from its unionized state employees. State workers received an average 3 percent increase in base salaries on April 1, 2009, and continue to receive longevity increases as well. Base pay in the fourth and final year of most current state employee union contracts will rise by another 4 percent on April 1, 2010, the start of a fiscal year during which the inflation rate is projected at 1.8 percent. The Governor and Legislature should invoke their powers to declare a financial emergency and suspend those pay hikes until the budget is permanently and sustainably balanced, for an annual savings of $328 million in 2010-11, growing to $882 million by 2012-13.[61] (See Section III on page 38 for more on the salary freeze proposal.)

State Employee 40-hour work week

Unlike most public-sector employees, who work a 40-hour week, the majority of New York State employees have a 37.5 hour weekly schedule. CBC estimated that expanding the work week would yield productivity savings worth $227 million a year. This would require collective bargaining to take effect with the next contract cycle in April 2010, so no savings can be budgeted from the change until 2010-11, at the earliest.

Require early retirees to pay a higher share of health care costs

Employees who are eligible for state pensions and retire at the end of at least 10 years on the state payroll can remain in the state health insurance plan for the rest of their lives, at a premium cost no higher than those charged to active employees (10 percent for individual coverage and 25 percent for family coverage). Retirees can also apply unused sick days to buy-down their premium costs. As a result, for most retirees, continued taxpayer-subsidized health insurance coverage is available at a steep discount or even free of charge—a perk virtually unheard of in the private sector. Retired employees who are younger than 65 and thus ineligible for federal Medicare coverage account for one-half the state's total retiree health care costs.[62] Billing early retirees for one-third of premium costs now covered by taxpayers would save $207 million in 2010-11, rising to $242 million a year by 2012-13.[63]

Require state retirees to pay Medicare Part B premiums

All retirees over 65 are eligible for the federal Medicare program, which charges a modest premium of $96.40 a month for individuals with incomes under $85,000 a year. Although retired state workers already receive more generous health benefits and guaranteed pension incomes than the vast majority of their private sector counterparts, New York is one of only six states that also reimburses a portion of its retirees' Part B premiums. Requiring retirees to pay this cost themselves would save state taxpayers at least $134 million a year.[64]

Modify state employee contributions for family health care

CBC has estimated the state could save $75 million by realigning its employee premiums for family coverage to match those of most public employers. However, this change would also be subject to collective bargaining, and thus no budget savings would appear until 2010-11 at the earliest.

28. Revenue actions

Collect taxes on Indian sales to non-Indians

The state has not exercised its right to collect taxes on retail sales to non-Indians by businesses on Indian lands, including the tribes' thriving cigarette trade. Convenience store operators say New York is losing $1 billion in taxes on cigarettes alone, while the Division of the Budget says the correct figure for lost cigarette tax revenues is more likely less than $100 million.[65] Other state officials have suggested the figure for cigarettes may be $220 million, before adjustments for likely non-compliance.[66] Including gasoline and other sales, it seems reasonable to estimate that $200 million might actually be generated by collecting taxes on Indian sales to non-Indians in New York.

Repeal unwarranted tax credits

The state could save at least $64 million next year, and $108 million by 2012-13, by eliminating tax credits that are economically inefficient or inequitable, as explained in further detail in Section V beginning on page 47.

29. Moratorium on open-space land purchases

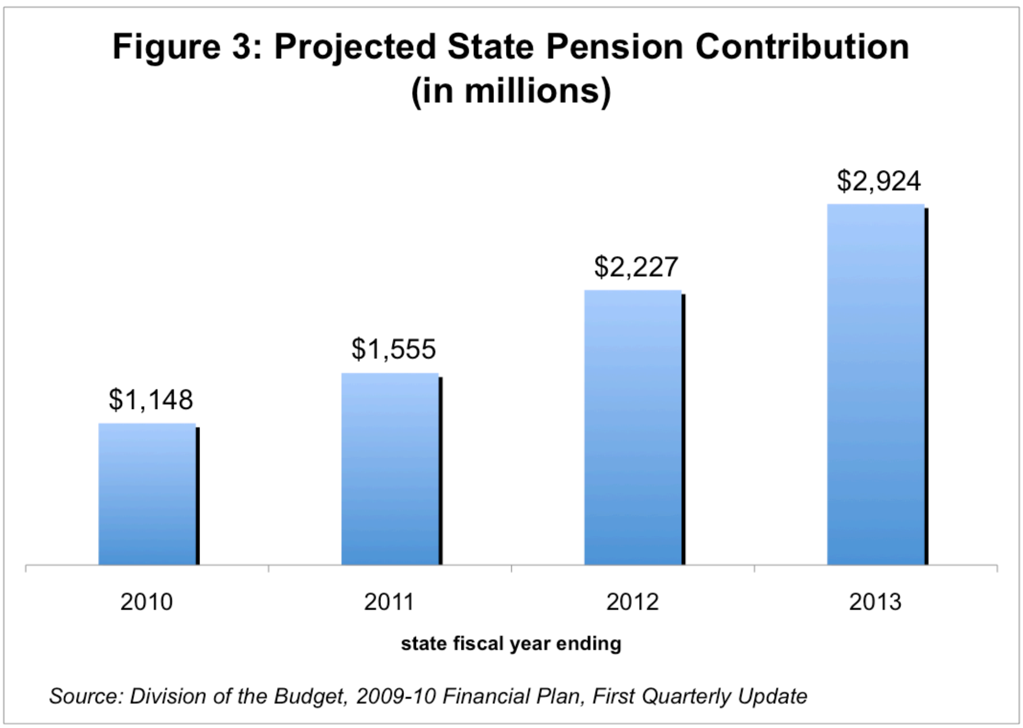
Senate Republicans have estimated the state could save $29 million annually by suspending the plan to expand its already extensive holdings of public land in areas such as the Adirondack and Catskill parks.

30. Pension reform and amortization

New York State and its local governments provide their employees with constitutionally guaranteed pensions based on workers' peak salaries and career longevity. This defined benefit (DB) system requires government employers to contribute annually to retirement funds to cover future pension payments. Employer contributions as a percentage of payroll vary depending on actuarial assumptions and market fluctuations. Earnings during bull markets reduce employer contributions, while losses during bear markets can force governments to drastically increase contributions. Since market crashes usually coincide with recessions, DB pension plans force governments to spend more when they are least able to afford it—which, for the second time in a decade, is about to happen in New York.

As illustrated in Figure 3 below, the state's annual employee pension contribution is poised to skyrocket over the next three years—and probably beyond as well. This is a delayed but inevitable result of substantial losses by the state pension fund in the falling stock market of 2007-08. While market conditions have improved, the extent of the losses over the past several years was such that the pension fund will be under-funded by tens of billions of dollars for years to come.

To reduce projected pension contribution increases, Governor Paterson, Comptroller Thomas DiNapoli and legislative leaders have sought to enact a bill allowing state and local government employers to "amortize" a potentially large portion of their pension contributions over six years, starting in 2011.[67] Contributions for state pension system at the end of the period (2015-16) would have been capped at 14.5 percent of salaries for civilian employees and 22.5 percent of salaries for members of Police and Fire System, compared to the 2009-10 rates of 7.3 percent and 15.3 percent respectively.



Where the actuarial formula calls for contributions exceeding the cap, the excess amounts would have been funded by a series of 10-year loans from the pension system, pushing pension obligations for the first half of the next decade all the way out to 2026—by which time, it is hopefully assumed, financial markets will have rebounded strongly enough to drag required contributions back to their "norm" of about 11 percent for civilian employees. Interest on delayed payments would have been set at roughly half the pension fund's 8 percent target rate of return on investments.

The proposal was based on the assumption that the pension fund's investment returns over the next 20 years will replicate its 1988-2008 experience, which included the strongest bull markets in history. However, it's equally likely the stock market will endure a 1970s-style "lost decade" of sharp ups and downs, leaving taxpayers to shoulder contribution rates in the 20 to 30 percent range for many more years. In that case, the multiyear borrowing authorized by the comptroller's plan would only make the funding problem worse as time went on.

So is there a fiscally responsible way to moderate the impact of looming increases in pension contributions for state and local government?

The answer is to recognize that the December 2009 enactment of "Tier 5," while a step backwards to a less generous and costly pension system, was not the kind of fundamental reform the retirement system needs. Amortization of scheduled pension contributions, which merely shifts the burden to future taxpayers, can be financially justified *only* on the condition that the DB pension system is closed to new members. This at least puts some boundary on potential losses from the current system. Newly hired civilian workers should be enrolled in a defined-contribution plan, which is the only sure way to permanently stabilize future retirement costs at a lower cost to the taxpayers in the long run. There's a proven model at hand: the defined-contribution retirement-savings programs that already cover tens of thousands of State University and City University employees.

Borrowing from the pension fund to avoid steep projected increases in pension costs over the next few years can only be justified if the state first closes its traditional defined-benefit retirement plan to new entrants, shifting to a more stable and predictable defined-contribution model.

Pension fund borrowing should be authorized only one year at a time, which would force the governor and Legislature to annually confront the costs that are being shifted to future taxpayers, and would allow the state to decide to raise the cap on contributions in years when revenues recover sufficiently to make that possible. The payback period should be limited to between five and seven years, with employers required to pay the same 8 percent interest rate that the fund needs to earn on its investments. The same conditions would be a prerequisite for amortization of local government and school district pension costs. Local governments might be given the option of assigning new employees to the SUNY defined-contribution plan; employers that choose to continue enrolling new hires in the traditional system would not have the option of deferring the impending increases in contributions for the DB system.

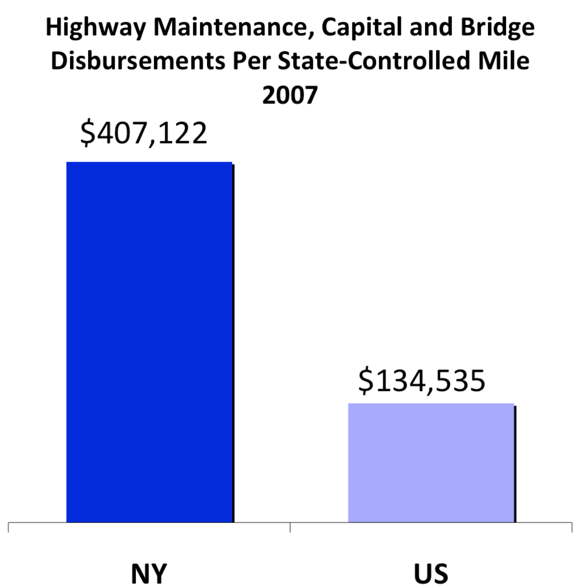
Under these conditions, we estimate that an amortization plan capping the state pension contribution rate at the projected 2010-11 level of 12.2 percent or one-half of the actuarial rate, whichever is higher, would generate net "savings" of $500 million in 2011-12 and about $850 million in 2012-13.[68] We should reiterate that this is not truly a savings, but a shift of pension costs from the next few years to later years. But again, it should be emphasized that such a shift is justifiable if—*and only if*—the state takes permanent steps to limit its now open-ended pension risks and costs by closing the traditional DB system.

Transportation — Getting More Bang for the Buck

The state has increasingly relied on off-General Fund sources to finance its transportation budget. In fact, the General Fund share of 2009-10 Department of Transportation (DOT) appropriations came to just over $100 million, or barely 2 percent of the $4.6 billion total state-funded budget for the agency. The rest was mainly classified as capital spending supported by the Dedicated Highway and Bridge Trust Fund, which in turn is financed by fuel taxes, highway use taxes and by motor vehicle fees. The vast majority of that fund now is consumed by debt service on past borrowing. General Fund baseline spending for DOT, in contrast to nearly every other major state program area, is projected to decrease over the next three years.

While transportation is a primary obligation of state government, the infrastructure share of the budget has been dwindling, as Lt. Governor Ravitch recently observed. "If you really think about our state and our country, the underfunding of infrastructure is a very, very serious problem," he said.[69] The late 2009 closure of the Champlain Bridge connecting Northern New York and Vermont has become a symbol of New York State's failure to tend to basic infrastructure.

BENCHMARK



New York State ranked sixth in total spending-per-mile on highways and bridges, triple the national average—yet New York also ranked among the bottom five in bridge and road conditions.

Source: Reason Foundation, 18th Annual Report on the Performance of State Highway Systems, 1984-2007/08

But a lack of money is not the primary problem here. In fact, New York State's transportation spending is extremely inefficient by national standards. New York State highway and bridge conditions are among the most poorly rated in the nation, yet its spending per mile is among the highest.[70] From a cost-benefit standpoint, the overall performance of New York State's highway system ranked an abysmal 45 out of 50 states, according to the Reason Foundation's 18th Annual Report on State Highway Systems. New York is one of 10 states whose road conditions worsened over the past five years, despite high spending, the report said.

Why do New Yorkers get such a paltry return on their transportation investment, both operating and capital?

A definitive answer to that question is beyond the scope of this report, but the costly contracting and procurement laws described in Section III are no doubt a big part of the answer. The staffing levels and work rules of DOT and the Thruway Authority also should be closely scrutinized and compared with those of transportation agencies in other states. Last but not least, New York needs to clearly articulate goals and priorities for infrastructure spending. While the Champlain Bridge was rusting into obsolescence, recent state transportation capital plans have included millions for local amenities like bicycle and pedestrian paths. Infrastructure development and operation, in particular, is a prime candidate for more competitive contracting and public-private partnerships, as explained below.

Privatization, Partnerships and Outsourcing

New York can (a) raise sorely needed one-shot cash to help finance its transition to more sustainable budgets, (b) realize recurring savings through increased productivity and avoided costs, and (c) tap the innovation and expertise of the private sector to undertake complex infrastructure projects by:

- selling government-owned assets and enterprises to the private sector,
- exploring the use of public-private partnerships to develop and maintain major infrastructure projects, and
- promoting competitive contracting of government services.

This section provides examples of potentially valuable initiatives to be pursued in these areas. Based on the experiences around the country, it also recommends *how* they should be approached.

Asset sales

Starting in 1995, a Privatization Commission appointed by then-Governor Pataki successfully pursued a series of asset divestiture deals involving high-profile government assets such as Stewart Airport (leased to a private operator but since sold to the Port Authority), New York Coliseum, surplus psychiatric facilities, the 14th Street Armory and the World Trade Center. Direct revenues from these sales were later estimated at $163 million. However, the state's asset privatization campaign for the most part had petered out by 2001, leaving some promising stones unturned.

The governor can restart this effort by exploring possible sales, including auctions, negotiated sales, management or employee buyouts, and placement with investors. The nature of the sale determines which method is best. Asset sales must be handled carefully and usually take a year or more to complete. Here are some recommendations on the right way to approach such transactions:

- Direct a special executive branch unit, like Pataki's commission, to identify opportunities. Any group like this is going to generate bureaucratic and political heat; to succeed, it requires top-level staff with transaction experience, a commitment to privatization, and unwavering support from agency heads and state policy makers, especially the governor.
- Provide a financial incentive for agencies to turn physical capital into financial capital: Some agencies are disinclined to sell nonproductive assets, fearing that any savings will only reduce their budget. The

easiest way to rectify this situation is to let the agency keep a share of the money earned from the sale, rather than having all proceeds revert to the General Fund. Another option is to agree to not reduce an agency's budget by the full amount of the operating savings generated.

- Adopt a capital charge system: Most agencies have little incentive to extract the greatest value from the use of their assets because the capital cost of land, buildings, and other assets is not reflected in their budgets. This can be rectified by assessing a "cost of capital" charge on all assets. A capital charge essentially applies an interest rate to all capital, creating an actual cost for using capital. The charge creates an incentive to balance a capital expenditure against its usefulness in achieving the agency's goals because suddenly, the once-invisible costs of land and buildings become very real to agencies that find themselves charged for their use.

Once the right process is in place, privatization opportunities include:

State Insurance Fund—Nationally, the largest state privatizations over the past decade have involved the sale of state-run workers' compensation funds such as New York's State Insurance Fund (SIF), a self-supporting off-budget agency staffed by state employees. The pioneer in this movement was Michigan, which sold its Accident Fund in 1993 through a public auction process to Blue Cross/Blue Shield of Michigan for $255 million. Several years later, Nevada followed Michigan's lead. It privatized its state-run workers' compensation insurance fund and opened the market to private insurers. Governor Arnold Schwarzenegger recently proposed the $1 billion sale of a portion of California's State Compensation Insurance Fund.[71] The value of New York's SIF, which is roughly half the size of the total California fund, will depend on a number of technical accounting issues and statutory considerations. But at the very least, these issues need to be painstakingly studied.

Off-Track Betting—There are six regional OTB corporations (Capital District, Catskill, Nassau, NYC, Suffolk, and Western New York). On a collective basis, these quasi-government corporations were profitable for years, even after paying pari-mutuel taxes and surcharge taxes. Despite the recent bankruptcy of New York City's OTB Corp.,[72] privatization of New York's regional OTB corporations could draw significant investor interest from local and international gaming concerns. The success of the Connecticut's OTB privatization in the 1990s provides a positive precedent. The collective value of OTB operations in the past has been estimated about $400 million, which would be shared among sponsoring localities.[73]

State University Properties and Operations—SUNY has a large number of potentially valuable properties, including the College of Optometry building on 42nd Street in midtown Manhattan, sprawling campus properties in downstate suburbs, a massive historic landmark headquarters in Albany, and three teaching hospitals (SUNY Downstate Medical Center in Brooklyn, Stony Brook University Hospital and Upstate Medical in Syracuse). By allowing the university to retain the proceeds of the sale or long-term lease of such properties, the SUNY flexibility policy recommended in this report would give the university system a strong incentive to pursue these opportunities. This also has been recommended by the Governor's Commission on Asset Maximization.

Ski Areas — The state owns three ski areas—Bellayre in the Catskills, and Whiteface and Gore Mountain in the Adirondacks—which compete to a degree with private operators. The Belleayre ski slope in particular, located with a few hours' drive of the New York City metropolitan area market, would be a prime candidate for a long-term lease to a private operator.

Golf Courses – The state Office of Parks and Recreation owns 27 golf courses around the state and could replenish its capital budget by selling or leasing more of these courses to private operators. In some cases, state land now devoted solely to golf might have higher economic value as multi-use developments.

Battery Park City — New York City, which will face added budget stress from inevitable cuts in state aid over the next several years, has a legal right to acquire this lower Manhattan development from the state Battery Park City Authority for a single dollar. A leading authority board member has said the city could then sell the Battery Park City commercial leases for $2 billion, or a profit of $1 billion after paying off the debt on the project. [74]

Roosevelt Island Operating Corp. — The state government built this middle-income housing complex in the East River and continues to own and operate it. The corporation valued its net assets, including the elevated tram connecting the island to Manhattan, at about $78 million as of 2009.

Public-Private Partnerships (PPPs)

PPPs have increasingly been seen as an option for state and local governments, particularly in the transportation and transit infrastructure arena. Under a PPP, a government entity transfers some aspect or aspects of a responsibility traditionally performed by the public sector to a private-sector partner under a well-defined, long-term contract. Some such transactions involve an up-front payment from the private-sector partner to the public-sector entity. In return, the private-sector partner receives rights to a future revenue stream—such as monies from toll collection—over a defined time frame. Other PPP structures involve a private-sector pledge to provide a service, such as operating and maintaining a free road or a subset of bus lines, in return for a regular payment from the government entity. In general, the government retains ownership of any physical infrastructure asset.

Governor Paterson’s Commission on Asset Maximization last year recommended 27 potential PPP projects including school construction and renovation in Syracuse and Yonkers, wind power on the Great Lakes, and bridge construction and renovation, most notably the Tappan Zee Bridge over the Hudson.

Unfortunately, as required by Paterson in his original executive order setting up the body, the Commission has significantly undercut the potential gains from PPPs in New York by insisting that all such deals include blanket “protections” for monopolistic labor unions, even in upstate regions where the construction sector is dominated by nonunion firms. The commission says PPP projects should promote project-labor agreements (PLAs) negotiated with organized labor. It also says that completed projects or transactions shifting state assets to the private sector should not just guarantee job security for current government workers but serve to *expand* unionized public-sector employment. [75]

Labor issues aside, the governor and Legislature will need to assess the payback from potential PPPs on a case-by-case basis, particularly when a project entails a complex, long-term contract. State officials need to evaluate whether higher borrowing costs for a private-sector partner are outweighed by the efficiencies that private developers and operators can bring to the table.

State officials seeking a quick fiscal fix from PPPs also need to understand that fluctuating private-market conditions will have an impact on the feasibility of such partnerships. Earlier in this decade, high-profile privatizations such as the Chicago Skyway and Indiana toll road privatizations may have given a skewed view of the PPP world. In retrospect, the transactions were evidence of a global credit bubble that allowed the private-sector partners to think that they could borrow at abnormally low rates over the life of the lease. Such deals may not be available on the same terms for New York.[76]

Competitive Contracting

The benefits of opening public services to private competition—in terms of cost savings and quality—are potentially enormous, as governors and mayors across the country have demonstrated. Despite Governor Pataki's early advocacy, however, competitive contracting has not taken root as the preferred approach to providing public services in New York. To the contrary: under Governors Spitzer and now Paterson, the state has reverted to “in-sourcing” jobs for transportation engineers and, most recently, information technology specialists.[77] These changes were advocated by state employee unions based on simplistic comparisons of hourly wages for state workers and private consultants. But the comparisons did not differentiate among different types of projects, did not attempt to measure productivity and did not evaluate the procedures used to select outside consultants. In fact, it could be true that state employees are less expensive in some cases while outside contractors are less expensive in others, or that one or the other is the most cost-effective choice in all cases. But at the moment, the state has no accounting procedures or evaluation process in place to definitely answer the question in any circumstance.

The process for weighing potential benefits from competitive outsourcing should be overhauled. This would begin with the Governor issuing an executive order establishing a new oversight body, the Empire Competition Council, as a vehicle for instituting competitive contracting as the standard way of doing business for every level of government in New York. The Council would include representatives from both the executive and legislative branches of state government, the state comptroller's office, and local governments. Public employee unions and the business community would be invited to designate observers on the panel.

Needed in New York: an oversight agency to conduct an annual statewide inventory of public services, develop accounting models for calculating unit costs, and establish priorities for managed competitions involving both outside firms and in-house employees.

With staff support from the Division of the Budget, the Council would conduct an annual inventory of all services and activities provided by New York State agencies and public authorities, as well as common activities of local governments. This would allow public authorities to distinguish between inherently governmental functions and potential commercial activities. The Council would also develop accounting models for determining the fully allocated and unit costs of commercial activities, since productive competition between suppliers depends on accurate and rigorous cost comparisons. Finally, the Council would establish priorities for competitive outsourcing of services and manage competitions between in-house workers and private firms to provide services. Budgets should be concentrated to give agency managers the strongest possible incentives to participate fully in the competition process.

Competition is ultimately aimed at getting better results for the taxpayer's money. To bolster this initiative, New York should also create a permanent Sunset Review Commission to recommend ways the government can cut costs, reduce waste, and improve efficiency and service levels. Specifically, the Commission would review 20 percent of state programs each year, assess the importance of each agency functions and recommend the elimination or consolidation of unneeded or outdated programs.

Given the dimensions of the state's current fiscal crisis, this is an optimal time to allow private providers to challenge New York's entrenched public-sector monopolies. For example, New York currently spends more than $3 billion in state funds on highway maintenance, bus transit subsidies, mental health facilities, motor vehicles record-keeping, human resources management, prisons, and welfare and Medicaid administration. In just these areas, efficiency gains at the low end of the 5 to 50 percent range (gains typically attributed to competitive sourcing) could translate into annual savings totaling hundreds of millions of dollars. The savings potential is even larger when viewed in the context of the more than $100 billion in total annual operating expenses of New York's state and local governments. By establishing an effective, permanent institutional framework for competitive sourcing, the state can provide much-needed practical guidance to counties, municipalities and public schools as well.

III. A FRAMEWORK FOR REFORM

State budget cuts and savings are only part of the cure for what ails New York. The cost of government in the Empire State is unaffordable and unsustainably high at every level. Reining in these costs requires fundamental reform of the rules and regulations that shape the way government does business on the state, local and school district level. This section begins by focusing on the immediate priority of controlling public-sector wages, then moves on to summarize other changes necessary.

Freeze Public-Sector Salaries

New York's fiscal crisis is in danger of becoming as severe an emergency as the New York City fiscal crisis of the mid 1970s, which prompted passage of the 1975 Emergency Financial Control Act and of later measures to remedy near-bankruptcies in Yonkers, Buffalo and Nassau County.

Taking their lead from the approach to prior local fiscal crises, the governor and Legislature should formally declare a *statewide* fiscal emergency, including an immediate statutory freeze on all public-employee salaries and wages at every level of state government. The freeze would cover both contractual pay hikes and the automatic step raises many employees get just for staying on the payroll another year. The freeze would expire in three years — if, and only if, the state has been able to balance its budget in the meantime.

> *"Increases in salary or wages of employees of the city and employees of covered organizations . . . are hereby suspended. All increased payments for holiday and vacation differentials, shift differentials, salary adjustments according to plan and step-ups or increments for employees of the city and employees of covered organizations which have taken effect . . . pursuant to collective-bargaining agreements or other analogous contracts requiring such increased payments . . . are hereby, in the same manner, suspended."*
>
> **- NYS Emergency Financial Control Act, Sec. 10, 1975**

Federal courts have twice upheld state-mandated wage freezes for public employees in New York. The most recent case came in 2006, when the US Second Circuit Court of Appeals ruled a freeze of Buffalo teacher salaries was "reasonable and necessary" despite the "substantial impairment" of the teachers' contract.[78]

In that case, the union argued that the city could have avoided the freeze by raising taxes or cutting services. But the court said, "We find no need to second-guess the wisdom of picking the wage freeze over other policy alternatives, especially those that appear more Draconian, such as further layoffs or elimination of essential services."[79]

The state government now faces similarly dire choices but on a much larger scale. After all, it has already dipped deeply into the revenue well. The 2009-10 budget included tax and fee increases of $8 million, including $1.75 billion on a regional basis to bail out the Metropolitan Transportation Authority. Yet the state still isn't even close to a sustainably balanced budget. The actions necessary to close next year's gap inevitably will have significant consequences for local governments dependent on state aid, especially New York City and local school districts elsewhere in the state.

State, local government and school district savings from a pay freeze would total roughly $1.6 billion in 2010-11 fiscal years, growing to over $2 billion a year by 2013.[80] The greatest relief would be felt by school districts, which on average have three-quarters of their budgets tied up in salary and benefit costs that have been rising by an average of 5 percent a year. A salary freeze would save school districts (including New York City's) more than $1 billion in 2010-11, lessening the impact of aid cuts that would otherwise result in significant staff reductions.

A pay freeze is a way of saving jobs and essential public services that would otherwise be jeopardized by necessary reductions in state aid.

Holding the line on salaries is just a first step. State officials in New York also need to overhaul public pensions, negotiate less expensive health insurance for government employees and clear away laws that prevent local officials from doing the same. But in the short term, a freeze will provide much-needed breathing room for implementing essential reforms, especially in health care, which will take several years to generate significant recurring savings.

Above all, a freeze can be justified on grounds of basic fairness. Government employees throughout New York have continued to receive pay increases at a time when many private-sector workers saw their wages frozen or reduced (assuming they didn't lose their jobs altogether). Given the problem's size, a freeze can't completely prevent layoffs, but it's a way of preserving jobs and public services that would otherwise be jeopardized.

Balance the Labor Bargaining Table

New York's Taylor Law was enacted to promote orderly resolution of labor-management disputes in state and local government. Unions were given the right to organize and collect dues from the vast majority of state and local government employees, in exchange for the outlawing of public employee union strikes.

While strikes are now rare and most contract disputes are settled without third party involvement, New Yorkers have paid a steep price for labor peace. Over the past 40 years, the number of state and local government jobs has grown at more than twice the rate of private-sector employment in New York, and the average pay of state and local government workers is higher than that of private-sector workers in most regions of New York.[81]

A 2007 report by the Empire Center reviewed the background of the Taylor Law and highlighted Taylor Law provisions and precedents in need of reform. The most important were:

- Compulsory "interest arbitration" for police and firefighters, which has tended to drive up salaries for uniformed services while hindering creative approaches to improving efficiency and reducing costs. The primary issue in binding arbitration should be a more rigorous standard of "ability to pay" on the part of the affected community, and the option of "last-best-offer" arbitration should be introduced.

- The Triborough Amendment, which has perpetuated generous pay arrangements, especially for teachers. The law should be repealed outright or amended to prevent longevity increases in an expired contract from continuing in the absence of a new contract. This was among the reforms supported by the Governor's Commission on Real Property Tax Relief (see below).

- State Public Employment Relations Board (PERB) rulings on "mandatory items of negotiation" that restrict the ability of government employers to pursue subcontracting of services and other cost-saving alternatives. These rulings need to overturned by statute to reaffirm management flexibility to consider competitive contracting.

Unfortunately, this is yet another area in which the governor and Legislature recently have moved in the wrong direction. The recently enacted Tier 5 pension bill (Chapter 504 of 2009) permanently extends what amounts to a prohibition on efforts by school districts to reduce the growing cost of health insurance benefits for their retirees. Unions representing state, county and municipal employees are already pressing for similar guarantees. Retiree health obligations for state and local government represent a massive unfunded liability for every level of government, exceeding $100 billion for the state and New York City alone.[82] To cope with economic and financial pressure, government managers need more flexibility, not less, to come up with equitable and imaginative ways of preserving affordable services while reducing expenses.

Address the High Cost and Number of Local Governments

Two commissions appointed by former Governor Eliot Spitzer reported back to Governor Paterson last year with scores of solid, detailed recommendations for relieving property taxes and improving the affordability of local governments.

A cap on school property tax levies was the key recommendation of the **Commission on Real Property Tax Relief**, chaired by former Nassau County Executive Thomas Suozzi.[83] The Suozzi Commission's report also recommended several other reforms, including uniform statewide property assessment standards administered at the county level, regional collective bargaining of teacher contracts, and a thorough cost evaluation of state mandates on local governments (but not a flat prohibition on unfunded mandates).

The **Commission on Local Government Efficiency and Competitiveness**, chaired by former Lt. Gov. Stan Lundine, issued 30 recommendations designed to promote the goals implied by its title.[84] Key recommendations included:

- centralization of some functions at the county level
- greater flexibility for local and county governments to share services
- reducing the number of elective offices
- improving local finance data for better benchmarking

Both commissions recommended minimum employee contributions to health insurance and reform of public construction and procurement laws. One key Lundine Commission goal was achieved when Governor Paterson signed a measure (Chapter 74 of 2009) modernizing the state Home Rule Law to make it easier to streamline town, villages and special districts. The bill, which had been spearheaded by Attorney General Andrew Cuomo, does not force change on a top-down basis. Rather, it creates a mechanism for local taxpayers to initiate referenda to bring about consolidations, mergers and shared-service arrangements between towns and villages.

Further changes came in December with the enactment of a mandate reform bill (Chapter 494 of 2009) that increases the bid threshold on public works contracts, reduces the number of municipalities required to form cooperative health plans and eases restrictions on shared services arrangements. The most significant change will eliminate double recoveries by plaintiffs in tort actions against local governments by giving municipal defendants the same right as private defendants to offset jury awards with income from collateral sources.

These were positive steps, but much more needs to be done. For example, tort claims against local governments, like those against the state, should be tried in the non-jury Court of Claims to guard against excessive jury awards. Moreover, the state's procurement laws remain outmoded and needlessly costly, according to many local officials; for example, New York is the only state that does not allow local governments to piggyback on procurement contracts bid by governments in other areas of the country or to participate in national purchasing cooperatives overseen by the federal Government Services Administration. The governor could broaden local government procurement opportunities by issuing an administrative order to that effect to the state Office of General Services.[85]

Albany legislative tradition would treat the Suozzi Commission and Lundine Commission recommendations for government consolidation, mandate relief as non-budget matters. However, cost-saving reforms for local governments should be addressed within the context of the state's multi-year financial plan as part of the comprehensive approach needed to dig out of the fiscal crisis in New York.

Curb contracting costs

Municipal officials, contractors, financial experts and design consultants agree that New York's laws governing public construction only add unnecessarily to the cost, complexity and time to completion for many projects.

The biggest problems are these:

- New York mandates that prevailing union wages be paid to workers on public construction projects; this adds 28 percent to total project costs upstate and 76 percent to project costs in downstate, according to a study by the Center for Governmental Research. Nonetheless, Governor Paterson is now pushing to extend prevailing wage requirements to projects funded by industrial development agencies.[86]

- The state Wicks Law—unique to New York—requires most public building construction projects to use multiple contractors, which is more time-consuming and costly than the prevalent private sector practice of using general contractors. Estimates of the savings to be realized from repeal of the law, which has been repeatedly proposed by governors since Mario Cuomo, range from 10 percent to 30 percent of project costs. Based on the low side of that scale, the state Association of School Business Officers said Wicks added $370 million to school construction costs in New York as of 2000-01. A recent "reform" of the Wicks Law raised the threshold triggering multiple contractor requirements—but only to levels that municipal officials say are so low they barely affect any projects.[87] The new law also further tilts bid competitions towards unionized firms—which will have the inevitable result of raising costs—by mandating that contractors have a pre-approved apprenticeship program in place for three years before bidding on significant big ticket projects.

- Project-labor agreement (PLAs) between project sponsors and labor unions have been increasingly encouraged by the state under an executive order signed by Governor Pataki in 1997. Their use has been further expanded under Governors Spitzer and Paterson. Like prevailing wage mandates and the Wicks Law, PLAs tend to drive up bids on public construction projects by steering contracts to unionized firms and encumbering projects with conditions and rules favorable to unions. For example, a study by the Beacon Hill Institute found that PLAs added 20 percent to school construction costs in New York.[88]

- New York currently prohibits both PPPs and "design build" contracting, an approach successfully used on major projects in other states, in which one firm both designs and builds the finished product.[89] Exceptions to these prohibitions have been made or proposed only in cases where project sponsors are willing to commit themselves to PLAs and other costly labor concessions.

Repealing these mandates would make it possible for the state, local governments and school districts to stretch their capital construction dollars much further. A more efficient and productive investment in capital infrastructure will yield both short-term benefits, in the form of added employment, and long-term gains from stronger capacity for economic growth in the future.

IV. BETTER BUDGET-MAKING

New York's 80-year-old Executive Budget law, rooted in Article VII of the state Constitution, has stood the test of time in many respects. But some glaring holes in the law have become more and more evident over the past couple of decades. As a result, the severity of New York State's latest fiscal crisis has been compounded by a lack of budgetary discipline, transparency and accountability. Specifically:

- There are no constitutionally binding limits on state spending or debt.
- The Legislature is not presented with and does not generate an updated four-year financial plan at the time it votes on appropriations, revenue bills and supporting legislation.
- The governor lacks permanent constitutional authority to take the steps he deems necessary to maintain a balanced budget during the fiscal year, even in the face of what he deems a cash-flow crisis.
- The current fiscal calendar is poorly aligned to revenue collection and spending patterns.

The flaws in the process were highlighted during New York's cash-flow crisis in the second half of 2009-10. Governor Paterson announced the state was facing a $3.2 billion deficit and proposed a Deficit Reduction Plan (DRP) to eliminate it. However, the Legislature ultimately produced a plan worth only $2.8 billion, most of it in the form of non-recurring "one-shot' savings that only made the 2010-11 gap larger. To avoid running out of cash at the end of the year, the governor took the unprecedented step of temporarily withholding $750 million in scheduled aid payments from school districts and other local governments. His power to act was immediately challenged in court on constitutional grounds by the statewide teachers' union and allied education groups.

Here are three statutory steps that would immediately address the most glaring shortcomings of the system:

1. Impose a binding "72-hour rule" requiring that key information about the budget be publicly available (including posting on the Internet) three days in advance of a final vote.[90] This information would include:
   a. an updated multi-year financial plan prepared by the Division of the Budget in consultation with the Legislature, and
   b. a joint report—in a uniform format for both houses—detailing the fiscal impact of changes to the governor's proposed appropriations and revenue bills.

2. Mandate budgetary balance according to Generally Accepted Accounting Principles (GAAP), which would disallow much of the timing-related gimmickry that can occur under New York's current (and atypical) cash-basis budgetary accounting.

3. Shift the start date of the fiscal year from April 1 to July 1, matching the norm for other states. Budget-makers would then have additional vital information on the April personal income tax settlement.

Other essential reforms require constitutional amendments. These would include the following:

- Impose a binding and airtight cap on state spending growth. This can best be accomplished by imitating the Tax Expenditure Limitation (TEL) laws implemented in states of Missouri, Washington and, most notably, Colorado. This approach effectively limits spending by capping the growth of revenues raised by the state, requiring that revenues in excess of inflation and population growth be refunded to taxpayers or deposited in a larger rainy day fund. A New York constitutional amendment adopting this approach was proposed in 2006 by then-Senator Raymond Meier and Assemblyman Robin Schimminger but never emerged from committee in either house.[91]

- Require voter approval of all state debt, with important exceptions for (a) a small amount of state facility upgrade debt, and (b) borrowing supported by specific project revenue such as tolls, rents and transit fares. In contrast to current law, voters could be asked to approve more than one bond proposition in a single election.

- Shift to a two-year budgeting cycle with the main budget adoption occurring in odd-numbered (non-election) years.

- Mandate that the state budget be GAAP balanced at the time of its presentation and adoption, and that it be kept in balance on a quarterly basis throughout the fiscal biennium.

- Empower the governor under limited circumstances to make uniform across-the-board reductions in appropriations, with exceptions for services essential to health and safety, in the event the Legislature first refuses to act on a plan for completely closing deficits projected by the Budget Division during a biennium.

Constitutional amendments need voter approval and can only be placed on the ballot after approval by two separately elected Legislatures. Thus, the earliest these reforms could go before voters, assuming legislative approval in 2010 and 2011, would be November 2011.

Some of these changes need not wait until then, however. For example, the next elected Governor could—and should—effectively inaugurate a two-year budget in 2011 by presenting a complete set of two-year appropriations bills along with a financial plan reflecting their amounts on an annual basis. In the absence of a constitutional provision giving the governor the power to reduce expenditures in the face of legislative inaction, the state's future bond covenants could be rewritten to include a statement to the effect that failure to correct a projected budget shortfall within a 30-day period would constitute a default requiring immediate repayment of interest and principal.

Managing—and Budgeting—for Results

Many states (but *not* New York) implemented performance measurement and budgeting systems during the 1990s. The idea was to spell out the precise outcomes that each department or private vendor is expected to accomplish and at what cost. So, for example, rather than funding asphalt, trucks, and employee hours (inputs) or even funding a certain number of repaired potholes (outputs), legislatures would purchase smooth streets (outcomes).

With a few exceptions, however, performance budgeting has not worked nearly as well in practice as in theory. One of the main stumbling blocks is a legislative reluctance to incorporate performance information into the budgeting process. This is unfortunate because, if done correctly, results-based budgeting and management can be a powerful tool for eliminating wasteful government spending. For example, as part of the Priorities of Government approach described on page 6, the state of Washington's budget office requires outcome descriptions to be added to each agency activity to better assess which programs' funding should be reduced or increased. Inspired in part by the New York City Police Department's "Compstat" program, Washington also has posted state agency performance reports online.[92]

The Empire State could benefit from imitating this approach. As a leading independent budget analyst observed several years ago:

> [T]he State of New York does not regularly measure and report on the performance of its programs, a system known as managing for results. In other words, no one in charge knows where our money is making a difference and where it isn't.
>
> Every spending cut is basically a shot in the dark. Until the state evaluates the efficiency and effectiveness of its services, and does so seriously and regularly, it will never have adequate information to make these important decisions, let alone debate the issues.[93]

If results-based budgeting is to be more than an academic exercise, there must be rewards for good performance and real consequences for poor performance. Programs that do not work should be reduced, eliminated, restructured, or consolidated into programs that do work.[94]

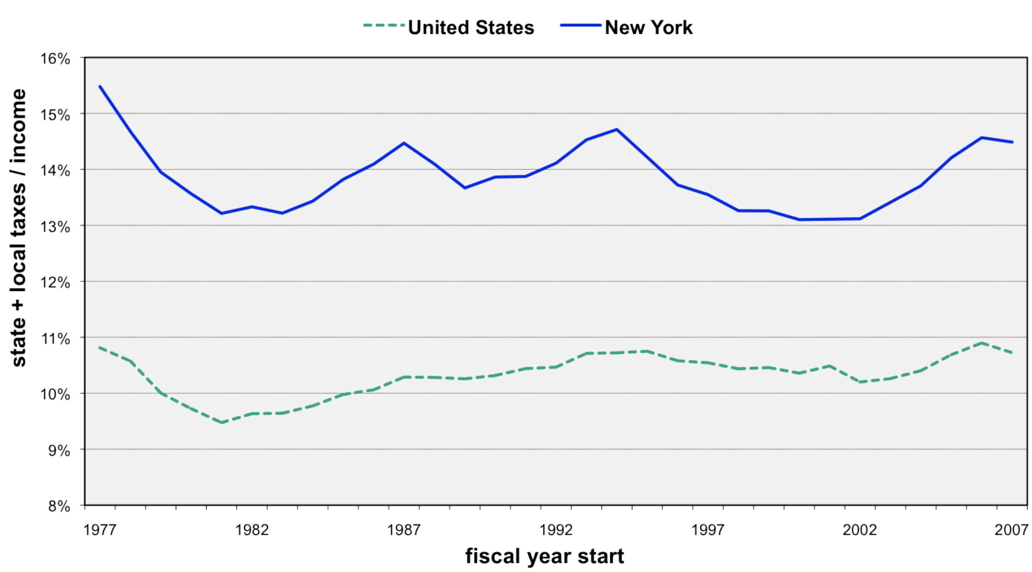
V. A Template for Pro-Growth Tax Reform

New York is a high-tax state by any measure. In 2006, New York State and its local governments and school districts collected $6,403 in taxes per resident, 160 percent of the national average. Relative to personal income, New York's state and local tax take is 133 percent of the national average.

State taxes alone in New York are 130 percent above the national per-capita average, but this figure does not reflect the full burden of local expenses effectively dictated by the state. To help finance those mandates, including a share of welfare and Medicaid expenses, New York's counties and New York City are authorized to impose their own sales taxes of up to 4.75 percent on top of the state's 4 percent state rate, and New York City adds its own resident income tax rate to the state income tax. If spending mandated by Albany was paid for entirely by the state with no further programmatic reform, the tax burden wouldn't be any lighter—it would simply be collected at a different level.

Taxes were even higher 30 years ago. In 1977, state and local taxes came to 15.48 percent of New Yorkers' personal income. This fell somewhat over the next two decades, reaching 13.10 percent in 2000 after the last significant round of state tax cuts. However, collections as a share of income rose through the current decade, due to the upward march of local property taxes, strong capital gains and Wall Street bonuses in most years, and the 2003-2005 temporary income tax surcharge. By 2006, tax collections reached 14.57 percent of personal income, less than one percentage point below the 1977 figure. [95]

Figure 4: State and Local Tax as a Share of Personal Income



Source: NYS Division of the Budget, U.S. Bureau of Economic Analysis, U.S. Census Bureau

Throughout this period, New York's tax take has far exceeded the national average. Because other states reduced their tax burdens during the 1980s and 1990s, New York's tax reforms did little to improve tax competitiveness with other states. As shown in Figure 4, New York's state and local taxes as a share of income were 143 percent of the national average in 1977. By 2007, they were still 135 percent of the national average.

While maintaining a high tax burden, New York has seen anemic private sector job growth over the last 30 years. During that period, we have matched or exceeded national private sector job growth only during three periods: the 1980-1983, 1999-2000, and 2007-2008. All of these periods came after the implementation of income tax cuts or expiration of temporary tax increases.

Falling tax rates have not meant falling tax burdens

In the last 30 years, New York's nominal income tax rates have fallen drastically. New York's top personal income tax rate peaked at 15.375 percent in 1977. By that point, a bipartisan consensus had emerged that high taxes hampered New York's competitiveness and were a driver behind the fiscal crisis that nearly bankrupted New York City. Taxes pose the same threat today.

In response, Governor Hugh Carey initiated a one-third reduction in the marginal tax rate, to a maximum of 10 percent on "earned" wages and salaries by 1981. Under Governor Mario Cuomo, higher rates on "unearned" income from dividends, interest and capital gains were eliminated, and the regular income tax rate dropped further, to under 8 percent. Finally, the top rate reached 6.85 percent under Governor Pataki. The reforms of the 1990s also expanded credits and deductions for low- and middle-income people, spreading more tax relief to all levels.

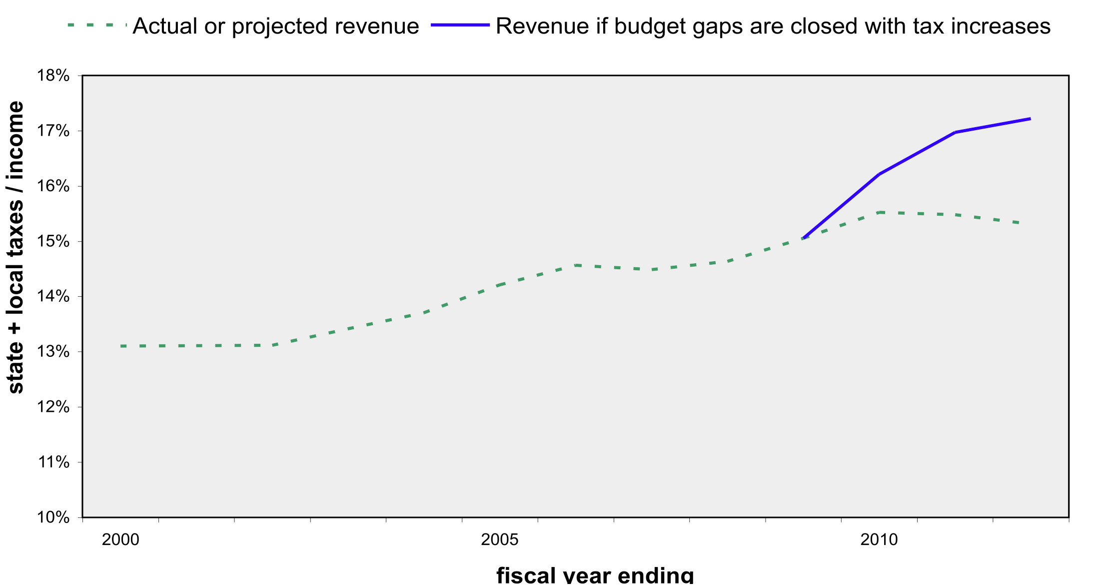
Why have drastic rate cuts only resulted in modest revenue cuts? The rate cuts were partially offset by two other phenomena: base broadening, which significantly increased the amount of income subject to tax; and "bracket creep", or tax brackets that remained fixed even as inflation increased nominal incomes.

The fall in personal income tax rates have led some observers to wrongly conclude that New York's tax system has been shifted to favor the rich over the last several decades. That is a misreading that ignores both the expansion of the tax base and the introduction of credits (principally the Earned Income Credit) that have reduced the tax burden on middle- and especially lower-income New Yorkers. Indeed, from 1995 to 2007, the share of New York income taxes paid by the top 1 percent of filers rose from 26 percent to 41 percent.

From bad to worse

The "temporary" personal income tax increase and other new taxes included in the 2009-2010 budget have increased tax collections, even as personal income falls in nominal terms. We estimate that New York state and local taxes as a share of income reached just over 15 percent in 2009, approaching the high-water mark of 1977. Current laws would produce tax revenues between 15 percent and 16 percent of income over the next three years; however, these revenues would be insufficient to fund New York governments as they are currently structured. If state taxes are increased to close the projected budget gaps based on the "current services" spending projections from the Governor's Office of the Budget, we project taxes will reach 16.21 percent of income for 2010 and 17.22 percent by 2012—far higher than peak 1970s levels.[96]

Figure 5: Actual and Projected State-Local Tax Burden



Source: Division of the Budget, U.S. Bureau of Economic Analysis, U.S. Census Bureau

A pro-growth tax policy agenda for New York

It is shocking that New York failed to reduce its tax burden further despite the windfall reaped by the state since the 1970s, in the form of a rapidly expanding financial sector. By 2006, financial sector salaries (including bonuses) accounted for 20 percent of all personal income in New York State, up from just 4 percent in the late 1970s. Over the same period, personal incomes rose from 110 percent of the national average in 1977 to 120 percent in 1996.

Just as Alaska used the discovery of oil reserves as an opportunity to repeal its income tax, New York could have seized on the historic growth in the financial industry as an opportunity to more significantly reduce taxes while continuing to grow government at a slower pace. Reducing the tax burden also would at least have lessened the anti-competitive impact of tax increases. However, raising taxes now will put New York even farther out of line with other states than it was to start with.

It is possible to balance the state's budget without repeating the mistakes of the past. We recognize that fundamental tax reform is not likely to be on the table this year, especially because across-the-board tax cuts are out of the question with the wide budget deficit. However, there are three key tax actions that New York can and should pursue immediately:

1. *Allow temporary income tax rates to sunset on schedule.*

2. *Index income tax brackets to inflation.*

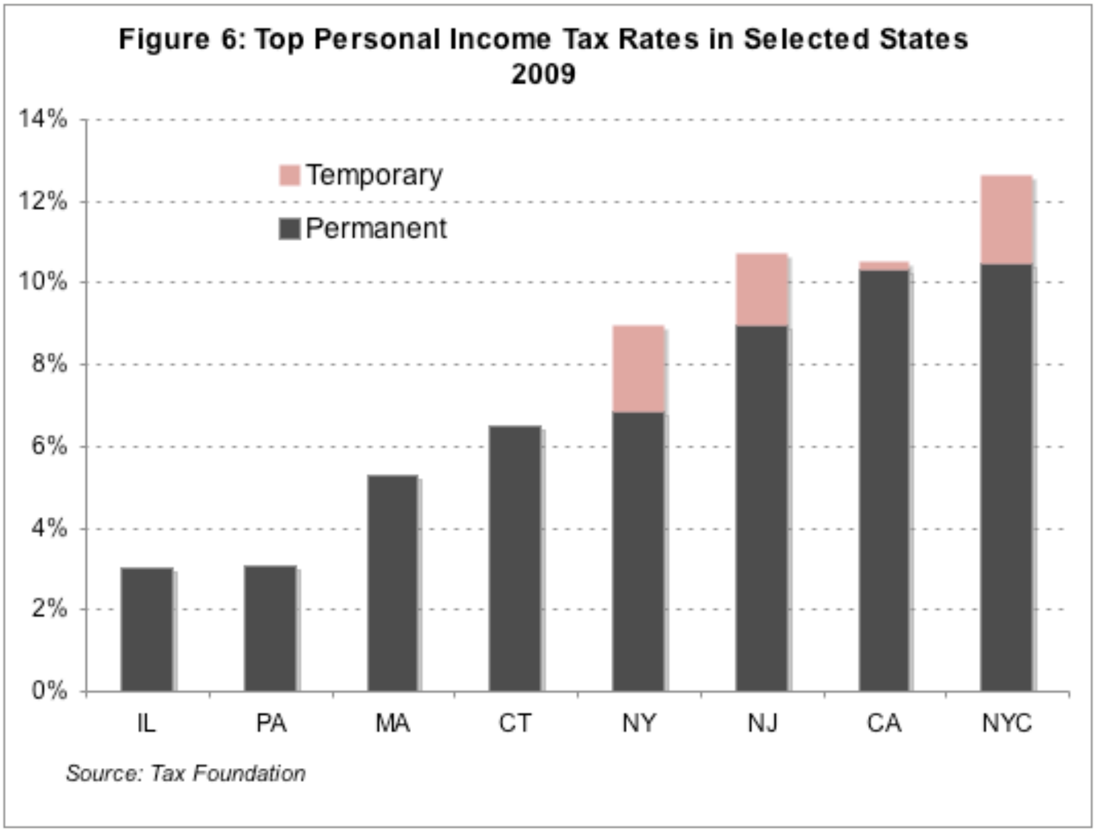
3. *Eliminate unwarranted personal income and corporate tax credits.*

In the long term, New York needs fundamental tax reform to encourage economic growth and end boom-bust budget cycles. Such a reform should reduce the total tax burden and make the tax code simpler, more neutral, and easier to comply with. At the end of this section, we lay out broad principles for such a reform.

1. Allow temporary personal income tax increases to sunset on schedule in 2011

Legislation enacted with the 2009-10 state budget raised New York's highest personal income tax rate by nearly one-third, from 6.85 percent to 8.97 percent for filers with incomes above $500,000. A second "surcharge" rate of 7.85 percent was imposed on taxpayers with incomes below $500,000 but above $200,000 for single filers (or $250,000 and $300,000 for heads of household and married joint filers, respectively). These tax increases have put New York further out of step with its surrounding states, especially in New York City where the largest concentration of high-income earners is located. New York cannot afford to permanently enshrine these rates, further discouraging wealth and job creation within its borders.

Substantial out-year budget gaps may serve as an excuse to extend the temporary tax increase —although the taxes alone raise barely enough revenue to close one-quarter of the projected 2012-13 gap. Enacting the spending-side recommendations in this report and aggressively pursuing other cost-saving options are a better alternative.



2. Index PIT brackets to inflation as part of 2010-2011 budget.

"Bracket creep" over the last 30 years, where tax brackets remained fixed while inflation devalued the dollar, led to New Yorkers' average and marginal tax rates rising from year to year through no action of the Legislature. This is unwise policy; tax rates should remain fixed on a real basis unless the Legislature acts. For this reason, the federal government annually adjusts tax brackets, personal exemptions and standard deductions in line with the rate of inflation.

New York should follow the federal government's lead and index its own tax brackets to inflation. Because inflation is near zero today, this reform has negligible short-term fiscal cost, but would protect New Yorkers from bracket creep over the long term.[97]

3. Eliminate unwarranted tax credits and preferences.

In 1986, the federal government implemented reforms that greatly simplified the income tax and broadened the tax base, while sharply cutting tax rates. Many of these reforms flowed through to New York's income tax due to the state's adoption of many federal definitions. Unfortunately, since 1986 the trend has been to create new credits and exclusions and make New York's taxes more complicated.

Some larger incentive programs—such as the Investment Tax Credit—should be eliminated in the long term in conjunction with a reduction in tax rates. However, businesses have made investment decisions in expectation that this credit would reduce their effective tax rates. Eliminating the credits now without an offsetting rate cut would be tantamount to a marginal tax rate increase on businesses—not a good act in a recession or a good way to burnish New York's image as a place to invest.

Other credits, however, do not resemble a complex reduction in tax rates. Rather, they are more akin to subsidy programs that could just as easily run through the expenditure side of the state's books. These programs should be viewed as what they fundamentally are—spending programs—and reviewed with the same critical eye as any other budget area. By eliminating the tax credits and preferences identified below, we believe New York could reduce its 2010-11 budget gap by about $95 million, with savings growing to $139 million in subsequent fiscal years.

Table 6: Estimated Savings from Eliminating Tax Credits
(dollars in thousands)

	2010-11	2011-12	2012-13
Empire State Film Production Credit		44,000	44,000
Empire State Commercial Production Credit	7,000	7,000	7,000
Green Buildings Credit	7,000	7,000	7,000
Biofuel Production Credit	10,000	10,000	10,000
Fuel Cell Electricity Generating Credit	2,000	2,000	2,000
Alternative Fuels Credit	1,000	1,000	1,000
Solar Energy System Equipment Credit	4,000	4,000	4,000
Qualified Emerging Technology Company Credits	16,000	16,000	16,000
Credit for Rehabilitation of Historic Properties	13,000	13,000	13,000
Historic Homeownership Rehab Credit	3,000	3,000	3,000
Rehabilitation Credit for Historic Barns*			
Security Training Tax Credit	1,000	1,000	1,000
Total savings	64,000	108,000	108,000

* No estimate provided for the cost of this credit

Source: Division of the Budget, 2009-10 Tax Expenditure Report

Empire State Film Production Credit

The Empire State Film Production credit subsidizes movie and TV productions in New York State. It's an expensive corporate welfare program whose costs are unjustified, and it should be abolished. A similar program subsidizing production of TV commercials should also be ended.

The film credit equals 30 percent of "below the line" production costs for film and television series in New York State. New York City provides an additional 5 percent credit for productions within its borders. "Below the line" expenses generally include all production expenses incurred in New York except payments to writers, directors, producers, and performers with speaking roles.

This credit is fully refundable against both personal and corporate income taxes, meaning that producers may receive credit payments in excess of income taxes due to New York State. As such, while the program operates through the tax code, it is economically indistinguishable from a simple subsidy program for film production.

And it's an expensive subsidy program: the state budgeted $515 million for credits in 2008 and allocated all of it to 120 projects within a year. With New York facing its greatest fiscal crisis since the Depression, Governor Paterson and legislative leaders authorized an additional $350 million. In announcing the renewal, Paterson's office touted the program's "enormous success," as though giving away free money to a favored industry is a surprising or difficult feat.

Supporters argue that the program creates jobs. On a gross basis, this is true, just as a negative 35 percent tax rate (on gross expenditures) for any industry would create jobs in that industry. What's not seen is the jobs and economic activity that are lost because New Yorkers must be taxed an extra $4 million for every production the program "brings" to the state—some of which would have been shot in New York anyway, as the TV series *Law & Order* has been since 1990. At that kind of expense, New York taxpayers should at least be getting a share of profits (or what Hollywood producers would call "backend points") on these productions, instead of serving as uncompensated partners.

There is no way of knowing for sure how much of the film production credit had been exhausted by the end of the calendar year—a lack of transparency that is yet another flaw in this program. However, assuming 25 percent of authorized funds remain unallocated, this would result in $87.5 million in savings spread over the next three fiscal years. Eliminating the advertisement subsidy would save $7 million per year.

Environmental Credits

The state offers tax incentives for environmentally friendly building practices, including the purchase of recycled building materials and installation of solar panels. Generally, the credits focus on high-visibility actions like installing solar panels and fuel cells, to the detriment of less sexy but often more efficient actions like improving insulation of existing buildings or placing enterprises in transit-served locations.

However, it is hard to see the rationale for subsidizing "green" activities at the state level. The benefits of reduced fossil fuel consumption accrue at the private level (lower energy bills), the national level (reduced dependence on foreign oil), and the global level (decreased atmospheric carbon dioxide levels). For this reason, the federal government has its own set of programs to encourage energy efficiency. What public good from installing solar panels or producing biofuels accrues specifically to New York taxpayers, and justifies state programs atop the federal ones?

These credits were intended to demonstrate a commitment to environmentally responsible practices. But as New York seeks a solution to its budget emergency, feel-good measures are the first place to cut. These credits just don't pass the necessity test. Eliminating them will save a total of $24 million a year.

Qualified Emerging Technology Company credits

New York's Investment Tax Credit (ITC) program is problematic, because it complicates the state's corporate tax code and provides an undue advantage to capital-intensive industries. However, ITCs are an embedded part of New York's tax code and serve to reduce the effective corporate income tax rate below the statutory 7.1 percent.

As part of a long-term reform, we would propose eliminating the ITC and steeply cutting the tax rate at the same time. For the short term, we recommend retaining the ITC program while making a "down payment" on reform by eliminating the Qualified Emerging Technology Company (QETC) credit program, which provides especially large (and refundable) ITC benefits to one sector.

QETCs receive favorable ITC treatment. They are eligible for credits equaling 18 percent of R&D facility costs, 9 percent of R&D expenses, and 100 percent of employee training costs up to $4,000 per employee. (ITC credits typically only cover 4 percent of eligible costs.) Unlike ITC credits available to most firms, QETC credits are fully refundable, and are estimated to cost $15 million in 2009 ($5 million on the PIT and $10 million on the CIT). QETCs are also eligible for smaller credits for capital investment and job creation, with an estimated 2009 cost of $1.4 million. Like the Film Tax Credit, these refundable credits are subsidies for a favored industry that happen to operate through the tax code, and aren't properly considered to be "tax relief." These programs should be repealed and QETCs placed on the normal, less-generous ITC schedule.

Repeal Miscellaneous Credit Programs

These programs aren't very big, but they also aren't very useful. They should be eliminated for a small budget savings, because every little bit helps.

- **Credit for Rehabilitation of Historic Properties**—The federal government already provides a tax credit for rehabilitating properties on the National Register of Historic Places; this program augments that credit by a further 30 percent. Eliminating New York's version will save $13 million a year, and ending the similar **Historic Homeownership Rehab Credit** program saves a further $3 million.

- **Rehabilitation Credit for Historic Barns**—It is difficult to come up with a more narrowly targeted tax break than this one, which allows firms and individuals to claim 25 percent of the rehabilitation cost as a credit against Corporation Franchise Tax. The fact that the cost estimate for the credit is too small to estimate does not justify its continuation.

- **Security Training Tax Credit**—Owners of buildings over 500,000 square feet—in other words, Manhattan office towers—get a $3,000 tax credit for every employee who has gone through a state-approved training program and receives at least a certain wage. This bill essentially represents a favor to a union representing building security guards. Its repeal will save New Yorkers $1 million a year.

Long Term Goals

While pursuing the short-term goals listed above, lawmakers should proceed with due speed to put New York on a course to fix its tax code for good, replacing the current tax system with one that fosters growth in the private sector.

We suggest that any reform should meet the following criteria:

- **Impose a lower tax burden overall**, measured by tax collections as a share of the economy. New York must stop being a tax and spending outlier, and especially must avoid its current trajectory which would take taxation to over 17 percent of income, a previously unseen level. Albany cannot achieve this goal without spending restraint, as emphasized in this report.

- **Apply low rates to a broad tax base.** The state should eliminate most preferences that exempt certain kinds of consumer goods and services, or certain kinds of income, from taxation. This broadening of the tax base will allow steep reductions in sales and income tax rates without reducing revenue. Equalizing tax treatment of different kinds of economic activity will encourage businesses and consumers to make choices based on what produces the best economic outcomes instead of the best tax outcomes.

- **Simplify the tax code to reduce the compliance burden.** The growing complexity of the New York State tax code is reflected in the size of the annual Tax Expenditure Report, a listing of tax preferences that over the past 10 years has swelled from 168 pages to 233 pages. Base broadening will have the added benefit of tax simplification, with businesses (for example) relieved of the obligation to figure out that Snickers is taxable candy and Twix is non-taxable food.

- **Raise more stable revenues.** New York's outsized reliance on personal income tax revenues, driven by high salaries in the financial industry, has led to a boom-bust budget cycle and massive budget gaps each time there is a recession. The imposition of new high-income tax brackets only worsens this volatility. New York should shift its revenue mix to rely more on taxing consumption and less on taxing income, as the sales tax base moves less drastically with shifts in the economy.

Tax Models from Other States

California's Commission on the 21st Century Economy has made some positive suggestions for tax reform in that state, including a flattening and simplification of the personal income tax structure.[98] This approach is also worthy of consideration in New York, although the California commission's proposal for a "business net receipts tax" to replace that state's corporate and sales tax deserves to be treated with more skepticism. This tax would be similar to value added taxes ("VATs") levied in most wealthy countries other than the United States. A key feature of the typical VAT is that it is charged on the value of imports and rebated on exports. Because this is not possible for trade across state lines, significant reliance on a VAT-style tax could introduce serious distortions in a state's economy, particularly harming firms that produce goods for final sale in other states.

Massachusetts is an example of a nearby northeastern state with a relatively large public sector that nonetheless finances itself with a relatively sound tax system. Positive features of the Bay State's tax code include a flat income tax of 5.3 percent and a 6.25 percent statewide sales tax with no local add-on. These low rates are made possible by a somewhat more frugal public sector and by broader tax bases. Property taxes in Massachusetts are lower than those in New York—despite the lack of local sales or income tax—in large part due to the Proposition 2 ½ tax cap approved by Massachusetts voters in 1980.

CONCLUSION

Trends in the world and national economy obviously will have a powerful effect on New York's own recovery over the next few years. Federal policies on health care and taxation also threaten to hobble the state's efforts to climb out of the deep hole it has dug for itself. But the greatest risk facing New York in the short term is that state officials will draw the wrong lessons from the experience of the recent past.

In the wake of terrorist attacks, an economic recession and a sharp Wall Street downturn in 2001 and 2002, New York State faced multi-billion dollar budget gaps almost as daunting as those confronted by Governor Paterson and the state Legislature at the beginning of 2010. The Legislature chose to balance the budget in 2003 with a combination of massive temporary tax increases, borrowing and other gimmicks—and virtually no significant spending reductions. New York dodged a bullet: the national economy recovered faster and more strongly than anyone had expected, spurred by tax cuts on the federal level and rock-bottom low interest rates that ultimately gave rise to a speculative bubble. Tax revenues surged, and between 2003 and 2008, New York's state government embarked on its biggest spending spree in two decades.

This time is different, however.

The economic landscape has been permanently altered, and notwithstanding the profitability of Wall Street's surviving big banks, the old financial sector model is not coming back to bail out Albany.

Billions in temporary federal stimulus funds have only postponed the inevitable. After living beyond its means for many years, the Empire State faces a day of reckoning. Raising state taxes even higher will only stifle the economic recovery. Continuing reliance on stopgap measures to balance the budget will prolong the crisis—leading to even deeper, more intractable problems in the future. Simply passing costs on to local governments and school districts will compound the already severe burden of local taxes across New York.

The solution is to permanently reduce the size and cost of both state and local government to a level New Yorkers can afford. That demands sweeping, fundamental and permanent changes in the way government does business—the kind of changes described in this report.

It *can* be done.

And if New York is to avoid a California-style collapse, it *must* be done.

SUMMARY OF RECOMMENDATIONS

Rightsizing State Government

- Save $7 billion in 2010-11, growing to nearly $14 billion over three years, through actions that include:
    - Reform and restructuring of Medicaid, more aggressive Medicaid fraud recovery targets, and reductions in other health spending commitments
    - Reduction and capping of growth in school aid
    - Merger and consolidation of state agencies
    - Targeted reductions in judicial and legislative budgets
    - Elimination or reduction of low-priority programs
    - Repeal of inequitable or inefficient tax credits

- Link school aid and municipal aid reductions to the following:
    - Cap on school property tax levies
    - Freeze on teacher salaries
    - Reform of teacher discipline statute
    - Eliminate the charter school cap
    - Repeal of prohibition on changes to retiree health benefits
    - Procurement and contracting reforms

- Pursue opportunities to raise needed cash, reduce recurring expenses and tap the expertise of the private sector through sale of state assets, public-private partnerships (PPPs), and competitive contracting.

Framework for Reform

- Provide temporary taxpayer relief through a three-year freeze on state, local and school district employee wages.

- Reform and repeal Taylor Law provisions including compulsory arbitration for police and firefighters, and the “Triborough” amendment that requires longevity pay increases in the absence of a new contract.

- Pursue Suozzi Comission and Lundine Commission recommendations for local mandate relief and savings.

- Repeal costly capital construction mandates including prevailing wages, Wicks Law, and project labor agreements.

- Modernize capital contracting requirements to allow more PPPs and “design-build” projects.

Better Budget-Making

- Impose a three-day rule for disclosure of budget bills and updated financial plans before legislative budget votes to improve transparency and accountability.

- Mandate a balanced budget on the basis of Generally Accepted Accounting Principles (GAAP).

- Shift start of the fiscal year to July 1.

- Move to a two-year fiscal cycle to promote long-term planning.

- Impose a binding constitutional limit on spending growth.

- Close the “backdoor” on borrowing by limiting circumstances under which debt can be issued without voter approval.

- Clarify the governor’s authority to postpone and impound spending during cash-flow emergencies.

- Manage for results by developing performance standards for state agencies, based on measurable outcomes compared to targets.

A Template for Tax Reform

- Focus on these short-term priorities:
  - Allow temporary income tax rates to expire on schedule.
  - Index state income tax brackets to inflation.
  - Eliminate economically inefficient or inequitable tax credits.

- Establish these long-term goals:
  - Impose a lower tax burden overall
  - Apply lower rates to a broader tax base
  - Simplify to reduce the compliance burden
  - Raise more stable revenues

APPENDIX

State Government Expenditures Per Capita FY 2008		
	Per Capita	Rank
ALABAMA	$4,756	31
ALASKA	$13,330	1
ARIZONA	$4,241	41
ARKANSAS	$5,027	24
CALIFORNIA	$5,680	15
COLORADO	$3,916	46
CONNECTICUT	$5,729	13
DELAWARE	$7,515	4
FLORIDA	$3,773	47
GEORGIA	$3,734	48
HAWAII	$7,427	5
IDAHO	$4,467	38
ILLINOIS	$4,210	43
INDIANA	$4,456	39
IOWA	$4,939	27
KANSAS	$4,870	29
KENTUCKY	$5,238	21
LOUISIANA	$6,798	7
MAINE	$5,659	16
MARYLAND	$5,383	19
MASSACHUSETTS	$6,217	9
MICHIGAN	$4,981	25
MINNESOTA	$5,796	12
MISSISSIPPI	$5,709	14
MISSOURI	$3,996	44
MONTANA	$5,606	17
NEBRASKA	$4,499	37
NEVADA	$3,584	50
NEW HAMPSHIRE	$4,311	40
NEW JERSEY	$5,391	18
NEW MEXICO	$7,263	6
NEW YORK	**$6,579**	**8**
NORTH CAROLINA	$4,566	36
NORTH DAKOTA	$5,908	11
OHIO	$4,752	32
OKLAHOMA	$4,725	34
OREGON	$4,769	30
PENNSYLVANIA	$4,884	28
RHODE ISLAND	$5,927	10
SOUTH CAROLINA	$5,132	23
SOUTH DAKOTA	$4,228	42
TENNESSEE	$3,953	45
TEXAS	$3,723	49
UTAH	$4,739	33
VERMONT	$7,577	3
VIRGINIA	$4,687	35
WASHINGTON	$5,205	22
WEST VIRGINIA	$5,335	20
WISCONSIN	$4,979	26
WYOMING	$8,569	2
UNITED STATES	$4,948	

Source: US Census Bureau

Medicaid Payments per Enrollee FY 2006		
	Per Capita	Rank
ALABAMA	$4,015	43
ALASKA	$7,644	5
ARIZONA	$2,206	50
ARKANSAS	$3,676	45
CALIFORNIA	$2,740	49
COLORADO	$4,759	29
CONNECTICUT	$7,598	6
DELAWARE	$5,152	18
FLORIDA	$4,204	37
GEORGIA	$3,296	48
HAWAII	$4,484	32
IDAHO	$4,799	28
ILLINOIS	$4,129	41
INDIANA	$4,907	24
IOWA	$5,600	16
KANSAS	$5,578	17
KENTUCKY	$4,870	25
LOUISIANA	$3,563	46
MAINE	$7,775	4
MARYLAND	$6,600	10
MASSACHUSETTS	$6,961	8
MICHIGAN	$4,199	38
MINNESOTA	$7,129	7
MISSISSIPPI	$4,144	40
MISSOURI	$4,387	35
MONTANA	$5,617	15
NEBRASKA	$5,915	12
NEVADA	$4,490	31
NEW HAMPSHIRE	$6,047	11
NEW JERSEY	$7,869	3
NEW MEXICO	$4,521	30
NEW YORK	**$7,927**	**2**
NORTH CAROLINA	$4,943	23
NORTH DAKOTA	$6,925	9
OHIO	$5,768	13
OKLAHOMA	$4,063	42
OREGON	$4,272	36
PENNSYLVANIA	$4,832	27
RHODE ISLAND	$8,082	1
SOUTH CAROLINA	$4,165	39
SOUTH DAKOTA	$5,072	20
TENNESSEE	$3,975	44
TEXAS	$3,367	47
UTAH	$5,005	22
VERMONT	$5,096	19
VIRGINIA	$4,840	26
WASHINGTON	$4,388	34
WEST VIRGINIA	$5,682	14
WISCONSIN	$4,440	33
WYOMING	$5,056	21
UNITED STATES	$4,575	

Source: Kaiser Family Foundation (www.statehealthfacts.org)

K-12 Spending Per Pupil 2006-07		
	Per Pupil	Rank
ALABAMA	$8,391	36
ALASKA	$12,300	8
ARIZONA	$7,196	47
ARKANSAS	$8,284	39
CALIFORNIA	$9,152	22
COLORADO	$8,167	40
CONNECTICUT	$12,979	5
DELAWARE	$11,829	9
FLORIDA	$8,514	35
GEORGIA	$9,127	24
HAWAII	$11,060	13
IDAHO	$6,625	49
ILLINOIS	$9,555	20
INDIANA	$8,938	29
IOWA	$8,769	31
KANSAS	$8,988	28
KENTUCKY	$8,309	38
LOUISIANA	$8,928	30
MAINE	$11,387	11
MARYLAND	$11,724	10
MASSACHUSETTS	$12,738	6
MICHIGAN	$9,912	17
MINNESOTA	$9,539	21
MISSISSIPPI	$7,473	45
MISSOURI	$8,529	34
MONTANA	$9,078	25
NEBRASKA	$9,141	23
NEVADA	$7,993	41
NEW HAMPSHIRE	$10,723	14
NEW JERSEY	$15,691	2
NEW MEXICO	$8,635	32
NEW YORK	**$15,981**	**1**
NORTH CAROLINA	$7,883	43
NORTH DAKOTA	$9,022	26
OHIO	$9,799	18
OKLAHOMA	$7,420	46
OREGON	$9,000	27
PENNSYLVANIA	$11,098	12
RHODE ISLAND	$12,612	7
SOUTH CAROLINA	$8,533	33
SOUTH DAKOTA	$7,944	42
TENNESSEE	$7,113	48
TEXAS	$7,818	44
UTAH	$5,683	50
VERMONT	$13,471	3
VIRGINIA	$10,210	16
WASHINGTON	$8,377	37
WEST VIRGINIA	$9,611	19
WISCONSIN	$10,267	15
WYOMING	$13,217	4
UNITED STATES	$9,666	
Source: US Census Bureau		

In-State Tuition and Fees 4-Year Public Colleges and Universities, 2009-10		
	Average	Rank
ALABAMA	$6,488	27
ALASKA	$4,920	42
ARIZONA	$6,554	26
ARKANSAS	$6,006	34
CALIFORNIA	$5,996	35
COLORADO	$6,309	30
CONNECTICUT	$8,540	12
DELAWARE	$8,994	9
FLORIDA	$4,382	48
GEORGIA	$4,968	40
HAWAII	$6,647	25
IDAHO	$4,887	43
ILLINOIS	$10,553	5
INDIANA	$7,676	16
IOWA	$6,714	24
KANSAS	$6,312	29
KENTUCKY	$7,118	22
LOUISIANA	$4,290	49
MAINE	$8,547	11
MARYLAND	$7,485	17
MASSACHUSETTS	$9,240	8
MICHIGAN	$9,784	6
MINNESOTA	$8,752	10
MISSISSIPPI	$4,947	41
MISSOURI	$7,247	20
MONTANA	$5,490	38
NEBRASKA	$6,233	31
NEVADA	$4,556	46
NEW HAMPSHIRE	$11,077	3
NEW JERSEY	$11,167	2
NEW MEXICO	$4,758	44
NEW YORK	**$5,761**	**36**
NORTH CAROLINA	$4,541	47
NORTH DAKOTA	$6,332	28
OHIO	$8,146	14
OKLAHOMA	$5,691	37
OREGON	$6,910	23
PENNSYLVANIA	$10,786	4
RHODE ISLAND	$8,508	13
SOUTH CAROLINA	$9,524	7
SOUTH DAKOTA	$6,146	32
TENNESSEE	$6,114	33
TEXAS	$7,347	18
UTAH	$4,614	45
VERMONT	$12,002	1
VIRGINIA	$7,952	15
WASHINGTON	$7,217	21
WEST VIRGINIA	$5,010	39
WISCONSIN	$7,261	19
WYOMING	$3,686	50
UNITED STATES	$9,666	
Source: The College Board		

State Mental Health Agency Spending Per Capita, FY 2006		
	Per Capita	Rank
ALABAMA	$64	38
ALASKA	$279	2
ARIZONA	$157	7
ARKANSAS	$39	47
CALIFORNIA	$123	15
COLORADO	$72	34
CONNECTICUT	$170	6
DELAWARE	$104	20
FLORIDA	$38	48
GEORGIA	$61	40
HAWAII	$136	12
IDAHO	$46	46
ILLINOIS	$83	29
INDIANA	$88	27
IOWA	$101	22
KANSAS	$91	25
KENTUCKY	$49	44
LOUISIANA	$61	41
MAINE	$354	1
MARYLAND	$145	9
MASSACHUSETTS	$112	17
MICHIGAN	$100	23
MINNESOTA	$140	11
MISSISSIPPI	$110	18
MISSOURI	$75	31
MONTANA	$146	8
NEBRASKA	$62	39
NEVADA	$61	42
NEW HAMPSHIRE	$127	13
NEW JERSEY	$143	10
NEW MEXICO	$26	50
NEW YORK	**$213**	**3**
NORTH CAROLINA	$126	14
NORTH DAKOTA	$72	33
OHIO	$68	36
OKLAHOMA	$49	45
OREGON	$117	16
PENNSYLVANIA	$209	4
RHODE ISLAND	$102	21
SOUTH CAROLINA	$66	37
SOUTH DAKOTA	$74	32
TENNESSEE	$88	28
TEXAS	$35	49
UTAH	$58	43
VERMONT	$198	5
VIRGINIA	$82	30
WASHINGTON	$99	24
WEST VIRGINIA	$71	35
WISCONSIN	$108	19
WYOMING	$89	26
UNITED STATES	$104	
Source: Kaiser Family Foundation (www.statehealthfacts.org)		

State Judicial Spending Per Capita FY 2008		
	Per Capita	Rank
ALABAMA	$61	25
ALASKA	$271	1
ARIZONA	$30	41
ARKANSAS	$46	35
CALIFORNIA	$114	8
COLORADO	$57	28
CONNECTICUT	$172	2
DELAWARE	$157	4
FLORIDA	$71	21
GEORGIA	$28	43
HAWAII	$164	3
IDAHO	$48	33
ILLINOIS	$27	44
INDIANA	$26	45
IOWA	$82	15
KANSAS	$54	29
KENTUCKY	$90	13
LOUISIANA	$48	34
MAINE	$70	22
MARYLAND	$84	14
MASSACHUSETTS	$132	6
MICHIGAN	$20	49
MINNESOTA	$74	18
MISSISSIPPI	$31	40
MISSOURI	$41	36
MONTANA	$80	16
NEBRASKA	$35	39
NEVADA	$23	47
NEW HAMPSHIRE	$80	17
NEW JERSEY	$102	10
NEW MEXICO	$133	5
NEW YORK	**$128**	**7**
NORTH CAROLINA	$65	24
NORTH DAKOTA	$59	27
OHIO	$30	42
OKLAHOMA	$60	26
OREGON	$72	20
PENNSYLVANIA	$39	38
RHODE ISLAND	$98	12
SOUTH CAROLINA	$18	50
SOUTH DAKOTA	$51	30
TENNESSEE	$40	37
TEXAS	$25	46
UTAH	$67	23
VERMONT	$101	11
VIRGINIA	$49	32
WASHINGTON	$21	48
WEST VIRGINIA	$74	19
WISCONSIN	$50	31
WYOMING	$114	9
UNITED STATES	$65	
Source: The College Board		

State Legislature Spending Per Member FY 2008		
	Per Member	Rank
ALABAMA	$258,343	27
ALASKA	$652,900	8
ARIZONA	$528,200	10
ARKANSAS	$279,081	26
CALIFORNIA	$2,783,008	1
COLORADO	$231,430	33
CONNECTICUT	$320,594	20
DELAWARE	$194,371	36
FLORIDA	$1,024,825	3
GEORGIA	$158,992	39
HAWAII	$380,724	16
IDAHO	$125,848	42
ILLINOIS	$390,056	15
INDIANA	$233,553	32
IOWA	$203,807	34
KANSAS	$128,436	40
KENTUCKY	$322,290	19
LOUISIANA	$409,500	13
MAINE	$125,140	43
MARYLAND	$338,346	18
MASSACHUSETTS	$282,635	25
MICHIGAN	$687,392	6
MINNESOTA	$284,189	24
MISSISSIPPI	$126,483	41
MISSOURI	$166,320	38
MONTANA	$79,813	45
NEBRASKA	$319,939	21
NEVADA	$720,238	5
NEW HAMPSHIRE	$33,177	50
NEW JERSEY	$624,642	9
NEW MEXICO	$198,518	35
NEW YORK	**$989,892**	**4**
NORTH CAROLINA	$257,976	28
NORTH DAKOTA	$52,596	48
OHIO	$354,341	17
OKLAHOMA	$243,879	31
OREGON	$394,144	14
PENNSYLVANIA	$1,261,708	2
RHODE ISLAND	$248,726	30
SOUTH CAROLINA	$310,247	22
SOUTH DAKOTA	$43,133	49
TENNESSEE	$255,894	29
TEXAS	$663,337	7
UTAH	$115,721	44
VERMONT	$54,117	47
VIRGINIA	$303,664	23
WASHINGTON	$519,088	11
WEST VIRGINIA	$187,134	37
WISCONSIN	$436,311	12
WYOMING	$64,300	46
UNITED STATES	$379,450	

Source: US Census Bureau, Empire Center calculations

State Arts Grants Per Capita FY 2009		
	Grants Per Capita	Rank
ALABAMA	$1.17	19
ALASKA	$0.97	22
ARIZONA	$0.29	48
ARKANSAS	$0.56	39
CALIFORNIA	$0.12	50
COLORADO	$0.32	47
CONNECTICUT	$2.70	2
DELAWARE	$2.26	8
FLORIDA	$0.39	44
GEORGIA	$0.39	45
HAWAII	$5.12	1
IDAHO	$0.62	33
ILLINOIS	$1.24	18
INDIANA	$0.62	35
IOWA	$0.42	43
KANSAS	$0.62	36
KENTUCKY	$0.83	27
LOUISIANA	$1.65	12
MAINE	$0.57	38
MARYLAND	$2.52	5
MASSACHUSETTS	$1.95	11
MICHIGAN	$0.76	30
MINNESOTA	$1.96	10
MISSISSIPPI	$0.65	32
MISSOURI	$2.46	6
MONTANA	$0.47	41
NEBRASKA	$0.83	28
NEVADA	$0.62	34
NEW HAMPSHIRE	$0.59	37
NEW JERSEY	$2.55	4
NEW MEXICO	$1.27	17
NEW YORK	**$2.56**	**3**
NORTH CAROLINA	$1.16	21
NORTH DAKOTA	$0.91	24
OHIO	$0.93	23
OKLAHOMA	$1.41	14
OREGON	$0.56	40
PENNSYLVANIA	$1.17	20
RHODE ISLAND	$1.99	9
SOUTH CAROLINA	$0.91	25
SOUTH DAKOTA	$0.80	29
TENNESSEE	$1.30	16
TEXAS	$0.15	49
UTAH	$1.34	15
VERMONT	$0.86	26
VIRGINIA	$0.68	31
WASHINGTON	$0.39	46
WEST VIRGINIA	$1.54	13
WISCONSIN	$0.44	42
WYOMING	$2.35	7
UNITED STATES*	$1.13	

* Includes DC and territories

Source: National Assembly of State Arts Agencies

State Public Assistance Spending* Per Capita FY 2007		
	Per Capita	Rank
ALABAMA	$0.86	45
ALASKA	$109.28	3
ARIZONA	$6.77	37
ARKANSAS	$48.33	9
CALIFORNIA	$170.64	2
COLORADO	$0.40	49
CONNECTICUT	$59.69	6
DELAWARE	$8.02	34
FLORIDA	$8.07	33
GEORGIA	$17.55	20
HAWAII	$59.77	5
IDAHO	$5.91	40
ILLINOIS	$6.59	38
INDIANA	$13.02	25
IOWA	$20.65	18
KANSAS	$13.92	24
KENTUCKY	$16.86	21
LOUISIANA	$0.45	48
MAINE	$30.38	13
MARYLAND	$7.81	35
MASSACHUSETTS	$198.99	1
MICHIGAN	$39.19	12
MINNESOTA	$22.22	16
MISSISSIPPI	$0.68	47
MISSOURI	$7.10	36
MONTANA	$14.47	23
NEBRASKA	$20.19	19
NEVADA	$12.69	26
NEW HAMPSHIRE	$26.60	15
NEW JERSEY	$27.76	14
NEW MEXICO	$9.57	31
NEW YORK	**$59.21**	**7**
NORTH CAROLINA	$5.64	41
NORTH DAKOTA	$-	50
OHIO	$9.84	30
OKLAHOMA	$21.69	17
OREGON	$11.08	29
PENNSYLVANIA	$49.24	8
RHODE ISLAND	$76.13	4
SOUTH CAROLINA	$6.47	39
SOUTH DAKOTA	$11.19	28
TENNESSEE	$5.15	42
TEXAS	$2.84	43
UTAH	$12.42	27
VERMONT	$41.85	11
VIRGINIA	$8.62	32
WASHINGTON	$43.67	10
WEST VIRGINIA	$15.43	22
WISCONSIN	$1.07	44
WYOMING	$0.86	46
UNITED STATES	$41.19	

* Includes expenditures for cash assistance under the Temporary Assistance for Needy Families (TANF) programs, and other cash assistance (i.e., state supplements to the Supplemental Security Income program, general or emergency assistance). States were asked to exclude administrative costs from reported expenditures.

Source: Kaiser Family Foundation (www.statehealthfacts.org)

State Prison Operating Costs Per Inmate 2001*		
	Per Inmate	Rank
ALABAMA	$8,128	50
ALASKA	$36,730	6
ARIZONA	$22,476	28
ARKANSAS	$15,619	43
CALIFORNIA	$25,053	23
COLORADO	$25,408	20
CONNECTICUT	$26,856	16
DELAWARE	$22,802	27
FLORIDA	$20,190	35
GEORGIA	$19,860	36
HAWAII	$21,637	33
IDAHO	$16,319	41
ILLINOIS	$21,844	31
INDIANA	$21,841	32
IOWA	$22,997	25
KANSAS	$21,381	34
KENTUCKY	$17,818	38
LOUISIANA	$12,951	47
MAINE	$44,379	1
MARYLAND	$26,398	17
MASSACHUSETTS	$37,718	3
MICHIGAN	$32,525	8
MINNESOTA	$36,836	4
MISSISSIPPI	$12,795	49
MISSOURI	$12,867	48
MONTANA	$21,898	30
NEBRASKA	$25,321	21
NEVADA	$17,572	39
NEW HAMPSHIRE	$25,949	19
NEW JERSEY	$27,347	14
NEW MEXICO	$28,035	13
NEW YORK	**$36,835**	**5**
NORTH CAROLINA	$26,984	15
NORTH DAKOTA	$22,425	29
OHIO	$26,295	18
OKLAHOMA	$16,309	42
OREGON	$36,060	7
PENNSYLVANIA	$31,900	9
RHODE ISLAND	$38,503	2
SOUTH CAROLINA	$16,762	40
SOUTH DAKOTA	$13,853	45
TENNESSEE	$18,206	37
TEXAS	$13,808	46
UTAH	$24,574	24
VERMONT	$25,178	22
VIRGINIA	$22,942	26
WASHINGTON	$30,168	10
WEST VIRGINIA	$14,817	44
WISCONSIN	$28,622	12
WYOMING	$28,845	11
UNITED STATES	$22,650	

* Latest year for which comparative statistics were calculated.

Source: US Bureau of Justice Statistics

Highway Spending* Per State-Controlled Mile 2007

	Spending per mile	Rank
ALABAMA	$125,019	27
ALASKA	$94,900	35
ARIZONA	$201,910	13
ARKANSAS	$53,089	44
CALIFORNIA	$455,529	4
COLORADO	$137,536	21
CONNECTICUT	$305,356	9
DELAWARE	$126,545	26
FLORIDA	$619,596	3
GEORGIA	$152,176	19
HAWAII	$335,135	8
IDAHO	$111,979	30
ILLINOIS	$270,192	10
INDIANA	$270,002	11
IOWA	$93,423	36
KANSAS	$101,544	33
KENTUCKY	$67,774	38
LOUISIANA	$115,022	29
MAINE	$64,255	40
MARYLAND	$376,099	7
MASSACHUSETTS	$660,456	2
MICHIGAN	$219,356	12
MINNESOTA	$116,836	28
MISSISSIPPI	$130,312	25
MISSOURI	$105,728	32
MONTANA	$54,407	42
NEBRASKA	$54,322	43
NEVADA	$179,450	16
NEW HAMPSHIRE	$163,611	17
NEW JERSEY	$1,155,149	1
NEW MEXICO	$67,658	39
NEW YORK	**$407,122**	**6**
NORTH CAROLINA	$40,567	48
NORTH DAKOTA	$47,673	46
OHIO	$135,749	22
OKLAHOMA	$91,211	37
OREGON	$196,358	14
PENNSYLVANIA	$131,997	24
RHODE ISLAND	$436,320	5
SOUTH CAROLINA	$34,382	49
SOUTH DAKOTA	$42,503	47
TENNESSEE	$95,364	34
TEXAS	$158,047	18
UTAH	$192,024	15
VERMONT	$106,656	31
VIRGINIA	$49,958	45
WASHINGTON	$134,461	23
WEST VIRGINIA	$30,810	50
WISCONSIN	$140,793	20
WYOMING	$61,643	41
UNITED STATES	$134,535	

* Highway Maintenance, Capital and Bridge Disbursements
Source: Reason Foundation

Overall Highway Performance* Rank 2007

	Ratio	Rank
ALABAMA	0.92	1
ALASKA	3.26	2
ARIZONA	0.91	3
ARKANSAS	1.08	4
CALIFORNIA	2.66	5
COLORADO	1.09	6
CONNECTICUT	1.21	7
DELAWARE	0.75	8
FLORIDA	1.26	9
GEORGIA	0.68	10
HAWAII	2.43	11
IDAHO	0.80	12
ILLINOIS	1.15	13
INDIANA	1.08	14
IOWA	0.99	15
KANSAS	0.50	16
KENTUCKY	0.69	17
LOUISIANA	1.48	18
MAINE	0.98	19
MARYLAND	1.32	20
MASSACHUSETTS	1.65	21
MICHIGAN	1.08	22
MINNESOTA	0.80	23
MISSISSIPPI	0.94	24
MISSOURI	0.91	25
MONTANA	0.55	26
NEBRASKA	0.61	27
NEVADA	0.82	28
NEW HAMPSHIRE	1.26	29
NEW JERSEY	2.64	30
NEW MEXICO	0.46	31
NEW YORK	**2.35**	**32**
NORTH CAROLINA	0.84	33
NORTH DAKOTA	0.41	34
OHIO	0.80	35
OKLAHOMA	1.12	36
OREGON	0.90	37
PENNSYLVANIA	1.24	38
RHODE ISLAND	3.00	39
SOUTH CAROLINA	0.54	40
SOUTH DAKOTA	0.62	41
TENNESSEE	0.84	42
TEXAS	0.81	43
UTAH	0.81	44
VERMONT	1.38	45
VIRGINIA	0.76	46
WASHINGTON	1.13	47
WEST VIRGINIA	0.94	48
WISCONSIN	0.86	49
WYOMING	0.55	50

* Calculated as a cost-benefit ratio adjusting for length and width of highway systems
Source: Reason Foundation

ENDNOTES

[1] Wendell Cox and E.J. McMahon, “Empire State Exodus: The Mass Migration of New Yorkers to Other States,” Empire Center for New York State Policy, October 2009. http://www.empirecenter.org/pb/2009/10/empirestateexodus102709.cfm

[2] Arthur B. Laffer, Stephen Moore and Jonathan Williams, “Rich States, Poor States: ALEC-Laffer State Competitiveness Index,” American Legislative Exchange Council, March 2009. http://www.alec.org/am/pdf/tax/09RSPS/26969_REPORT_full.pdf

[3] New York’s All Funds budget, which totaled $133 billion at the time of its adoption in 2009-10, consists of state government spending financed by all sources, including federal aid that is passed directly to local governments. The State Funds budget, which totaled nearly $86 billion, includes all spending supported by non-federal revenues, including special-purpose spending supported by dedicated taxes, fees, fines, Lottery receipts and college tuition. The state’s budget-balancing efforts are focused on the General Fund, initially pegged at just under $55 billion in 2009-10, which is comprised solely of spending supported by unrestricted state revenues. The actions proposed in this report are thus designed to produce General Fund savings. Some proposals would close portion of the General Fund budget gap by freeing up money that would otherwise be committed for State Funds spending, such as increases in STAR tax breaks or health spending financed through the HCRA (HealthCare Reform Act) fund.

[4] Ravitch remarks at “States’ Long-Term Budget Gaps: Are There Any Solutions,” conference co-sponsored by Levin Institute and Rockefeller Institute, Nov. 30, 2009. Audio at http://rockinst.org/forumsandevents/

[5] Division of the Budget, “Mid-Year Financial Plan Update, 2009-10 Through 2012-13,” http://www.budget.state.ny.us/budgetFP/midYear_update/2009-10_MidYearUpdate.pdf

[6] Revenue estimates from both the state Comptroller’s Office and Assembly Ways and Means Committee would place the 2009-10 deficit over $4 billion.

[7] New York seemed to be heading in a similar direction in 2008 when Governor Paterson directed executive agencies to produce “core mission statements” assigning low, medium or high priorities to their activities. However, this exercise appeared to have a minimal impact on the 2009-10 budget. Most agencies identified the vast majority of activities as “high” priorities, usually reserving “low” grades for programs added to their budgets by the Legislature. The “medium” grade was often applied to administrative overhead, data gathering (which aids accountability) and public access to records. Few agencies could consistently identify meaningful performance standards or measures for their activities. The governor’s directive did not cover education, higher education, the Judiciary or the Legislature

[8] In keeping with the state’s accounting focus on the General Fund, the figures in Table 2 are reductions compared to the General Fund baseline under current law; in some categories, spending would continue to increase, but at a slower rate or with expected added support from special revenues (such as tuition).

[9] Comparative data on state Medicaid expenditures are from the Kaiser Family Foundation’s statehealthfacts.org website. http://www.statehealthfacts.org/profileind.jsp?cat=4&sub=47&rgn=34

[10] Tarren Bragdon, “Medicaid In Depth: A Special Research Series,” Empire Center for New York State Policy, February 2007, http://www.empirecenter.org/pb/2007/02/ny_medicaid_rec.cfm

[11] Division of the Budget, "Mid-Year Financial Plan Update, 2009-10 Through 2012-13." See table on page 24. Due to fund shifts including the expiration of federal stimulus, the General Fund share of Medicaid was projected to increase 138 percent between 2009-10 and 2012-13.

[12] Division of the Budget, "2009-10 Enacted Budget Financial Plan," page 129. http://publications.budget.state.ny.us/budgetFP/2009-10EnactedBudget-FINAL.pdf

[13] Nelson A. Rockefeller Institute of Government, "Health Reform Poses Major Cost Questions for State Counties," forum summary at http://www.rockinst.org/forumsandevents/2009/12-16-federal_health_reform.aspx

[14] Programs are described at http://www.flmedicaidreform.com/

[15] University of Florida, "Evaluating Medicaid Reform in Florida: An Analysis of Medicaid Expenditures Before and After Implementation of Florida's Medicaid Reform Pilot Demonstration," June 2009, http://mre.phhp.ufl.edu/publications/

[16] Based on federal data, the Citizens Budget Commission estimated that New York's personal care utilization rate was 30 hours a week, compared to a national average of 11 hours. Citizens Budget Commission, "Options for Budgetary Savings in New York State: A Background Paper," October 17, 2007. http://www.cbcny.org/content/options-budget-reform-new-york-state

[17] Citizens Budget Commission, "Options for Budgetary Savings in New York State: A Background Paper," October 17, 2007. http://www.cbcny.org/content/options-budget-reform-new-york-state

[18] Ibid.

[19] State of New York, Executive Chamber, "Fact Sheet: $2.7 Billion Enacted Deficit Reform Legislation," http://www.state.ny.us/governor/press/press_1202091_factsheet.html

[20] Citizens Budget Commission, op. cit.

[21] "Senate Republicans Propose Budget Cutting Measures," News Release from State Senate Minority Leader, Oct. 14, 2009.

[22] Senate Republicans estimated this would save $100 million.

[23] Tarren Bragdon, op. cit

[24] Citizens Budget Commission, op. cit.

[25] "Senate Republicans Propose Budget Cutting Measures," op. cit.

[26] "New York Medicaid Fraud May Reach Into Billions," The New York Times, July 18, 2005, page 1A. http://www.nytimes.com/2005/07/18/nyregion/18medicaid.html?_r=1&pagewanted=2

[27] State of New York, Executive Chamber, op. cit.

[28] "DiNapoli: New York's Medicaid System Leaking Millions," New Release from Office of the State Comptroller, Dec. 22, 2009, http://www.osc.state.ny.us/press/releases/dec09/122209b.htm

[29] This is equivalent to less than 2 percent of the non-federal Medicaid spending in New York.

[30] "Closing the Gap: County Recommendations for Closing the State Budget Deficit without Shifting the Burden to Property Taxpayers," New York State Association of Counties, Oct. 6, 2009.

[31] Ibid.

[32] Federal health care "reform" legislation may complicate this task by replicating many New York insurance mandates on a national level; however, this does not constitute an argument for subsidizing one form of coverage for some employers.

[33] Two similarly affluent, urbanized and expensive northeastern states, Maryland and Massachusetts, spent $4,257 and $3,243 less per pupil than New York, respectively, but placed above New York in a recent national ranking of state educational systems. If New York spent at the Maryland rate in 2006-07, it would have saved $11.7 billion; if it had spent Massachusetts rate, it would have saved $8.9 billion.

[34] E.J. McMahon, "Enough is Enough: Why and How to Cap New York's School Property Taxes," Empire Center for New York State Policy, March 2008. http://www.empirecenter.org/Special-Reports/2008/06/PropTaxCap.cfm

[35] Terry O'Neil and E.J. McMahon, "Taylor Made: The Cost and Consequences of New York's Public-Sector Labor Laws," Empire Center for New York State Policy, October 2007. http://www.empirecenter.org/Special-Reports/2007/10/TaylorMadeReport.cfm

[36] *Manhasset Union Free School District*, 42 PERB.

[37] E.J. McMahon, "Teachers clean up on pension reform, NYFiscalWatch commentary, Dec. 2, 2009, at http://www.nyfiscalwatch.com/?p=2244

[38] New York State Schools Boards Association (NYSSBA), *Quality Educators in Every School*, 2008, at www.**nyssba**.org/clientuploads/**nyssba**_pdf/gr_3020a**QualityEducators**.pdf. According to NYSSBA, "a 3020-a proceeding takes an average of 520 days from the date charges were brought to the date a decision was issued, at an average cost of $128,000. Proceedings addressing charges of pedagogical incompetence are even longer, spanning on average 830 days and costing on average $313,000."

[39] "Paterson: Let's Not Race to the Middle," *New York Observer*, Dec. 15, 2009, http://www.observer.com/2009/politics/paterson-lets-not-race-middle

[40] *See* Tae Ho Eom, William Duncombe and John Yinger, "Unintended Consequences of Property Tax Relief: New York's STAR Program," October 2005, Abstract. Center for Policy Research, Maxwell School of Citizenship and Public Affairs, Syracuse University, http://www.cpr.maxwell.syr.edu/cprwps/pdf/wp71.pdf, and Rockoff, Jonah E., "Community Heterogeneity and Local Response to Fiscal Incentives," December 2003. http://www0.gsb.columbia.edu/faculty/jrockoff/papers/rockoff_local_response_dec_03.pdf

[41] Including tuition, fees and other non-General Fund revenue, total state operating funds spending for SUNY and CUNY was over $7.7 billion in 2009-10.

[42] Data for 2007-08 from U.S. Department of Education, National Center for Education Statistics, Integrated Postsecondary Data System, as reported by the National Association of State Student Grant and Aid Programs in its *39th Annual Survey Report on State-Sponsored Student Financial Aid*.

[43] State Higher Education Executive Officers, "State Tuition, Fees, and Financial Assistance Polices for Public Colleges and Universities, 2005-06," at http://dev.sheeo.org/finance/tuitsurv-home.htm

[44] Given the state Constitution's requirement that all funds spent by state agencies be appropriated, the greater flexibility recommended here for SUNY and CUNY might require that the two university systems be statutorily reclassified as public benefit corporations.

[45] State of New York, 2003-04 Executive Budget Message, page 70.

[46] Cities would save $48 million and towns would save $63 million, assuming 3 percent average growth in personal service costs, based on 2008 financial data for local governments collected by the Office of State Comptroller at http://www.osc.state.ny.us/localgov/datanstat/index.htm.

[47] *See* "State Court Statistics 2007," A joint project of the Conference of State Court Administrators, the Bureau of Justice Statistics, and the National Center for State Courts' Court Statistics Project, 2008. New York's statistics are among those classified as incomplete for comparison purposes.
http://www.ncsconline.org/D_research/CSP/2007_files/State Court Caseload Statistics 2007.pdf

[48] US Census data for fiscal 2007 indicate New York's combined state and local judicial expenditures were 37 percent above the national average.

[49] "A Court System for the Future: Report by the Special Commission on the Future of New York State Courts," February 2007, www.courts.state.ny.us/reports/courtsys-4future_2007.pdf

[50] The state Constitution does not allow the governor to make changes to the legislative requests of the Judiciary or the Legislature. However, the Legislature has the power to reduce expenditures for any branch of government.

[51] Jacob Gershman, "New York's Bloated Legislature," *New York Post*, Nov. 25, 2009.
http://www.nypost.com/p/news/opinion/opedcolunists/ny_bloated_legislature_QrkhIVY5rKNT0yVzWr0WWL

[52] City of New York, Financial Plan, Fiscal Years 2010-13, Fiscal Year 2010 November Plan, p. 40.
http://www.nyc.gov/html/omb/downloads/pdf/nov09_fp.pdf

[53] The state population outside New York City is 11,215,000 and the national per capita average for arts grant spending is $1.13.

[54] "Welfare Reform Turns 10: The Impact of Welfare Reform in New York," Transcript of an Empire Center Forum in Cooperation with The Donald and Paula Smith Family Foundation, October 2006.

[55] The Core Mission reports are posted online at http://publications.budget.state.ny.us/budgetFP/coreMissionBudgeting/coreMissionBudgeting08.html

[56] Citizens Budget Commission, op. cit.

[57] *See* http://www.texaspolicy.com/commentaries_single.php?report_id=1774

[58] "Construction of $4.2 billion computer chip plant begins near Saratoga," Associated Press, July 23, 2009. http://www.syracuse.com/news/index.ssf/2009/07/construction_of_42_billion_com.html

[59] Center for Government Research, "Capital Pork: How State Politicians Divvy Up Billions for Favored Capital Projects," by Kent Gardner and Erika Rosenberg, March 2006, http://www.cgr.org/articles/

[60] The Amtrak Adirondack Montrealer carried 112,000 passengers in FY 2008. See Amtrak "Monthly Performance Report for September 2008," p. A-3.5

[61] This calculation assumes a freeze in personal service costs for state agencies at 2009-10 levels, based on figures on page 249 of the Budget Division's "Economic, Revenue, and Spending Methodologies" report, dated Nov. 5, 2009.

[62] See Exhibit 8-2 in "New York State/SUNY GASB 45 Postemployment Healthcare Benefits, April 1, 2006 Actuarial Evaluation," May 15, 2007, Buck Consultants.

[63] Assumes the change would take effect on June 1. Ideally, the retiree contributions would be restructured so that employees who worked the minimum vesting period of 10 years received the smallest premium subsidy, as Governor Paterson proposed unsuccessfully in 2009.

[64] Memorandumin Support, 2009-10 PPGG Article VIII Section AA. http://publications.budget.state.ny.us/eBudget0910/fy0910artVIIbills/PPGGConsBMwtoc.htm#partAA

[65] New York State Association of Convenience Stores, "Perspectives on the Cigarette Tax Fairness Issue," November 2008, at http://www.nyacs.org/documents/PerspectivesBook.pdf

[66] Testimony of William J. Comiskey, Deputy Commissioner, Office of Tax Enforcement, before the Senate Standing Committee on Investigations and Government Operations, Tuesday, October 27, 2009

[67] The bill, A.9037, was passed by the Assembly on June 22 but defeated in the Senate on July 9. For more background on this measure, see the analyses linked at http://www.nyfiscalwatch.com/?p=1411.

[68] This proposal also assumes the rate for members of the police and fire system would be capped at the greater of the current rate of 18.4 percent or twice the required actuarial rate. The proposed capped rates are slightly higher than those proposed in the original amortization bill supported by the governor and the comptroller in 2009.

[69] Ravitch remarks at "States' Long-Term Budget Gaps: Are There Any Solutions," conference co-sponsored by Levin Institute and Rockefeller Institute, Nov. 30, 2009. Audio at http://rockinst.org/forumsandevents/

[70] Specifically, 38 percent of New York bridges were rated deficient, the fifth worst of any state; 7.69 percent of rural Interstate miles were rated in poor conditions, the second worst performance of any state; and 10.76 percent of urban interstate miles were rated in poor condition, the seventh worst performance of any state.

[71] See http://sanfrancisco.bizjournals.com/sanfrancisco/stories/2009/06/22/daily24.html and http://www.sacbee.com/static/weblogs/capitolalertlatest/2009/11/scif.html

[72] "New York City OTB to File for Bankruptcy," *Thoroughbred Times*, Dec. 3, 2009. http://www.thoroughbredtimes.com/national-news/2009/December/03/New-York-City-OTB-to-file-for-chapter-nine-bankruptcy-protection.aspx

[73] Maryland Tax Education Foundation, "New York State's $2 Billion Trifecta: NYRA, VLTs & OTB: Competitive Auctioning of Racing Assets Could Narrow NYS Budget Gap," February 2006. Posted at http://www.marylandtaxeducation.org/nystudyfeb27.pdf

[74] Charles Urstadt and Avrum Hyman, "A Battery Park Bargain," *The New York Times*, page A35, Oct. 21, 2009.

[75] State of New York, Commission on State Asset Maximization, Final Report, June 2009. http://nysamcommission.org/pdf/SAM_FINAL_REPORT.pdf

[76] Nicole Gelinas, "Financing Crucial Infrastructure," Manhattan Institute Center for Civic Innovation, http://www.citiesonahill.org/infrastructure/

[77] The latter measure, passed in December 2009, is Chapter 500 of the Laws of 2009. http://nysa.us/leg/?bn=A.40011

[78] *Buffalo Teachers Federation et., al. v. Tobe et. al*, 464 F.3d 362, http://cases.justia.com/us-court-of-appeals/F3/464/362/617048/

[79] Ibid.

[80] Based on annual municipal reports filed with the Office of the State Comptroller, the estimated salary freeze savings are $49 million for cities, $63 million for towns, $24 million for villages and $158 million for counties, and $688 million for school districts outside New York City. Annual pay base growth, based on prior-year averages, is assumed at 3 percent for counties and municipalities, and 4 percent for schools. The city's fiscal 2010 budget set aside $340 million for possible teacher salary hikes of 4 percent a year.

[81] O'Neil and McMahon, op. cit.

[82] City of New York, Comprehensive Annual Financial Report of the Comptroller for the Fiscal year Ended June 30, 2009, p.16; State of New York, Comprehensive Financial Report for Fiscal Year Ended March 31, 2009, pp. 86-87.

[83] http://www.cptr.state.ny.us/

[84] http://www.nyslocalgov.org/Default.asp

[85] "Closing the Gap," op. cit.

[86] Kent Gardner, Rochelle Ruffer, "Prevailing Wage in New York State: The Impact on Project Cost and Competitiveness," Center for Governmental Research, January 2008, http://www.cgr.org/reports/08_R-1532_PrevailingWage.pdf

[87] Chapter 57 of the Laws of 2008 raised the Wicks Law project threshold to $3 million in New York City, $1.5 million in downstate suburbs, and $500,000 upstate.

[88] Paul Bachman and David Tuerck, "Project Labor Agreements and Public Construction Costs in New York State," Beacon Hill Institute, April 2006.

[89] For example, the Minnesota Department of Transportation recently used design-build to accelerate completion of the I-35W Mississippi River replacement bridge project. The award-winning project came in under budget and ahead of schedule. See http://www.dot.state.mn.us/i35wbridge/rebuild/designbuild.html

[90] The existing legislative requirement that bills "age" on lawmakers' desks for three days before a vote is frequently waived under "messages of necessity" issued by the governor. The 72-hour rule proposed here would prohibit such waivers from affecting any budget legislation, except in case of emergencies involving single appropriations or temporary spending bills.

[91] The bill was A.9480 and S.6327 of the 2005-06 session.

[92] http://www.accountability.wa.gov/

[93] Cynthia B. Green, "The Way to a Better Budget," *The New York Times*, Aug. 4, 2003, p. A13

[94] William D. Eggers, "Show Me the Money: Budget-Cutting Strategies for Cash-Strapped States," Manhattan Institute Center for Civic Innovation and American Legislative Exchange Council, July 2002.

[95] As an alternative, tax burdens may be compared to state Gross Domestic Product, which is a broader measure of economic activity including corporate profits. State GDP reflects economic activity performed by people who work in New York State but do not reside here; it excludes economic activity that New York residents perform out of state. In practice, GSP and Personal Income are extremely closely correlated, and New York is similarly a tax outlier on either measure. In 1977, New York's tax burden equaled 12.55% of GSP, 141% of the national average. In 2007, this figure was 12.13%, 130% of the national average.

[96] State taxes are actual through 2008 and as projected in the Mid-Year Update thereafter. The increase in tax revenues needed to close out-year budget gaps is also as reflected in the Mid-Year Update. Local taxes are actual through 2007 and projected to grow at 4 percent per year from 2008 and onward. This is a conservative estimate; average growth from 1977 to 2007 was 6 percent per year. Personal income growth is actual through 2009, 2 percent for 2010 consistent with the Mid-Year Update, and 4 percent thereafter.

[97] However, the Legislature has not neglected to regularly adjust campaign contribution limits to reflect inflation.

[98] The Commission's findings and reports are at http://www.cotce.ca.gov/.

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