STAFF REPORT TO THE NEW YORK STATE SENATE SELECT COMMITTEE ON BUDGET AND TAX REFORM

On Improving Transparency, Forecasting and Flexibility in New York State's Budget Process

CHAIR: Senator Liz Krueger

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Contents

Executive Summary

The weeks-long debate that concluded early in December 2009 with the Legislature's approval of a $2.8 billion Deficit Reduction Plan, made one thing abundantly clear: New York State's fiscal planning process continues to be inefficient, short-sighted and anything but transparent. Although three years ago the Legislature and former Governor Eliot Spitzer passed a series of budget reforms intended to improve this process, their impact has been marginal at best.

Even with slightly improved transparency and revenue forecasting, New York still has a political environment where the Governor and Legislature reduce budget negotiations to a costly game of chicken. Too often, the public and rank-and-file elected officials are left guessing what their leaders are doing behind closed doors and who will flinch first.

As a November 2009 report released by Citizens Union of the City of New York highlighted, the Legislature and Executive have stumbled in implementing the 2007 rules. For example, in 2009, no conference committees were formed to resolve budget bill differences between the two houses and the Governor did not submit all budget amendments within the required 21 days after submitting his Executive Budget.[1] The Citizens Union's assessment: the end result has been a process that "remains opaque and rushed." That is not to say the Senate made no progress earlier this year on budget reform. Along with satisfying the three-day review period for final budget documents, the Senate also issued user-friendly spreadsheets detailing member items.[2]

Clearly next steps to further reform of our State's budget process are necessary. Albany has managed to operate, albeit dysfunctionally, in this opaque and rushed environment for decades. But decades of growth in borrowing and the recession's long-term impact on revenues—particularly those from Wall Street—threaten to expose the State budget's structure and process to debilitating levels of stress.

Regardless of the economy's strength, recurring revenues have long been insufficient to sustain ongoing spending. The end result is a structural imbalance, which lawmakers have managed to ignore mostly through a heavy reliance on huge temporary surcharges, bonding actions or the sweeping of special funds. Such "one-shots" over the past decade have totaled between $20 billion and $24 billion.[3]

New York can no longer rely on this one-fell-swoop strategy, which is actually encouraged by the State's budget process. Recognizing this predicament, the New York State Senate Select Committee on Budget and Tax Reform held a public hearing in Manhattan on December 17, 2009 to explore ways to improve transparency, forecasting and flexibility in the budget process. The six-member, bi-partisan committee heard testimony from eight experts on state fiscal issues and received written testimony from two others. The committee, chaired by Senator Liz Krueger, also examined the effectiveness of the 2007 budget reforms and how they can be improved or better implemented.

Key findings and conclusions from the public hearing are detailed in this staff report to the Select Committee. They include:

Forecasting

The 2007 budget reforms significantly improved the process for achieving revenue consensus early in negotiations. But the lack of a binding estimate established either between the Executive and Legislature or by the Comptroller continues to produce problems that reverberate later in the fiscal planning process. The tendency for the forecast agreement to unwind pushes revenue estimate negotiations later into the budget process and digs into time that should have been devoted to other procedures. One result of this trend is seen in the shortened or abandoned conference committee meetings.

- A later start date for the fiscal year could reverse this trend caused by a "soft" official state revenue forecast and provide forecasters with more accurate revenue information. Either way, the budget process is in dire need of a revenue consensus with teeth.
- A legislative budget office or an independent budget office could play a role in establishing a more accurate and less politicized revenue forecast.
- A new budget office, the Office of the Comptroller or an arbitration panel could also assist in establishing a binding official state revenue forecast.

Transparency

Improvements to the revenue consensus process promise to benefit fiscal transparency and public involvement in the budget process, particularly by affording conference committees more time to meet and giving lawmakers more time to review fiscal legislation. An independent budget office could also keep the public and legislators better informed throughout the budget process.

- Even when there was adequate time to meet, conference committees saw their credibility diminished because the sums of appropriations they oversee account for a fraction of total spending in their jurisdictional categories. For conference committees to be viewed as more than mere "window dressing," larger sums of funding need to be authorized to them by leadership as they work out difference between Senate and Assembly budget bills.

Flexibility

New York's practice of budgeting on a cash basis has created the impression that it has a flexible planning process. But it is one that does not accurately represent the income earned in a fiscal year or the liabilities incurred during the same period. This non-accrual budgeting blurs the State's actual fiscal reality and lures it deeper into debt, resulting in more rigid legislative actions.

- Lawmakers need a truer presentation of the State's financial condition, which can be provided through the adoption of Generally Accepted Accounting Principle (GAAP) standards. An accrual (GAAP) basis of budgeting would prohibit the "gimmickry" that has been used to obscure deficits and it promises to curtain a temptation for overspending.
- While GAAP standards are a remedy for New York's dangerous habit of budgeting primarily for the short-term, they alone do not guarantee long-term financial stability. A multi-year budgeting process paired with GAAP standards would shift lawmakers'

focus to the long-term and afford them the time to anticipate, prepare for and respond to changes in the state's fiscal picture.

- New York's lack of performance measurements for state-funded programs leads to irregular appropriation practices and rigid across-the-board cuts. A performance budgeting system that ties funding to results would provide lawmakers with more flexibility in making budget decisions.

Conclusions

Looking to make the budget process operate more efficiently and publicly, the Select Committee will explore what steps are necessary to achieve the following:

- Implementing a biennial budget process balanced under GAAP standards and approved by the Legislature during non-election years.
- Establishing performance budgeting measurements and goals for state-funded programs.
- Establishing a legislative budget office that would provide legislators in both houses with revenue and cost estimates in a non-partisan way.
- Including a legislative budget office or arbitrators in the revenue consensus process to establish an official state revenue forecast to which the Executive and Legislature branches are bound throughout the budget negotiations.
- Moving the start of the state fiscal year to June 1 or July 1.

I. Introduction
A Brief Review of New York State Budget Reform

In January 2007, when the Legislature and Governor Spitzer announced their agreement on the budget reforms, the governor called them "common-sense measures." He said they were "an excellent first step" toward opening up New York's budget process. Highlights from the 2007 Budget Reform Act include:

- The creation of a Rainy Day Reserve Fund that can hold up to 3 percent of General Fund spending and can be used during economic downturns or in response to catastrophic events.
- The prohibition of lump sum appropriations for Legislature member items, Temporary Assistance for Needy Families, Environmental Protection Fund and Medicaid.
- A mandate for the itemization of member items in resolutions.
- The requirement for the Senate and Assembly to adopt joint rules to establish conference committees.
- The establishment of the "Quick Start" budget negotiation process, under which the Executive, Senate and Assembly must begins discussing revenue forecasts in November and reach a consensus by March 1. In cases when there is no consensus, the Comptroller decides on a non-binding forecast.
- The requirement for detailed fiscal impact statements on legislative changes to the budget plus for the public issuance of lists for public hearings and conference committee reports.
- The requirement for the governor to submit all budget amendments within 21 days after the submission of the Executive Budget.

Governor Spitzer's "first step" toward budget reform was among many that lawmakers have attempted to make in the name of that cause. Some other significant proposals came during the 1996-1997, 2001-2002 and 2004-2005 fiscal years.

In his 1996 Executive Budget, former Governor George Pataki introduced a series of budget reforms, which called for three constitutional amendments. The proposed amendments would have required the enactment of a balanced budget, the enactment of an austerity budget if a budget is not passed by the April 1 deadline and the requirement for two-thirds approval in both the Senate and Assembly if a budget would increase taxes over $50 million annually. Pataki also proposed requiring public conference committee meetings and annual economic and revenue consensus forecasting meetings between the Division of Budget (DOB), Senate Finance Committee and Assembly Ways and Means Committee.[4]

However, Governor Pataki's reform aspirations fell short. The budget that year was passed over 100 days late, even after Governor Pataki took the unprecedented step of submitting the fiscal plan to the Legislature a full month early.[5] Of his proposals, only consensus forecasting was adopted.

In his 2001-2002 Executive Budget, Governor Pataki introduced another budget reform package, which proposed doubling contributions to the State's "rainy day" fund, moving the start of consensus forecasting meetings to March 1 from March 10 and directing DOB to furnish legislators with fiscal impact reports on a proposed budget agreement. He also revived the 1996 proposal for a two-thirds vote on budgets that increase taxes by over $50 million annually.[6] Many of these proposals and their 1996 predecessors were not passed during the Pataki administration. However, versions of them were adopted in the 2007 reform package, particularly those concerning conference committees and advanced consensus forecasting meetings and fiscal impact reports.

In the years leading up to the 2007 reforms, one of the Legislature's key approaches for budget reform likewise included elements redefining the Executive Budget writing process. In 2004—at the peak of the public outcry over what culminated in New York's 20-year streak of late budgets—former Senate Majority Leader Joseph Bruno and Assembly Speaker Sheldon Silver introduced legislation proposing to move the start of the fiscal year to May 1. They also proposed to create an independent budget office and to impose a contingency budget based on the previous year's spending if a budget is not passed by the start of the fiscal year.

The Bruno-Silver legislation passed both houses, but Pataki vetoed it in November 2004. He said it would have incentivized the Legislature to delay passage of a fiscal plan further and threaten the State's ability to cover its financial obligations.[7]

A month after Pataki vetoed the Legislature's budget reform package, the New York Court of Appeals delivered rulings in two cases involving Governor Pataki and the Legislature. The first case, Silver v. Pataki, arose from the governor's 1998 budget; the second, Pataki v. New York State Assembly, stemmed from the governor's 2001 budget. In both cases, the Executive and Legislature clashed over the "no-alteration" provision that plays an important role in the Executive budgeting process. It prohibits the Legislature from altering the governor's budget, except to reduce or strike out items. The Legislature is allowed to add a spending line to Executive appropriation bills or add language to non-appropriation bills, but both can be subjected to a governor's veto. Ultimately, the court said while a series of the governor's actions might have been "politically controversial," he was "clearly within the authority given him by the Constitution."[8]

In Silver v. Pataki, the Legislature passed the governor's appropriation bills without altering them, except to strike out or reduce items. But problems arose when the Legislature changed the language in the governor's non-appropriation budget bills. While not changing the enacted appropriation for items such as a $180 million Franklin County prison and $80.8 million for an Insurance Department regulatory program, this action altered the purposes for and conditions upon which money could be spent for them. In response, Pataki vetoed 55 items he deemed unconstitutional. The Speaker of the Assembly, who was later joined by the Senate, filed the lawsuit seeking a declaratory judgment on the unconstitutionality of the vetoes.[9]

In Pataki v. New York State Assembly, the Legislature deleted language from the governor's appropriation bills it deemed unconstitutional. The Legislature opposed the inclusion of such language in the bills because it dealt with non-appropriation matters, such as funding formulas and computations for school aid and education programs. The Legislature then passed its own appropriation bills that mirrored the governor's bills except for different conditions and restrictions. Although Pataki deemed the Legislature's 37 single-purpose bills passed on these items unconstitutional, he signed them and then sought a court's judgment declaring them so.[10]

Despite the outcome of the lawsuits, the Legislature in 2005 passed its first on-time budget since 1984. At least half of the annual budgets during the 20-year tardy streak were over 100 days overdue, peaking at 208 days late in 2002.[11]

In 2005, the November ballot featured a proposal to amend the State Constitution. The referendum item, dubbed Proposal One, would have empowered the Legislature to draft appropriation bills if it did not act on the governor's budget bills by the start of the fiscal year. This proposal would have reversed part of the Executive Budget process that Governor Al Smith won with a constitutional amendment in 1927 and former Governor Franklin Delano Roosevelt defended two years later in court.[12]

Voters rejected Proposal One by an almost two-to-one ratio (734,844—yes; 1,368,120—no), meaning that, for all of its faults, New Yorkers largely approved of the current process that places substantial budget writing authority in the hands of the governor (i.e, the Executive Budget process).[13] Two years later, Governor Spitzer's budget reform package remained within this framework, unlike many of the previous initiatives pursued by Governor Pataki, Majority Leader Bruno and Speaker Silver.

II. Forecasting

Revenue Consensus

One of the stickiest parts of the budget process comes at its beginning and involves reaching a consensus between the Executive and Legislative branches over how much revenue will be available for spending in the next fiscal plan. Another problem is sticking to a revenue forecast after an agreement is reached. These revenue consensus problems often reverberate through the rest of the budget process as last-minute discussions over revenues dig into time that should have been devoted to other scheduled negotiations and meetings.

For the past 14 years, a key strategy governors have employed to resolve revenue forecasting disputes has revolved around requiring earlier and earlier start dates for revenue consensus negotiations. Governor Pataki initiated this strategy in 1996, under which the fiscal arms of the Executive and Legislative branches were required to meet in early March and reach a consensus revenue estimate later that month. In the 2001-2002 Executive Budget, he proposed moving the start date for revenue consensus from March 10 to March 1 and also requiring the Legislature to convene conference committee meetings by the beginning of March.

"Unfortunately, the 1996 reforms did not include provisions to ensure that the consensus revenue forecast was used. Moreover, in at least some years, the consensus revenue forecast did not actually include a consensus forecast, but rather discussions of each of the principals' own forecast," said George Sweeting, deputy director of the New York City Independent Budget Office (IBO).[14]

The 2007 reforms vastly accelerated the consensus process by requiring "Quick Start" discussions to begin in early November and bumping back the March consensus revenue conference to February. The deadline for a final consensus report was set for March 1, and in cases where an agreement could not be reached then the Comptroller is required to issue a non-binding revenue estimate by March 5.

Sally Robinson, the issues and advocacy vice president for the New York State League of Women Voters, said the decision to not create a state independent budget office (IBO) was "the single most important reform not accomplished by the 2007 budget reforms." An IBO could have served as the final arbitrator instead of the Comptroller. She said the Comptroller, as an elected official, "does not have the same public perception of objectivity, particularly in election years."[15]

Despite making some changes to the process, the 1996 and 2007 reforms ultimately failed to "fundamentally change the revenue estimating dynamic in the State," Sweeting said."The three parties still spend much of the time leading up to adoption fighting over how much money will be available before turning to spending priorities for the budget."

Other states have established a less politicized process for revenue consensus by determining that figure through the use of panels of outside experts or arbitration. For example, Delaware's binding official state revenue forecast is set by the Delaware Financial Advisory Committee. Iowa's binding forecast is determined by the Legislative Services Agency director's designee, the governor or an executive designee and a third member on which the other two arbitrators agree.[16] Out of the 50 states, as of October 2009, 26 had budget processes that include an official state revenue forecast that is binding. Twenty two states determine their official forecast through consensus negotiations while executives in 11 states set that figure.[17]

States with Official Revenue Forecasts Development through Consensus

State	Participants in the Development of an Official State Revenue Forecast	Binding or Non-binding Official State Revenue Forecast
Alabama	Executive Budget Office, Legislative Fiscal Office	Non-binding
Arizona	Executive and Joint Legislative Budget Committee staff	Binding
Delaware	Delaware Financial Advisory Committee	Binding
Florida	General Fund Revenue Estimating Conference	Non-binding
Indiana	Revenue Forecast Technical Committee	Non-binding
Iowa	Legislative Service Agency director or designee, governor designee and a third party agreed upon by the other two.	Binding
Kansas	Department of Revenue, Executive Division of the Budget, Legislative Research Department, three consultants from three different state universities.	Non-binding
Kentucky	Consensus Forecasting Group	Binding
Louisiana	Revenue Estimating Conference (governor or designee, Senate President or designee, Speaker of the House or designee, state university faculty member).	Binding
Maine	State Budget Office, State Tax Assessor, State Economist, University Economist, Fiscal and Program Review Office director, Legislative Council non-partisan appointee.	Binding
Massachusetts	Secretary of Administration and Finance, Senate and House Committees on Ways and Means.	Binding
Michigan	Senate and House Fiscal Agencies directors, Department of Management and Budget director or designee.	Non-binding
Mississippi	Revenue Estimating Group	Binding
Missouri	Senate and House appropriation chairs and staff, governor, Executive Division of Budget and Planning, University of Missouri economist.	Binding
Nebraska	The Economic Forum.	Non-binding
New Mexico	Taxation and Revenue Department economists, Department of Finance and Administration, Legislative Finance Committee, Highway and Transportation Department.	Non-binding
New York	Executive Division of Budget, Office of Fiscal Planning, Senate Finance Committee, Assembly Ways and Means Committee.	Non-binding
North Carolina	Legislative Fiscal Office, State Budget Office.	Binding
Rhode Island	Senate and House Fiscal Advisors, State Budget Director.	Binding
Tennessee	Governor, Committee of Finance and Administration, Comptroller, Secretary of State, Treasurer.	Non-binding
Vermont	Emergency Board, Joint Fiscal Office, Secretary of Administration	No
Washington	Economic and Revenue Forecast Council	Binding
Wyoming	Legislative Service Office budget/fiscal manager, Executive Economic Analysis Administration, State Auditor and Treasurer representatives, Superintendent of Education, Department of Revenue director, state geologist, oil and gas commissioner, University of Wyoming economist	Binding

Fiscal Year Start Date

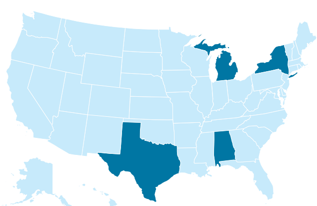
Debate over revenue estimates could be eased if Executive and Legislative tax forecasters had access to more precise information from final income tax returns, which are due April 15. But for tax forecasters to include those figures into budgetary calculations, the start of the State fiscal year would have to be pushed back a few weeks or months. E.J. McMahon, the director of the Empire Center of New York State Policy, noted: "The current fiscal calendar is poorly aligned to revenue collection and spending patterns."[18]

The New York City IBO, Empire Center and Citizens Budget Commission recommended a July 1 fiscal year start date, which is the most common date among the 49 other states. New Yorkers for Fiscal Fairness Executive Director Ron Deutsch identified May 1 as an alternative start date.[19] In 2009, Chairwoman Krueger reintroduced legislation (S.5221) proposing to move the start of the state fiscal year to June 1. Select Committee member Senator Neil Breslin also reintroduced a June 1 fiscal year bill (S.377). Forty-six states begin their fiscal years in July. The remaining states begin their fiscal years in April, October or September.[20]

STATES WITH FISCAL YEARS THAT DO NOT START IN JULY

State	Fiscal Year Start
New York	April
Michigan	October
Alabama	October
Texas	September

Fiscal year data according to the National Conference of State Legislatures



"Even more important than adding time for the Legislature to consider the governor's Executive Budget…this change would give budget makers additional information about spring tax receipts and therefore a sounder revenue estimate," Sweeting said.

The start of New York's fiscal year used to be on Oct. 1, but in 1916 former Governor Charles Whitman moved it to July 1. In the late-1930s and early 1940s, the legislative session usually ended by mid-March or April—months before the fiscal year—partly prompting the April 1 switch.[21]

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>
> —GEORGE SWEETING
>
> Deputy Director of the New York City Independent Budget Office

IBO v. LBO

Another proposal mentioned at the public hearing to reduce the troubles with revenue estimates involves the creation of an independent budget office (IBO) or legislative budget office (LBO). It also promises to empower rank-and-file lawmakers in the financial planning process.

In the Senate in 2009, Chairwoman Krueger and Senator Jeff Klein introduced legislation proposing the establishment of an LBO modeled after the federal Congressional Budget Office (CBO) in Washington D.C.[22] At the same time, Senators David Valesky and Joseph Griffo introduced bills proposing the creation of an IBO modeled after both the CBO and New York City IBO.[23]

The CBO was established in 1974 through the Congressional Budget and Impoundment Control Act and it began operating a year later. In 1989, New York voters approved the charter for the New York City IBO, which began operating a year later. While modeled after the CBO, the New York

City IBO is different in that it is independent of both the city's executive and legislative branches.[24]

At the public hearing, experts agreed the Legislature needs a professionally-staffed, nonpartisan entity that provides them with fiscal information. However, there was debate over whether lawmakers should pursue an IBO or CBO model. Experts' chief concern over the creation of either an IBO or LBO was whether the Legislature would embrace a third-party's budgetary information.

"There needs to be an independent, nonpartisan office. Would it have the credibility the CBO has or the New York City IBO? It wouldn't. The hope would be that over time it would gain that credibility," said Deutsch at New Yorkers for Fiscal Fairness.[25]

McMahon cautioned that a budget office's independence could dash hopes of it ever becoming a credible, efficient and effective entity. He favored an LBO approach and said "that word, 'independent,' which is so attractive to political reformers in many other ways, is not the word you want in front of it."

Contrarily, Sweeting saw the acceptance of an IBO by the Legislature as hinging on its independence. He said the city's structure "might need to be tailored to fit the state structure" and "some similar arrangements [regarding funding and the appointment of directors] would be necessary to ensure the IBO has the independence to command credibility for its estimates and analysis."

Carol O'Cleireacain, a senior fellow for the Brookings Institution, said an IBO focused solely on revenue forecasting would be counterproductive. She warned that such an IBO would not be "a game changer" and it would lack "the level of respect and authority I think you need." New Jersey's IBO suffered from a poor reception among legislators for this reason.

"What happened in New Jersey was the entire focus was on the revenue estimate and not much else. And once the entire focus becomes on the revenue estimate it becomes political by definition, and nothing else they do matters." said O'Cleireacain, a former New Jersey deputy treasurer. She also served as the New York City finance commissioner and budget director in the early 1990s.

A nonpartisan budget office could better serve the Legislature if it focused more on long-term cost estimates than on revenue estimates, O'Cleireacain said. In New York City, the IBO is required to make a revenue estimate and the city comptroller provides a revenue analysis, though the mayor is the main authority for setting revenues in the budget.[26]

Regarding revenues, the CBO is required to provide a 10-year spending and revenue estimate that serves as a neutral benchmark against which the fiscal impacts of proposed legislation can be measured. It also provides a re-evaluation of the president's budget proposal, including an analysis of its spending and revenue estimates.[27] However, the CBO also provides Congress with very influential cost estimates on how pending legislation would change spending and revenue levels. Rarely in New York City do lawmakers rely on such scoring from the city IBO when weighing legislation, according to McMahon.

"That's not the case [in New York City]. That's what you want," McMahon said.

O'Cleireacain concurred: "The CBO doesn't make a revenue estimate. Instead the CBO costs programs, and they have to cost them five years and 10 years. And if that's all you ask of your legislative budget office, it would be a great step forward because it would be contributing to the multi-year financial plan process you're trying to get into; it would be a real change."

III. Transparency

Conference Committees

Improvements to the revenue forecasting process could lend themselves to making the overall budget process clearer to the public and rank-and-file lawmakers. For example, a state IBO or LBO could provide the public and legislators with more pertinent and timely fiscal information.[28]

"Certainly the public has nowhere to go to get an independent source of information to judge who is most accurate in the fight over whether there is more or less money on hand," said Blair Horner, legislative director of the New York State Public Interest Research Group.[29]

Ideally, a firmer revenue consensus could allow conference committees more time to settle spending priorities at public meetings. Elizabeth Lyman, the deputy research director at Citizens Budget Commission, said, "The tendency to negotiate budget items at the last minute has pressured the conference committee calendar so that in years when the process was used, they were rushed and not meaningfully utilized."[30]

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>
> —DICK DADEY
> Executive Director of
> Citizens Union of the City of New York

Deutsch attributed the ineffectiveness of the conference committees more to their narrow scope than to their short time table. He said their meetings amounted to "window dressing," because the "table targets" (the amount of money authorized by leadership) account for a fraction of total spending in each conference committee's jurisdictional category. For example, while New York regularly spends billions of dollars for economic development annually, the economic development sub-committee's table tablet usually is approximately $30 million, according to Deutsch.

To better facilitate the conference committee process, Deutsch added, the governor should cease the practice of issuing the Executive Budget in a package of bills covering executive operations, debts services and appropriations for the Legislature and Judiciary branches. Instead the bills should better correspond to the nine jurisdictional categories of the budget conference sub-committees.

To bolster conference committees' credibility, Deutsch recommended granting them discretion over the full amount of proposed spending in their jurisdictional areas. At the beginning of the legislative session, members should also be appointed to conference committees to allow them time to better familiarize themselves with the issues they will soon review.

"Without conference committees, there was also no formal role for rank-and-file members to engage in substantive policy discussions regarding expenditures and taxes," said Citizens Union Executive Director Dick Dadey.[31]

Citizens Union called for changing the law to explicitly require the creation of joint conference committees and that they hold meetings. Robinson, at the League of Women Voters, added that public notices for these meetings should be mandated.

"We believe that increased public awareness of the budget process and participation in the budget process would result in more accountability in the final budget," said Robinson.

IV. Flexibility

Generally Accepted Accounting Principles

New York has long maintained the impression of having a very flexible budget process by operating on a cash basis. Under this system, bills are recorded as paid when funds are spent, not when a liability is incurred.[32] This non-accrual basis is what allows lawmakers to roll expenses from the current year to the next and claim the current budget is balanced. It also allows lawmakers to use the next fiscal year's revenues to pay the current year's expenses.[33] The result is less a matter of financial planning than of "timing–related gimmickry," McMahon said.

The State's cash-basis budgetary accounting has turned the concept of financial planning into a farce, and its claims to financial flexibility are built around an illusion. More and more it brings the State into a rigid position with no optimal options. Many experts' recommendations, such as those regarding more comprehensive accounting standards and multi-year budget cycles, restrict the flexibility afforded by cash budgeting. But the tradeoff is a different kind of flexibility; one that affords lawmakers a clearer picture of the State's financial situation and the time to make adjustments to it.[34]

"The culture of cash accounting is one of fiscal manipulations as long as payments to creditors can be deferred and cash can be found somewhere. However, sometimes money runs out," O'Cleireacain said.

Lyman noted that the Comptroller's 2008 annual financial report showed New York having a $13.5 billion deficit on an accrual Generally Accepted Accounting Principles (GAAP)-basis. Meanwhile the State's cash report showed a $1.9 billion balance at year's end. She attributed the balance differences on the postponement of cash toward year's end. Lyman called the GAAP presentation a "truer picture of state obligations in that fiscal year."

To provide lawmakers with a more realistic picture of the State's fiscal outlook, experts such as McMahon, Lyman and O'Cleireacain advocated for New York's adoption of a GAAP-basis budgetary accounting on year-end results. Lyman added GAAP should also be applied on State Funds, State Operating Funds and All Funds for each of the fiscal plan's out-years. GAAP reporting is already required for the General Fund for one out year, along with a cash-to-GAAP reconciliation that is "virtually unintelligible."

The 2007 budget reforms required that New York's General Fund budget be balanced on a cash basis. They also extended the budget's three-year financial planning mandate to four years. Also, the reforms required the identification in budget documents of certain "off-budget" spending by public authorities. These requirements were fulfilled in all three budgets since 2007.[35]

"The longer financial planning horizon and the improved presentation of off-budget spending have been helpful," Lyman said. "The budget balance requirement, on the other hand, based only on the General Fund, has no visible impact."

This General Fund focus as a basis for budget balance is a shortfall of the 2007 budget reforms, Lyman added. Traditionally, the greatest emphasis has been placed on the General Fund because it is mainly supported by tax revenues. But a General Fund focus provides only a narrow view of the State's fiscal picture. For example, in the 2008-2009 fiscal year, the All Funds cash total was $121.6 billion while the General Funds share of that was $54.6 billion. Lyman called the General Fund "outdated and artificial construct that is not serving the public's interest."

Multi-Year Budgeting

Cash has made it too easy for New York to take short views. GAAP could make it harder for the lawmakers to focus primarily on the short-term, but it would not guarantee long-term views. To establish a more forward-looking mindset in Albany, some experts recommended a multi-year financial planning process based on GAAP budgeting.

"A multi-year financial plan counters the all-too-human preference for the 'short-term' by making visible and ongoing the consequences of policy decisions: new programs, collective bargaining agreements, tax changes," said O'Cleireacain.

McMahon advocated for a two-year budgeting cycle with the main budget adoption occurring on non-election years. Robinson said the League of Women Voters in the early 1990s established a position in opposition to a biennial budget process. The organization views the two-year cycle as not being responsive enough to meet New York's needs and it said lawmakers do not need a year off from their primary duty of passing a fiscal plan. It found that biennial budgeting worked well in Texas. However, the two-year cycle works in the Lone Star State primarily because its legislature meets every other year, unlike New York's annual legislative sessions. New York legislators already have a hard enough time passing a budget for one year and a two-year budget would likely be doubly hard, according to Robinson.

Stephen Acquiraio, executive director of the New York State Association of Counties, favored a "rolling" two-year budget cycle with minor adjustments made in intervening years.[36] O'Cleireacain and McMahon likewise advocated for mandatory quarterly fiscal revisions to keep the annual budget in balance throughout the multi-year cycle. This long-term financial planning process would provide school districts, municipalities, businesses and families with a better picture of "what to expect from the State in the year ahead," said Acquario.

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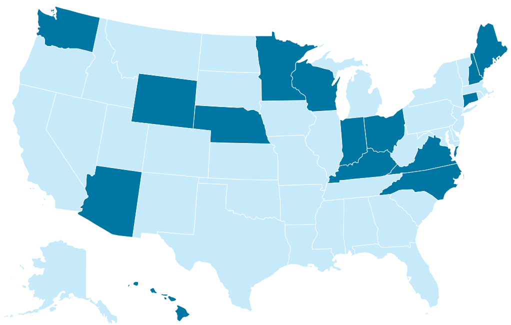
> —CAROL O'CLEIREACAIN
>
> Senior Fellow at the Brookings Institution

As of 2008, 30 states, including New York and California, had annual legislative sessions and annual budgets.[37] Fifteen states, including North Carolina, Connecticut and Ohio, had annual sessions and biennial budgets. Five states, including Texas, had biennial sessions and biennial budgets. According to the National Conference of State Legislatures, research on annual and biennial state budgeting has not found one type of budget cycle being vastly better than another, But Connecticut analysts reported the governor and legislators ramped up their long-term budget forecasting and analysis after the state went from having an annual budget to a biennial budget in 1991.[38]

Twenty States with Biennial Budgeting

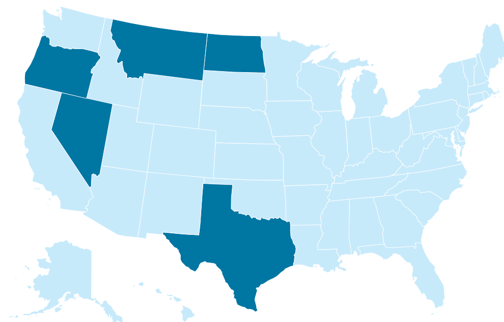
States with Annual Sessions and Biennial Budgets

Arizona, Connecticut, Hawaii, Indiana, Kentucky, Maine, Minnesota, Nebraska, New Hampshire, North Carolina, Ohio, Virginia, Washington, Wisconsin, Wyoming



States with Biennial Budget Sessions and Biennial Budgets

Montana, Nevada, North Dakota, Oregon, Texas



Budgeting data according to the National Conference of State Legislatures

In New York, a constitutional amendment would be required to implement a biennial budget because the State Constitution specifically calls for an annual budgetary process. Such an amendment would require voter approval, but a referendum could only come after the proposal is passed by two separately-elected Legislatures. The earliest a biennial budget vote could be put on the ballot is 2011, so long as the proposal is passed by the Legislature in 2010 and the following year.[39]

Performance Budgeting

In cases when lawmakers need to reduce spending in the budget, they commonly rely on across-the-board cuts. While such actions demonstrate lawmakers' reaction to revenue realities, across-the-board cuts are more of an indicator of rigidity than of flexibility. And it is largely a rigidness that stems from the State's lack of a way for measuring the effectiveness of state-funded programs and services.

To ensure the State is receiving an adequate return on its investments and to provide it with more flexibility in budget-making decision, both Citizens Union and Citizens Budget Commission recommended the adoption of a performance budgeting system.

Under performance budgeting, metrics are developed to gauge whether programs are meeting a defined set of goals. Performance indicators and statistics can also help lawmakers establish a more rational method for appropriating state funds. Since the early 1990s, Florida, Texas and North Carolina have incorporated performance management strategies in their budget processes.[40]

"This will really be trying to get a look at what you're getting for the money and how much of a bang for the buck," Lyman said "...If you don't start thinking about the quality of service that you're getting, it's hard to leverage that cost-effectiveness and get more for your money, which we need to be thinking about obviously as we're closing these budget gaps without slashing services."

Dadey at Citizens Union identified New York City's Mayor's Management Report and Preliminary Management Report as possible models for the State. The city's performance reporting requirements were added to its charter in 1975 and they largely influenced the nationwide trend toward performance budgeting in the 1980s and 1990s.[41]

Under the charter, each city agency must submit by January 13 a preliminary management report that includes a statement detailing its performance during the first four months of the fiscal year in relation to that year's performance goals and measurements. Agencies must also state goals and measures for the next fiscal year. By September 17, agencies must submit a full management report that includes a statement detailing their performance goals for the fiscal year and an explanation of their measurements. They must also detail their actual performance in relation to goals, along with statements on their internal control environment and summaries on rulemaking decision and procurement actions.[42]

Governor Pataki introduced performance management techniques for state operations in the 2005-2006 Executive Budget. Under this Executive-led effort, agency policymakers were directed to define goals and priorities and "focus on the relationship between performance outcomes and financial decision-making." During the 2005-2006 fiscal year, pilot performance management programs were set for the Department of Taxation and Finance and the Office of Mental Health. Pataki envisioned rolling out a statewide financial management system that would have extended performance evaluation and reporting capacities to all State agencies.[43] However, Lyman said this initiative was "marred" by a poorly coordinated approach. In late 2006, then Governor-elect Eliot Spitzer announced plans to require State agencies to adopt performance measurements, "but the leadership change and higher priority budget problems have stalled this movement," Lyman said.

V. Conclusions

Fiscal crisis after late budget after fiscal crisis all point to the same thing: the need for budget reform in New York that promotes better transparency, forecasting and flexibility. However, a more transparent budget process—or even an efficient one—is not necessarily the panacea for a State's financial problems. As McMahon said: "Some of the states with good systems in writing and traditions of a more orderly process of sharing information with members are a mess." Debt-laden California is an example of one such state, whose budget process is complicated more by constitutional and statutory measures.

In some cases, McMahon added, New York's budget hiccups stem partly from a "matter of habit," such as the Legislature's reluctance to abide to a budgetary routine. "There is not a this-is-Thursday-so-we-have-to-be-doing-this mentality." Deutsch questioned whether it is accurate to say New York even has a budget process, because "It's hard to call something a 'process' when it changes from year to year and really to a great degree at the whim of leadership."

In the end, New York has a budget process, but it is one that it is undermined by the shortcuts and short views its procedural rules permit or encourage. Looking to make the budget process operate more efficiently, responsibly and publicly, the Select Committee will explore what steps are necessary to achieve the following:

- Implementing a biennial budget process balanced under GAAP standards and approved by the Legislature during non-election years. A constitutional amendment would be needed to change New York from a one-year budget cycle to a two-year cycle.
- Establishing performance budgeting measurements and goals for state-funded programs.
- Establishing a legislative budget office that would provide legislators in both houses with revenue and cost estimates in a non-partisan way.
- Including a legislative budget office or arbitrators in the revenue consensus process to establish an official state revenue forecast to which the Executive and Legislature are bound throughout the budget negotiations.
- Shifting the start of the fiscal year to June 1 or July 1.

SENATE SELECT COMMITTEE ON BUDGET AND TAX REFORM

On Improving Transparency, Forecasting and Flexibility in New York State's Budget Process

THURSDAY, DECEMBER 17, 2009

Participants

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Empire Center for New York State Policy

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Deputy Director
Independent Budget Office of New York City

Ron Deutsch
Executive Director
New Yorkers for Fiscal Fairness

Carol O'Cleireacain
Senior Fellow
Brookings Institution

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Citizens Budget Commission

Dick Dadey/Rachael Fauss
Executive Director/Policy and
Research Associate
Citizens Union of the City of New York

Sally Robinson
Issues and Advocacy Vice President
League of Women Voters of New York State

Written Testimony Only Received From

Blair Horner
Legislative Director
New York Public Interest Group

Stephen Acquario
Executive Director
New York State Association of Counties

SENATE SELECT COMMITTEE ON BUDGET AND TAX REFORM

NOTICE OF PUBLIC HEARING

New York City
Thursday, December 17
12:30 p.m.
Senate Hearing Room
250 Broadway, 19th floor
New York, NY

CHAIR: Senator Liz Krueger
Senator Neil Breslin
Senator Kenneth LaValle
Senator Kevin Parker
Senator Bill Perkins
Senator Michael Ranzenhofer

Improving transparency, forecasting and flexibility in New York State's budgetary process.

Once again, New York finds itself in the midst of a fiscal crisis. While the economic downturn drove many of the state's budgetary problems, they have been agitated severely by inadequate planning procedures that impede transparency, forecasting and flexibility. While the Legislature in 2007 passed a series of budget reforms, which required everything from the creation of joint conference committees to the itemization of member items in resolutions, many of these new rules are not being implemented as initially intended, or at all. Many proposals, such as the creation of an independent budget office and changing the start of the fiscal year, remain outstanding. Clearly, more changes are necessary to establish a more stable fiscal environment at multiple levels of government throughout New York.

Testimony should relate to proposals to improve budgeting in New York as well as the budgetary procedures of the Legislature and Executive. Some of the questions testimony should address include:

- What budget reforms from 2007 have worked well at improving the fiscal planning process?
- Which budget reforms have not worked as intended?
- Are there any budget reforms from 2007 the Legislature and Executive are not properly implementing, and how can this trend be corrected?
- What types of budget reforms should the Legislature consider to improve its ability to address fiscal crises, such as the current one?
- How can the state enhance its long-term planning capabilities to ensure greater fiscal stability?

About the Select Committee on Budget and Tax Reform

On February 5, 2009, the New York State Senate adopted Senate Resolution No. 315, which created the Select Committee on Budget and Tax Reform. Since then, the six-member, bi-partisan committee chaired by Senator Liz Krueger has sought to look at New York State's entire tax structure. It aims to determine what aspects of it are working smoothly and where there are inequities and complications that must be rectified.

Select Committee activities in 2009 have included:

Personal Income Tax Reform

Exploring progressive changes to New York State's personal income tax system.

- Public hearing: Albany, March 12.

Business Tax Reform

Evaluating the equitability of New York State's business and banking tax structures and their effectiveness to foster economic growth statewide.

- Public hearings: Rochester, April 30; Manhattan, May 21.

Telecommunications Tax Reform

Modernizing New York State's telecommunication taxes.

- Roundtable: Albany, August 12.

Property Tax Exemption Reform

Evaluating the needs for and costs of New York State property tax exemptions.

- Roundtable: Albany, October 13.

Budget Reform

Improving transparency, forecasting and flexibility in New York State's budget process.

- Public hearing: Manhattan, December 17.

The Select Committee's members also include Senators Neil Breslin, Kenneth LaValle, Kevin Parker, Bill Perkins and Michael Ranzenhofer. Select Committee staff includes Executive Director Michael Lefebvre, Principal Analyst Richard Mereday and Administrator James Schlett.

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Senators Liz Krueger and Bill Perkins at the Select Committee on Budget and Tax Reform public hearing on improving New York State's budget process in Manhattan on December 17, 2009.