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Dutchess

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Memo

TO: Dutchess County Legislature

FROM: Valerie J. Sommerville, Budget Director

DATE: September 23, 2009

RE: Update on the County's Fiscal Position

Consistent with past practice, we are again this year providing the County Legislature with periodic fiscal updates as we did last year on September 15, 2008. With the first half of 2009 complete, there are several key budgetary issues of concern which are identified in this report.

In view of the year long global and national financial crisis that began in September 2008 as well as the predicted length of the recovery before us, it is more important than ever legislators understand and come to terms with the County's current fiscal position. There is no doubt the 2010 legislative budget process will be a daunting one.

Dutchess County's fiscal standing continues to be threatened by factors beyond our control. This is true with counties across the state regardless of size, major revenue streams, per capita income of its residents or property values.

Other counties across New York State are proposing unprecedented measures to fill extraordinary budget gaps, such as:

- Onondaga County's proposed budget includes a property tax hike, layoffs, pay cuts, a hiring freeze, job furloughs and increased fees.
- Putnam County's proposed budget includes layoffs, a freeze on filling vacant positions and a 15% reduction in funding to community agencies.
- Sullivan County has directed departments to submit across the board budgets cuts, and is considering the elimination of positions through attrition, a freeze on filling other vacancies, and is not ruling out raising taxes and laying off workers.

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- Broome County has instituted a hiring freeze and is considering all options to trim costs, including possible layoffs.

- Albany County has implemented furloughs to help close their budget gap.

- Tioga County has directed departments to submit across the board budget cuts, and is considering furloughs.

- St. Lawrence County is considering employee layoffs, program cuts and a wage freeze, and may be forced to consider a sales tax increase.

- Nassau County is vowing to not raise property taxes by holding positions vacant, maintaining low overtime for police and correction officers, consolidating services and implementing a county cigarette tax.

- Warren County is considering a lag payroll and layoffs.

- Delaware County has decided to freeze salaries and cost-of-living raises for all county employees.

These sobering factors, as well as new fiscal exposures, are highlighted below.

<u>State Budget</u>

Legislators were previously provided with an update on the 2009-2010 state budget impact in the May 1st fiscal update memo which Commissioner Barrack and I provided you.

While there may be minor signs of either moderating declines or stability, the national, state and local economies continue to experience downward trends in job losses, unemployment, and wage declines. According to a report released in July by the *Rockefeller Institute of Government*, the first three months of this year showed the steepest drop in state revenue collections in the 46 years quarterly data has been available. As bad as the first quarter was, the report indicates the second quarter is likely to be even worse. This suggests states, including New York, will have to resort to more spending cuts or higher taxes to balance budgets.

Yet to exacerbate its financial and budgetary problems, New York State government officials used billions of federal stimulus dollars to further increase spending in its 2009/2010 budget. When the stimulus money runs out after the 2010 fiscal year, what revenue or spending cuts will be necessary to offset it? This creates an alarming picture of New York's fiscal health as we look out to 2010 and beyond. We know New York's troubled fiscal health will be a direct indicator of more fiscal challenges that will domino to counties.

State Comptroller DiNapoli recently cautioned, "New York has a very real and growing current year deficit." Governor Paterson held a meeting with Legislative leaders today to discuss how to close the state's budget gap which is now expected to total $3 billion before the end of the state's fiscal year. The NYS Budget Office has previously projected a $4.6 billion deficit in next year's budget and a $13.3 billion deficit by 2011, forecasts that have continually worsened over the year.

Just last month, the Governor warned, "There's no other place to go now than either to cut from the actual budget or agree to a spending cap." And just this past week at the annual fall conference of the New York State Association of Counties (NYSAC), county officials were warned by state budget officials that New York's fiscal position is even more dire than previously known. Major cash flow problems exist on a month to month basis, and it was admitted the state is behind in reimbursing counties for services the counties have already provided.

Clearly, this ominous warning from state officials is unlike any seen or heard in New York in recent memory. We know from past experience, budget pressures in Albany mean cost shifts to county governments and local property taxpayers who are already dealing with their own fiscal challenges.

At the New York State Association of Counties (NYSAC) budget briefing last week to Chairs of Legislatures, and County Executives, the state budget director provided some insights to the state budget fiscal challenges.

State Budget Director Megna offered the following:

- NYS income tax revenues are down 35% YTD.

- Shrinkage of sales tax revenue is unprecedented – with declines worse than post 9/11 and expected to worsen. Sales tax slippage is across the board – big box, autos, jewelry, etc

- Commercial real estate will be the next big downturn and that few bank loan or investment dollars are available from the lending industry to commercial real estate.

- NYS can not grow out of this financial problem - even if NYS returns to strong growth rates of prior years it will not be sufficient to close budget gaps of 2010-2011-2012.

<u>Economic Impact</u>

Last month State Comptroller DiNapoli announced, "Although there were some small signs that the national economy is slowly turning around, economists project it will take longer for New York State to recover."

According to a study released in early July by the *Brookings Institute,* a Washington think tank, the Mid-Hudson Valley is among the top five U.S. metropolitan areas with the most severe wage declines in recent months. The study, which measures the economic health of 100 American metropolitan areas each quarter, found salaries of those employed by companies in the Poughkeepsie-Newburgh-Middletown region rank fifth hardest hit by falling wages.

Unemployment in Dutchess County for June reached 8.1%, the highest unemployment rate since 1994 and significantly higher than the average annual unemployment rate of 4.0% for 2007 prior to the economic downturn. August 2009 unemployment figures just released show Dutchess unemployment remains high at 8%, compared to the 5.2% annual average for 2008.

One of the areas of county government hardest hit by the economic downturn is the Department of Social Services, which continues to see a significant increase in the demand for services. Caseloads for food stamps, Medicaid, temporary assistance and HEAP are rising significantly as residents continue to struggle with the impact of the economy.

Recently the local housing market has shown some signs of improvement over 2008 figures. However, the County is still dramatically below 2007 statistics. Statistics released by the Mid-Hudson Multiple Listing Service show Dutchess County's home sales for August are up nearly 19% compared to the previous month of July, and sales are up 24% compared to August 2008. This must be viewed with caution, however, because on a cumulative basis year-to-date home sales are down 7% and the average selling price is down nearly 13% compared to the same period last year. Compared to August 2007, before the economic downturn, home sales are still down nearly 9%.

As we reported to you last year, once again the decline in the housing construction market coupled with reassessment activity of the past few years at the municipal level has resulted in a **further decrease of more than $1.5 billion in the County's 2010 tax base**. This will impact the 2010 property tax rate legislators will adopt in December.

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The following information highlights key county budgetary issues and revenue and expenditure areas where there exists a real or potential exposure. We continue to work closely with departments to control spending and maximize revenues to avoid year end shortfalls.

It's important to note the revenue and expense projections outlined herein are purely projections based on what we know today as is the case every fiscal year.

There are many other factors and variables which are not known at this time that will impact the county's 2009 year end fiscal position.

Revenues

The continuing downturn in the economy has resulted in exposure for the county's major revenue sources:

- Year-to-date sales tax receipts show a decline of $5.4 million or nearly 7.3% compared to last year at this time. Should this downward trend continue, the county will face a $6-$7 million budget shortfall this year in sales tax revenue.

- Mortgage tax revenue through August has declined by $1.2 million or 34% compared to last year at the same time. The current 34% rate of decline is slightly lower than the decline experienced in the first half of the year. However, if this trend continues, county government will still face a $1 million budget shortfall this year due to the decline in mortgage tax coupled with the Legislature's vote not to extend the mortgage tax beyond the November 30, 2009 expiration date.

- Hotel tax revenues are projected to be under budget by $653,000. This is due primarily to the Legislature's amendment during the budget process to include $550,000 in additional hotel tax revenue for a proposed rate increase from 4% to 6%. Although the revenue was included for 2009, there was not the level of support in the legislature to enact the increase.

- Interest earnings are projected to be under budget by $1.3 million as a result of the banking crisis, a severe decline in interest rates below 1% and lower than normal cash levels in the county's bank accounts.

- Mass Transportation Operating Assistance revenue paid to the County from the MTA is projected to be short by close to $100,000 compared to budget. This revenue has been steadily declining over the past few years as the State's distribution formula is factored on declining mortgage recording fees.

- Environmental Health permit fees and DPW-Engineering permit fees continue to be down due to the slowdown in construction, another indicator of the impact of the economy. If the current trend continues, the combined shortfall is estimated at approximately $40,000.

- At the end of the 2nd quarter, Mass Transportation (LOOP) was projected to end the year with a shortfall of $400,000. This shortfall is due primarily to legislative budget cuts and a delay in the Legislature's approval of the

LOOP fare increases causing the implementation of the new fee structure to be delayed until July.

- County government has had to use $8.5 million in county funds to pay for the state mandated Preschool Special Education Program for services provided from July 1, 2008 to February 28, 2009; however, we are still waiting for the state's reimbursement payment of $5 million. The State's reimbursement due to the county is lagging well beyond the historical payment date of June. I refer you to the County Executive's September 4th letter to NYS delegates asking for their assistance to release the funds the state owes county government, and to advise when Dutchess County can expect payment of past due amounts. As noted earlier, information received at NYSAC last week was not at all reassuring that payments will be timely in the future.

- As of the end of the 2nd quarter, a revenue shortfall of nearly $1.4 million was projected for the Department of Mental Hygiene (DMH) for 2009. This was primarily due to a unilateral change by the state in reimbursement methodologies for the clinics and Continuing Day Treatment (CDT) Programs. To offset this projected shortfall, we are working with the department to minimize this impact.

  Additionally, DMH has informed the NYS Office of Mental Health (OMH) that the state has made a mistake in its calculations of the Continuing Day Treatment COPS rate. DMH expects to receive approximately $700,000 if the state corrects their error retroactively to January 1st, 2009. Also, increased revenues of $300,000 to $400,000 are expected from the state and the federal government under the Medicaid Salary Sharing program, through which the county receives reimbursement for a portion of the cost of county staff time associated with the administration of Medicaid funded mental health programs.

- Based on receipts through the first half of the year, the County Clerk's Office is projecting legal revenue will exceed budget estimates by at least $127,000 due to the increase in recording fees effective February 1, 2009. DMV revenues are also up due to increases in motor vehicle fees. The County Clerk's Office is projecting motor vehicle fee revenue will exceed budget estimates by $72,000.

- OTB is projected to meet the $500,000 budget estimate for this year.

Expenses

Cost containment measures continue to be implemented across spending categories to minimize adverse impacts to Dutchess County taxpayers. It's not possible to quantify the total operational savings as department heads, recognizing our fiscal challenges, have also constricted operational spending internally and are restricting spending across various diverse appropriation line items.

Key expenditures and areas with potential significant fiscal exposure include:

- At this point, year end net vacancy savings is projected to meet the $2.2 million net to county vacancy factor adopted by the Legislature in the 2009 budget. However despite our efforts to control vacancy factor to achieve above the $2.2 million target, additional vacancy savings have been negated again this year due primarily to over expenditures by the Sheriff for personnel costs. The year end over expenditure in the Sheriff's payroll is projected at approximately $230,000.

- The MTA Mobility Tax imposes a .34 percent payroll tax on the wages and compensation paid by most employers within the counties comprising the Metropolitan Commuter Transportation District, which includes Dutchess County. This tax applies retroactively to March 1, 2009 with the initial payment due in November. This new mandated expense will cost the county approximately $337,000 this year with a reoccurring annual expense of more than $400,000 moving forward. These funds were not budgeted since the state law was adopted by the state legislature in the middle of the county's fiscal year.

- At this time, gasoline costs for DPW-Highway and the Central Services Auto Center are projected to be within budget. It's possible additional funding may be needed for fuel oil to heat our county buildings as these costs tend to be volatile.

- The Department of Social Services (DSS) projects state mandated foster care expenses will be over budget by nearly $1.5 million in net to county cost. Additionally, DSS projects a loss of $700,000 in state reimbursement due to the state's unilateral change in the administrative funding stream. Expenditures for State Training School placements is a concern as the county does not receive bills for these mandated services until the 2nd half of the year making it difficult to project whether budgeted appropriations will be adequate. Economic stimulus FMAP revenue will offset these and other shortfalls for this year.

- In the state mandated Pre-School Special Education Program, the Health Department is projecting additional expenses of nearly $700,000 due to an increase in the number of children and an increase in services required, as well as increased transportation costs. We have worked closely with the Health Department to find ways to cover this shortfall by limiting overtime spending to mandated coverage only, by reducing expenditures in various other expense categories and by maximizing revenues where possible.

- Other non-discretionary costs for pension and health insurance continue to grow and make up a significant portion of the budget, however, at this point we anticipate ending the year within budget. Earlier this month, the State Comptroller's Office announced the employer contribution rates for pension costs will increase considerably next year. We are advised the impact of the recession on the NYS Retirement Fund will drive the average rate up to 11.9% of payroll for 2010 compared to the current year average rate of 7.4% of payroll.

County departments have pursued ARRA funding opportunities for housing, transportation, energy improvements, infrastructure projects, public safety and technology. It's too soon to know the full impact of the federal economic stimulus funding. However, we do know Dutchess County, as well as all counties across the state, have serious concerns when faced with the challenge of maintaining fiscal stability once federal stimulus funding expires in 2010.

The county's fiscal picture dictates continued spending restraint with a tight focus on our core mission and how to continue to provide essential services with limited and declining resources. The Budget Office will continue to evaluate expenditures and revenues and work with departments to deal with the impacts of this unprecedented national and state financial crisis. With state funding cuts and other revenue shortfalls, we have been working with department heads and elected officials to take a hard look at the programs and services the county provides; there is no doubt the county will be faced with difficult decisions.

Unprecedented fiscal challenges will continue to face county government this year, next year and in the future. Legislators must anticipate how these uncertainties and exposures will impact the county budget and fund balance, as well as the property tax levy for the 2010 budget legislators will adopted this December and in future years. This will certainly require difficult 2010 budget choices.

cc: Barbara Hugo, Clerk of the Legislature
Department Heads & Elected Officials
Supervisors & Mayors
School Superintendents