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This paper is one in a series of reports prepared as part of New York State Lieutenant Governor Richard Ravitch's project, undertaken at the request of Governor David Paterson, to develop proposals that would lead New York State to structural budgetary balance. Lieutenant Governor Ravitch's initial report in March 2010 outlined the deep fiscal challenges facing the state and recommended a series of steps to eliminate future budget gaps. Other reports have examined gubernatorial powers to address midyear budget shortfalls, Medicaid expenditures, transportation infrastructure, and the cost of health benefits for public employees and retirees.

This final report in the series reviews the 2010-11 budget process and the resulting gaps. In that context, it highlights an international trend toward fiscal accountability mechanisms that force attention to the long-term implications of current budget practices – an area of ongoing failure in New York.

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STRUCTURAL BALANCE FOR NEW YORK

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Hidden in Plain Sight: New York's Unbalanced Budgets

Carol O'Cleireacain

Introduction

In the throes of the Great Recession, New York, like states all across the country, faced a huge budget deficit in 2010: a $9.2 billion gap between expected revenues and spending, and larger, growing gaps in the coming three years. Recession and past fiscal gimmickry had caught up with Albany. Governor David Paterson warned the Legislature and the voters that the state's fiscal practices must change dramatically. As part of his effort to put New York on a sustainable path, Governor Paterson appointed Richard Ravitch as lieutenant governor and charged him with developing proposals that could lead the state to structural budget balance. Anticipating a budget crisis of the magnitude New York City faced during the 1970s, Lieutenant Governor Ravitch concluded that New York State's long-term imbalance was so big there was no way to close it in one year without unacceptable damage to essential services or massive tax increases. So, he put together a plan to solve the problem over the course of five years. The plan called for more discipline: in the numbers, the accounting, borrowing, and interbranch cooperation.

The plan was not adopted. Instead, more than four months into the fiscal year, New York finally completed action on a budget. Barely three months later, it became abundantly clear that the enacted budget was not in balance. The state Budget Division estimated a potential year-end deficit of more than $300 million. State Comptroller Thomas DiNapoli warned that the gap could approach $1 billion and stated that the budget does not make progress toward achieving balance in the coming years any easier. An apt description of this year's budget would be a "wasted opportunity." The problem is not going away; we still have to confront the budget challenge.

This paper seeks to explain what happened and why. Section 1 lays out the context of New York's budget problem: Albany's rules, constraints, and learned behavior. It explains the enormity of the problem of trying to balance the state's increasingly unbalanced budget. Section 2 describes the current year budget, including the process of adoption, and how the budget was put together. Section 3 examines Lieutenant Governor Ravitch's plan as a way to break the mold and change the way budgeting is done in Albany. Section 4 provides an update on the current fiscal year and the outlook for the future years.

Section 1. The Budget Games Albany People Play

Budget balance is an interesting concept in New York.

For decades, regardless of the strength of the economy, recurring revenues have been insufficient to sustain ongoing spending. This is the definition of a structural imbalance.[1] Not only are revenues inadequate to sustain spending at a given point in time, but revenues typically grow more slowly than spending, creating a diverging path into the future. The combination of high spending and a volatile revenue structure has not been addressed, so the imbalance gets worse.

Early in 2010, the Division of the Budget estimated that the annual growth path for state spending over the ensuing four years would average about 7.5 percent a year, while revenues were projected to grow at about 3.6 percent annually.[2] The nearly four percentage point spread between the annual growth of spending versus revenue generates the large multibillion dollar gaps that must be closed to achieve sustainable budget balance. Prior to this recession, most analysts of New York's finances warned of the structural imbalance, which has fluctuated over time with permanent and temporary changes in taxes and other revenues and program spending. The lieutenant governor's March 10, 2010, report to the governor, entitled "A Five-Year Plan to Address the New York State Budget Deficit," estimated the structural gap, then, as being about $13 billion — a not unreasonable estimate at the time. Such a gap reflects years of budgetary actions that merely paper over the imbalance, in effect, "kicking the can" farther down the road. This growing structural imbalance took years to accumulate; it will take more than one year to eliminate it.[3] It is not realistic to imagine that the state's budget woes will disappear in one fell swoop.

In any given year, rather than address the structural problem, New York lawmakers struggle to wrench the upcoming year's budget into balance, temporarily and on a cash or checkbook basis, through heavy dependence on one-shot actions (about $25 billion in the past ten years), making the next year's balancing even harder.[4] Common practices in Albany are to transfer "excess" revenues from other state funds and public authorities; refinance outstanding bonds while realigning debt service payments to achieve front-loaded savings; roll or delay payments to suppliers and contractors, localities, and school districts from one fiscal year to the next; and delay payment of tax refunds into the following fiscal

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year. These kinds of machinations are possible because the state measures budget balance on the narrow basis of cash in the Treasury on the last day of the fiscal year. If there is a small positive balance or even a "zero balance," budget makers can claim that the budget for this year is "balanced."

As a result of this reliance on cash manipulations and one-shot transactions, the typical budget projections associated with the enacted budget will show that the adopted spending plan is in balance, but projections for future years will show ever-growing potential budget gaps.

Projections are always difficult. In the state of New York, revenue projections are even more difficult because the fiscal year begins on April 1st, prior to the April 15th filing deadline for the personal income tax — the state's largest tax source, producing more than one-quarter of total state revenue.[5] To construct an accurate budget, it is helpful to have accurate revenue forecasts. Forty-six states have fiscal years beginning on July 1st, which is well after income tax filings and generally coincides with school budgets. New York is the only state using April 1st. Further, enacting the budget occurs at one point in time. With even minor manipulation of cash, one can produce "balance" at that one moment, especially if "balance" is required for only 40 percent of the total activity. Governing daily to achieve balance is a whole other story.

The state's constitution and laws do not require the total budget to be in balance — only part of it.

The state's constitution, laws, rules, and practices do not require the state's total budget to be in balance — only part of it. The law requires only that the budget's General Fund be balanced when enacted, and only for the budget year (not for future years), and only when measured on a cash basis. New York's General Fund — accounting for only 40 percent or so of all state spending — is no longer an accurate representation of the state's spending and revenues, much less an illustration of its priorities, as a budget is classically described.

Further adding to difficulties is the learned behavior generating these persistent and growing gaps.[6] The state spends out of hundreds of accounts within four main groups of funds: the General Fund; special revenue funds (with dedicated taxes, fees, tuition, patient revenue, fines, federal aid, etc.); capital projects funds; and debt service funds. The General Fund — the main operating fund — receives all miscellaneous and undedicated revenues and has been thought of as the main "budget." However, special revenue funds have grown 351 percent — to more than 720 separate accounts — since 1985, resulting in a diminution of the General Fund's share of state spending.

With a system of cash accounting and multiple fund accounts, "balance" becomes a game of timing, involving decisions about which receipts to count and which bills to choose to pay when. With the legal requirement for balance applying only to the General Fund, there is every incentive to transfer resources into and spending out of it in ways to create the illusion that it is balanced.

As a result, none of New York's recent budgets have been structurally balanced, except perhaps in the eyes of those who vote or agree to deem it so. "The Deficit Shuffle," as the comptroller has aptly named it, now passes for budgeting.[7] As that report notes, "The State dips into dedicated funds here and shifts money over there, all to cover cash shortfalls and avoid making the difficult decisions needed...."[8]

The game of transferring revenues from other accounts to support General Fund spending is done with "sweeps." These have been rampant: $1.8 billion in the past three years.[9] The Environmental Protection Fund has been "swept" of almost a billion dollars over the past ten years and severely impaired in meeting its original programmatic intentions.[10] A traditional "sweep" involves budget bill language that specifies the transfer of a designated sum of money from a specified fund or account. "Blanket sweeps" now authorize the Budget Division to transfer moneys it determines are not needed for operations from undesignated funds or accounts, with only the aggregate amount of the sweep stated in the budget. The reliance on the use of "sweeps" is obvious; the state budget has employed easily identifiable "blanket sweeps" since FY 2007-08. These undesignated sweeps began with a $100 million authorization in FY 2007-08, an additional $350 million in FY 2008-09, and $575 million in FY 2009-10.[11] The FY 2010-11 budget authorizes half a billion dollars in blanket sweeps, with $231 million budgeted initially in the Financial Plan.[12] The choice of particular funds "swept," or denuded of their earmarked revenues, on the other hand, is opaque, without any required public disclosure upon enactment. In an accountant's terminology of "sources and uses of funds," the sources are secret but the uses are obvious, producing "balance" in Albany-speak.

The game of artificially lowering General Fund spending by shifting the costs elsewhere is known as "off-loading." The off-loading of ordinary state costs into the Dedicated Highway and Bridge Trust Fund has made it "effectively bankrupt," according to the comptroller.[13] Initially envisioned to provide revenue to pay for capital improvements on the state's roads and bridges, its "dedicated" revenues now pay for many other things — ferries, airports, snow and ice removal, bus inspections, and the entire Department of Motor Vehicles. The Trust Fund also pays a huge amount of state obligated debt service on a variety of transportation-related bonds issued by the Thruway Authority. Not surprisingly, the Dedicated Fund no longer has the funds necessary for its stated purpose — capital improvements — without a direct subsidy from the General Fund. That subsidy is now estimated at $578 million in 2010-11, and growing, contributing to the state's projected budget gaps.[14]

Section 2. The FY 2010-11 Budget

As the state entered budget preparations for FY 2010-11, the gap was huge, the rabbits remaining to be pulled out of the hat were fewer and thinner, and the magicians were exhausted. The national recession was wiping out 364,000 jobs in New York; the unemployment rate in the state peaked at 8.9 percent by the end of 2009.[15] The state's personal income fell in 2009 by more than 3 percent — for the first time in 70 years.[16]

As the fiscal year began, the estimated gap for FY 2010-11 was $9.2 billion (including spending carried-over from FY 2009-10); between the governor's Executive budget in January 2010 and March, the estimated deficit increased from $7.4 billion. This was largely because of worsening revenue projections (about $850 million) and the state's inability to contain the then-current year (2009-10) deficit, which had grown from $500 million to more than $1.6 billion and was being carried forward into 2010-11.[17] The state managed to end FY 2009-10 with a positive fund balance and restricted reserves intact only because the governor delayed an additional $1.1 billion in payments on the last day; a total of $2.9 billion in state payments and tax refunds was delayed from FY 2009-10 into FY 2010-11.[18] This delay only further worsened the situation for the 2010-11 budget year.

The state's "Deficit Shuffle" now passes for budgeting.

The future did not look any better. The Division of the Budget projected future deficits of $5.4 billion in 2011-12, $10.7 billion in 2012-13, and $12.4 billion in 2013-14 (based on the Executive 2010-2011 Proposed Budget Plan).[19] Growing out-year gaps indicate a chronic imbalance, and at $28.5 billion over three years, the numbers are large, even for a state that has the nation's third largest government — after only the US government and California.[20]

Contemplating the task of conquering these growing "gaps" last spring, staff at the Rockefeller Institute concluded that the budget-balancing actions facing policy makers were of a severity unlike the "normal" budget actions they were used to.[21] Simply doing the arithmetic, without paying attention to the policy or human damage, demonstrated that if one wanted to close the gap largely with new revenue, it would require tax and fee increases of the magnitude of 15 percent to 25 percent. If one wanted to close them largely though spending cuts, it would mean steps such as repealing the School Tax Relief program (STAR) and cutting most major programs about 15 percent. Even a balanced approach could mean tax and fee increases of roughly $520 a year for the average working New Yorker and the elimination of about 25,000 school-district positions, among other options. Based on past history, these choices were not conceivable in New York. When the state faced a $9 billion gap for 2003-04, much of the budget pain was avoided by the securitization of New York's share of the national settlement with the tobacco companies. That action helped generate an estimated $3.6 billion of short-term revenue, along with other budget gimmicks. (Unfortunately, the tobacco scheme eliminated nearly $1 billion in annual income for the state's health programs, contributing to the magnitude of the current budget gaps.)

Trying to bring balance to an unbalanced budget puts cash manipulation at the fore. Running out of money was the nightmare of the prior year, 2009-10, and cash management preoccupied budget officials as that fiscal year worsened. In November, 2009, the comptroller warned of a severe cash flow crunch: "without timely legislative action, the state's General Fund may incur a cash flow deficit…."[22] It did, even with a legislated Deficit Reduction Plan. For the first time since 1981, the General Fund ended a month — December 2009 — with a negative balance.[23] Projections indicated this would be repeated in the following year (FY 2010-11); it was. In June 2010, the General Fund ended in negative balance, again.[24] Estimates by the Budget Division indicated that very low balances were likely in November and December of 2010. Even if the General Fund did not go negative, the strain of the cash position has lowered the available balances on hand in the state's internal source of short-term borrowing — the Short Term Investment Pool (STIP) — compared to previous years.[25] Delayed payments and temporary loans from STIP have been used repeatedly over these two fiscal years to keep the state going. The practice is now, through new budget language, expanded from single month to multimonth loans, indicating "a more severe cash flow problem."[26]

In the prior year, Budget Division personnel practically tied themselves into knots working to avoid "formal" borrowing: i.e., selling notes in the public credit markets. Issuance of intrayear Tax and Revenue Anticipation Notes (TRANS) or interyear deficit notes (to be repaid the following year) would have raised significant fiscal, legal, and political issues. The Debt Reform Act of 2000 limits state debt issuances to capital purposes, although it does not apply to short-term tax and revenue anticipation notes that do not remain outstanding. New York's Local Government Assistance Corporation (LGAC) was established in 1990 to bond out the state's annual intrayear cash flow borrowing, known as the annual "spring borrowing"; some $3.4 billion of LGAC debt still is outstanding.[27] Borrowing to cover the FY 2009-10 cash flow problem would have required invoking LGAC's "emergency" provisions. This would have been a very public admission to the financial markets that the LGAC reforms had been circumvented, signaling in a very transparent way the state's return to past, discredited behavior. Instead, the state avoided public market borrowing by utilizing cash manipulations, which were effectively borrowings from local governments, suppliers, clients, taxpayers, and from the STIP.

With decision makers facing a host of huge and unpalatable choices, this fiscal year began on April 1st without a budget in place. Given his constitutional powers, this is not such a bad position for the governor to be in when revenues are deteriorating. When the governor submits temporary budget legislation because no annual appropriations are in place, the Legislature cannot amend such bills — their option is simply a yes/no response.

Without weekly budget bills to pay salaries and certain other expenses, the state would shut down, so the governor proceeded to submit twelve (weekly) interim appropriations bills that kept the state running.[28] Further, as E. J. McMahon, of the Manhattan Institute, has pointed out, these budget extender bills contained the governor's program cuts, and the Legislature had little choice but to pass them rather than shut down the state.[29] This is in contrast to the inability of the governor, alone, to significantly adjust spending once the budget has been passed. In that case, if the governor is worried that revenues will not be able to cover spending already enacted, his only option is to cap or reduce spending on state agency operations and go back to the legislature for changes in local assistance programs. The governor cannot impound state aid funds — for example, aid to school districts or Medicaid — appropriated by legislation.[30] This year, the governor, using another effective weapon, vetoed significant amounts of spending that he believed could not be supported by available revenue.

By the end of June, the Legislature completed all annual appropriations bills; at the beginning of August they passed the revenue bill, which completed budget enactment. There remained a back-and-forth over the fate of federal Medicaid money (FMAP), which was resolved with a contingency plan for spending reductions in case Congress did not pass an extension. The federal extension did pass, but at a level $280 million short of the state budget's expectation, so local assistance payments have received uniform reductions since September 2010.[31]

The enacted budget projected total (All Funds) spending for 2010-11 at $136 billion, a 7.1 percent increase over the prior year. However, this total includes some $2.0 billion in spending that was delayed from 2009-10 as fiscal managers pulled out all the stops to ensure that the state Treasury did not simply run out of cash. When adjusted for these payment delays, All Funds spending would be $133.8 billion, an increase of $4.9 billion or 3.8 percent, according to the Comptroller.[32]

The 2010-11 budget includes provisions through which the state will effectively "borrow" some $3.5 billion over the next several years from other sources to cover the cost of operations. First, $2 billion will be realized over the four-year period 2010-11 through 2013-14 by deferring tax credits owed to businesses; this amount will be repaid, without interest, over the three years from FY 2013-14 onward. The state will "save" a further $1.5 billion over three years by stretching out over 10 years its required contributions to the state pension fund. The legislation authorizing the pension fund stretch-out requires the state to pay interest (although at below-market rates) and allows the practice to continue indefinitely. The final irony, to paraphrase Alair Townsend, a former New York City budget director, is that the enacted budget gave New Yorkers more of the usual borrowing to cover operations but none of the budget rules, discipline, and oversight that

Lieutenant Governor Ravitch had proposed as the price to finally bring this practice to an end.[33]

Now, with the fiscal year more than half over, any illusion of balance has disappeared. The Budget Division has reduced its revenue estimates, but not nearly enough according to the comptroller, who suggests a gap of more than $1 billion above the mid-year, all-funds budget estimates.[34] Tax revenues would have to grow more than twice as fast in the second half of the year, compared to the first half, to meet even readjusted budget expectations, which is most unlikely.

Section 3. The Ravitch Plan

An alternative to "kicking the can down the road" was presented by Lieutenant Governor Ravitch in a "Report to the Governor" in early March 2010.[35] The report provided both a description of the state's structural budget problem and a prescription for solving it.

The report described three sources of the structural budget problem: the structure of state spending, reflecting both history and politics; the economy and its impact on budget revenues; and the ongoing tensions between legislative and Executive branches of the state government. New York's spending is concentrated on Medicaid — the most expensive Medicaid program in the country; school aid — with the second highest spending per pupil in the country; employee costs (including salaries and health and pension benefits); and debt service.[36] The economy of New York, relative to that of the nation, has been shrinking for decades; it is characterized on the one hand by slow employment growth, and on the other by high income and strong income growth. Government revenues, highly dependent on income taxes, are more volatile than is ideal when trying to pay for ongoing spending and also more volatile than those of most states.[37] In many respects, the two elements of public budgets operate in countercyclical patterns: when the economy is weak, spending pressures surge and vice versa. This phenomenon is accentuated in New York with its heavy dependence on the personal income tax payments of wealthy residents.

The economy of New York, relative to that of the nation, has been shrinking for decades.

The report, in focusing on the size of the problem, illustrated the long-standing nature of the structural imbalance and the inability of the Executive and Legislature to face up to it. One component of counterproductive state behavior has been an increasingly acrimonious tug of war between the Executive branch and the Legislature over spending authority. The governor and his budget staff bristle at their limited ability to control spending midyear, when economic reality changes. This limited Executive ability to make intrayear budget corrections, together with New York's focus on cash budgeting, invites stop-gap measures that push the problem into subsequent year(s), limiting the likelihood that the state can achieve ongoing budget balance.[38] New York is not the only government to wrestle with the question of Executive authority to impound, delay, retract, or otherwise contain already appropriated funds, but a number of states provide governors with such powers to promote budget balance.[39] Meanwhile, leaders and members of the Legislature bristle over what they see as the governor's over-reach in the use of program language to make law in budget bills, where the Legislature's ability to make changes is restricted by the state Constitution.[40] The legacy of mistrust on each side is palpable; it shapes the governance context in which the structural budget imbalance resides. It cannot be ignored.

Lieutenant Governor Ravitch's report presented an integrated set of budget and fiscal reform proposals designed to force the state to eliminate its structural budget imbalance: a multiyear financial planning process, based on more accurate accounting standards, that would require a strictly balanced state budget by the end of five years. Mandatory quarterly revisions of the plan, requiring spending and revenue actions by the Executive and the Legislature if necessary, would keep the current year budget in balance and the out-years of the financial plan closely linked to current reality. Lieutenant Governor Ravitch argued that the structural imbalance is too big to eliminate in a single year and too big not to require some transitional financing (short-term borrowing) to eliminate it. The lieutenant governor proposed permanently changing the start date of the fiscal year to July 1 (from April 1), increasing the levels of reserves, and adopting tighter accounting standards — Generally Accepted Accounting Principles (GAAP for government). GAAP is the standard for accurate financial reporting in both the public and private sectors. In contrast to the state's current cash accounting, which recognizes receipts when a check is received and disbursements when a check is cut, this accrual-based system requires recognition of revenues when they are actually earned and expenditures when the liability is incurred.

A multiyear financial planning process counters the all-too-human preference for the "short-term" by making visible and ongoing the consequences of policy decisions, whether they are new programs, collective bargaining agreements, or tax changes. Policy actions are examined through the lens of their ongoing (out-year) impact. A multiyear financial plan may offer some incentive to pair one-time revenues with one-time spending actions. Most important, the quarterly budget review and rebalancing process is designed to highlight the implications of a worsening situation in time for elected officials to take actions to prevent an emerging fiscal problem from turning into a crisis.

The discipline and rigor of a multiyear plan and "strict balance" requirements resemble the types of changes that some states have imposed on their cities in fiscal crisis.[41] For example, the state of New York mandated all of these changes for the city of New York when state action saved the city from bankruptcy in the mid-1970s. In addition, the state supported the city's borrowing, established a number of additional watchdogs on the city's finances, and imposed a Control Board that remained in place for a long time. (It still monitors and reports on the city's finances.)

New York State has sovereignty; no external body can impose a control board on it. If the state is to adopt a multiyear financial plan process — with the strict accounting and reporting discipline it involves — and stick to it, state lawmakers will have to do it because they are convinced that things can no longer continue on the current path. A self-enforcing mechanism would be needed to bind the state, voluntarily, to continue along the road to structural balance. But how does New York put in place a mechanism to oversee, monitor, and, ultimately, enforce this discipline for longer than a single electoral term?

Lieutenant Governor Ravitch proposed that the governor and Legislature create just such a monitoring mechanism. Combined with covenants written into any "transition bonds" issued during this five-year implementation period, a sufficiently prestigious board would have the influence to ensure that both the governor and the Legislature participated in the transition to structural balance and took it seriously. Independent oversight, technical reviews of budget data, and the need for the board's opinion on progress toward structural balance with each installment of "transition borrowing" would serve as credible enforcement mechanisms for budget discipline. The board — outside professionals with their own reputations at stake — would impose on the state's elected officials the threat of public criticism and, through the bond markets, strong punishment for failure.

In the end, the Ravitch plan failed to be adopted. The lieutenant governor put his considerable prestige and energy behind promoting the plan, but there were strong forces working against it that cannot be ignored. The justifiable distrust of Albany borrowing is understandable. Many chose "to make the perfect the enemy of the good"; in this case, perfection would have meant no more borrowing, not even for transitioning to a stricter, more disciplined system.

Yet, in many ways, the lieutenant governor's proposal was ahead of its time; a similar approach in the future may well benefit from this year's exercise.

Around the rest of the world, sovereign countries have recognized the speed at which bond markets can abruptly turn against them, requiring sudden budget adjustments where internal discipline has been lacking. They have put in place independent fiscal boards and, occasionally, strict budget rules to help bring greater discipline and less volatility to their budgeting and reduce budget deficits. This global trend serves as a hallmark of best practice, twenty-first century fiscal policymaking.[42]

Advisory bodies, generally known as "fiscal councils" and somewhat like the Congressional Budget Office in their independence and expertise, have come into being in Canada, Sweden, the

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Netherlands, Hungary, and the United Kingdom. Key to their success is their independence and the caliber of their members.[43] These examples demonstrate that sovereignty is not the issue. The common objective is to create an incentive structure that rewards attention to the longer-term implications of fiscal actions. As one journalist asked earlier this year, "…how can we get politicians elected on a short-term basis to think about the long-term good…?"[44]

Chile's elected leadership chose, over a number of administrations, to impose rules creating massive reserves, which preserve spending stability against its volatile revenues.[45] As Professor Jeffrey Frankel of Harvard University points out, "this may be just the sort of structural reform needed … where the politicians have repeatedly proven themselves unable to maintain long-term budget discipline."[46] Ireland learned this year that multiyear financial plans, monitored and revised quarterly, are the only anchoring for annual budgets that creditors trust. Also, in its agreement with the International Monetary Fund (IMF) and the European Union (EU), it has committed to adopt by mid-2011 a budgetary advisory council following the recommendations to the Parliament of Trinity Professor Philip R. Lane for the "adoption of numerical fiscal rules and a substantive role for an independent fiscal council … charged with the independent monitoring of fiscal policy."[47]

New York State, by contrast, has lived by its own rules for a long time. The culture around 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. The global financial crisis has shown us the catastrophic failures that occur when liquidity dries up. It has produced a move towards greater discipline, regulation, and transparency in a wide range of our public and private institutions. The state of New York cannot risk being left behind. Capital markets are unforgiving in their judgments, which they provide with little warning.[48]

Section 4. Where We Are Now

Given the delays in budget adoption, had the will for change been there, the state had a major opportunity for necessary and meaningful reform in developing its budget for the succeeding year and its budget process going forward. The months of budget delays offered a window of time, for example, to change the start of the fiscal year — something many observers and participants see as necessary for more reliable revenue estimation — from April 1st to July 1st. At the same time, the state could have begun in these interim months, as Ravitch proposed, the multiyear transitioning of systems and personnel to Generally Accepted Accounting Principles (GAAP) for budgeting. Finally, the extra time and deteriorating fiscal picture could have been used to begin a restructuring of New York's operating programs, the state's relationship to its local governments and school districts, and revenue measures to whittle away at the multiyear budget imbalance.

Instead, policy makers played the well-practiced game of "kicking the can down the road," displaying Albany's persistent preference for short-term expediency rather than permanent solutions. New York State not only failed to enact a solidly balanced 2010-11 budget that could withstand these adverse developments, but also failed to address the structural imbalance between underlying spending and recurring revenues.

The state's growing reliance on temporary budget resources is the primary cause of its long-term budget outlook. Extensive use of nonrecurring resources in a budget means that in subsequent years, when those resources are no longer available, revenues are not adequate to support spending. That is exactly the difficult situation that for several years has plagued New York policymakers.

There is often a difference of interpretation in New York about the exact definition of a nonrecurring resource. The Budget Division's Enacted Budget Report puts the number at $660 million in 2010-11, largely because most of the nonpermanent resources will be available for more than one fiscal year. Using a more expansive definition that includes resources that are available for more than one year but not on a permanent basis, the state comptroller calculates that $16.7 billion in nonrecurring or temporary resources support the 2010-11 state budget.

Two major elements of these nonrecurring resources are federal stimulus funds for Medicaid and education, and the temporary personal income tax increase. Federal stimulus funds decline sharply next year from the $5.9 billion expected in 2010-11 to just over $700 million in the subsequent year. Receipts from the temporary income tax increase drop more slowly, from nearly $5.8 billion in 2010-11 to under $4 billion next fiscal year. The decline in revenue from these two items alone, $7 billion, points to a very difficult FY 2011-12 budget season ahead for the new governor and Legislature.

Unfortunately, after 2011-12, the outlook does not improve, but instead grows still worse. Assuming no new one-shots are found to replace the nonrecurring resources being used to support state spending, the level of nonrecurring receipts and savings included in the multiyear projections will drop from $16.7 billion in 2010-11, to $2.1 billion in 2012-13. Overall, it is estimated currently that General Fund spending will grow nearly three times faster than revenues in the period ending with FY 2013-14, while all-funds spending (where federal stimulus funds are accounted for) grows more than twice as fast as revenues.

Even as the state faces the loss of these major nonrecurring resources, the underlying imbalance between recurring spending and revenue has widened. With every release of updated fiscal projections throughout 2010, the state's multiyear budget outlook has worsened steadily. January's Executive Budget projected a 2011-12 gap of $5.4 billion but after the 2010-11 budget plan was finally in place, the 2011-12 gap had mushroomed to $8.2 billion. More recently, the Budget Division's Mid-Year Update (FY 2010-11) puts next year's gap at $9 billion; the state comptroller warns it could exceed $10 billion.

A review of the cumulative gap for the upcoming three fiscal years reveals the same pattern. For example, in the January 2010 Executive Budget, the cumulative budget imbalance for 2011-12 through 2013-14 stood at $28.5 billion; it grew to $37.3 billion with the Enacted Budget; in November's Mid-Year Budget Update it ballooned to $40.8 billion. If the state comptroller's warning that the current year (2010-11) deficit is $1.0 billion materializes, the cumulative out-year gap will be that much larger.

Conclusion

While the state of New York is not technically insolvent, it is struggling to pay bills and meet its obligations to its citizens and local jurisdictions. This year's budget cut some growth in spending but, because it relies on more than $16 billion of one-shots or temporary revenues, makes achieving balance in the coming years even harder. Even as the current year imbalance grows (perhaps approaching the comptroller's estimate of more than a billion dollars), the Legislature and governor have been unable to approve a plan to restore balance.

Despite a long delay in adoption, the 2010 budget actions included no longer-term solution to the state's structural imbalance. There will be other opportunities; New York State's chronic problems have not improved. Economic events of the past decade — and particularly those of the past two years — have exposed large and growing structural imbalances and the Albany fiction of "balance." The ever-more-frantic "deficit shuffle" scars the state's accounts through repeated short-run, one-shot, temporary actions. New York has chosen to roll the deficit from one year to the next for the past two years; without intervention, such will again be the case on April 1, 2011.

New administrations, by definition, brim with optimism. As both Vaclav Havel and Cornel West have suggested, "optimism" is the belief that things will turn out as we would like, regardless of what we may or may not do to make that so. "Hope" is the belief that if we do the right thing, it is possible that *our actions* may make things turn out right. I have provided this review of New York's FY 2010-11 budget, in some historical context and with a look forward, in the desire that it may breed the "hope" and the conviction to do the right thing in those who take on the challenge of making New York's future budgets. The state has suffered enough from a sloppy "optimism."

Endnotes

1 A budget is not balanced when revenues and spending do not match; a deficit results when revenues are less than spending. A structural imbalance is when that is chronically the case because revenues grow more slowly than spending over the business cycle. In the case of New York, the Office of the State Comptroller's reports going back years have pointed out a worsening structural imbalance — with annual spending growth exceeding revenue growth.

2 Carol O'Cleireacain, "Remarks Before the New York Senate Select Committee on Budget and Tax Reform, " Testimony, New York , NY, December 17, 2009.

3 Richard Ravitch, *A Five Year Plan to Address the New York State Budget Deficit*, (Albany, NY: The Nelson A. Rockefeller Institute of Government, March 2010), p. 4, www.rockinst.org/pdf/budgetary_balance_ny/2010-03-10-LG_FYFP.pdf.

4 The Office of the State Comptroller documents the one-shot and temporary actions in each annual report on the state's enacted budget. This number adds them for FYs 2002-03 through 2009-10.

5 Office of the New York State Comptroller, *Report on Estimated Receipts and Disbursements State Fiscal Years 2010-11 through 2012-13*, November 5, 2010**,** p. 1, http://www.osc.state.ny.us/press/releases/nov10/quickstart2010.pdf.

6 Office of the New York State Comptroller, *New York's Deficit Shuffle*, April 2010, http://www.osc.state.ny.us/reports/budget/2010/deficitshuffle.pdf.

7 Ibid.

8 Office of the New York State Comptroller, "DiNapoli: Stop Playing Games With State Deficit," April 5, 2010, http://www.osc.state.ny.us/press/releases/apr10/040510.htm.

9 Office of the New York State Comptroller, *New York's Deficit Shuffle*, April 2010, p. 4, http://www.osc.state.ny.us/reports/budget/2010/deficitshuffle.pdf.

10 Ibid, pp. 4 -5.

11 A list of "blanket sweeps" prepared by OSC, covering actions from 4/1/07-2/28/10, enumerates 105 different accounts that have supplied the General Fund with more than $600 million over this period, so that it might be "balanced." See Office of the New York State Comptroller, *New York's Deficit Shuffle*, April 2010, Appendix A, http://www.osc.state.ny.us/reports/budget/2010/deficitshuffle.pdf.

12 Ibid. p. 5. See also Office of the New York State Comptroller, *Report on the State Fiscal Year 2010–2011 Budget Analysis Review of the Enacted Budget*, September 2010, p. 18, http://www.osc.state.ny.us/reports/budget/2011/2010-11enactedbudgetreport.pdf.

13 Ibid, p. 8.

14 Ibid, Appendix B.

15 Office of the New York State Comptroller, *Report on Estimated Receipts and Disbursements State Fiscal Years 2010-11 through 2012-13*, November 5, 2010, p. 5, http://www.osc.state.ny.us/press/releases/nov10/quickstart2010.pdf.

16 Ann E. Dunbar, "Regional Quarterly Report. State Personal Income and More…," Bureau of Economic Analysis," April 2010, p. 66, last updated: Wednesday, October 20, 2010, http://www.bea.gov/scb/pdf/2010/04%20April/0410_regreport.pdf, and Office of the New York State Comptroller, *Economic Trends in New York State. Report 8-2011,* October 2010, http://www.osc.state.ny.us/reports/economic/nys_economic_trends.pdf.

17 New York State Division of the Budget, *2010-11 Enacted Budget Financial Plan,* August 20, 2010, p. 7, http://publications.budget.state.ny.us/budgetFP/2010-11FinancialPlanReport.pdf.

18 Office of the New York State Comptroller, *Fiscal Update: Closeout Analysis of SFY 2009-10*, April 2010, p. 3, http://www.osc.state.ny.us/reports/budget/2010/yearend0410.pdf.

19 Office of the New York State Comptroller, *Current Status of the State Fiscal Year 2010-11 Budget,* Executive Summary, July 2010, p. 7, http://www.osc.state.ny.us/reports/budget/2011/budget10-11status.pdf.

20 Note that the out-year estimates lack precision, which may be the result of cash manipulations at year end. The estimated gap for SFY 2010-11, for example, began as $6.6 billion when it first appeared in DOB documents in April of 2007; it grew to $7.7 billion in 2008, but fell to $2.2 billion with the adopted budget in 2009; it ended up being $9.2 billion when 2010-11 budget needed to be enacted. See enacted budget documents from SFY 2007-08 onwards.

21 Robert Ward, "Four-Year Financial Plan Report: Section One," (unpublished draft, Albany, NY: The Nelson A. Rockefeller Institute of Government, March 3, 2010).

22 Office of the New York State Comptroller, "New York's Cash Flow Crunch," November 2009, p. 1, http://www.osc.state.ny.us/reports/budget/2009/cashflowcrunch.pdf.

23 Office of the New York State Comptroller, *Comptroller's Fiscal Update: Closeout Analysis of State Fiscal Year 2009-10*, April 2010, p. 4, http://www.osc.state.ny.us/reports/budget/2010/yearend0410.pdf.

24 New York State Division of the Budget, *2010-2011 Financial Plan Mid-Year Update,* November 1, 2010, p. 16, https://www.budget.state.ny.us/budgetFP/1011midyear/2010-11_MidYearUpdate.pdf.

25 Ibid.

26 Ibid. p. 5. See also Office of the New York State Comptroller, "New York's Cash Flow Crunch," November 2009, p. 1, http://www.osc.state.ny.us/reports/budget/2009/cashflowcrunch.pdf.

27 Office of the New York State Comptroller, *New York Local Government Assistance Corporation*, http://www.osc.state.ny.us/pension/debtlgac.htm.

28 These extender bills are not particularly transparent; there is no consistent order as to what category or amount is allocated in which section, making it very difficult for anyone not personally involved to understand how the process unfolds. New York State Finance Law Article 4, Section 53, governs Special Emergency Appropriations "necessary or essential to the proper and efficient functioning of the government of the state."

29 See E.J. McMahon, "Ugly Budget — But a Pretty Precedent," *New York Post*, June 30, 2010, http://www.nypost.com/p/news/opinion/opedcolumnists/ugly_budget_but_pretty_precedent_Bu2aHMgWg6vJWFkk3gRcJO; and E.J. McMahon, "Is New York Ungovernable? Certainly Not, and David Paterson Has Helped Show The Way," *The Post-Standard*, August 29, 2010, http://blog.syracuse.com/opinion/2010/08/is_new_york_ungovernable_certa.html.

30 Robert Ward, "Gubernatorial Powers to Address Budget Gaps During the Fiscal Year," (Albany, NY: The Nelson A. Rockefeller Institute of Government, June 17, 2010). See also *County of Oneida, et al., v. Berle*, 49 N.Y.2d 515 (1980).

31 New York State Division of the Budget, *2010-11 Enacted Budget Financial Plan*, August 20, 2010, http://publications.budget.state.ny.us/budgetFP/2010-11FinancialPlanReport.pdf.

32 Office of the New York State Comptroller, *Report on the State Fiscal Year 2010–2011 Budget Analysis Review of the Enacted Budget,* September 2010, p. 3, http://www.osc.state.ny.us/reports/budget/2011/2010-11enactedbudgetreport.pdf.

33 Alair Townsend, "State budget lives on borrowed time," Crain's New York, July 18, 2010, http://www.crainsnewyork.com/article/20100718/SUB/307189987.

34 Office of the New York State Comptroller, *Report on Estimated Receipts and Disbursements State Fiscal Years 2010-11 through 2012-13*, November 5, 2010, http://www.osc.state.ny.us/press/releases/nov10/quickstart2010.pdf.

35 Richard Ravitch, *A Five Year Plan to Address the New York State Budget Deficit*.

36 Citizens Budget Commission, *Medicaid in New York: Why New York's Program is the Most Expensive in the Nation and What to Do About It,* April 2006, http://www.cbcny.org/MedicaidREV4Web.pdf.

37 Robert Bifulco and William Duncombe, "Budget Deficits in the States: New York," *Public Budgeting and Finance*, 30 (2010): 69.

38 To understand restrictions and prohibitions on the impoundment of appropriated funds see *County of Oneida, et al., v. Berle*.

39 Robert Ward, "Gubernatorial Powers to Address Budget Gaps During the Fiscal Year," (Albany, NY: The Nelson A. Rockefeller Institute of Government, June 17, 2010).

40 *Silver v. Pataki*, 4 N.Y.3d 75; 824 N.E.2d 898 (2004).

41 Early examples were Ohio with Cleveland and Pennsylvania with Philadelphia. Together with New York and New York City, they served as models for the US Congress when the District of Columbia lost access to the credit market. See Carol O'Cleireacain, *The Orphaned Capital: Adopting the Right Revenues for the District of Columbia* (Washington, DC: The Brookings Institution, 1997).

42 Recent events in Europe illustrate this. The European Commission has proposed that all 27 European Union (EU) member states tighten their fiscal frameworks, including recommendations for publicly available pre- and postbudget audits and multiyear financial plans. These recommendations need to be adopted by two groups of elected officials — those of the European Council and the European Parliament. See European Commission, "Proposal for a Council Directive on requirements for budgetary frameworks for member states," COM (2010) 523 final, Brussels, September 29, 2010, Chapter III, Section 4. http://ec.europa.eu/economy_finance/articles/eu_economic_situation/pdf/com2010__523en.pdf.

43 There is a growing literature on this subject, including studies by the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF). The EU's Stability and Growth Pact, agreed in 1997, which is its set of fiscal rules, currently under reform for tightening and improved accountability and enforcement, has generated a multitude of commentary and analysis. Easily accessible information may be found in the bibliography of Phillip R. Lane'report (see endnote 46). For the UK, see the Parliamentary discussion on the need for independence for the Office of Budget Responsibility (OBR) http://www.publications.parliament.uk/pa/cm201011/cmselect/cmtreasy/385/38507.htm.

44 Catherine Rampell, "Stiffening Political Backbones for Fiscal Discipline," *The New York Times*, February 14, 2010, http://www.nytimes.com/2010/02/14/weekinreview/14rampell.html.

45 See Jeff Frankel's Weblog, "Achieving Long Term Fiscal Discipline: A Lesson from Chile," January 31, 2010, http://content.ksg.harvard.edu/blog/jeff_frankels_weblog/2010/01/31/achieving-long-term-fiscal-discipline-a-lesson-from-chile/.

46 Jeff Frankel, "Achieving Longer-Term Fiscal Discipline: A Lesson from Chile," *Global Macro Economic Monitor*, February 1, 2010, http://www.roubini.com/globalmacro-monitor/258349/achieving_long-term_fiscal_discipline__a_lesson_from_chile.

47 See Irish Government, "EU/IMF Programme of Financial Support for Ireland," December 1, 2010, p. 13; and Philip R. Lane, "Report on Macroeconomic Policy and Effective Fiscal and Economic Governance," September 23, 2010, in preparation for the Joint Oireachtas Committee on Finance and the Public Service, http://www.oireachtas.ie/documents/committees30thdail/j-financepublicservice/reports/20101111.pdf.

48 Based on information provided by OSC sources, in 2010 there were, in Moody's and Fitch's judgment, only three states with lower ratings on their general obligation debt than New York. As we painfully know, the actions of rating agencies generally follow, not lead, bond market judgments.

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The Nelson A. Rockefeller Institute of Government, the public policy research arm of the University at Albany, State University of New York, was established in 1982 to bring the resources of the 64-campus SUNY system to bear on public policy issues. The Institute is active nationally in research and special projects on the role of state governments in American federalism, and the management and finances of both state and local governments in major areas of domestic public affairs.

The Rockefeller Institute maintains a particular focus on New York State studies with an ongoing series of forums on major public-policy issues, publication of the *New York State Statistical Yearbook*, special studies, and other initiatives. This report is part of the Institute's research support for Lieutenant Governor Richard Ravitch's project to develop proposals that would lead New York State to structural budgetary balance.

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