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Report on Deficit Declaration Remediation Plan

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Erie County Legislature
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Dear Honorable Members:

On May 4, 2020, I submitted to your honorable body a declaration that a deficit existed in the 2020 Erie County budget. I did this as required by the Erie County Charter.

As mandated by the Charter, the County Executive was to submit a written plan to remediate the budget deficit to the Legislature by May 11, 2020. To date, no such plan has been submitted. As such, and in an effort to address this fiscal crisis, our office considers the failure to submit a plan as required as a failure to have a plan. We consider the failure to have a plan as a plan to do nothing. The Charter provides the Comptroller with seven days to comment on the plan submitted by the County Executive.

Elected officials should not engage in partisan sniping about the size of the deficit nor whether it exists. This is reminiscent of how politicians behaved at the start of the “Red-Green” budget crisis. All economic indicators are pointing to the majority of municipalities, if not all municipalities in the state, are facing a deficit. No one foresaw the COVID-19 pandemic nor the economic ruin it has brought. It is the fault of no one within the walls of Erie County government. Yet it is our responsibility to offer you multiple options on how to close anticipated gaps.

This report serves as our comments to the plan to do nothing.

As you will see, the comments offer a menu of options available to remediate the budget deficit. It is not intended as an exhaustive list, nor is it intended, unless noted, to demand that any of the actions be taken. Rather, it serves as a guide to assist you with your actions to maintain a balanced budget.

Erie County Executive Mark C. Poloncarz himself acknowledged the existence of a deficit in his letter to the Legislature on Friday, May 8, 2020.

“That (federal) financial aid could reduce the county's deficit by tens of millions of dollars or more.”
Source: Erie County Executive Mark C. Poloncarz, letter to the Erie County Legislature, May 8, 2020

Despite assertions to the contrary, a budget deficit exists based on readily available information and forecasts. The deficit must be addressed and will only worsen without action to fix it. Of course, fiscal conditions during these unprecedented times may change rapidly. As such, actions taken to reduce the deficit now can and should be revisited throughout the year to ensure that services are provided in the best way possible while also maintaining a balanced budget.

It is important to realize that under no circumstances should raising taxes be considered. This area is overtaxed. Past deficits were fixed by new taxes. Temporary sales tax increases and higher property taxes will not work. One lesson that must be learned is that building government with economically driven taxes will lead to deficits when the economy fails.

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Background

The Erie County budget was passed by the Legislature on December 5, 2019. The County Executive notified the Legislature of his acceptance of the budget as amended on December 12, 2019, weeks before news of COVID-19 began spreading outside of China. Since then, worldwide events have occurred with devastating physical, fiscal and operational consequences. While many parts of the world, and state, have begun phased in approaches to reopening, as of the submission of this report, Erie County remains closed for most business. Each day of closures impacts the revenue projections upon which the Erie County budget heavily relies, especially but not limited to, sales tax revenue.

Sales tax accounts for a significant amount of the revenue that Erie County uses to fund its spending decisions. In the 2020 budget, Erie County anticipated county use share of sales tax revenue to be $491,338,760. This is separate from the $337,955,669 that the county anticipated sharing with cities, villages, towns and school districts. The Niagara Frontier Transportation Authority (NFTA) also receives a contracted amount equivalent to one-eighth of one percent of sales tax. By way of comparison, the Erie County budget anticipated $305,272,912 in property tax revenue. As such, in any situation where sales of taxable goods are expected to decrease, it should also be expected to experience a reduction in sales tax revenue.

The New York PAUSE Order has effectively shut down economic activity in the county. All economic activity has ceased except what the state has determined to be essential. A number of standards have been set by the state that the Western New York region, defined as the counties of Niagara, Erie, Cattaraugus, Chautauqua and Allegany must meet. They are:

- 14 Day Decline in Net Hospitalizations or Under 15 New Hospitalizations (3 Day Average)
- 14 Day Decline in Hospital Deaths or Fewer than 5 Deaths (3 Day Average)
- New Hospitalizations (Under 2 per 100,000 residents – 3 Day Rolling Average)
- Share of Total Beds Available (Threshold of 30%)
- Share of ICU Beds Available (Threshold of 30%)
- 30 per 1,000 Residents Tested Monthly (7 Day Average of New Tests per Day)
- Contract Tracers: 30 per 100,000 Residents or Based on Infection Rate

To date, the Western New York Region has not met the following metric:

- Contract Tracers: 30 per 100,000 Residents or Based on Infection Rate

Meeting the criteria starts a four-phase re-opening of the economy. Included in the phases are:

- Phase 1: Construction; Manufacturing and Wholesale Supply Chain; Curbside pick-up Service for Retail; and Agriculture, Forestry, Fishing and Hunting

- Phase 2: Professional Services; Finance and Insurance; Retail; Administrative Support; and Real Estate/Rental Leasing

- Phase 3: Restaurants/Food Services and Hotels/Accommodations

- Phase 4: Arts/Entertainment/Recreation and Education

Each of the phases open based on continuation of meeting the criteria. It is also unclear if there will be two weeks between each phase of reopening, although that is the anticipated time frame.

Based on these criteria, it is anticipated that Erie County will re-open soon. Forty-seven counties have been cleared to conduct elective surgeries, although Erie County has not. While the Finger Lakes, Southern Tier, Central New York, North Country and Mohawk Valley regions have met the metrics to commence phase one, Western New York has not. This creates opportunities for Erie County taxpayers to seek certain goods and services from neighboring counties, such as Genesee, Orleans and Wyoming counties. Hopefully the success of neighboring counties is a harbinger of future success for Erie County.

However, reopening doesn't ensure that sales tax revenue will resume pre-closing levels. The phased in approach means that businesses will gradually be made available to the public. Social distancing will remain in effect for the foreseeable future. Entertainment events, such as sporting events, concerts and festivals, will be postponed or cancelled. A number of cancellations have already occurred. Not only will this result in less sales tax revenue from local revelers, it will result in less tourists traveling to the area to enjoy events. This will also result in continued reduced bed tax revenues. Further, consumers may delay purchases while economic uncertainty remains.

The New York State Association of Counties (NYSAC) issued a report that estimated a 9.3% - 22.5% drop in sales tax for the year. Its estimate for Erie County was $73,554,855-$150,232,622. Our Deficit Declaration put the estimate at $127,933,095, close to the middle of this projection. This is within the NYSAC range. NYSAC has also opined on other revenue sources like Hotel Occupancy Tax, Casino Revenue and State Aid. All estimates included in our Deficit Declaration are within NYSAC's estimates. A copy of this report, as well as additional data from NYSAC and the National Association of Counties (NACo) are attached as Appendix A.

On May 11, 2020, the Office of the New York State Comptroller notified the county that for the month of March County Share sales tax revenue is down 19.5% or $6,998,856. The County Share sales tax revenue totaled $28,925,700 for March 2020, compared to $35,924,557 for March 2019.

As discussed in a separate report, the New York State 2021 budget allocates over $100 billion in expenditures. Included in the budget are significant expenditures to assist local governments. Upon passage of the budget, it was announced that the state anticipated revenue to be $10 billion to $15 billion less than necessary to fund the expenditures. This estimate appears to be growing.

As such, the budget includes a provision giving the budget director the ability to make uniform cuts in expenditures, with certain areas excluded from the cuts. Erie County anticipated state funding of $182,539,939 in operational aid, as well as additional capital and grant aid. A 20% to 50% reduction could result in a revenue shortfall of $36.51 million to $91.27 million.

In addition to the above, Erie County anticipates revenue budgeted in the county's General Fund that is noted as Fees and Other Local Sources. These are detailed in the attached Appendix B. Fees revenue was budgeted to be $33,564,387 and Other Local Sources was budgeted to be $38,928,413. Included in the Other Local Sources is $11,600,000 in Hotel Occupancy Tax. All of these revenue sources are anticipated to decrease as a result of changes in behavior caused by the COVID-19 pandemic.

Throughout the pandemic, this office has been reviewing a number of financial services' guidance documents to monitor the rapidly changing economy. Information from these sources, as well as others as noted in this report, helped lay the foundation for our Deficit Declaration. The services include:

- Moody's Rating Services
- Fitch Rating Agency
- Kroll Rating Services
- Standard & Poor's
- The Wall Street Journal
- Citibank
- JP Morgan Chase
- FHN Services
- Hilltop Securities
- Jefferies

Deficit Reduction Tools

It is clear that Erie County will not achieve revenue as anticipated in its 2020 budget. These revenue shortfalls are significant. They will require action by the Legislature to address these shortfalls. In order to assist the Legislature with its responsibility, this report serves as the Charter offered opportunity for a response by the Comptroller. The following tools are not intended as an exhaustive list, nor is it intended as a directive that the Legislature must or must not undertake. As always, the Office of the Erie County Comptroller remains available for consultation and assistance with your responsibility to maintain a balanced budget.

1. Utilization of Third COVID-19 Fiscal Package

On March 25, 2020, the United States Senate passed the “Coronavirus Aid, Relief and Economic Security Act” (CARES) as amended. The United States House of Representatives approved the measure on the following day, and the bill was signed into law on March 27, 2020.

The CARES act is the largest relief act in United States history. It is the third of four relief measures passed to counter the physical and economic impacts of COVID-19. To date, the four relief bills have cost more than $3 trillion.

As a component of the CARES Act, Erie County received $160 million from the federal government to help pay for the unexpected financial toll this has taken. According to the legislation, the $160 million must be spent directly on Coronavirus related expenses only. This means the $160 million cannot be used to offset what is going to be the biggest negative impact on our budget: the anticipated loss of sales tax revenue.

However, certain employee expenses are eligible to be compensated through this federal government assistance. Such expenses include:

- Payroll expenses for public safety, public health, health care, human services, and similar employees whose services are substantially dedicated to mitigating or responding to the COVID-19 public health emergency.

- Expenses to improve telework capabilities for public employees to enable compliance with COVID-19 public health precautions.

- Expenses of providing paid sick and paid family leave, and medical leave to public employees to enable compliance with COVID-19 public health precautions.

Because at this time the $160 million can only be used for COVID-19 expenses, it is imperative that all qualifying expenses be attributed to this fund. There may be opportunities to apply these funds to individuals whose duties have been substantially shifted to addressing COVID-19. For example, if it is identified that due to present circumstances, a position is not a priority for providing services at this time, that individual could be reassigned duties to serve as a contact tracer. As such, experienced government civil servants could use their skills and knowledge to benefit the community and meet state-imposed metrics, while not adding to the budget deficit. Special attention should be given for identifying these expenses and adjusting the budget as necessary.

2. Elimination of Vacancies

When addressing a revenue deficit, it can be helpful to reduce or eliminate spending that was previously identified as a priority. This prioritization allows for the targeting of specific expenditures, with consideration given to whether the spending is mandated or if certain priorities are valued over other priorities.

Consideration must be given to the triggering of matching funds. For example, if the priority is subject to matching funds and is eliminated, this may cause a further revenue shortfall. Further, elimination of a service may have impacts on other services provided. This may render the other service more costly to provide, thus merely transferring costs, rather than eliminating them. Certain programs may be exceedingly difficult or impossible to provide with even partial cuts. These, as well as other considerations, must be given to every cut.

The County has budgeted $1,800,000 turnover savings in the 2020 adopted budget. Attached as Appendix C are two reports detailing the General Fund vacant positions as of May 5, 2020. The first lists 355 full time positions that are vacant. The gross 2020 budgeted salary is $15,416,345 and a net county share of $9,804,166. The second details the General Fund vacant part time positions. This list totals 143 vacant positions with 2020 budgeted salaries totaling $1,480,094 and a county share of $1,097,180. These numbers do not include the budgeted fringe benefits that will total in the millions.

Eliminating vacancies is preferable to layoffs. It would be advisable for the Legislature to obtain a report from the Administration detailing how the county has been able to provide services while the positions have remained vacant.

The County Executive has requested that elected officials submit a plan to reduce their budget by 13.1% of the total annual budget. That percentage equates to approximately $203,700,000 in general fund cuts. These plans were requested to be returned to his office on May 15, 2020. Such a plan places the responsibility of determining cuts on each elected official. However, it does not suggest that each program or service will experience a 13.1% decrease in funding. Due to the mandatory nature of certain programs and services, some programs will experience no cuts. However, other programs may experience severe or total elimination in order for the 13.1% metric to be met.

Because the date has passed for the County Executive to submit a written deficit remediation plan to the Legislature, and because the legislature may wish to adopt such a plan as part of its own deficit reduction plan, the Comptroller's Office plan to reduce expenses by 13.1% is attached hereto as Appendix D. The plan actually reduces expenditures in excess of 13.1%.

3. Fund Balance

The fund balance is a pool of money accumulated when revenues exceed expenses for any given year. That money can be accessed to fund spending priorities of the Legislature. It can also be used to balance a budget that becomes out of balance during the fiscal year. As such, it is sometimes referred to as a "rainy day fund."

Given the current COVID-19 pandemic and resulting fiscal distress, it may be helpful to examine Erie County's fund balance and the availability of funds to make intra-year adjustments to the budget.

For the end of 2019, Erie County's total fund balance was $173,750,000 while the undesignated fund balance was $102,898,785. This is an increase of $2,631,000 since 2015 and $57,101,000 more than fund balance at the end of 2008, in the midst of the "Great Recession." The undesignated fund balance is more important than total fund balance for the purpose of utilizing these funds to address revenue shortfalls.

According to section 2505 of the Erie County Charter, "the County shall maintain an unassigned Fund Balance in the General Fund equal to or greater than five percent of the amount contained in the adopted budget of the General Fund of the County's last audited financial statements."

At the end of fiscal year 2018, the unassigned General Fund balance was $102,490,000. This equated to 6.59% of the $1,554,964,341 contained in the adopted 2020 General Fund budget. Given the General Fund budget, the Charter requires that Erie County maintain a fund balance of at least $77,748,217. This allows $24,741,783 to be used for deficit reduction. It should be noted that if the budget is amended to reduce appropriations, the required level of fund balance will concurrently decrease, leaving additional funds to be used for deficit reduction. For example, if spending cuts are made in the hypothetical amount of $4,964,341, that would leave $25,490,000 available for deficit reduction.

There is fund balance available to utilize for the purposes of addressing revenue shortfalls. Usage of fund balance may have an impact on the county's credit rating and ability to borrow. The potential for future ratings impact should be weighed against the immediate need to address a revenue shortfall when deciding to utilize fund balance.

Fund balance can be an effective funding source for addressing unanticipated revenue shortfalls while minimizing impact on the provision of services. A reason for this is that if unanticipated revenue becomes available, such as unbudgeted funding from the federal or state government, these funds may then be utilized, either directly or indirectly, to replace previously utilized fund balance.

4. Hiring Freeze

Hiring freezes can be an effective tool for addressing shortfalls. True hiring freezes allow savings from vacant positions, as well as prevent the creation of new positions. Since 2013, the number of employees included in the Erie County budget has risen more than 380 positions, from approximately 5,690 to 6,072 in the 2020 budget.

Understanding that true hiring freezes are not always possible due to the existence of mandated positions, it should be noted that hiring freezes are most effective when strictly adhered to.

On March 23, 2020, the County Executive directed implementation of a hiring freeze. Between that time and May 15, 2020, Erie County hired 16 individuals into county employment. These positions include but are not limited to a Parks Superintendent and Consumer Advocate.

Hiring freezes are generally preferable to layoffs. Layoffs have an impact on live bodies, who are actual people, many times with families, who use their earnings to support businesses in the community. Vacancies exist because the positions are not occupied by an actual person. Further, because Erie County is self-insured, the salary savings from layoffs is dampened by the county's obligation to fund unemployment payments. The true savings from layoffs occurs in the future, after unemployment benefits are terminated. As such, layoffs should be considered if it is determined that the positions are not needed now, and will not be needed in the future.

5. Freeze Position Count in the 2021 Budget

By all appearances, the economic and health impacts of the COVID-19 pandemic will not end on December 31, 2020. As such, the Legislature must carefully balance the provision of services with available resources. This will be challenging for the 2021 budget. The final determination of the exact sales tax shortfall will not be known until February 2021, when it receives its final 2020 sales tax distribution. These economic realities must be addressed during the 2021 budget process.

Because of these realities, it may be advisable to avoid adding new positions in the 2021 budget, unless they are crucial to the response to the pandemic and are offset with equal deletions. The temptation to expand government during economically challenging times may have ripple effects, which result in further economic distress.

6. Voluntary Furloughs

While layoffs do not provide the full impact of savings, layoffs may be considered as a way of saving limited amounts of money in the short term. Several New York State counties, realizing that they were facing a revenue shortfall as a result of COVID-19 impacts, have offered employees voluntary furloughs. In these arrangements, employees request and are approved to be temporarily laid off, with a projected return to work in August 2020. This allows employees to qualify for an extra $600/week in unemployment benefits, while also maintaining their health insurance.

Although the cost savings would not be massive for such a program, it would allow Erie County to save some funds to be used to address revenue shortfalls. For some employees, the extra money received would result in payments higher than their normal income. This would result in more money available to employees to spend at businesses in our community. Such an advantage for the employee would dissipate upon the termination of the extra $600 per week benefit.

7. Early Retirement

Early retirement incentives must be viewed carefully and skeptically. In general, far reaching early retirement incentives rarely justify the costs of implementation. However, carefully executed early retirement incentives may be an effective tool to reduce some costs.

Given the New York State employment tier system, there may be opportunities to offer incentives to encourage some individuals that are Tier 4 or better to be replaced with an individual who is Tier 6. Consideration must be given to the position to ensure that the position vacated by the Tier 4 individual is one which would typically be refilled, if at all, by an individual at the Tier 6 level.

Further, consideration must also be given to the cost of the incentive. Obviously, an incentive that costs more than salary and fringe benefit savings is not a cost-saving measure.

The savings, if any are identified, may not be large in the current year. Instead, the impact of the savings may be more apparent in out years. This is due to cumulative savings derived over the initial costs. However, simply because the savings may be smaller initially does not mean that a tool should be ignored. Because it is anticipated that fiscal challenges will persist into 2021, it may be advantageous to explore the use of this tool now.

8. Deficit Financing

Under current law, the County is authorized to borrow on a limited short-term basis to cover revenue shortfalls in its current fiscal year by issuing “deficiency notes”. The amount of this deficit borrowing is limited to 5% of the County’s total budget, and would have to be repaid by December 31, 2021. Legislation has been proposed for approval by the State Legislature which would remove the current law 5% cap and authorize the County (and all other municipalities and school districts) to issue deficiency notes in any amount deemed necessary by the County Legislature. Such proposed legislation would also allow such notes to be repaid up to five years after the first borrowing, and as an option long-term bonds could be issued to finance the deficit caused by revenue shortfalls over a longer period up to 10-15 years.

Ultimately, if this proposed State legislation is enacted, the amount and length of the deficiency note borrowing would be decided by the Erie County Legislature. Under State Law, the Legislature is the body that authorizes debt to be issued by County government. Since the duration of the COVID 19 pandemic and related economic disruption is unknown, forecasting interest rates and market acceptability is unknown. The Office of the Comptroller will continue to monitor the credit markets in determining the feasibility and need for such debt and will make its recommendation to the Legislature at the appropriate time.

In the meantime, using the powers delegated by the County Legislature, the Office of the Comptroller has selected underwriters and is continuing its work with the County’s bond counsel and financial advisor to issue a Revenue Anticipation Note (“RAN”) in the amount of $125,000,000 to ensure that adequate cash flow is available to pay the County’s obligations. The current plan is to close the RAN transaction in the time period of late June or early July, as noted in the First Quarter Financial Statements submitted to the Legislature.

9. Additional Federal or State Aid

At this time, it cannot be said with certainty that federal aid is forthcoming. Even less certain is the amount of federal aid if it is allocated to local governments. Proposals have been discussed that would provide more funds than actual revenue lost; proposals which would provide $81 million; proposals which would allow the previously granted money to be used to address revenue shortfall; and other proposals as well.

Regardless, it is difficult to quantify the hope for federal aid into a specific dollar amount. We do know that currently, the amount is $0. Additional federal, or even state aid, would be very helpful in addressing Erie County's revenue deficit.

Any aid received from outside sources should be used to address the revenue shortfall, provided that use of the funds for that purpose is allowed. If the timing of the receipt of such funds is such that it postdates the implementation of remediation efforts, remediation plans could be altered to account for these funds. In short, the hope for other funds should not serve as a deterrent for planning to address the deficit.

10. Layoffs

The last option that we are offering is actual layoffs of filled positions. As discussed above, eliminating a filled position in 2020 will have little to no impact on the deficit. Civil Service and Union Contracts are very specific on executing job retrenchments. The county is required to compensate a departing employee for all vacation and compensatory time previously accumulated. In addition, because the county is self-insured for unemployment, the county is responsible for the laid-off employee's normal unemployment benefits. The positive fiscal impact would not be realized until the 2021 budget. As such, layoffs would be minimally effective, if at all, in addressing the deficit that exists in the 2020 budget.

Conclusion

As stated in section 2511 of the Erie County Charter:

"If at any time during the fiscal year it appears, from cash flow projections or other generally accepted accounting principles, that the revenues available, as projected through the end of the fiscal year, will be insufficient to meet either (a) the amounts appropriated, or (b) expenses anticipated to be incurred through the end of the fiscal year, such that the cumulative effect thereof is a projected year-end deficit in excess of fifty percent of the County's undesignated, unreserved

fund balance as of the end of the immediately preceding fiscal year, the County Executive or the Comptroller shall submit a report to the Legislature setting forth the estimated amount of the deficit with appropriate details and explanations."

Based on reports from financial services providers and the New York State Association of Counties, and the assertions of the Governor, County Executive and others, and application of this information to the Erie County budget, the Comptroller declared a deficit as required by the Erie County Charter.

The failure of the County Executive to submit a remediation plan within seven days was deemed to be a plan to do nothing. This triggered the Comptroller's Charter mandate to submit comments on the County Executive's plan. This report comprises the comments to this plan.

As such, WE RECOMMEND that the Legislature consider this information, as well as other information, to address the deficit declared on May 4, 2020. The Legislature now has 21 days to act on the County Executive's plan and Comptroller's comments thereto. The Legislature can choose to adopt the County Executive's plan in its entirety, or utilize the tools provided in these comments, or make other adjustments as they deem appropriate, or implement the 10 recommended deficit reduction options throughout the year, or do nothing. You can also explore the possibility of the Erie County Fiscal Stability Authority, commonly referred to as the Control Board, entering into a so-called "hard status" once the budget and deficit reduction process is complete.

This office also strongly recommends collaboration amongst elected officials, employees and unions to work together on cost cutting measures to reduce spending, which in turn will reduce the deficit.

We can work together to establish efficiencies and ideas to run a leaner government. With the exception of tax increases, all ideas are on the table. All partners within Erie County government can work collaboratively to survive the crisis and thrive when it subsides.