ULSTER COUNTY
COMPTROLLER'S OFFICE

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Budgeting Revenues and Expenditures

4th Quarter 2016

The mission of the Ulster County Comptroller's Office is to serve as an independent agency of the people and to protect the public interest by monitoring County government and to assess and report on the degree to which its operation is economical, efficient and its financial condition sound.

Comptroller's Quarterly Report: Budgeting Revenues and Expenditures

Notwithstanding the regularity of such reports throughout the year, it is our Office's practice to produce Quarterly Reports highlighting particular financial issues on timely topics impacting taxpayers. Our 2016 3rd Quarter Report focused on fund balance and the resulting consequences of extensively utilizing it within the budgeting process. This report specifically focuses on revenues and expenditures in relation to budgeting.[1]

The goals of this report are as follows:

- to define a structurally balanced budget and explain why striving toward one is essential for County operations;
- to compare the actual revenues and expenditures of Ulster County to its budgeted amounts in order to evaluate the accuracy of County budgets; and
- to evaluate the largest revenue streams and expenditures of interest to the County for consistency, comparing actual amounts to what has been budgeted.

A Structurally Balanced Budget and Budgeting Revenues

Budgets are required to balance revenues and fund balance utilization with expenditures to ensure that a governmental entity will have the ability to deliver necessary services through the use of available resources. For a budget to be *structurally balanced*, recurring expenditures must be supported by recurring revenues – not by fund balance.

Structurally Balanced Model:

Recurring Revenues = Recurring Expenditures

Examples of recurring revenues include: property taxes, sales taxes, state aid, and other taxes and fees. While recurring revenue totals are subject to some variability, they are generally collected with regularity and continue year after year. It is essential for the County to implement a budget process that works toward a **true structural balance** in order to ensure equilibrium is reached between revenues and expenditures. These recurring revenues should be used to fund regular expenditures, such as salaries, benefits, and other routine expenses that are expected – as opposed to one-time revenues, such as the sale of property or receipt of monetary compensation as part of a lawsuit, which usually add to fund balance that should be reserved for capital expenditures.

Ulster County Budget Model:

Recurring Revenues + Fund Balance Appropriated = Recurring Expenditures

Under the current model, Ulster's budget includes an overreliance on the County's savings each year to support its expenditures. If the current model proceeds as is without any real effort to achieve a structurally balanced budget and the County relies on fund balance to bridge this gap then fund balance will run out, leaving future Administrations with few options to avoid fiscal deficits.

[1] The data presented herein relies upon the accuracy of Ulster County and national data available at the time of its preparation. This report is intended to inform taxpayers and local officials of general trends and Ulster's positioning in the midst of those trends. Future reports will continue to identify fiscal and performance issues relevant to the effective operation of government, with a constant goal of encouraging educated public discourse and decision making by voters and policy makers in Ulster County.

In order for Ulster County to reach a structural balance, revenues and expenditures should be analyzed first in order to see where there are potentially missed revenue streams, as well as areas of expenditures that could be streamlined. Once this analysis is completed, the discussion of the reasonableness of real property tax levy should occur. The 2017 budget was enacted with expenditures exceeding revenues by $93.2 million prior to the real property tax levy. As a result, $16.3 million of fund balance was appropriated in addition to the real property tax levy that represented the remaining $76.9 million.

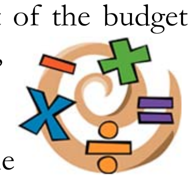
If the 2017 budget was structurally balanced (i.e. absent the use of fund balance) then an increase in the real property tax levy of about 21.2% would be required, assuming that budgeted expenditure and budgeted revenue levels were maintained as they are now.

For instance, let's compare the aforementioned practice to a regular household's yearly budget, keeping in mind that the household's income should cover or exceed its normal expenses. Picture

this example of a family household's 2016 financial plan: annual expenses totaling $100,000, a planned income of $95,000, and $13,400 in available savings (or 13.4% of budgeted expenses). In this scenario, expenditures would exceed revenues by $5,000. The easiest, but not necessarily the most prudent, route for them is to simply budget $5,000 from their savings in order to cover their extra costs. However, what about future budgets or larger deficits that could not be easily remedied through tapping into savings? Their savings has been lowered, and if they continue to overly rely on these funds and not modify their budget then they will soon exhaust themselves of extra monies to cover this gap. Over the course of time, the utilization of these "rainy day funds" becomes an unsustainable practice.

Revenue Analysis[2]

Revenue analysis provides valuable insight into projecting future earnings as part of the budget process. Some key factors to consider when evaluating revenues include growth, liquidity, stability, diversity, and the overall efficacy of administration. These aspects outline how well a government maintains its financial standing by using available funds, increasing its operating capacity, adjusting to changes in the economic landscape that affect revenues and expenditures, supporting the constituency it governs, and holding to a manageable budget.



Consistent and material variances over a period of time indicate a fundamental flaw in budgeting techniques. By analyzing changes in the actual revenue structure, we should be able to determine if variances are common and whether the revenue sources have shifted from one sector to another. Once it is determined that the revenue structure is consistent, the budgeting process becomes simplified as minimal differences from year to year should make budgeting revenues fairly straightforward.

[2] Actual revenues include governmental funds listed in each year's CAFR, excluding Capital Projects, UTASC, UCEDA, and "Other Financing Sources (Uses)" as these funds/items are not budgeted. Budgeted revenues include all governmental funds listed in each year's budget, plus property tax revenues which were allocated to non-governmental funds prior to 2014, less fund balance amounts appropriated.

Table 1: Actual Revenues by Source, with a Comparison to Budgeted Revenues (Governmental Funds)

Revenue Source	2011	2012	2013	2014	2015
Property Tax	$ 78,848,343	$ 84,757,051	$ 82,016,732	$ 82,658,744	$ 82,712,045
User Fees and Charges	2,779,509	2,881,007	3,389,574	3,451,270	3,845,275
Departmental Income	17,685,371	17,169,138	14,738,028	10,749,619	9,196,246
Sales Tax	100,922,906	103,582,388	102,010,008	104,667,661	107,996,028
Intergovernmental	4,744,119	8,294,111	5,784,772	4,280,472	2,569,831
Interfund	12,569,586	14,465,749	15,018,861	8,399,911	6,680,582
Federal & State Aid	78,203,524	85,450,235	75,927,191	77,727,994	79,683,120
Miscellaneous	2,668,508	3,310,902	14,056,352	2,899,975	2,421,617
Total Actual Revenues	$ 298,421,866	$ 319,910,581	$ 312,941,518	$ 294,835,646	$ 295,104,744
Total Budgeted Revenues	305,587,357	316,771,389	314,527,641	305,907,871	305,444,259
Revenue (Shortfalls) or Surpluses	**$ (7,165,491)**	**$ 3,139,192**	**$ (1,586,123)**	**$ (11,072,225)**	**$ (10,339,515)**

In 2012, the County surplus can be attributed to a favorable variance in sales tax of $3.9 million along with a favorable variance in the amount of federal and state aid of $6.2 million, combined with other unfavorable and favorable variances.

Table 1 shows the breakdown of significant revenue sources over the five-year span from 2011-15. The largest three sources have remained fairly consistent. There is some consistency in actual revenues from 2014 to 2015, yet 2015 had a revenue shortfall over $10.3 million due to repeat over budgeting. The 2016 Budget called for $304.6 million in revenues for governmental funds; it will be worth paying attention to whether revenues underperformed for the fourth straight year once financial statements become available.

Largest Revenue Streams in Governmental Funds:

Table 1 shows that the three largest revenue streams of the County have consistently and primarily been attributed to Sales Tax, Property Tax, and Federal & State Aid. These revenue streams have the largest impact on County revenue stability; since 2014, the combination represents over 85% of the actual operating revenues. The relative stability of these revenue streams should result in accurate budgeting for a large portion of revenues. The following chart analyzes these revenue streams compared to their budgeted amounts.

1. Sales Tax

Sales tax	2011	2012	2013	2014	2015
Actual	$ 100,922,906	$ 103,582,388	$ 102,010,008	$ 104,667,661	$ 107,996,028
Budgeted	97,713,384	99,667,652	105,428,186	104,059,402	108,002,757
Over (Under) budget	$ 3,209,522	$ 3,914,736	$ (3,418,178)	$ 608,259	$ (6,729)

Sales taxes are comprised of general sales and compensation use tax, which is imposed on all taxable retail sales within the County. The Ulster County sales tax rate is currently 8%, 4% of which goes directly to New York State and the remainder returns back to the County (a portion of which is disbursed to its municipalities based on a distribution agreement). The base tax rate is 3%; however, the County traditionally receives State authorization to levy an additional 1%. The amounts listed above represent the entire 4% levied by the County; however, the sales tax rate for December 2013 and January 2014 was 3%. The budgeting of sales tax revenue does not incorporate the distribution agreement among the County, City of Kingston, and the County's Towns and Villages, as the County is required to account for all sales tax received as revenue and then account for the disbursement as expenses, which will be discussed in the expenditure analysis.

Actual sales tax has shown moderate growth over time, and sales tax revenue has increased each year since 2013. The 2016 budgeted sales tax grew by $1.96 million from the previous year. The County's budget analysts projected the actual revenues for 2016 to surpass the budgeted amount by only approximately $500,000, reaffirming the accuracy of the County's initial projections. This area has been budgeted accurately since 2014, as there was a less than 1% variance for both 2014 and 2015, and a projected variance of less than 1% for 2016, as actual revenues follow fairly predictable trends.

2. Property Tax

Property tax, unlike sales tax, is predominantly determined at the local level and is the revenue that County management has the most discretion over to balance its budget. Each year, the County sets the tax levy for its residents; however, with the imposition of the state's property tax cap, the ability of the County to increase its tax levy at-will has been greatly diminished. **Therefore, it may not be in the County's best interest to decrease property taxes until such time that it nears a structurally balanced budget**. Reducing property taxes instead of closing the gap on recurring revenues and recurring expenditures postpones the County's ability to obtain a truly balanced budget. From 2014 to 2017, the budgeted property tax levy decreased $1.84 million, while the County only reduced its budgeted fund balance usage by $365,000.

Property tax	2011	2012	2013	2014	2015
Actual	$ 78,848,343	$ 84,757,051	$ 82,016,732	$ 82,658,744	$ 82,712,045
Budgeted	80,464,960	82,730,389	83,524,708	83,280,408	82,678,104
Over (Under) budget	$ (1,616,617)	$ 2,026,662	$ (1,507,976)	$ (621,664)	$ 33,941

The difference between budgeted and actual property tax revenues generally occurs due to uncollected taxes and because government accounting principles state that property taxes may not be accounted for as revenue unless they are collected within the fiscal year or sixty days thereafter. The chart includes other real property tax items (i.e. gains on tax acquired property, payments in lieu of taxes, and interest and penalties) that can vary from year to year. The chart shows the County has experienced little variances between actual and budgeted since 2014.

3. Federal & State Aid

Federal & State Aid	2011	2012	2013	2014	2015
Actual	$ 78,203,524	$ 85,450,235	$ 75,927,191	$ 77,727,994	$ 79,683,120
Budgeted	81,888,858	79,219,704	79,257,737	81,744,716	84,964,534
Over (Under) budget	$ (3,685,334)	$ 6,230,531	$ (3,330,546)	$ (4,016,722)	$ (5,281,414)

A significant portion of the County's revenue comes from the Federal and State government through numerous aid programs. Each program has a specific purpose, unique operations and activities, as well as different eligibility, application, and compliance requirements that must be followed in order to receive and retain funding. The amount of funding can vary from year to year depending on several things, including federal and state budget cuts and what program revenues are ultimately passed through to the County, making this a difficult revenue area to budget.

Since 2013, there have been annual shortfalls in Federal and State aid – the average shortfall being approximately $4.2 million of the budgeted amount. If this trend continues, budget officials should evaluate this area and adapt to become more accurate in the budgeting of these revenues. The destination for the majority of these monies within the County is programs run through the Ulster County Department of Social Services ("DSS"). About $56.26 million in Federal and State aid revenue was budgeted through DSS in 2015, while the actual amount received was about $2.5 million less (at $53.74 million). The remaining differences in Federal and State aid are comprised of revenues budgeted to other departments.

Revenue Recap

While the top three revenues are budgeted relatively accurately, the remaining revenues, as a whole, are not being budgeted with a similar level of certainty. In 2015, total actual revenue in governmental funds was $295.1 million while the total budgeted revenue was $305.4 million.

Moreover, the combined actual revenues for the top three revenue streams were $270.4 million (accounting for nearly 92% of total actual revenue) while the combined budgeted revenues were $275.6 million – a shortfall in revenue of only 1.91%, which equates to $5.25 million. The remaining $24.7 million in actual revenue (representing about 8% of the total actual revenue) was budgeted at $29.8 million – a shortfall in revenue of **17.02%**, which equates to $5.09 million.

Expenditure Analysis[3]

Analyzing trends in expenditures assists in the budget process by helping to identify another area where variances may lie. The consistency of the expenditure profile can be utilized to assist budgetary planning because this information should be utilized to prevent major variances in budgeted to actual expenditures. The historical expenditure structure indicates those expenditures that are declining, remaining consistent, or growing in each area as seen in Table 2.

Table 2: Actual Expenditures by Source, with Comparison to Budgeted Expenditures (Governmental Funds)

Expenditures	2011	2012	2013	2014	2015
General Government	$ 49,108,657	$ 50,968,979	$ 46,668,790	$ 47,392,213	$ 48,325,190
Public Safety	27,420,300	27,712,159	29,127,814	30,859,624	30,792,159
Public Health	19,923,701	18,217,111	14,744,280	14,430,587	14,852,089
Transportation	22,358,390	22,499,919	21,656,690	22,600,448	24,079,460
Economic Assistance	109,343,898	119,435,033	125,254,103	115,174,274	112,227,827
Employee Benefits	40,102,026	45,749,685	49,251,747	47,572,681	46,222,967
Other	25,690,218	27,629,783	22,483,655	23,205,661	21,874,989
Total Actual Expenditures	$ 293,947,190	$ 312,212,669	$ 309,187,079	$ 301,235,488	$ 298,374,681
Total Budgeted Expenditures	313,699,265	322,712,356	318,163,073	322,617,871	324,909,659
Expenditures (Under Budget)	$ (19,752,075)	$ (10,499,687)	$ (8,975,994)	$ (21,382,383)	$ (26,534,978)

[3] Actual expenditures include governmental funds listed in each year's CAFR, excluding Capital Projects, UTASC, UCEDA, and "Other Financing Sources (Uses)" as these funds/items are not budgeted. The 2014 and 2015 AUD, along with the County financial system, was utilized in extracting salary and employee benefit information from other cost centers. Budgeted expenditures include all governmental funds listed in each year's budget.

The County's excessive budgeting of expenditures over the past five years in the Governmental Funds can be noted from Table 2. **The County over budgeted governmental expenditures an average of $17.43 million each year from 2011 to 2015 (for a combined total of $87.14 million). In 2015, governmental expenditures were over budgeted by $26.5 million.**

The categorical differences between budgeted and actual for 2015 are shown below:

2015 Governmental Expenditures				
	Actual	**Budget**	**Difference**	**%**
General Government	48,325,190	57,525,178	(9,199,988)	-15.99%
Education	9,485,726	10,053,546	(567,820)	-5.65%
Public Safety	30,792,159	32,418,181	(1,626,022)	-5.02%
Public Health	14,852,089	15,455,553	(603,464)	-3.90%
Transportation	24,079,460	26,337,718	(2,258,258)	-8.57%
Economic Assistance	112,227,827	123,258,713	(11,030,886)	-8.95%
Culture & Recreation	825,409	777,589	47,820	6.15%
Home & Community	2,489,153	2,679,777	(190,624)	-7.11%
Employee Benefits	46,222,967	45,002,137	1,220,830	2.71%
Debt Service	9,074,701	9,383,964	(309,263)	-3.30%
Transfers	-	2,017,303	(2,017,303)	-100.00%
Total Expenditures	**298,374,681**	**324,909,659**	**(26,534,978)**	**-8.17%**

The majority of the budget differential is found within the General Government, Transportation, Economic Assistance, and Transfers categories:

- General Government support consists of services provided by the County for the benefit of the public or the County as a whole. In 2015, this area was over budgeted by $9.2 million, which is a 16% gap from the budgeted amount.

- Transportation expenditures represent services provided for the safe and adequate flow of vehicles and pedestrians. This area was over budgeted by $2.3 million in 2015, which was an 8.6% difference from the budgeted amount.

- Economic Assistance provides for the development and improvement of the welfare of the community and individual. In 2015, this category had the largest dollar difference ($11.0 million) in actual expenditures compared to the budgeted amount. There was 8.9% less in actual expenditures as compared to the budgeted amount.

- The Transfers category budgeted interfund activity, which the Road Machinery Fund transferred to the County Road Fund. This area saw the largest percentage over budget due to a budgeted expenditure (transfer) of $2.0 million with no transfers actually being made.

Expenditures of Interest

The following will discuss some of the more interesting areas of County expenditures, such as Salaries, Employee Benefits, as well as Sales Tax Distribution.

1. Salaries

Salaries represent approximately 25% of the County's actual expenditures and are allocated throughout the cost centers mentioned in Table 2. Slight increases in salary costs are expected as the pay for most positions are included in contract agreements. It is the historical budget practice of the County to budget salaries as if every vacant position will be filled at the beginning of the year and every County position will remain filled for the entire year. This practice creates a trend of over budgeting within salaries every year, creating a budget cushion of about $2 million in a given year. The following chart represents the budgeted amounts for salaries compared to the actual amounts reported for governmental funds.

Salaries	Actual	Budgeted	Difference
2014	$ 74,620,259	$ 76,576,973	$ (1,956,714)
2015	$ 76,420,564	$ 78,976,492	$ (2,555,928)

The average difference in actual salaries and budgeted salaries for 2014 and 2015 reaffirms the over budgeting of salary lines. This practice continues in 2016, as salaries were projected to be over budgeted by $3.94 million by the County budget analysts. The 2017 Budget funds $2.58 million worth of currently vacant positions (i.e. at the time of budget preparation). The County should refine this practice by determining which unfilled vacancies have remained unfilled for a certain length of time, decide if those positions are essential, and defund the non-essential positions rather than continuing to budget for positions that have remained unfilled.

2. Employee Benefits

Employee benefits account for approximately 15.5% of the actual expenditures and are mainly comprised of State retirement, social security, unemployment insurance, disability insurance, and hospital and medical insurance. Health insurance costs are unpredictable; Social Security and Medicare are directly correlated with salaries; and State retirement contributions are subject to fluctuation based on an established state retirement contribution percentage, which was recently reduced. Table 3 displays the major fringe benefit categories and their actual costs over a two year period.

Table 3: Employee Benefits Over a 2-Year Period

Expenditure Category	2014	2015
State Retirement	$ 14,721,617	$ 13,709,822
Social Security	5,593,659	5,691,398
Unemployment Insurance	191,961	57,398
Disability Insurance	99,800	103,495
Hospital and Medical Insurance	22,923,622	22,530,241
Other Employee Benefits	4,042,022	4,130,613
Total Employee Benefits	**$ 47,572,681**	**$ 46,222,967**

Employee benefits as a percentage of salaries decreased from 2014 to 2015 by over 3.25% due to the reduction in the state retirement contribution percentage, as well as a reduction in the cost of hospital and medical insurance in relation to salaries. From 2014 to 2015, salaries increased $1.8 million while hospital and medical insurance decreased.

3. **Sales Tax Distributions**

As mentioned in the revenue section, the County collects sales tax and distributes a portion to the City of Kingston, Towns, and Villages within the County. The expenditure for the distribution of sales tax is included in the General Government category. The sales tax agreement in place during 2014 and 2015 required a distribution to the City of 11.5% of the revenue and the remaining 3% to be split among the Towns and Villages based on their equalized value. The following chart shows a comparison of the budget to actual amount of sales tax distributed for the respective years:

Sales tax distribution	2014	2015
Actual	$ 15,176,161	$ 15,658,313
Budgeted	15,088,613	15,660,400
Over (Under) budget	$ 87,548	$ (2,087)

The budgeting of the sales tax distributions calculates to 14.5% of the budgeted sales tax revenues, as it should, and the budgeted amounts are close to the actual amounts disbursed for both years. The budgeting of sales tax distributions may become more difficult in the future years as the sales tax agreement among the County, City of Kingston, and Towns and Villages was recently modified to include provisions, shared services, and caps that were not previously in place.

Conclusion

Ulster County should strive to pass a structurally balanced budget, and the Executive and Legislature should analyze the structural balance of the budget prior to allowing reductions in tax levies in order to determine whether revenue sources are at a sustainable amount. A multi-year budget should be considered to demonstrate how the County plans to strive toward a truly balanced budget in future years. This practice would afford the County Legislature an extended view of the projected fund balance over time, while also providing an outlook on how the County intends to retain its fiscal strength and create safeguards from significant tax increases.

The generous appropriation of fund balance in the County's budget process – as opposed to budgeting revenues and expenditures more accurately and increasing the contingency fund – reduces the power of the Legislature to monitor the budget. The budget is constructed to assume that expenditures will be at a maximum, and because the expenditures are over budgeted at the onset, the Legislature would only need to approve situations in which there is an extreme variance. Budgeting a greater portion in contingency, which normally requires legislative action for use, may inspire greater efficiency and would increase Legislative involvement.