COUNTY OF ERIE, NEW YORK
OFFICE OF THE COMPTROLLER

COMPTROLLER'S REVIEW OF THE COUNTY EXECUTIVE'S PROPOSED 2007 BUDGET AND FOUR YEAR FINANCIAL PLAN

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EXECUTIVE SUMMARY

Erie County's Charter requires the county executive to present his proposed budget for the following fiscal year by October 15 of the preceding year. This year October 15 fell on a Sunday. As a result, County Executive Joel A. Giambra proposed presenting his proposed fiscal year 2007 budget ("FY 07 Proposed Budget") on Monday, October 16, 2006. However, due to the "October Surprise Storm," the county executive did not present the FY 07 Proposed Budget to the legislature until October 18, 2006. The budget was also presented to the Erie County Fiscal Stability Authority ("ECFSA") on October 18 with the new Four Year Financial Plan for the fiscal years of 2007 – 2010 ("Four Year Plan"), as is required by the ECFSA's enabling act.

The Erie County Comptroller's Office has reviewed the FY 07 Proposed Budget and the revised Four Year Plan. This report is not a line-by-line review of the proposed budget, but instead highlights material revenue and expense items, and areas of potential significant risk.

In general, the revenue estimates contained in the FY 07 Proposed Budget for the largest source of county revenue, sales tax, is based on future actions that must take place. For example, the FY 07 Proposed Budget and Four Year Plan assume the extension of the 0.75% sales tax beyond its expiration date of November 30, 2007. As proceeds from the sales tax make up the majority of the county's local share revenue, it is imperative that the 0.75% portion of the sales tax be renewed in order for the FY 07 Proposed Budget to be balanced. Additionally, this tax must not only be renewed for 2007, but it must be renewed for the out years. The existing 1.0% local sales tax must also be renewed beyond February 2008 in order for the Four Year Plan to be balanced. On November 2, 2006, the County Legislature memorialized its intention to request the extension of the 0.75% sales tax through November 30, 2009, the maximum extension permitted under state law at one time. Based on the latest sales tax receipts received from the State, the FY 07 estimated growth rate for sales tax appears to be strong. While it is impossible to determine the actual base sales tax for 2006 until February 2007, this item continues to require constant monitoring and if the estimated growth is not attainable corrective measures may be necessary.

While the property tax rate is not increasing, revenue growth from property taxes is increasing due to increased reassessments at the city and town levels, thereby resulting in a projected increase in the total tax levy of approximately $8.7 million dollars for 2007. This revenue estimate appears to be in line with assessment growth. In addition it appears that the Administration is continuing the practice of selling the current year tax liens for 2007 and the out years of the Four Year Plan. This Office is reviewing Government Accounting Standards Board ("GASB") Statement #48, "Statement to Clarify Guidance on Accounting for Sales and Pledges of Receivables and Future Revenues," concerning how this will effect accounting for this transaction. There is the potential of a $6-$8 million negative impact on the 2007 Budget and a lesser impact on the out years of the Four Year Plan, if it is determined that GASB #48 will require a different accounting treatment then what has been done in the past (and which would result in the County's annual tax lien sale being discontinued).

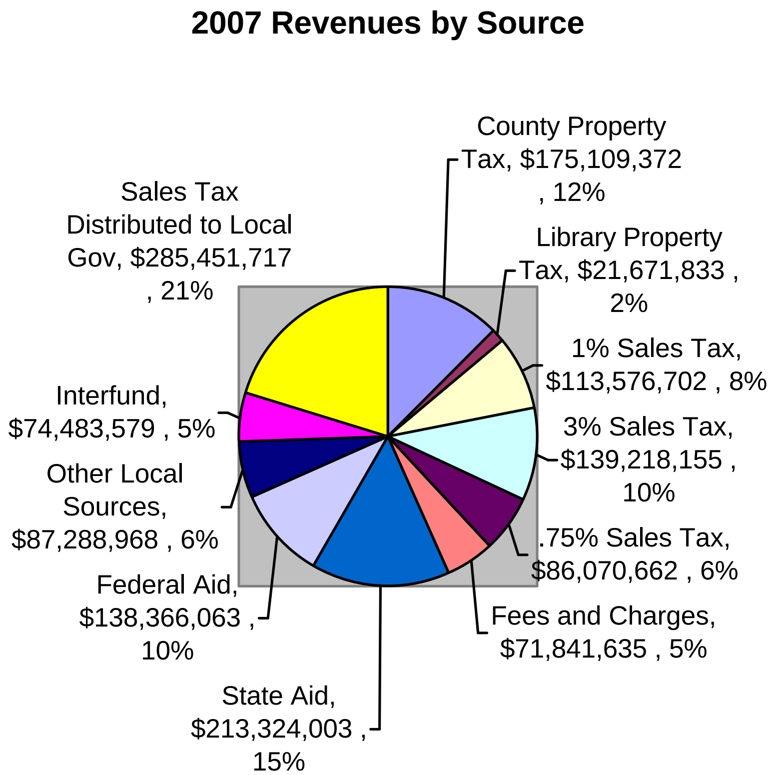
Some of the estimates projected for other smaller revenue lines are questionable in nature. For example, revenues derived from environmental health fees, market based revenue programs, parks parking fees, and youth detention fees are significantly greater than the 2006 projected results, or are based on actions that require legislative approval that has not been forthcoming in the past (i.e. approval of county parks parking fees).

In regard to expenditures, certain risks exist. For example, Erie County may be faced with an additional multi-million dollar expenditure for the Erie County Medical Center Corporation ("ECMCC") that is not provided for in the FY 07 Proposed Budget. Presently, the county is negotiating with ECMCC for $5.7 million dollars in lost reimbursement due to inter-governmental transfer payments related to Medicaid. Though the dollar amount is unknown at this time, such a multi-million dollar transfer is possible in 2007 and beyond. The county is pursuing its options at this time, including possible litigation against ECMCC.

Keeping in mind our above concerns on certain revenue estimates, the FY 07 Proposed Budget is balanced, but there is little margin for error. If the County Legislature and/or State Legislature fail to reauthorize the 0.75% sales and compensating use tax during 2007, the County will lose significant revenue for the final month of 2007. Depending on the final determination under GASB #48, the County could experience a loss of $6-$8 million in revenue in 2007. If certain other revenues in the Four Year Plan do not materialize in 2007 or are under budget (as we project), those gaps will need to be closed. If certain expenditures exceed appropriations (such as claims against the Risk Retention Fund, community college chargebacks, or employee overtime), those gaps will need to be closed. If certain revenue projections are not met and/or certain expenditures exceed projections, mid-year budget adjustments may be necessary.

On November 3, 2006, the ECFSA initiated a control period based on their analysis of imbalances in the out-years of the four-year plan. Without commenting on the legality of that action, we must point out that any future projections done by any County government in this state made under the premise of not increasing taxes and assuming inflationary growth in expenses and growth in state mandated expenses will result in multi-million dollar gaps. The projection merely provides a best guess of what will happen under certain assumptions and serves as another reason for management to determine the most cost effective way to deliver services to our taxpayers.

PROPOSED 2007 REVENUES



Property Tax

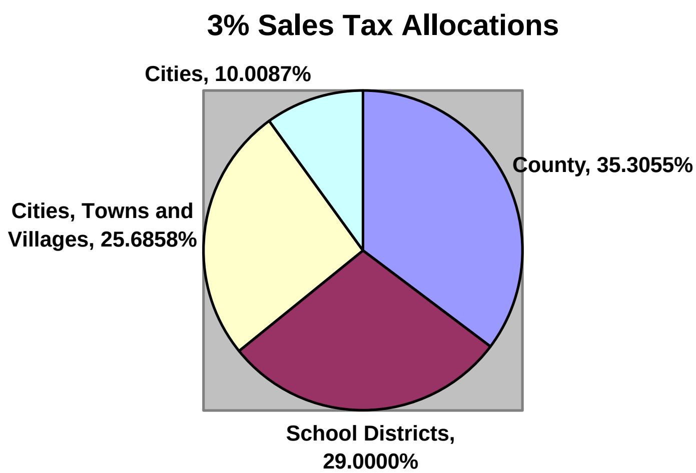
There is no increase in the countywide property tax rate in the FY 07 Proposed Budget. The property tax rate per $1,000 of equalized taxable full value is $4.86, down from $4.94 in 2006. Though the tax rate has not been raised, due to reassessments in some towns, the total property tax levy will increase from $188.1 million (adjusted) in 2006 to $196.8 million in 2007. That is a 4.65% increase from 2006. The general government property tax levy for 2007 is $175,109,372, up from $166,422,612 in 2006. The library tax remains the same for 2007 at $21,671,833. Our office believes that these estimates are accurate based on assessments and to balance the 2007 budget.

We note that the FY 07 Proposed Budget does not fund the net increase in deferred revenue nor the allowance for uncollected taxes accounts. In 2005 approximately $6.6 million was expensed to those accounts along with the recognition of $6 million in interest and penalties revenue. The 2007 budget has $3.9 million budgeted for interest and penalties-property tax revenue. This account requires careful monitoring.

Sales Tax

A sales and compensating use tax of 8.75% is levied on applicable items in Erie County. Of that total, 4% is levied and allocated to the State, and 4.75% is the County share. Of the

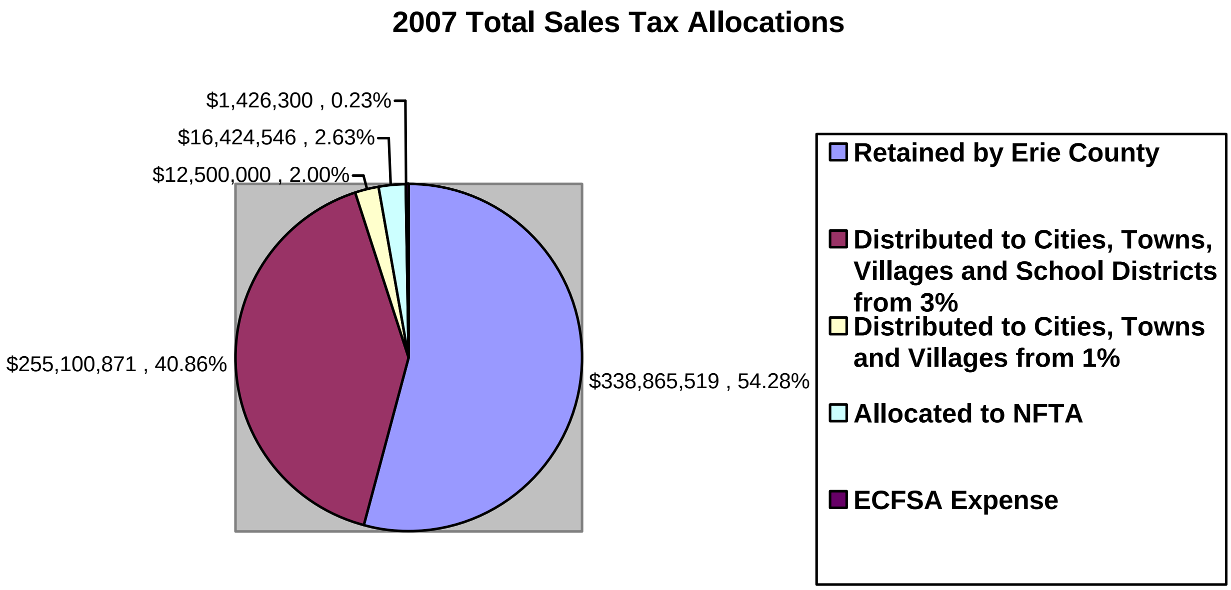
4.75%, 3% is allocated as revenue between the County, cities, towns, villages and school districts in Erie County according to the sales tax sharing agreement. The 3% allocation formula is as follows:



The County retains 35.3055% of the total revenue derived from the 3% sales tax. 10.0087% is allocated to the Cities of Buffalo, Lackawanna and Tonawanda on the basis of population. 25.6858% is divided among the Cities of Buffalo, Lackawanna, Tonawanda and the towns on the basis of population. The amount belonging to the towns is divided on an alternating basis of full value and population. Full value is used to distribute the receipts for the quarters beginning January 1 and July 1, and population is used for the quarters beginning October 1 and April 1. Villages receive a portion of the town amount based on the ratios that the full valuation of real property in such village or portion thereof within the town and the full valuation of real property in the portion of the town outside of such village or villages, respectively bear to the aggregate full valuation of the entire town. 29.0000% is divided among all the school districts with territory in the County on the basis of the average daily attendance of public school pupils who are residents of the County.

Since 1985, the County has maintained an additional 1% sales and compensating use tax exclusively for County purposes, with all revenue retained by the County. That additional 1% sales tax was established in response to a 1984 Erie County budget crisis and deficit. The authorization for the County to levy the 1% sales tax has traditionally expired at the end of February of each year. Since 1985, upon a request of the county executive, the Erie County Legislature has annually requested the approval of enabling legislation by the New York State Legislature, and subsequent to the passage of the enabling legislation, the Erie County Legislature has acted to extend the 1% County sales tax. In 2006, the New York State Legislature reauthorized the 1% sales tax for a two-year period, expiring on February 29, 2008.

In June 2005, due to the County's budget crisis, and pursuant to Home Rule Requests of the Erie County Legislature and the approval of enabling legislation by the New York State Legislature, an additional 0.25% sales tax was instituted for County purposes. In November 2005, the Erie County Legislature approved a further additional 0.5% sales tax for County purposes, with that 0.5% sales tax commencing on January 15, 2006. The 0.75% sales tax revenue is retained exclusively for the County. Absent future reauthorization, the total 0.75% sales tax expires on November 30, 2007. The FY 07 Proposed Budget (and Four Year Plan) assumes the Erie County Legislature and State Legislature will approval the renewal of the 0.75% sales tax beyond November 30, 2007. On November 2, 2006 the County Legislature memorialized its intention to renew the 0.75% sales tax through November 30, 2009.



Total revenue generated by the sales tax in the FY 07 Proposed Budget is $624,317,236. The 2007 budget presents sales tax in a very confusing manner. This is due in part to an accounting change required by the Office of New York State Comptroller concerning sales tax sharing. While it is correct in treating the amount that is being shared with the various municipalities and school districts under the sales tax sharing agreement of 1977 ($255,100,871), as the "expense" side of this transaction, that has never been budgeted previously. It is this Office's opinion that should have been the only change to the revenue presentation. The budgeting of $30,350,846 as additional sales tax distributed to other jurisdictions is misleading. This includes payments to the Niagara Frontier Transportation Authority (which began in 1991), payments to the Erie County Fiscal Stability Authority (which began in 2005) and the $12,500,000 distribution to various municipalities due to the State legislation enabling the County to continue the additional 1% sales tax (which will start January 1, 2007).

Eliminating the $255,100,871 leaves a total of $369,216,365 in sales tax budgeted for County purposes. Comparing this to the 2006 budgeted amount of $355,254,231 results in an approximate growth of 3.8% from budget to budget. While the additional 0.5% sales tax did not take effect until January 15, 2006 it was budgeted for a full year. The last ten years have averaged 2.9% annual growth while the last five years has averaged 2.24% growth.

In addition based on the year-to-date cash distributed to the County by the State through the month of October 2006, the County is experiencing a growth rate of 1.46% in 2006, comparing regular and additional 1% sales tax only. It is impossible to determine what the final numbers will be for 2006 as final cash distributions for 2006 will not be received until February 2007. Because the rate of growth is a projection, it will have to be monitored as the year progresses.

The revised Four Year Plan states that sales tax is predicated on a 2.5% annual growth every year based on a 2006 base sales tax of $358,941,851. This base number as mentioned above appears to be a strong estimate based on the year-to-date receipts and will have to be monitored.

Absent reauthorization, the 0.75% sales and compensating use tax expires on November 30, 2007 and the 1% sales tax expires on February 29, 2008. The FY 07 Proposed Budget assumes a request by the Erie County Legislature and passage by the New York State Legislature of enabling legislation to extend the .75% sales tax beyond November 2007.

On November 2, 2006, the Erie County Legislature, in a 10-5 vote (the minimum vote necessary to pass such action) approved a resolution expressing their support for extending the 0.75% sales and compensating use tax beyond November 30, 2007, to November 30, 2009. The process for formalizing this extension cannot start until January 2007 when the new State Legislature session begins, at which point the County can start the formal legal process for extending the sales tax in conjunction with the State.

Should the County Legislature fail during 2007 to send a Home Rule request to the State Legislature or affirmatively approve of the continued imposition of the .75% sales tax, the County will face significant negative financial consequences, both from the loss of revenue for the last month of the year, as well as from a significant loss of revenue in 2008 and other out years in the Four Year Plan. The failure to continue the 0.75% sales tax will result in a multi-million dollar shortfall in taxes received in 2007. It also could cause adverse reactions amongst the County's rating agencies and the County's bondholders.

Pursuant to the state legislation in February 2006 reauthorizing the County's 1% sales tax, during 2007, the County is required to share $12,500,000 of the 1% sales tax with the cities, towns and villages in Erie County. That money will be allocated to the County's three cities, 25 towns and 16 villages according to the formula that allocates the County's 3% sales tax. The exact amounts to be allocated to each these local governments in 2007 will be calculated in early 2007.

Other Revenues

Interest Earnings:

Due to aggressive cash management, higher interest rates, and more cash available for investment, the County expects to receive higher interest earnings in 2007 than prior years. The FY 07 Proposed Budget proposes General Fund interest earnings revenue of $4,890,000, almost $2.5 million more that the 2006 budgeted amount of $2,500,000, and more than the actual 2006 earnings which are projected to be approximately $4,500,000. We note that our estimate to the

Division of Budget, Management and Finance was $4,500,000, and the administration increased the estimate.

The County has benefited from the Federal Reserve policy of increasing interest rates. The last three Federal Reserve meetings have not resulted in an interest rate hike. The estimated earnings are based on current interest rates remaining stable. Under current market conditions we believe the projected revenue derived from interest income is achievable.

County Clerk Fees:

The County Clerk Registrar Division has a new Clerk Fees revenue line totaling $750,000 in the FY 07 Proposed Budget. This revenue has heretofore not existed. To effectuate this new revenue, the County Legislature will be asked to approve Home Rule requests to the State Legislature for permission to levy said fees for an April 1, 2007 implementation. Given the State Legislature's rejection of similar fees in 2006, we are concerned that these fees may not be attainable in 2007 or future years.

In 2006, as per the Four Year Plan, and after legislative approval, the County Clerk Auto Bureau Division began receiving revenue from a new Motor Vehicle Use Tax levied upon drivers when they renew their motor vehicle registrations. The adopted 2006 Budget included $1,900,000 in revenue from the tax. Through September 2006 the County has recognized $2,171,658 in this account. The County Clerk requested 2007 revenue of $4,900,000, and the administration's submission and revised Four Year Plan includes $5,200,000 in 2007. We believe that this revenue estimate is very optimistic and bears careful monitoring as the year progresses.

Medicare Part D Subsidy:

We note that the revenue from the Four Year Plan initiative, Medicare Part D Subsidy, which was budgeted for $600,000 in 2006 is not included as revenue in 2007 and was not requested. This in itself is not material; however, the Four Year Plan includes the initiative and states that $1,080,000 in revenue is in the 2007 Budget, and that the program is "successfully being implemented for 2007." This discrepancy needs to be addressed either adding the initiative back into the budget (assuming it is attainable) or it should be stricken from the Four Year Plan for 2007. It is possible that this credit was included in the fringe benefit appropriation. We were not able to determine if it was or was not.

Environmental Health Fees:

The adopted 2006 Budget included increases in environmental health fees in the Department of Health, based on Health Department inspections of certain facilities, such as restaurants, food service establishments, non-profit food events, and so forth. These fees, some of which were doubled from their previous rates, were recommended and required in the Four Year Plan. During 2006, non-profit groups expressed concern that they had to pay the fees – fees for which they were previously granted waivers. As a result, the Legislature reversed the fees for such groups, granted waivers, and directed the Health Department to refund said groups their food service inspection fees. These fees, denoted as community sanitation and food revenues in the Public Health Laboratory budget, were budgeted for $607,775 in 2006, and are shown as adjusted to $1,121,909 in the proposed 2007 Budget. Our review of 2006 results shows actual 2006 fees generated $779,962 in revenue as of September 30, 2006. The proposed 2007 Budget includes $1,395,718 in revenue from these fees. Our office believes that this account will bear careful monitoring throughout the year. We also note an increase in public health lab fees from $130,000 in the adopted 2006 Budget to $800,000 in 2007. Because no revenue for this account has been recognized in 2006 we have no basis by which to verify the accuracy of this estimate.

Parks Revenues:

The Four Year Plan recommended that the County institute a parking fee at County parks. In 2005, despite a request from the county executive for said fee in the 2006 Budget, the County Legislature expressly rejected that concept and removed the fee from the adopted 2006 Budget. In the proposed FY 07 Proposed Budget, parking fees are again included with revenue of $500,000, though the Four Year Plan only shows revenue of $400,000, not $500,000 (possibly discounted due to the costs to hire staff to collect the parking fees).

After an increase in Greens Fees for the two County golf courses in the adopted 2006 Budget (a Four Year Plan recommendation), the FY 07 Proposed Budget reduces revenue from Greens Fees from $1,474,282 in 2006 to $1,200,000 in their 2007 request. We note that as of September 30, 2006, 2006 revenue from this fee totaled $1,062,305.

Forestry Management Program Revenues:

In 2006, after approval from the County Legislature, and as per the Four Year Plan, the Parks Department initiated an active Forest Management Plan, which included revenue from the sale of harvested timber from County forest lands. Budgeted 2006 revenue was $490,600. In mid-2006, this office conducted an in-depth review of the program and issued a major report raising a range of significant concerns and issues that our office has with the program – including the potential for not meeting revenue estimates in the 2006 Budget. Current 2006 year-to-date revenue from the program is $195,771 (the administration’s October 18, 2006 revised Four Year Plan says revenue is $120,000). Following our report, the County Legislature’s Energy and Environment Committee held a series of hearings concerning the program. As a result of those discussions, the Legislature halted the program and imposed a moratorium on any harvesting of trees in County forests until a full environmental review process is conducted (a process that could take 6-9 months). Despite this development, the proposed 2007 Budget includes revenue of $270,000 (which we note is even greater than the department’s own request for only $200,000 of revenue in 2007). Due to the Legislature’s recent actions, we note that there will almost certainly be no revenue from forest management in 2007 and as such, the administration’s inclusion of $270,000 of revenue in the proposed 2007 Budget should be deleted.

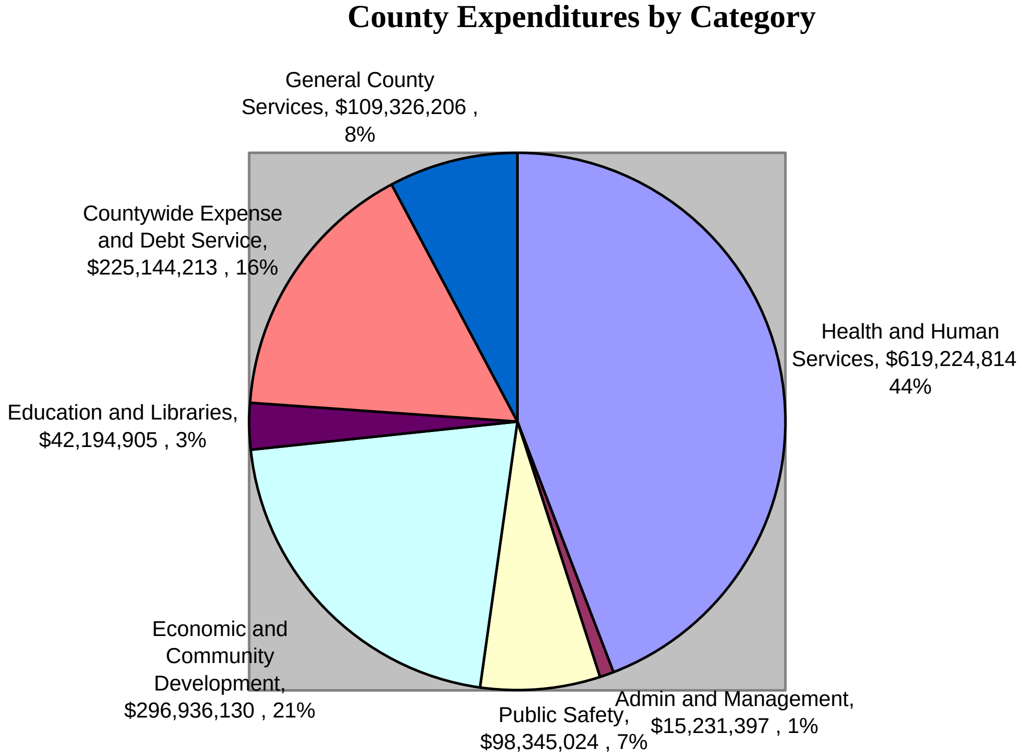
Youth Detention Revenue:

The County operates a secure Youth Detention Facility located in the City of Buffalo. The County receives revenue from other counties for detention costs. 2004 actual revenue in this account was $823,722, $1,285,503 in 2005 and $978,744 (budgeted) in 2006. Proposed 2007 revenue in this account is $1,811,400, or a near 100% increase. Significant increases in revenue in this account through increasing other counties' detainees' presence at the facility is included as a Four Year Plan initiative. We note that while the administration's October 18, 2006 revised Four Year plan shows no revenue in this line (from increased attendance) in 2006, it projects $400,000 in new revenue in 2007, conditioned on agreement from other counties. Because no agreements are yet in place with other counties, we question this revenue estimate for 2007.

Wireless Surcharge:

In 2006, in keeping with the Four Year Plan, a new $0.30 per wireless device surcharge was created. The FY 07 Proposed Budget projects $1,775,800 in revenue, though the department requested $1,675,800, increased from the adopted 2006 Budget estimate of $830,000. The 2007 estimate is based on a full twelve months of revenue, whereas the 2006 estimate was based on only six months of revenue due to delays in the State approval of the new surcharge.

PROPOSED EXPENDITURES



The FY 07 Proposed Budget is $1,406,402,689 for all funds, and the County's share is $1,151,301,818.[1] This does not include the shared 3% sales tax with cities, towns, villages and school districts. Total sales tax revenue proposed to be provided to these entities in 2007 is $255,100,871.

The adopted 2006 Budget for all funds was $1,089,559,278. As such, the proposed 2007 Budget is $61,742,540 more than the adopted 2006 Budget, or 5.7% growth over 2006.

Personal Services

For all funds, the net change in full-time positions from the adjusted 2006 Budget to the FY 07 Proposed Budget is +89. The proposed 2007 Budget of 4,352 full-time positions is 364 more than the adjusted 2005 Budget. The most noteworthy additions include: Department of Social Services (60 new positions), Central Police Services (19 new positions), Jail Management (9 new positions), Probation (5 new positions), Public Health Laboratory (5 new positions), and Mental Health (3 new positions).

[1] Unlike in past years, the Office of State Comptroller now requires county governments to record as a revenue and a corresponding expenditure all amounts received in sales and compensating use taxes regardless of whether they are shared with local governments. As such, the County's FY 07 Proposed Budget includes revenues for and equals expenditures related to all sales taxes collected and shared with local governments.

Full-time salary costs increase from $186,569,325 for all funds in the adjusted 2006 Budget to $193,039,805 in 2007 (not including Board of Elections staff). That represents a 3.3% increase. $5,025,153 of this $6,470,480 in increased full-time salary costs in 2007 comes from the Department of Social Services ($3,395,567) and the Sheriff's Office Division of Jail Management ($1,629,586).

The FY 07 Proposed Budget includes a turnover account (reductions from personal services) of $2,300,000. The 2006 Budget included no turnover account. Past budgets have included significant turnover accounts that have not met the target and helped contribute to budget deficits and financial pressure on the County. This account should be closely monitored during 2007.

Unbudgeted overtime costs, particularly in the Division of Jail Management, where annual overtime costs have routinely exceeded the annual adopted budget appropriations, remain a concern. The Sheriff requested $7,500,000 in overtime for Jail Management, and the 2007 Budget appropriates $8,600,000. We note that overtime costs in that division have routinely significantly exceeded budget and will probably do so again in 2007. We also note that the proposed budget increases Sheriff Division (i.e., road patrol) overtime appropriations from $600,000 in the adopted 2006 budget ($618,930 adjusted) to $1,200,000 in the FY 07 Proposed Budget.

Debt Service

Since 1999, the County's total net indebtedness (excluding self-financing Sewer Districts) has increased significantly – from less than $200 million in 1999 to the current level. At December 31, 2006, the County's calculation of total net indebtedness is $562,359,817, including a $101,375,000 bond guaranty for the sale of the Erie County Medical Center Corporation. This does not include Sewer Bonds or Revenue Anticipation Notes. The December 31, 2005 calculation was $460,279,076.

During the same period, net bonded debt per capita has also increased significantly, rising from $190.69 in 1999 to an estimated $604.23 in 2006 and $626.37 for 2007. This growth in debt has consequences on the County's finances, as well as county government's ability to provide services.

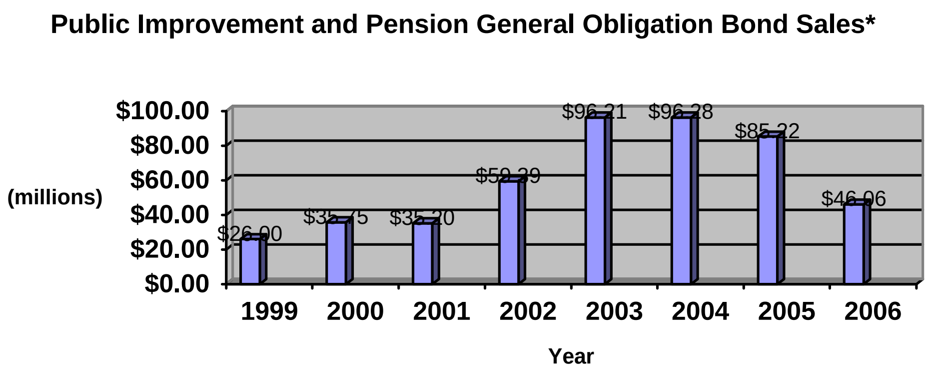
Due to the County's growing bonded indebtedness, appropriations for debt service have risen significantly in the past three years. The General Fund ID transfer for General Debt Service in the proposed 2007 Budget is $48,208,133 – a 478% increase in the amount appropriated in 2004 ($10,085,447). The General Fund ID transfer increases from $42,125,571 in 2006 to $48,208,133 in 2007. Increasingly, limited General Fund monies are being used to make required debt service payments on the County's growing bonded indebtedness.

Payments from the Debt Service Fund have also correspondingly risen significantly since 2004. The total appropriation (principal, interest and bond issue costs) has risen from $35,298,715 in 2004 to $59,602,804 in the proposed 2007 Budget – a 40% increase in three years. Principal payments have increased from $18,858,160 in 2004 to $37,264,751 in 2007 – a near 100% increase, but a positive and necessary development for the paying down of debt.

The four-year plan projects General Debt Service (principal and interest) increasing from $59,252,804 in 2007 to projected $71,498,789 in 2010. This is based on the 2007 Capital budget of $59.2 million and a $30 million capital budget each year thereafter.

Within the Debt Service Fund is an appropriation for bond issue costs. Our office, which makes the estimate, requested $800,000 for costs associated with the sale of bonds in FY 2007, but the administration reduced the appropriation to $350,000. Doing so will force the County to engage in a "premium" bond sale in 2007, instead of an anticipated "discount" bond sale.

Erie County has no choice – it must pay its debt service. However, it should be a goal of the County to reduce its debt to levels where debt service is not as large a component of the annual budget as it is today and in the foreseeable future. Therefore, it is important that in 2007 and the out years the County must make a conscious effort to take on as debt only that which is related to mandated and contractual obligations (such as the Erie County Medical Center Corporation settlement, Ralph Wilson Stadium, etc.) and for needed capital projects.



* Includes ECMCC but does not include Sewer District bond sales. 2006 statistic is for forthcoming sale, including 2007 ECMCC capital requirement of $15 million.

Capital Budget

The proposed 2007 Budget includes a Capital Budget totaling $59,200,000. This does not include the $4 million for the Buffalo Zoo which was approved by the Legislature in 2006 but which will be bonded in 2007. This is not the largest proposed Capital Budget in recent years, but it is one of the larger proposed Capital Budgets in County history. We note that the proposed Capital Budget is almost double the $30 million borrowing "cap" proposed in a prior Four Year Plan for 2007, though a substantial component of that amount is related to the Erie County Medical Center Corporation settlement and consent decree.

In the out years (2008-2012), the Capital Budget includes significant proposed appropriations for specific capital projects, including $27,000,000 for security improvements and the expansion of the Correctional Facility, $100,000,000 for an expansion of the Holding Center, $6,000,000 for the 800MHZ Communications System, $4,000,000 for the County's training center, $8,000,000 for capital improvements at ECMCC, and $57,500,000 for the ECC City Campus master plan. These are large projects that will have a significant impact on the County's debt service if effectuated.

It is important to keep in mind that a number of these projects have been discussed, in-development, or already present in prior year Capital Budgets, but have not been started or funds borrowed for the projects. The presence of many of these projects starting in 2008 (after the current County administration has departed office) is in effect, a deferral of responsibility to the next administration – as well as a significant increase in proposed borrowing.

Employee Health Insurance Costs

Active County employee health insurance costs are projected to increase from $26.3 million (adopted budget) in 2006 to $29.7 million in 2007. Through September 30, 2006 $20,279,137 has been expensed. Retiree health insurance costs increase from $9.1 million to $11.1 million. $8,699,911 has been expensed through September 30, 2006.

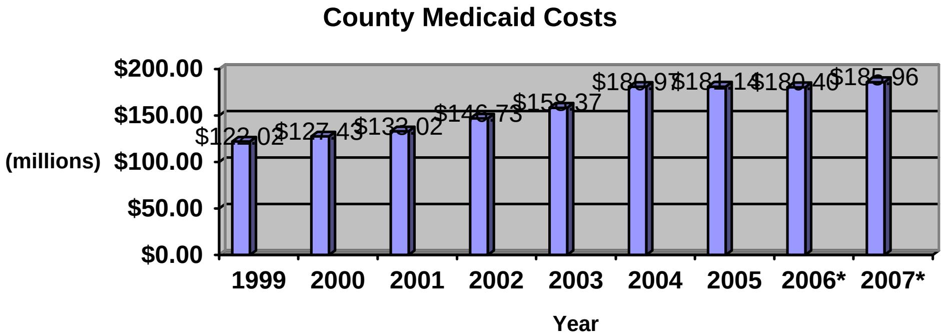
The October 18, 2006 revised Four Year Plan projects $2,400,000 in savings in 2007 due to changes in 2006 in the way in which the Labor Management Healthcare Fund administers prescription drug coverage. In July 2006, County employees were shifted to a prescription program in which they purchase "maintenance" prescription drugs in 90-day supplies, either via mail-order or at a pharmacy. This is a major expenditure and requires careful monitoring.

Pension Costs

The County's pension payment to the State Comptroller decreases from $24.4 million in 2006 to $20.9 million in 2007. The administration's estimate is based on the growth in income from investments made by the Office of State Comptroller and the corresponding reduction in required payments to the retirement system by local governments. This is a positive development for 2007, but attention must be paid for future years as it is uncertain that such reduction will occur again. These expenses are also controlled by the State Comptroller and our payments are regulated by that office.

Medicaid

In 2006, following legislation enacted by the State in 2005, county governments across New York State saw their local share of Medicaid spending capped, with the growth in Medicaid spending limited, and the State absorbing more of the cost. Erie County benefited significantly from the cap in Medicaid spending growth. The administration's most recent projection of the County's actual 2006 Medicaid cost is approximately $180.4 million, while the budgeted 2006 appropriation was $193,098,941, resulting in a large part of the 2006 positive variance. The FY 07 Proposed Budget appropriation is $185,962,536.



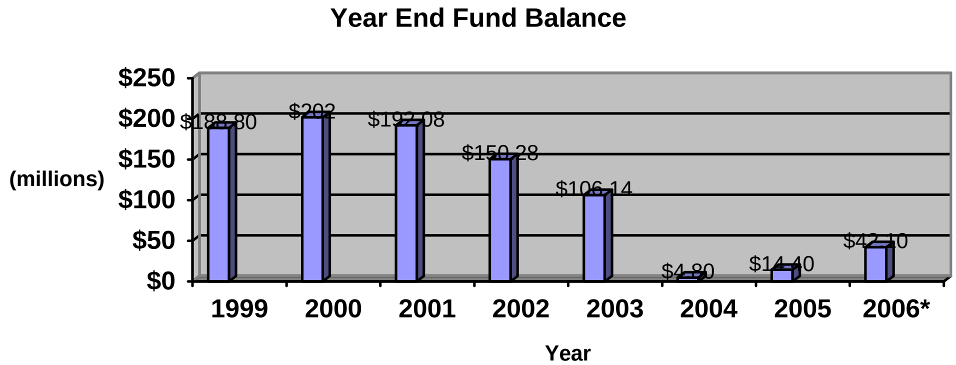
Using the initial Medicaid cap calculated with 2005 as a baseline, out year expenses are derived by annual increases of approximately 3%. For 2008, the County will be given the option of continuing to pay the cap amount plus 3% annually or give the state a percentage of its sales tax revenues. The sales tax option would be fiscally prudent if it is expected that sales tax receipts increased less then 3% each year. The choice must be made by September 2007 and cannot be changed once implemented.

Fund Balance

For the second year in a row, the proposed budget does not appropriate undesignated fund balance (though it should be noted that the County is trending towards ending 2006 with a surplus of over $20 million dollars, which surplus will be used to help restore fund balance). Given the requirements of the Four Year Plan, as well as sound municipal finance practice and Government Finance Officers Association ("GFOA") recommendations, the replenishment of fund balance is a positive and necessary development.

The Four Year Financial Plan requires the reestablishment of fund balance totaling $75 million by 2010, meeting the 5% rule recommended by GFOA. After replenishment of fund balance in 2005 and expected significant replenishment in 2006, the proposed 2007 Budget includes no provision for restoration of fund balance. The County Executive has made a policy decision that based on the County's fund balance at the end of 2005, and based on positive variances in various expense and revenue accounts during 2006, the County can achieve the fund balance target in the Four Year Financial Plan without adding to fund balance in 2007. Regardless of the administration's decision, it is imperative that fund balance be restored to appropriate levels.

The County's Comprehensive Annual Financial Report ("CAFR") for 2005 showed a general fund balance of $14.4 million at year end 2005. The administration believes that the County will end 2006 with a surplus of approximately $27.7 million. This office is only willing to project a $20 million surplus at this point. However, neither of these estimates will be confirmed until the County's independent audit and 2006 CAFR is completed in June/July 2007.



* An estimate using administration's projection of $27.7 million positive variance for 2006.

In 2006, the Erie County Charter Revision Commission recommended, the Legislature approved, and the County Executive signed a local law revising the County Charter. That local law was approved by the voters on November 7, 2006 in a public referendum. As of January 1, 2007, the Charter now requires the maintenance of a fund balance equal to or greater than 5% of the amount contained in the budget of each fund in the immediately preceding fiscal year. That means that for 2007, for a budget for all funds of $1.15 billion (adjusted for the sales tax prescription), the general fund balance must be at least $57.5 million. Given 2005 fund balance of $14.4 million, and potential 2006 fund balance of $27.7 million (using the administration's estimate), total fund balance at year-end 2006 would only total $42.1 million, or $15.4 million less than required under the Charter 5% rule.

The Four Year Plan requests the option to utilize $9 million of New York State efficiency grant funds as a contingency fund in 2007. In the event the contingency fund is not needed, the administration would designate the funds to fund balance at year-end 2007. The legality of this potential action is subject to approval by ECFSA and confirmation or approval by the State or State Legislature.

Risk Retention Fund

The proposed 2007 Budget does not appropriate any funding for the Risk Retention Fund ($1 million is included for Erie County Medical Center Corporation settlements or judgments as per the County's consent decree with the hospital, but that money is not available for County uses). That lack of an appropriation is a sharp difference from the adjusted $4,650,000 appropriation in 2006. While the large 2006 appropriation (after none in 2005) for the Fund may cover any potential 2006 and 2007 settlements or judgments against the County, there is always the potential for a shortfall in this account in 2007 which would require a mid-year budget appropriation in an already tight 2007 Budget with little room for error. We also note that the Four Year Plan projects a 2008 appropriation for the Risk Retention Fund of $4,000,000 – in effect, a deferral of cost to the next fiscal year.

Workers Compensation

The proposed 2007 Budget appropriates $9,692,000 for workers compensation claims through the Law Department. This is down from $12,219,447 (actual) in 2004, $13,187,841 (actual) in 2005, and $10,350,000 (adjusted) in 2006. The reduced appropriation leaves open the possibility of a shortfall in mid-year, if claims and costs exceed the appropriation.

In addition, in Countywide Budget Accounts, workers compensation costs increase from $1,472,825 (budgeted) in 2006 to $7,771,416 in 2007. This significant increase in cost to the County recognizes prudent budgeting and is a welcome departure from the under budgeting of the past.

Erie County Medical Center Corporation

The FY 07 Proposed Budget includes all amounts related to the consent decree and settlement entered into by the County and The Erie County Medical Center Corporation ("ECMCC").

However, we are very concerned about the possibility of a shortfall existing in expenditures due ECMCC under a recent development related to the disproportionate share ("DSH") intergovernmental transfer ("IGT") payments by the New York State Department of Health ("NYSDOH") to ECMCC and the debiting of County accounts by the State. Presently, the County and ECMCC are involved in a dispute whereby ECMCC refuses to transfer approximately $5.7 million dollars it owes to the County for reimbursement payments related to the DSH IGT. While the Comptroller's Office believes that the County is entitled to such funds, ECMCC contends otherwise, meaning the County may have to pursue litigation to enforce its rights.

While one cannot accurately determine the amount of DSH IGT debited from the County's accounts in 2007 at this point, if this matter is not resolved in a favorable manner for the County, the County could potentially find itself paying to ECMCC millions of dollars more in a new annual operating subsidy related to these payments. Payments related to this potential new expense are not included in the FY 07 Proposed Budget.

Erie Community College

The County's FY 07 Proposed Budget operating subsidy for the community college remains the same as 2006 - $13,570,777. In fact, the subsidy has remained the same for the fourth year in a row despite annual requests from the college for additional operational support. The administration's revised Four Year Plan states the County will increase the operating subsidy to the college to $15,420,780 for Erie County Fiscal Years 2008-2010. This is not a real increase to ECC but the end of a fiscal practice that called for borrowing the capital equipment portion of the subsidy. We welcome the recognition that this is a recurring expenditure and should not be funded by bonds.

The proposed 2007 Capital Budget includes $3,200,000 in borrowing for ECC capital projects, as well as $15,000,000 for the master plan reconstruction of the college's City Campus. In fact, the 2007-2012 Capital Program includes $72,500,000 in proposed County borrowing for the City Campus redevelopment plan. Excepting the City Campus plan, the 2007 Capital Budget projects annual borrowing for capital projects at ECC at $7,000,000 annually between 2008 and

2012 – a significant increase in potential borrowing and commitment by the County which has included capital funds for the college in recent years in the $3,000,000 range annually.

Considering the current issues related to the County's increasing debt service, any capital appropriation to ECC beyond the required maintenance of effort needs to be closely scrutinized and appropriately justified.

Community College Chargebacks

Community college sponsors – county governments – in New York State are required to pay community colleges in other counties a fee for local residents attending the community college in the other county. For example, Erie County is required to pay a fee to Niagara County Community College ("NCCC") for each Erie County resident-student attending NCCC. This process is referred to as the "chargeback" and the formal name of the account is "County Residents Enrolled Community College." In 2006, the County's cost was budgeted at $2,460,700. The FY 07 Proposed Budget appropriation is $3,150,000.

This office, which monitors the chargebacks, has been concerned about the appropriations throughout 2006. At October 23, 2006, based on invoices to-date (and some smaller community colleges has not yet invoiced the County), our office was estimating a 2006 deficit in the account of $1,042,593. Based on invoices not yet received from smaller colleges, the gap could grow. While current results of operations for 2006 and positive variances in other accounts can and will cover this 2006 deficit, based on an administration request for $3,150,000 for 2007, we would recommend a larger appropriation.

Tourism, Visitors and Convention Services

Erie County owns the Buffalo/Niagara Convention Center and the Buffalo Niagara Convention and Visitors' Bureau ("BNCVB", or Convention Center Management Corporation) operates and manages the complex for the County. Under the terms of a local law establishing the Hotel Occupancy Tax in 1975 which is levied on all guests at lodging establishments in the county, the tax produces revenue to be used to offset debt service expenses at the Convention Center, as well as to promote tourism in Erie County.

The Hotel Occupancy Tax is budgeted for revenue of $5,947,181 in 2007, the same amount as 2006. Since 2004, the County has increasingly utilized revenue from the tax to support County operations, and has reduced appropriations to the Convention Center Management Corporation and/or convention and visitors services. In 2004, the County appropriated $4,400,000, down to $3,140,292 in 2005, and down to $2,750,000 in 2006. The FY 07 Proposed Budget appropriates $2,300,000, with funding for Tourism, Visitors and Convention Services reduced from $1,450,000 to $1,000,000.

Based on discussions with representatives from the Division of Budget, Management and Finance, we agree that the Hotel Occupancy Tax (revenue) estimate for 2007 may be underestimated by $600,000 and the actual revenue in FY 2007 will be approximately

$6,500,000. The Legislature is not allowed under the Charter to amend this revenue estimate; only the County Executive may do so.

On October 25, 2006, seven days after he released the FY 07 Proposed Budget, the County Executive stated that he had reached an agreement in principle with the BNCVB to allocate all Hotel Occupancy Tax revenue to the organization in 2007. The sudden announcement, made by representatives of the BNCVB at the Legislature's budget hearings on October 25, has taken members of the Legislature and the public by surprise. To-date, no formal or informal written agreement, proposal or document has been created or introduced. Lacking any written proposal or any real details, it is difficult to make informed opinions concerning this potential amendment. That said, any amendment to the FY 07 Proposed Budget reallocating any revenue from the Hotel Occupancy Tax would have significant negative consequences to the General Fund Budget and would create a new gap. It is our understanding, based on discussions with staff from the Division of Budget, Management and Finance that this proposal will not move forward in 2007.

Buffalo City Parks

In 2006, this office issued an audit of the City of Buffalo Parks Agreements concerning the financial and other agreements between the City of Buffalo and the County whereby the County operates and manages the City's parklands under a contract. Among other findings, the audit revealed that in 2005 it cost the County $1.3 million more than the City's payment to operate and manage the parks. We believe that trend will continue in 2006 and future years without corrective actions. In fact, our analysis of the proposed 2007 Budget for the Buffalo City Parks Division shows that the administration estimates total 2006 appropriations at $3,280,348 (including fringe benefits), significantly beyond the city $1,800,000 payment to the county and 2006 budgeted revenue of $1,917,900. We project a similar result for 2007. Without corrective measures, the Buffalo City Parks Division will continue to be a negative drain on the County's General Fund and the County will have to continue to subsidize the city parks.

Utilities Fund

There is a significant increase in utility charges from $40,486,977 in the adopted 2006 Budget to $56,035,000 in the proposed 2007 Budget. Revenue from charges to the local governments in the Utilities Aggregation that purchase utilities through the County increase from $24,000,000 in the adopted 2006 Budget to $29,267,879 in the proposed 2007 Budget.

We note the fund includes new revenue of $8,000,000 ("NFG Pace Credit") that offsets part of the approximate $15.6 million increase in this fund. The General Fund portion of this fund is $5,606,000, an increase of $762,599 or 15.7% from the 2006 adopted budget. Given the volatile nature of utility expenses this is another account that requires careful monitoring.

Road Fund

The Road Fund ended 2005 with a total negative fund balance of $1.615 million and a negative undesignated fund balance of $7.808 million. While the Road fund is a Special

Revenue Fund and not a major fund, these results continue the deficits that this fund has been recording since 2001. We are advising the administration and the Legislature that corrective measures must be taken to balance the Road Fund. We have found no acknowledgement of this issue or corrective measures proposed in the Four Year Plan.

Errors in Interfund and ID Billing Estimates

Our office has reviewed all Interfund and Interdepartmental ("ID") billings and transfers, including those within and between grant fund projects and the Sewer Districts. For the most part, the billings and transfers between departments correspond and correlate; in a few instances, the appropriation and revenue lines do not match 100%, but are close. For instance, the ID billing (revenue) to the Law Department is shown as $849,858 in that department, while our review sums the appropriations from other departments and accounts to $840,858.

We did find some examples where the Interfund transfers (appropriations) from departments to the Utilities Fund do not match. Fleet Services appropriates $80,000 to the fund, while the fund budgets for $460,000 in revenue. The County Clerk-Auto Bureau appropriates $15,000 to the fund, while the fund budgets for $8,700 in revenue. The Road Fund appropriates $397,401 to the fund, while the fund budgets for $392,000 in revenue. The Library system appropriates $1,372,285 to the fund, while the fund budgets for $930,000 in revenue. Similar discrepancies can be found in the four Sewer District Interfund transfers.

Budget Resolutions

Annually, the FY 07 Proposed Budget includes a series of Budget Resolutions designed to address gaps in the adopted budget, and to codify certain issues. We observed several noteworthy budget resolutions which we bring to your attention.

Budget Resolution # 3

The FY 07 Proposed Budget includes Budget Resolution #3, granting the County Executive and Commissioner of Personnel the continued ability to award Variable Minimums, or higher than permissible salaries to new or existing County employees when they assert that they cannot recruit a person for the position without increasing the salary of the title outside of the normal Job Group and Step.

After the Erie County Legislature raised concerns about this authority in early 2006, we note that language has been added to this Budget Resolution for 2007 limiting the County Executive's authority to award Variable Minimums. Under the proposed new language, any such award may only be conducted after approval of both the County Executive and County Legislature.

We concur with this amendment and agree that legislative approval should be granted for all such awards or upgrades. However, as indicated in Appendix A, we note that the proposed 2007 Budget includes funding for some managerial-confidential positions at Steps higher than the normal starting Step (Step 0).

Budget Resolution # 67

The proposed 2007 Budget includes new Budget Resolution #67, authorizing the transfer of cash from completed capital accounts to be used for debt service or for other completed capital projects. This resolution enables the administration to transfer remaining cash from completed capital projects to be used for other capital projects or to be applied against debt service in the 2007 Budget. Available funds to be utilized total $2,160,362. This office supports this resolution.

COMMENT ON FOUR YEAR PLAN PROJECTED DEFICITS (2007 - 2010)

The October 18, 2006 revised Four Year Plan projects using four broad categories to reduce County costs and avoid deficits in 2008, 2009 and 2010. They are: managed attrition, reducing Sheriff road patrols, collective bargaining concessions and matrix efficiencies. Most significantly, we note that these major categories of proposed savings are not being pursued in 2007 and are being delayed until 2008.

Managed Attrition:

The revised Four Year Plan utilizes managed attrition to reduce the County workforce by $2.7 million in 2008, $3.6 million in 2009, and $3.4 million in 2010 for a total savings of $9.7 million over the three out years of the Plan. We are skeptical about the County's ability to generate these total managed attribution savings. We note that despite the existence of hundreds of budgeted but vacant positions in the County throughout 2006, no steps were taken to manage those personnel costs, and in fact, the administration is engaging in steps to fill positions and appropriate more funds in 2007 for more positions.

If the plan is attainable, this office believes that it should be implemented immediately. At present, there are approximately 160-200 funded vacant positions, and there are another 89 full-time positions added to the General Fund in the FY 07 Proposed Budget. We question the logic behind adding jobs in 2007 and eliminating jobs in 2008, 2009 and 2010. This is an area that should be examined carefully and if attainable should be implemented earlier. Delaying the implementation of this initiative until 2008 merely obligates the next administration.

Sheriff Division ("Road Patrols"):

The original Four Year Financial Plan projected the gradual phasing out of the Sheriff Division over a three year period starting in 2006. In late 2005, the County administration and Legislature amended the plan to initiate the phase-out in 2007, with a 33% reduction in appropriations for the division starting in 2007. In 2006, the County Executive established a commission including himself, the Sheriff, Chairman of the Legislature's Public Safety Committee, police chiefs, police union officials and supervisors from towns with and without Sheriff police/patrol services to examine the concept of phasing out or charging fees for police services. The status of any discussions, study, or findings is not known. The FY 07 Proposed Budget does not include any such provision to phase-out patrols in 2007, and in fact, the administration's revised Four Year Plan proposes starting the phase-out in 2008, with $1.9 million annually reduced from the Sheriff Division budget. Again, delaying the implementation of this initiative until 2008 merely obligates the next administration.

Collective Bargaining Concessions:

Several of the County's collective bargaining units are, and have been working without contracts for several years. The County's contract with the largest bargaining unit, the Civil Service Employees Association ("CSEA") expires on December 31, 2006. Under New York State Law, while negotiations are underway, the terms of the existing contract remain in effect.

In 2007, the administration has budgeted for no cost-of-living wage increases and has only included longevity step increases. Those steps are projected to cost $3 million.

The Four Year Plan includes significant savings estimates from concessions and changes in work rules and employee benefits (such as employees paying for a portion of the cost of their health insurance). Savings of $3.2 million in 2008, $3.3 million in 2009, and $3.4 million in 2010 are included in the October 18, 2006 revised Plan. To-date, the County has had no success and little progress in discussions with the County unions concerning their contracts (such as union employees paying for health insurance as managerial-confidential employees do). No progress has been made in attaining cost reductions through these negotiations. While the Four Year Plan has not included union concessions as a component towards offsetting the projected budget gaps in 2008 – 2010, we note that such savings are speculative.

Matrix Efficiencies:

All approved and revised versions of the Four Year Plan have included a range of matrix initiatives to either reduce appropriations or generate new or enhanced revenue to the County. Throughout 2006, ECFSA has routinely reviewed with the County Director of Budget, Management and Finance the initiatives, receiving status reports concerning the progress in implementing initiatives. Some initiatives implemented in 2006 have generated partial or full targeted revenues, and others have successfully reduced partially or fully expenses.

It is clear that many initiatives in the original and revised versions of the Plan have not and will not come to fruition. However, it would be speculative at this point to comment on matrix efficiency projections in the out years without further hard financial data to use as a comparison.

Appendix A
Noteworthy Personal Services Changes

Budget, Management and Finance:

The title of Director-Center for Cooperative Economic Growth, which has been vacant since July 5, 2006, remains in the 2007 Budget (JG 17/5, $91,466).

One title of Billing Account Clerk in the Revenue Recovery Unit, which has been vacant all of 2006, is deleted.

Law:

The County Attorney is receiving a longevity step increase from Step A ($127,100) to Step B ($130,204) for which he may not be eligible to recieve.

One Assistant County Attorney is receiving an upgrade from JG 14 ($67,758) to JG 15 ($75,306).

One Assistant County Attorney is receiving an upgrade from JG 15 ($75,306) to JG 16 ($83,356).

Personnel:

Two new managerial-confidential titles of Risk Manager JG 14/D ($74,408) and Assistant Risk Manager JG 10/5 ($46,592) appear in the Budget. (Note: the Risk Manager title technically is not new, as it was created on September 28, 2006).

Information and Support Services:

The managerial-confidential title Director of Support Services, which has been vacant since March 2005 and vacant (but funded) during all of 2006 remains in the budget and has its appropriation increase from $66,980 (JG 16/1) to $83,356 (JG 16/5).

In late 2006, the Legislature approved the transfer of seven SAP positions from the Capital Fund to the General Fund in the Division of Information and Support Services. Those positions now appear in the General Fund. We agree that such transfer should take place as the positions are a recurring expense and not related to a capital project.

The title of Business Process Engineer (SAP) which has been funded but vacant during all of 2006 remains in the budget at JG 13/1 ($52,248).

Environment and Planning:

The title of Director, Intermunicipal Cooperation and Planning which was eliminated in March 2005 and not funded in 2006 is re-established at JG 15/1 ($60,511).

The managerial-confidential title of Deputy Commissioner of Planning and Economic Development, which has been vacant all year, is budgeted at $82,210 (this proposed salary does not correspond to the county salary scales). We note that a new employee was hired for the title on September 18, 2006 at JG 17/0 ($66,964). The budgeted salary is incorrect.

The title of Community Planning Coordinator, JG 16/E ($100,331) is reallocated from the General Fund to the Grant Fund.

Mental Health:

A vacant title of Supervisor of Administration JG 13 ($52,248) is deleted and a new title of Director of Contract Administration JG 15 ($80,700) is created.

Special Needs:

A new title of Assistant Preschool Coordinator JG 9 ($41,527) is created to support the Preschool Coordinator.

Senior Services:

The title of Transportation Director and six Truck Drivers, funded but vacant all of 2006, are deleted for 2007.

The title of LTC Coordinator JG 13/5 ($64,881) is created.

Social Services:

There are 60 net new positions created.

Health Division:

The incumbent Health Commissioner is receiving an upgrade from JG 21/5 ($124,008) to $153,460 (no job group exists), an increase of $29,452.

The filled title of Contracts Specialist JG 9/5 ($46,378) is deleted and replaced with the upgraded title of Senior Contract Specialist JG 12/5 ($59,259).

Emergency Medical Services:

All 13 MERS Coordinators and the 2 Senior MERS Coordinators are transferred to Central Police Services.

Public Health Laboratory:

There are seven net new positions created.

Medical Examiner:

A new title of Chief Medical Examiner (no job group) is created ($178,008).

The two incumbent Associate Chief Medical Examiners are upgraded from JG 19 to JG 23 (total salaries increasing from $231,594 to $308,830).

Three incumbent Pathological Laboratory Worker titles are upgraded from JG 5 ($95,175) to JG 6 ($103,385).

Probation:

Five new titles of Probation Officer created.

Sheriff Division:

Four new titles of Confidential Aide created.

The incumbent title of Personnel Clerk is upgraded from JG 6 ($37,140) to Senior Personnel Clerk JG 7 ($40,843).

One new title of Sergeant in the Police/Patrol Services unit created.

Ten titles of Dispatcher are transferred to Central Police Services as per the Four Year Financial Plan.

Jail Management:

One new title of Confidential Aide created.

One new title of Correction Lieutenant created.

Ten new titles of Correction Officers created.

Central Police Services:

The incumbent Commissioner of Central Police Services is receiving an upgrade from JG 18 ($96,462) to JG 19 ($105,855).

The managerial-confidential title of Director of Information Services JG 16 ($71,777) is restored after being deleted in March 2005 and not funded in 2006.

One new title of Senior Complaint Writer created.

Eight new titles of Police Complaint Writer created.

21 Police Complaint Writers are upgraded from JG 6 to JG 7.

Emergency Services:

The title of Senior Administrative Assistant-Homeland Security JG 13/D, which has been vacant since August 5, 2006 remains funded at $71,230.

Board of Elections:

Rather than delineating specific titles, the Budget includes a total appropriation of $1,297,233 for Democratic Personnel and $1,297,233 for Republican personnel.

Public Works – Commissioner:

A double-fill in the title of Construction Inspector JG 11 is not shown in the Budget, resulting in under-funding of $52,341 in that department.

Public Works – Buildings & Grounds:

The title of Deputy Commissioner JG 16/1 ($65,209), which has been vacant since March 13, 2006, continues to be funded.

Two new titles of Building Guard created.

Utilities Fund:

The title of Principal Engineer-Energy, Utility, Grants JG 16/1 ($71,777), vacant since late 2003 or early 2004, is re-established.

Parks:

The managerial-confidential title of Deputy Commissioner of Recreation JG 15 (58,750), vacant since February 19, 2005, continues to be funded.

Buffalo City Parks:

The incumbent title of Supervisor of Rinks and Pools is upgraded from JG 7 ($37,775) to JG 8 ($41,157).

Highways:

A title of Senior Accounting Analyst JG 13 ($52,248) is created despite the presence of an existing Systems Accountant and an Accountant on staff.