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This paper is one in a series of reports prepared as part of New York State Lieutenant Governor Richard Ravitch's project, undertaken at the request of Governor David Paterson, to develop proposals that would lead New York State to structural budgetary balance. Lieutenant Governor Ravitch issued his initial report in March 2010. That report outlined the deep fiscal challenges facing the state and recommended a series of steps to close future budget gaps, including strict new requirements for adoption and maintenance of balanced budgets.

The lieutenant governor's March 2010 report also proposed that New York's governor be granted broader power to address midyear budget gaps by implementing across-the-board expenditure reductions, in the absence of legislative action to deal with fiscal emergencies. This report compares New York's existing rules regarding midyear budget reductions to those in other states, and explores issues state policymakers may wish to address during consideration of expanded gubernatorial authority to preserve budgetary balance.

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STRUCTURAL BALANCE FOR NEW YORK

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Gubernatorial Powers to Address Budget Gaps During the Fiscal Year

New York Governors Lack Broad Authority Commonly Found in Other States

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Executive Summary

The governor of New York lacks a major budgetary power that is taken for granted in other states: the authority to make unilateral, across-the-board reductions when necessary to maintain fiscal balance. The chief executive's ability to control expenditures after adoption of the budget is weak compared to gubernatorial powers in Massachusetts, Ohio, and Oregon, among other states.

In New York, the governor's office is often described as among the most powerful in the nation. That is true, with respect to the initial adoption of the state budget. As a result of constitutional reforms championed by Alfred E. Smith and others, the governor structures each year's appropriation bills; can force the Legislature to act on those proposals before considering any others; and has a strong, line-item veto power.

Yet, once the budget is adopted, a governor of New York has only limited powers to make mid-course corrections that will keep the budget from being thrown out of balance by unanticipated costs or revenue shortfalls. Under longstanding practice in New York, the executive's authority to determine midyear spending adjustments is confined to state agency operations — which represent about 26 percent of nonfederally funded spending. With such limitation, spending reductions imposed by the governor may disproportionately affect certain services while failing to adequately address the state's overall budgetary imbalance. Even that limited authority has no clear basis in New York State's Constitution or statutes, and thus could be open to legal challenge.

Studies by the National Conference of State Legislatures, the National Association of State Budget Officers, and the U.S. General Accounting Office conclude that the majority of states grant governors broad authority and responsibility to keep their states' budgets in balance. As a result of revenue shortfalls caused by the recent recession, such powers are assuming a larger role in states' overall strategies to maintain fiscal stability.

New York State faces budgetary challenges greater than any in recent decades. The state's inability to fully address an imbalance between revenues and expenditures in 2009 resulted in $2 billion in liabilities being rolled over into the 2010-11 fiscal year — the functional equivalent of the state borrowing from itself. For the foreseeable future, gaps between planned expenditures and projected revenues are extraordinarily large, and significant imbalances will likely remain even after the national economy recovers fully from the recent recession. Increasingly dependent on personal income tax, the state's revenue system has become more volatile, meaning that midyear gaps may become more frequent even when annual budgets appear to be balanced at the time of adoption. Albany's inability to manage such imbalances has led to repeated fiscal crises that harm school districts' and municipalities' ability to plan effectively, degrade services from maintenance of parks to processing of tax refunds, and reduce public confidence in government.

As part of a broader plan for achieving structural budgetary balance in New York, Lieutenant Governor Richard Ravitch has proposed that the governor be given greater power and responsibility to limit spending when necessary to close gaps during the fiscal year. Assembly Speaker Sheldon Silver has also proposed additional gubernatorial authority in this area. Creation of statutory or constitutional guidelines could, at a minimum, assure preservation of authority that New York governors have exercised without clear legal mandate. Extending such authority beyond agency operational expenditures would enhance the state's ability to deal effectively with future budget gaps and to avoid further shifting of current costs into the future. At the same time, expansion of executive power could be accomplished with certain limitations to preserve the Legislature's role in establishing the state's fiscal priorities.

Executive Budget Powers in the States

New York and other states across the country face grave fiscal challenges. Most states that produce multiyear forecasts are projecting large, recurring imbalances between revenues and expenditures, even if the nation's economic recovery continues as expected. Meanwhile, governors and legislatures are attempting to eliminate current-year gaps without enacting harmful service reductions, economically damaging tax increases or inappropriate borrowing. In this difficult environment, gubernatorial powers to address gaps that arise after budget enactment are drawing increasing attention in a number of states.

The extent of gubernatorial authority over the budget has been a recurring issue, in New York and other states, for more than a century. From the nation's founding through the early 1900s, the power of the purse was held almost entirely by legislatures. States generally did not adopt a budget in the modern sense — there was no unified plan of appropriations, little organized effort to

weigh the value of expenditures against the cost of taxes, no broad consideration of implications for the future. The lack of a budget system was a relatively minor matter, however, because states' expenditures and activities were limited. Until the early 1900s, their primary fiscal responsibilities were to build and maintain highways, provide partial funding for public schools, and operate a few prisons and institutions for the mentally impaired. Local school districts and municipalities collected, allocated, and spent the largest share of taxpayer dollars.

During the first decades of the twentieth century, rapid population growth and industrialization of the economy created both the need for more public services, and the wealth to pay for them. In response, state governments took on major new responsibilities — expanding public education and transportation systems, caring for the indigent and disabled, regulating businesses, providing parks, and more. The need for systematic budgeting and enhanced executive leadership, to establish clear priorities and effectively manage new responsibilities, became apparent.

In New York, Smith and other reformers created a budget process giving the governor clear dominance over the initial stage of budget enactment — the sole power to initiate appropriation bills which the Legislature must use as the basis for final budgets — and a strong, line-item veto power. Numerous other states also adopted constitutional or statutory changes that expanded the governor's leadership role.

Rankings of gubernatorial budget powers often overlook the task of managing the budget during the year.

Since the provisions creating the Executive Budget process were added to New York's Constitution in 1927, various court rulings have clarified the extent of the governor's power, in many cases enhancing the authority spelled out in the constitutional text. The most recent major decision in this area, the Court of Appeals' December 2004 ruling in *Silver v. Pataki*, held that the governor can — within some unspecified limits — include significant changes to nonbudgetary laws within appropriation bills, as long as such statutory proposals relate to the items of appropriation. Today, independent researchers generally rank New York's gubernatorial office among the strongest in the nation — with its strong role in the shaping of the enacted budget among the key reasons.

Such rankings, however, emphasize powers related to adoption of the budget, and generally overlook the important task of managing the financial plan during the year.[1] For example, one frequently cited analysis, by Thad Beyle of the University of North Carolina, rates the budget power of each state's chief executive on a scale of 1 to 5, with 5 being most powerful. The five points relate to the sharing of power between governors and legislatures in constructing the budget, and the extent of each governor's veto power. Two governors, those in Maryland and West Virginia, attain ratings of 5 in Beyle's most recent analysis. New York and one other state, Nebraska, receive ratings of 4, higher than all but 46 states. The average rating of gubernatorial budget powers is 3.1, according to Beyle.[2]

Broadly speaking, New York's Constitution allows two distinct paths from the governor's proposal to an adopted budget. In most years, the Legislature negotiates changes to the Executive Budget with the governor. Such changes typically include an increase in the overall level of expenditures, redirection of funding within some programs, changes in tax and other revenue proposals, and modification of some proposals for program restructuring. When the two branches agree on such changes, the Legislature may insert its own changes in the governor's budget bills and rely on an agreement that the governor will not veto any spending additions; or lawmakers may require the governor to submit amendments to his own budget proposals, for legislative action, as the Constitution allows. (This cooperative approach may include some relatively minor gubernatorial vetoes of items the Legislature has added.) Such legislative-executive agreement is the norm, and with some variation was the process that produced final budgets for the fiscal years starting in 2007, 2008, and 2009.

The second path to a final budget occurs when the governor and the Legislature cannot agree. The state Constitution provides that the Legislature may strike or reduce items in the Executive Budget. Any reductions the Legislature makes to the governor's budget take effect upon legislative approval of the Executive Budget bills; the governor has no power to reject or amend any such reductions. (The governor may propose new appropriation bills to replace any such reduced funding, but the Legislature is under no requirement to consider such proposals.) The Legislature may also increase or add items of appropriation (and thus increase the overall size of the budget) "provided that such additions are stated separately and distinctly from the original items of the bill and refer each to a single object or purpose."[3] The governor has the power to veto such additions; the Legislature can override any vetoes with two-thirds approval in both the Senate and Assembly. This letter-of-the-law approach to reaching a final budget is relatively uncommon, but has occurred several times since creation of the Executive Budget. Most recently, the Legislature completed action on the 2006-07 budget by overriding more than $1 billion of vetoes by Governor Pataki, and approving various tax changes — some increases and some decreases — over his objection. (In a rare development, the Pataki administration refused to recognize some of the Legislature's 2006 overrides, pronouncing them unconstitutional — creating a stalemate over certain elements of the budget that was never resolved.) As evidenced that year and in 2003, lawmakers have the ultimate power to shape the final plan largely as they wish if there is strong, veto-proof consensus in the legislative branch.

Understanding the process for adoption of New York's annual budget is useful in analyzing the powers of the governor to manage expenditures after enactment. Having played a leading role in the shaping and adoption of the budget, New York's governor —

like chief executives in most states — has primary responsibility for implementing the financial plan that results from interplay of the adopted budget bills and permanent state laws. Each year, that role requires officials in the executive branch to make hundreds of major decisions, and thousands of smaller choices in areas including timing of expenditures, shaping of policies, hiring of personnel, and other management issues. Carrying out those responsibilities represents the executive-branch function of implementing the appropriation decisions and policy-formulation choices the Legislature has made in adopting the budget. (Appropriations represent upper limits on authorized expenditures for particular purposes; actual expenditures are often less than appropriated amounts.) At the same time, the governor's Budget Division closely monitors the level of state revenues to ensure that adequate resources are available throughout the year and that the fiscal year will end in balance. Maintaining such balance often requires the Budget Division to time payments carefully, and in more limited instances to hold certain particular expenditures below the levels that are approved by the Legislature and included in the year's financial plan.

Now, Another Era of Intense New Budget Challenges

The constitutional structure of New York's budget process was created in response to a dramatic increase in the scope of the state's fiscal responsibilities during the early 1900s. Just as occurred then, the start of the twenty-first century finds the state once again facing broader and more difficult financial choices.

Over the past two years, as the nation has undergone a sharp and protracted economic slowdown, states have experienced historic fiscal challenges as tax revenues weakened and expenditures in many areas continued to outpace inflation. In New York, the enacted budgets for fiscal 2009 and 2010 both included overall spending increases more than twice the rate of inflation, due to a combination of policy choices and rising costs.

Having accumulated over several years, New York's fiscal difficulties reached critical stages during the fall of 2009 after dramatic revenue declines starting in spring 2009 were not addressed adequately in that year's budget process. Both the governor's Budget Division and the Office of the State Comptroller (headed by a separately elected statewide official) warned that the state was in danger of running out of cash if revenue projections proved accurate and if expenditures were carried out as envisioned in the enacted 2009-10 budget. In early October, Governor Paterson ordered executive-branch agencies to reduce expenditures for the remainder of the fiscal year by $500 million. Later in October, he asked the Legislature to approve midyear reductions, including $1.3 billion in funding for school districts and local governments.

Several weeks after the governor's request, the Senate and Assembly approved a smaller level of reductions, including $550

Spending Outpacing Revenues: Sharply Growing Gaps for New York State

					2010-11 Through 2013-14	
	2010-11	*2011-12*	*2012-13*	*2013-14*	*Total Growth*	*Average Annual Growth*
Projected gap, General Fund	$7.4 billion	$14.3 billion	$18.3 billion	$20.7 billion		
Change in GF receipts	1.9%	4.4%	0.6%	4.8%	12.2%	2.9%
Change in GF disbursements	0.7%	16.1%	7.3%	6.5%	33.6%	7.7%

Data on budget gap from “Revised Current Services Estimate, Before Actions,” 2010-11 Executive Budget, New York State Division of the Budget, January 2010.

Data on change in General Fund receipts and disbursements from *Report on the State Fiscal Year 2010-11 Executive Budget*, Office of the State Comptroller, February 2010.

million in local assistance. After accounting for such changes, the Budget Division warned of continuing danger that the state would run out of cash and be unable to make scheduled payments to school districts, local governments, vendors, and other recipients of state funding. Such an outcome was averted when Governor Paterson ordered the Budget Division to temporarily withhold a small percentage of scheduled payments to school districts. In response, advocates for education funding — the New York State School Boards Association, New York State United Teachers, and others — filed suit challenging the governor’s power to order such temporary withholding of appropriated expenditures.[4]

In December 2009, for the first time since the state’s General Fund was reconstituted to its current structure in 1981, the General Fund ended the month with a negative balance. Cash flow forecasts included in Governor Paterson’s FY 2010-11 Financial Plan, which includes all the executive’s proposed spending and revenue actions, project that the General Fund will end the months of May through August with negative balances. The state ended fiscal 2009-10 in balance only by effectively rolling $2 billion of liabilities into the 2010-11 fiscal year.[5] In April 2010, the governor, the Budget Division, and the State Comptroller warned once again that the state was approaching a cash crisis. Governor Paterson prepared to delay state payments to school districts to deal with the shortage, and education groups filed a second lawsuit. At this writing, both lawsuits are pending.

Tax revenues in New York and other states can be expected to resume growth in coming years as the nation’s economic recovery continues. However, most observers agree that serious budgetary challenges are almost certain to remain even after the economy and state revenues regain strength. In New York, both the Budget Division and the Office of the State Comptroller project large annual budget gaps into the foreseeable future. Nationally, the Government Accountability Office predicts that — absent policy changes — the scope of overall gaps between state and local governments’ revenues and expenditures will double during the coming decade, and double again over the following decade.[6]

The likelihood of significant, ongoing fiscal pressure implies that, for years to come, enactment of balanced annual budgets will require New York State to restrain or cut spending on major services, and to increase taxes and/or other revenues. The combination of political pressure to avoid such choices, and unpredictable revenue, often results in financial plans that do not remain in balance without midyear corrective action by the governor, the Legislature, or both.

How Do Other States Address Midyear Budget Gaps?

In developing annual budgets, state policymakers must make many assumptions and estimates about factors that will affect revenues and spending. Tax revenues are strongly influenced by economic factors such as personal income and retail sales; projections of such trends by even the most highly respected economists are typically imperfect. Demand for expenditures can vary based on uncertain factors, including the number of students enrolled in public schools, and the number of low-income individuals who qualify for Medicaid and other assistance. As a result, state budgets historically are more likely to develop gaps or surpluses, than to end the fiscal year in precise balance.

As part of the twentieth-century movement to adoption of formal budgeting and gubernatorial fiscal management, most states enacted laws giving the governor or other executive branch officials certain powers to adjust spending amounts from those appropriated by the Legislature. Often, such provisions are considered essential elements of constitutional or statutory schemes to promote budgetary balance, some form of which is required in 49 states.

Most states allow or direct the governor (or a designee such as the budget director) to reduce budgeted expenditures under conditions such as development of an actual or potential deficit. Specifics vary from state to state. In many states, the legal foundation for such powers is not fully clear, and governors' use of impoundment authority is based partly on tacit approval from legislatures. Often, such powers are poorly understood because they are based on longstanding practice rather than law; or because constitutional or statutory provisions on which they are based are written only in general terms. Generally, reflecting concern for separation of powers, such executive authority does not include the ability to make unilateral reductions in legislative or judicial budgets. To avoid damage to a state's creditworthiness, payments of principal and interest on debt also are often excluded. Some states — including Massachusetts, Ohio, and Oregon — expressly allow governors to reduce aid to municipalities and public schools.

Two organizations representing state officials across the country — the National Conference of State Legislatures (NCSL), and the National Association of State Budget Officers (NASBO) — have undertaken independent analyses of gubernatorial powers to reduce enacted budgets in all the states. The organizations use

More Volatile Revenues = Increased Risk of Midyear Budget Gaps

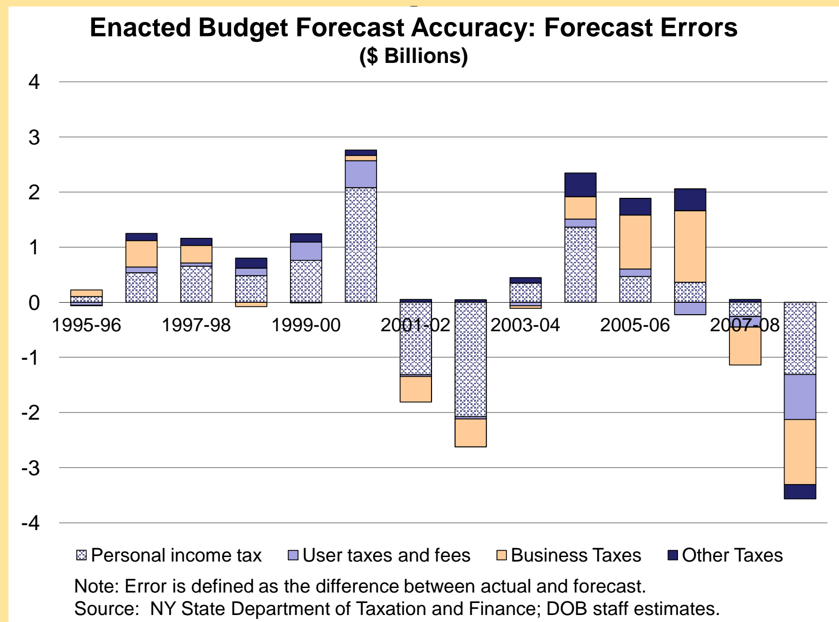
Beyond the increasing difficulty in matching recurring revenues to recurring expenditures, the changing natures of New York's tax structure and sources of taxpayers' personal income present further obstacles to maintenance of budget balance. As in many other states, revenue systems have become more volatile in recent years, making it harder to ensure that revenue estimates included in the annual financial plan prove reliable as the fiscal year proceeds.

"Greater reliance on the income tax and increases in the more volatile sources of income such as capital gains, have made state revenues more responsive to the business cycle since 1998," according to Richard Mattoon and Leslie McGranahan, economists at the Federal Reserve Bank of Chicago.[7]

In recent decades, many states have devoted increased resources to technical analysis of their revenue streams, seeking to enhance their ability to forecast revenues accurately. Yet despite such efforts, average errors in states' revenue forecasts have grown larger during the last two national recessions, compared to those in past recessions.[8] In New York, the average absolute error in revenue forecasts for adopted budgets (without netting the effects of positive and negative errors) was 2.4 percent in fiscal 1996 through 2000, and rose to 4.2 percent in fiscal 2002 through 2007, according to the Budget Division.[9] Most of the increase was due to increased difficulty in forecasting revenue from the personal income tax.

Over the nine years from fiscal 2001 through fiscal 2009, New York's adopted budgets included five years with revenue projections that were too low and four with projections that were too high. In total, the overestimates and underestimates were very nearly equivalent at slightly more than $9 billion. If New York's budget system included automatic stabilizers to balance such ups and downs, forecast errors would cause little damage. But the state tends to spend unexpected revenues, thus raising the level of structural expenditures in areas such as school aid and health care. When inevitable downturns arrive, policymakers find it very difficult to respond to unexpected gaps. The nearby graph shows multibillion-dollar revenue shortfalls in fiscal 2002, 2003, 2008, and 2009. None of the budgets adopted in the wake of those shortfalls were balanced on a structural basis.

Compared to other states, New York is especially susceptible to revenue volatility and thus heightened risk of unexpected budget gaps. In fiscal 2009, income taxes made up 57 percent of the state's tax revenue, compared to a national average of 34 percent, according to Census Bureau data. Taxes on capital gains, bonus income, and other activities generated by the financial sector have represented 20 percent of the state's overall tax revenue base, according to the Budget Division. "Income sources that are most closely tied to the fate of the financial sector, capital gains and bonus payments, always exhibit a high degree of volatility and are difficult to forecast with precision," the Budget Division states.[10] Recent increases in tax rates for upper-income earners exacerbate such difficulty, according to the Division.



Source: New York State Division of the Budget

different methodologies to assess impoundment powers, so their conclusions are not directly comparable. Despite their representing opposite sides of the executive-legislative balance of power, both find that unilateral authority to reduce expenditures during the fiscal year is a common element of governors' budgetary powers.

"Very few states mandate that the governor must consult with the legislature to reduce the enacted budget," NCSL staff commented in a 2008 paper. Illinois, Missouri, and Ohio are among states that grant governors "unlimited authority to reduce the budget when fiscal conditions require," according to NCSL.

According to NASBO, 38 governors have some authority to cut an adopted budget without legislative approval. Of those, 32 states (including New York) impose some restrictions.

The U.S. General Accounting Office (now the Government Accountability Office) reviewed state laws and practices in this area for a 1993 report on states' balanced-budget requirements. It concluded, among other things: "Governors have broad powers to cut budgets during the year."[11]

In a recent decision on the "unallotment" power granted to Minnesota's governor, the state's Supreme Court reviewed a number of court decisions relating to analogous powers in other states. It found: "Most courts conclude that the executive branch has some inherent authority and discretion over spending, particularly to spend less than appropriated, but only within the scope of legislatively enacted spending priorities."[12]

The major elements missing from gubernatorial impoundment authority in New York are aid to school districts, general assistance for municipalities and Medicaid, which together make up close to half of state-funded spending. States where the governor may implement midyear reductions in those areas include Maryland, Massachusetts, Minnesota, Ohio and Oregon. In those and many other states, governors' powers to implement midyear spending reductions are well defined in law. Discussion of several examples follows.

Connecticut

In Connecticut, General Statute 4-85 provides authority for the governor to reduce total General Fund appropriations by up to 3 percent on her own authority. Additional rescissions within individual appropriations, up to 5 percent, may be made with approval of the Finance Advisory Committee. Its nine members include the governor and lieutenant governor; the comptroller and treasurer, both of whom are elected independently of the governor; and five members of the General Assembly.

As the state's attorney general summarized the law in an October 2009 opinion:

> …the Governor is authorized to reduce allotments if the Comptroller projects a General Fund deficit greater than one percent of total General Fund appropriations or the

> governor determines that estimated budget resources during the fiscal year will be insufficient to finance all appropriations in full.[13]

Most municipal aid, including general state assistance for schools, is exempt from such reductions. "In addition, as a practical matter, a Governor is constrained from cutting appropriations for entitlement programs or pension and health benefits for state employees and retirees — expenditures that comprise much of the budget," according to Governor Jodi Rell's office.[14]

In November 2009, Governor Rell announced $34 million in rescissions as a first step toward dealing with a projected deficit of nearly $400 million.

Maryland

Maryland law provides that the governor may reduce any appropriation by up to 25 percent, with approval of the state Board of Public Works.[15] The board has a wide range of powers over state borrowing, expenditures, and procurement. It is composed of the governor, the comptroller (who is elected separately by the voters), and the state treasurer (who is elected for a four-year term by the state's General Assembly). Thus, the governor must obtain agreement from either another statewide constitutional officer or from the representative of the legislative branch. Areas that are exempt from such reductions include appropriations for the legislature and judiciary, principal or interest on state debt, and mandated aid to public schools.

In fiscal 2010, the governor proposed and the board approved three series of reductions totaling a record-high $957 million, some 4.3 percent of the nonfederally funded expenditures in the state's enacted budget. In fiscal 2009, midyear reductions totaled $506 million.[16]

In fiscal 2009, Massachusetts Governor Deval Patrick reduced budgeted allotments by $887 million, including $120 million in aid to cities and towns.

Massachusetts

Massachusetts' State Finance Law authorizes the governor to reduce allotments to state agencies whenever "available revenues … will be insufficient to meet all of the expenditures authorized to be made from any fund." The governor must notify legislative fiscal committees 15 days before any reductions, and "submit in writing a report stating the reason for and effect of such reductions, or submit to the general court specific proposals to raise additional revenues by a total amount equal to such deficiency."[17]

The governor's reductions may include aid to cities and towns, which fund public schools. In October 2009, Governor Deval Patrick imposed $229 million in midyear reductions, roughly 1.2 percent of nonfederally funded expenditures projects for the year. Those reductions did not include general aid to municipalities. During the previous fiscal year, Governor Patrick reduced budgeted allotments by $887 million, including more than $120 million to cities and towns.

Minnesota

In Minnesota, expenditure reductions adopted administratively in response to revenue shortfalls are known as "unallotments." While the law authorizing such cuts was enacted in 1939, governors have used the tool sparingly. For example, during the three decades up to 2008, only three such actions were taken: reductions of $195 million in 1980, $110 million in 1986, and $281 million in 2003.[18]

Executive-branch officials must notify the Legislative Advisory Commission, which is made up of six high-ranking legislators, at least 15 days before unallotments occur. The legislative commission has no power to stop the unallotment. The state law governing budget actions also includes provisions requiring that unexpected revenues be deposited into cash-flow and reserve accounts, providing some cushion to help avert unallotments during future fiscal crises.[19]

"It's been common practice to wait for the Legislature to act before unalloting," said Mark Shepard, legislative analyst in the nonpartisan House Research Department. "That's the way the executive branch acknowledges that this is an extraordinary power."

Minnesota's gubernatorial budget-cutting authority has been challenged in court on state constitutional grounds, and upheld on at least three occasions. In May 2010, the state's highest court, the Supreme Court, overturned Governor Tim Pawlenty's use of the power for certain appropriations in 2009. The court clearly reaffirmed the existence of such authority. But it found that the governor used the unallotment process inappropriately to achieve budgetary balance before the fiscal year had begun, rather than to deal with an unexpected shortfall during the year.[20] In the aftermath of that ruling, lawmakers began to consider proposals that would cap unallotments at 2 percent of general fund appropriations, and 10 percent within a particular appropriation.[21]

Ohio

Ohio state law requires the budget director to report each month on the status of receipts and expenditures, and not only permits but requires the governor to order spending reductions sufficient to prevent a deficit, under certain conditions.[22] Section 126.05 of the state's Revised Code provides: "If the governor ascertains that the available revenue receipts and balances for the general revenue fund for the current fiscal year will in all probability be less than the appropriations for the year, the governor shall issue such orders to the state agencies as will prevent their expenditures and incurred obligations from exceeding such revenue receipts and balances." In January 2008, Governor Ted Strickland imposed $733 million in midyear reductions, including some cuts to K-12 education.[23]

Oregon

Oregon law, amended just last year, gives the state Department of Administrative Services the power to reduce allotments to agencies with approval of the governor. Statute 291.261 requires the department and the governor to "follow legislative funding priorities as expressed in statutes and in the legislatively adopted or approved budget for the biennium." Unless statutes or the biennial budget indicate otherwise, "the department and the Governor shall assume that all General Fund appropriations have the same priority and shall reduce allotments of General Fund moneys for each state agency receiving General Fund moneys by the same percentage."

Governor Ted Kulongoski announced on May 25, 2010, that he planned to impose across-the-board agency reductions of up to 9 percent — including more than $200 million in school aid — after the state's chief economist reported revenue projections had fallen by some $560 million.[24]

Other States

As more governors respond to fiscal crises by exercising their authority to reduce appropriations, the lack of clear legal definitions in some states is producing uncertainty over the status of such steps. For example, New Jersey Governor Chris Christie has used the impoundment power aggressively. Soon after taking office in January 2010, Governor Christie signed an executive order directing the state's budget office to "identify and place into reserve items of appropriation ... in an amount sufficient to ensure that the State budget is in balance." In support of such executive action, he cited the state Constitution's requirement that the state maintain a balanced budget, and several statutes with relevant provisions — one of which, for example, authorizes the governor to freeze expenditures deemed to represent "extravagance, waste, or mismanagement." Some legislators and others have raised questions about the extent of the governor's legal authority to act unilaterally. "The governor's order is expected to be appealed to state courts," according to a February 10, 2010, news report.[25]

Executive impoundment power can be an effective tool in maintaining fiscal balance, but does not appear to shift policymaking influence from legislatures to governors, according to a study by James W. Douglas of the University of South Carolina and Kim U. Hoffman of the University of Central Arkansas.

"Gubernatorial impoundment authority is generally used to maintain balanced budgets during times of revenue shortfall," the authors wrote in a 2004 paper. "To a lesser extent, impoundments are used to promote fiscal responsibility. We also find that impoundments do not serve as an effective policy tool for governors in most states (e.g., they do not increase the governors' ability to promote their political agendas) because of political and structural restrictions placed on rescission authority and the weakness of impoundments relative to other gubernatorial powers."[26]

Gubernatorial Power to Manage the Budget in New York

New York's Constitution gives the governor clear leadership in formation of the annual budget, and clear responsibility for implementation and management of the financial plan. The chief executive's power to respond to fiscal emergencies once a budget is adopted, however, is limited — and poorly understood because it is not clearly outlined in law.

Section 1 of Article IV of New York's Constitution provides that "the executive power shall be vested in the governor.…" Section 3 of the same article provides, in part, that the governor "shall expedite all such measures as may be resolved upon by the legislature, and shall take care that the laws are faithfully executed." As Galie observes, these elements of the state's fundamental law "provide the governor with power to supervise and control the executive branch."[27] Section 4 of Article V empowers the governor to appoint and remove the top officers of all departments, with specified exceptions including the departments of education, law, and audit and control. Such powers, too, convey broad management authority over operations of the executive branch. Taken together, these constitutional provisions are sometimes cited as implying or necessitating some gubernatorial power to control agency spending without legislative approval.

Still, "under the State Constitution, the executive possesses no express or inherent power — based upon its view of sound fiscal policy — to impound funds which have been appropriated by the Legislature," the Court of Appeals found in a 1980 case, *Oneida v. Berle*.[28]

In Minnesota and some other states, gubernatorial authority to enact midyear budget cuts flows, in part, from constitutional requirements that the budget remain in balance through the year. Unlike many other states, New York's Constitution does not require adoption of a balanced budget or maintenance of fiscal balance through the year — and thus does not charge the governor or the Legislature with fulfilling such a responsibility. Article VII, the source of the governor's extensive authority over initiation and enactment of the annual budget, is silent as to implementation of the financial plan.

The state's statutes do outline additional powers not contained in the Constitution. The State Finance Law contains various sections providing executive authority. Of particular importance for discussion of midyear budget adjustments, Section 42 of the State Finance Law provides: "The several amounts appropriated in any act shall be deemed to be only for so much thereof as shall be sufficient to accomplish in full the purposes designated by the appropriations…"

While New York's Constitution does not provide specific authority for the governor to refuse to spend funds appropriated by the Legislature, governors did so consistently through much of the twentieth century. The decades from Smith's introduction of the Executive Budget process to Hugh L. Carey's leadership in

response to the mid-1970s fiscal crises for New York City and the state saw strong chief executives using a range of constitutional, statutory, and political powers to exercise broad control over fiscal and other policies. As Joseph Zimmerman has noted, "Until 1980 it was assumed that once the legislature approved appropriation bills, the governor was in charge of budget execution and was under no requirement to spend all the funds that were appropriated. In other words, the governor could order a freeze on spending for a specific purpose, including a freeze on the hiring of personnel."[29]

The Legislature itself did not question that assumption. In a 1985 law review article, the counsel to the New York State Senate Minority (then the Democratic members of the Senate), Eric Lane, wrote that executive impoundments represented an "excessive aggregation of executive power" and were not valid under the state Constitution. Nevertheless, the article observed that impoundments had been a "common" practice over time. Lane wrote that impoundments the Cuomo administration implemented in 1983-84:

> …reflected an executive practice at least informally condoned until this time by legislative acquiescence. As correctly stated by a spokesman for the Division of the Budget, "[the 1983-84 impoundments are] part of what the state has done and part of what the Legislature has watched happen for years. We didn't pick on these agencies. We did what we always do." What was unusual was the legislative response to a previously common executive practice.[30]

In the decades before the early 1980s, broad budget impoundment by New York's governors was a common practice.

By the early 1980s, the Legislature had begun to push back against executive impoundment by writing language into annual budget bills that required specific levels of staffing and otherwise attempted to reduce executive-branch discretion. Such steps did not question the governor's constitutional authority to impound appropriated funds in the absence of such language. Local officials in Oneida County and elsewhere took that issue to the courts, however. The resulting Court of Appeals decision in *Oneida v. Berle* remains the most important case law relating to executive impoundment in New York.

The case emerged from the Carey Administration's refusal to spend $7 million the Legislature appropriated in 1976 to aid municipalities in operating and maintaining sewage treatment plants. Speaking of the impoundment decision, the budget director stated that "action in this matter is one instance of a necessarily comprehensive effort to tighten State spending." As the Court of Appeals summarized the argument of the executive branch:

> The director urges that the Governor, as the Chief Executive Officer of the State, has an obligation to maintain a balanced budget throughout the fiscal year and, to accomplish that goal, possesses implied constitutional power to reduce duly enacted appropriations. Alternatively, respondents maintain that the appropriation statute invested the director with discretionary authority to withhold funds designated for the sewage treatment aid program.[31]

The state's highest court ruled against the executive branch, saying "…the executive branch may not override enactments which have emerged from the lawmaking process. It is required to implement policy declarations of the Legislature, unless vetoed or judicially invalidated."

While the text of the *Oneida v. Berle* ruling provides no exceptions to that requirement, three decades later a tacit understanding remains — that the Legislature will allow governors to make some unilateral budget reductions, as long as such actions are limited to the area of state agency operations.

That limitation renders a large majority of the budget untouchable. In fiscal 2010-11, under the proposed Executive Budget, state operations expenditures would total $20.4 billion, just over 25 percent of all expenditures aside from federal and capital funds.[32] In other words, any gubernatorial actions to address midyear gaps must ignore three-quarters of state expenditures. Major programs thus excluded include state aid to school districts and municipalities, Medicaid, funding for community colleges and City University of New York senior colleges, and the STAR property-tax relief program.

In both 2008 and 2009, Governor Paterson ordered state agencies to implement substantial current-year spending cuts. An August 2008 memorandum from then-Budget Director Laura L. Anglin to state department heads provides a detailed look at recent use of the impoundment power. Governor Paterson had ordered state operations spending reductions of 7 percent, or $630 million. Among other instructions for carrying out the governor's directive, the memo provided:

> As with our earlier efforts, agencies' 7% savings strategies should focus on delivering core programs more efficiently and eliminating non-core functions and non-essential spending. …
>
> In general, your approach to achieving the required savings must balance the following main objectives … Preserving significant policy/program goals to the extent possible, while still identifying opportunities for efficiencies …
>
> All agency programs and operations should be critically reviewed to identify opportunities to eliminate less essential activities and spending on non-essential items, increase efficiency and improve outcomes. You should identify fundamental cost-saving changes to provide recurring savings.
>
> … it is expected that agencies will propose increased attrition savings and reduced staffing levels. Current and planned staffing patterns should be evaluated to determine the optimal allocation of numbers and types of staff to specific functions. Lower-priority activities should be considered for elimination or reduced staffing.
>
> Significant NPS [nonpersonal service] economies must be achieved to help generate the State Operations savings required at this time. Spending must be limited to essential needs and all non-essential NPS must be eliminated. All NPS obligations must be approved by the agency head,

> either as specific transactions or pursuant to a plan approved by the agency head. Spending for technology acquisitions, office equipment and supplies, conferences, publications, travel (particularly out of state travel), and contractual services must be subjected to particular scrutiny, and should not be approved unless it is critical to sustaining the agency's core mission activities.[33]

Directions in the August 2008 memo were implemented by state agencies (perhaps to varying degrees) with little or no objection from the Senate, Assembly, or outside organizations that were affected by spending reductions. The impoundments appear to go well beyond the authority provided by Section 42 of the State Finance Law, which states that appropriations should be followed by actual expenditures only to the extent that is "sufficient to accomplish in full the purposes designated by the appropriations." The Budget Division asked agencies not to determine a level of expenditures necessary to carry out certain purposes, but instead to meet certain targets for spending reductions. Nor were reductions required to follow policy priorities expressed in appropriations by the Legislature; rather, agency leaders were instructed to determine "core" and "non-core" programs, along with "less essential" and "lower-priority" activities, and make significant funding decisions accordingly. If performed well, such assessments represent model leadership in public administration. It is unclear, however, whether they are supportable by existing statutory and case law in New York.

New York governors have no clear statutory authority even for the limited impoundment actions implemented in recent years.

Conventional wisdom in Albany often suggests that such gubernatorial authority is settled law. For example, a November 2009 *New York Times* article reported, "The Paterson administration has already squeezed the budgets of state agencies, an action it can take unilaterally."[34]

A handbook for state agency administrators that was published eight years after the *Oneida v. Berle* decision explained this point in more careful terms. The handbook, *Governing the Empire State: An Insider's Guide*, cited the provision in Section 42 of the State Finance Law regarding appropriations serving as an upper limit on spending, with the executive branch being expected to expend "only … so much thereof as shall be sufficient to accomplish in full the purposes designated by the appropriations." The authors of the handbook commented: "Of course, the question of what is needed to live up to legislative intent can be a controversial one."[35]

The handbook, produced by employees of the executive branch, went on to describe the practice that has developed in the wake of *Oneida v. Berle* and the resulting inability of the governor or Budget Division to make certain midyear cuts without legislative approval:

> Since over sixty percent of the state budget is used for assistance to local governments, when legislative, judicial, capital and debt-service appropriations are taken into account, DOB's flexibility is substantially restricted. Cuts necessary to maintain a balanced budget fall upon the operations

> (State Purposes) budget, magnifying the impact on state agencies.[36]

While *Oneida v. Berle* did not end the practice of governors making unilateral reductions in expenditures, it apparently led to more caution in the use of such power. *Governing the Empire State* also includes this observation:

> One DOB examiner stated that, in recent years, the practice of allocating an amount less than appropriated has become less common. The Legislature and DOB have to work together each year in the budget process. If Budget were routinely to allocate less than the amount appropriated, this would create unnecessary tensions between it and the Legislature, making everyone's job more difficult.[37]

Assembly Speaker Sheldon Silver has said the governor can unilaterally reduce expenditures by using layoffs or other measures to reduce the number of state employees: "He can manage the state work force in any way that he chooses. He doesn't need the Legislature to do that."[38] While having acquiesced to governors' reductions of nonpersonnel agency expenditures — including the impoundments of the past two years outlined above — the Legislature has not formally indicated a position on whether such impoundment is constitutionally permissible.

Should New York's Governor Have Clearer Authority to Address Midyear Gaps?

If inability to restrain the growth of spending is one cause of New York's chronic budget problems, and if midyear gaps are likely to occur with increasing frequency in the future, strengthening the governor's ability to deal with imbalances that arise after enactment of the annual budget may be one useful reform.

Such was the thinking behind one of the key recommendations proposed by Lieutenant Governor Ravitch in March 2010, as part of a broader plan to produce long-term, structural budget balance. The lieutenant governor proposed creation of an independent Financial Review Board to assess whether the state's financial plan is in balance or is making adequate progress toward structural balance. If the board were to find that the financial plan is not projected to achieve or maintain such balance, the governor and the Legislature would have 15 days to agree on remedial action. If such agreement were not forthcoming, the governor would have new power to "reduce current-year appropriations pro rata on a permanent basis, only to the extent necessary to achieve or maintain Balance." No reductions in appropriations for debt service, binding contractual obligations, or for the legislative or judicial branches would be permitted.[39]

How would such a new power for New York's governors work in practice?

The Ravitch proposal relates to "current-year appropriations." With the Minnesota controversy as informative context, such an approach would not change the existing gubernatorial

A Broad Grant of Authority to the Budget Division?

In the years after World War II, when the state was in the midst of a large capital construction program, the Budget Division began to use Certificates of Approval to authorize allocations from funds appropriated for specified purposes. The certificate process "permitted the Budget Director to control the rate of expenditure ... and facilitated the release of funds for individual projects on the basis of priority and urgency."[40] In 1995, the Executive Budget appropriation bills submitted by Governor Pataki's Budget Division added language formally extending the division's certification authority to all appropriations, no longer limiting the requirement to capital expenditures.

"That language made clear that payment of all appropriations are conditioned upon issuance of Certificates of Approval, and has been enacted by the Legislature in each appropriation bill thereafter, including all those set forth in the enacted budget for FY 2009-10," Budget Director Robert Megna wrote in an affidavit filed in a 2010 lawsuit challenging delays in state payments to school districts. "Specifically, all appropriation bills now contain the following language: 'No moneys appropriated by this chapter shall be available for payment until a certificate of approval has been issued by the director of the budget.'"

That broad grant of authority to the budget director is the law of the state (relative to each year's appropriations, at least), as enacted by the Legislature. One way to interpret such language would be to conclude that, if the budget director chooses not to issue a certificate of approval at all, the statutory language not only allows but requires appropriated moneys to be withheld permanently. An alternative argument could hold that, under *Oneida v. Berle*, such impoundment power is unconstitutional in the absence of more clear and detailed legislative delegation of power.

In filing a legal challenge when Governor Paterson delayed certain payments to school districts in 2010, the New York State United Teachers union and New York State School Boards Association argued: "The Executive Branch, which includes the Governor and the Division of the Budget, has no inherent, express, or discretionary power to permanently or temporarily impound funds that have been appropriated by the Legislature, or to otherwise delay the payment of such funding beyond the payment dates set by the Legislature...."[41]

Thirty years after the *Oneida v. Berle* ruling, and 83 years after creation of the Executive Budget process, that point remains unsettled.

powers in adoption of the annual budget. (Another element of the Ravitch plan would place new guidelines on governors' ability to propose statutory revisions within the Executive Budget.)

A number of states whose constitutions or statutes clearly allow for gubernatorial impoundment place specific limits on such authority. There are good arguments for such limitations. Governors can always call lawmakers into session to vote on large changes to enacted budgets. As described earlier in this paper, New York's Legislature enacted significant reductions to the 2009-10 financial plan at the request of Governor Paterson in late 2009. (Yet that same action illustrated that, at least sometimes, legislators find it difficult or impossible to take all the steps necessary to achieve budgetary balance. With no further action by the Senate and Assembly before the end of the fiscal year, the state began the 2010-11 year with $2 billion in liabilities that had simply been shifted from one fiscal year to the next — in effect, borrowing that amount from itself.)

Many states that allow governors to enact midyear reductions require such cuts to be the same percentage in a wide range of appropriations, or impose limitations on the amount to be taken from any individual area. Such provisions prevent an executive from favoring certain programs at the expense of the legislature's priorities. The Ravitch proposal echoes such requirements by calling for reductions to be made "pro rata," or by roughly equivalent proportions across agencies and programs.

The overall framework for executive and legislative authority over the budget is enshrined in the state Constitution. Amendment of the Constitution would be the strongest approach to clarifying the governor's responsibility and ability to maintain budgetary balance in case of midyear fiscal emergencies.

Pending any amendment, such provisions could at first be written into statute. Statutory authority alone, in the absence of constitutional change, might result in a court challenge to any governor's use of such power. The existing constitutional grants of budgetary and general executive authority to the governor would provide some defense against any such challenge. In *Oneida v. Berle*, the Court of Appeals left open the possibility that a limited legislative delegation of power could pass constitutional muster. The Carey administration had argued that the 1976 Legislature conferred such power on the executive branch with language in an appropriation bill that required certain approval by the governor's budget director before disbursements were made. The unanimous Court of Appeals rejected that argument, saying: "…the appropriation did not confer unfettered discretion upon the director to withhold all or any portion of the appropriation." It added: "Such a legislative delegation would be drastic indeed, and may not be inferred from ambiguous language. This is especially so in instances where the Legislature has provided no guidelines for the exercise of discretion." In other words, if the Legislature were to make a clear grant of budget-balancing authority to the governor, and provide guidelines for use of such power, the *Oneida v. Berle* precedent might be cited as evidence that such a delegation would be constitutionally permissible.

A new provision authorizing the governor to make midyear spending reductions, within limits, would also fit well within the overall concept of budget-making powers that Governor Smith and other reformers first envisioned nearly a century ago. Smith's plan — still the essential framework in New York — has elements of a bias in favor of achieving budgetary balance by limiting expenditures rather than encouraging higher taxes. The governor initiates the appropriation bills that the Legislature must use in adopting the budget. The Legislature may strike or reduce items of appropriation from such bills, and the governor has no authority to veto such changes. The Legislature may add items of appropriation, or increase the level of items the governor included in the Executive Budget. In such cases, the governor may veto new items or increases. The Legislature may override such vetoes, but

only with a super-majority of two-thirds in both the Senate and Assembly. Thus, either of the two branches may check the other's desire to increase spending, but the executive and Legislature must act together to approve such increases or to change the tax law.

Conclusion

Absent major policy changes, New York's budgetary environment is likely to be characterized for some years to come by significant imbalances between trendline growth in revenues and expenditures. The political environment in the state often makes it difficult for policymakers to achieve real budgetary balance in the environment of annual budget adoption. And increased volatility in the state's revenue system makes fiscal crises more likely than has been the case in the past.

Over the last decade, state policymakers have increasingly resorted to "fiscal manipulations" to balance the state's revenues and operating expenditures, according to the Office of the State Comptroller. Such manipulations include sweeps of non-General Fund accounts to produce more cash, off-loading of expenditures to other funds, and "temporary" loans from funds that were established to assure that certain revenues would go to pre-determined purposes.

"This 'deficit shuffle' reduces budget transparency, creates funding instability for critical State programs and allows the State to avoid making the difficult decisions needed to effectively align spending with available revenue," according to a report by the comptroller's office. Some $6.4 billion in the 2009-10 budget resulted from sweeps of dedicated funds, temporary loans, use of debt rather than pay-as-you-go capital financing, and other "gimmicks," the report found.[42]

Numerous other states avoid or reduce the need for such practices by giving chief executives the responsibility and authority to maintain fiscal balance by reducing appropriated expenditures in moderate amounts when necessary. In New York, longstanding informal agreement between the Legislature and the executive branch permits use of such impoundment power, only for operations expenditures by executive agencies. While limited, such authority plays an important role in the governor's ability to reduce fiscal imbalances — as the state has seen clearly over the past two years.

Informal understandings, however, are not a secure legal basis for such authority. In the past year, public-employee unions and recipients of state funding have challenged gubernatorial authority to act in two related areas — delays in payments to school districts, and furloughs for state employees. There is every possibility that, as the state deals with continuing fiscal challenges, the longstanding use of executive impoundment power may also come under judicial challenge. Legislation and/or constitutional amendment could usefully clarify the status of this existing gubernatorial power.

While the Ravitch plan does not spell out details, it would provide firm legal authority for existing impoundment practices while extending such powers further. In addition to the lieutenant governor's recommendations, Assembly Speaker Sheldon Silver has proposed expanding the governor's powers to address midyear budget gaps. The Assembly Majority's fiscal reform legislation, A. 10408 introduced in March 2010, empowers the state budget director in certain circumstances "upon consultation with the comptroller, the chair of the Senate Finance Committee and the chair of the Assembly Ways and Means Committee … to exercise his or her powers to segregate budgeted appropriations as if a sufficient pro rata reduction to rectify such imbalance had been implemented via amendments to all state fiscal year appropriations except appropriations required to pay debt service or appropriations for the operation of the legislative and judicial branches of state government."

As policymakers consider proposals to expand gubernatorial impoundment authority, key questions include:

- How would broader impoundment actions be triggered? Options include a determination of imbalance by the governor alone; by the governor and the Legislature (or chairs of the legislative fiscal committees); by the governor with approval of the comptroller; and by an independent board of experts who would be appointed by the governor, legislative leaders and comptroller. Currently, the governor may impound state agency operations expenditures entirely on his own initiative.
- Would the impoundment power cover aid to school districts and local governments, as is the case in Massachusetts, Ohio, Oregon, and some other states?
- Would such authority be limited to a certain percentage of appropriations? In fiscal 2009-2010, when Governor Paterson and the Legislature faced sizable midyear budget gaps that were only partially addressed by legislative action, impoundment of up to 10 percent of state-funds appropriations would have allowed the governor to reduce spending by $7.8 billion; a 5 percent limit would have permitted impoundment of $3.9 billion. The state closed out the 2009-10 fiscal year by rolling $2 billion of unmet liabilities into the following year. Executive authority to eliminate those liabilities would have required impoundment of roughly 2.5 percent of state-funds appropriations.
- Should notice to the Legislature be required before spending reductions take effect, to allow the opportunity for legislative-executive action before executive-only impoundment?
- If the chief executive has only strictly limited authority to reduce expenditures, how can the state respond if

available cash is depleted — as the Budget Division and the Office of the State Comptroller have said could happen this year?

Ultimately, achieving and maintaining structural budgetary balance in New York will likely require a new political culture — one that makes a priority of fiscal integrity, rather than support for increased spending and opposition to new revenues. Clarifying and strengthening executive authority to manage midyear fiscal imbalances may help solve looming gaps while promoting such a change in the political culture.

Endnotes

1 The financial plan, a comprehensive estimate of projected financial resources and spending requirements, is what most nonspecialists would consider "the budget." The "budget" proposed by the governor and adopted by the Legislature is actually a series of bills containing appropriations and changes to state laws governing revenues and use of appropriated funds; the governor's Budget Division constructs the financial plan based on those appropriations, statutory changes, and understanding of legislative intent.

2 Thad Beyle, "Governors' Institutional Powers 2007," accessed online March 25, 2010, at http://www.unc.edu/~beyle/gubnewpwr.html.

3 New York State Constitution, Article VII, Section 4.

4 *Becker et al. v. Paterson et al.*

5 Office of the State Comptroller, *Comptroller's Fiscal Update: Closeout Analysis of State Fiscal Year 2009-10*, April 2010.

6 See, for example, U.S. Government Accountability Office, *State and Local Governments' Fiscal Outlook: March 2010 Update*, report # GAO-10-358, March 2, 2010.

7 Richard Mattoon and Leslie McGranahan, "Revenue Bubbles and Structural Deficits: What's a State to Do?" Federal Reserve Bank of Chicago Working Paper 2008-15, November 1, 2008.

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25 Claire Heininger and Lisa Fleisher, “NJ governor Chris Christie freezes spending to address budget gap,” *The Record*, Woodland Park, NJ, February 10, 2010.

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28 *County of Oneida, et al., v. Berle*, 49 N.Y.2d 515 (1980). Peter Berle was the state commissioner of environmental conservation, charged with administering state funding for a sewage treatment program. When the Carey administration attempted to halt funding that had been approved by the Legislature, county officials in Oneida and other counties sued to restore the program.

29 Joseph F. Zimmerman, *The Government and Politics of New York State*, New York University Press, New York, 1981; p. 315.

30 Eric Lane, “Legislative Oversight of an Executive Budget Process: Impoundments in New York,” *Pace Law Review* 5:2, Winter 1985; p. 215.

31 *Oneida v. Berle*, ibid.

32 New York State Division of the Budget, *2010-11 Executive Budget Five-Year Financial Plan*, pp. 13 and 19.

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36 Ibid., p. 52.

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