

**NASSAU COUNTY
OFFICE OF THE COMPTROLLER**



**REPORT ON THE COUNTY'S FINANCIAL CONDITION
FOR THE FIRST SIX MONTHS OF FISCAL YEAR 2007**

**Howard S. Weitzman
Nassau County Comptroller**

July 31, 2007

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NASSAU COUNTY
OFFICE OF THE COMPTROLLER

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REPORT ON THE COUNTY'S FINANCIAL CONDITION FOR THE FIRST SIX MONTHS OF FISCAL YEAR 2007

Executive Summary

The Nassau County Charter requires that the Comptroller report on the status of the budget for the first six months of the current fiscal year, and give an opinion concerning whether there will be a surplus or deficit at year-end (Charter §402[9]). This mid-year report for the County's fiscal year 2007 also presents comments on certain estimates included in the County's Multi-Year Financial Plan Update for the years 2007-2010.

Our analysis of revenues and expenses through the end of June, together with our forecast for the remaining six months of fiscal year (FY) 07, indicates that the County will finish the year on budget, possibly achieving a small budgetary surplus for its primary funds.¹

These results will only be achieved if the County Executive aggressively controls expenditures through year-end and if the administration and Legislature agree to use dedicated reserves to fund higher than budgeted police termination pay obligations, if needed.

¹ The County's primary funds now consist of the General Fund, Fire Safety, Debt Service, Police Headquarters and Police Districts. The FY 07 budget consolidated the Recreation and Parks Fund into the General Fund.

TABLE 1

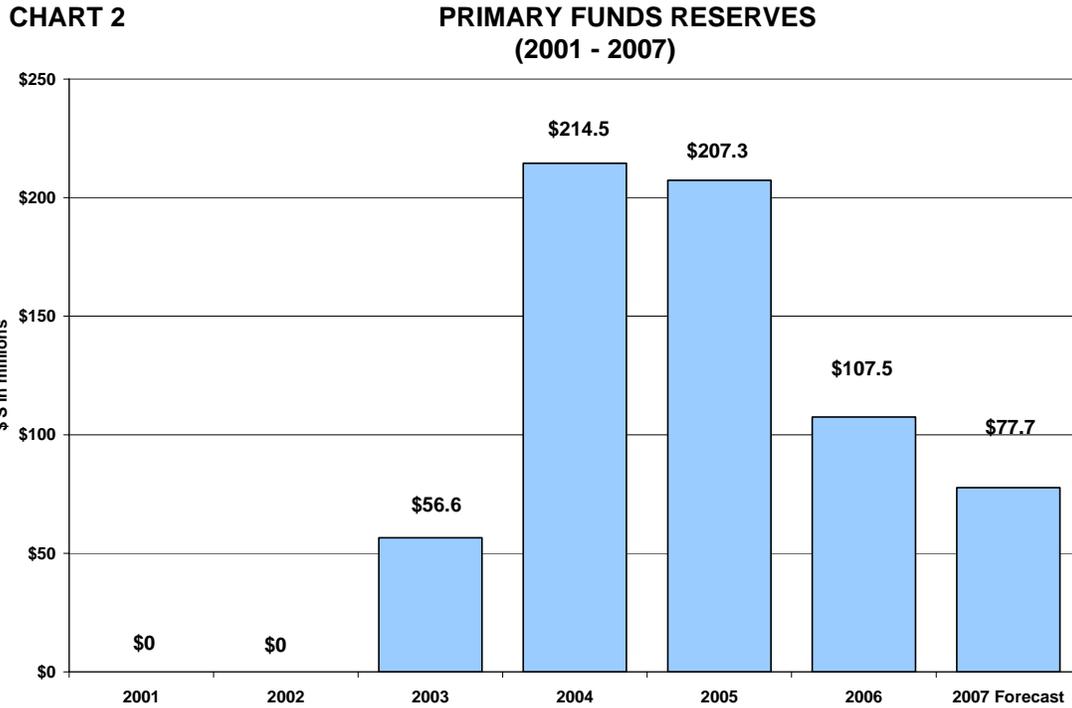
Revenue and Obligations Forecast for 2007*
(\$'s millions)

	2007 Budget	2007 Projected Actual	Variance
Revenues:			
Sales Tax	\$ 1,030.9	\$ 1,017.1	\$ (13.8)
Property Tax	758.4	761.8	3.4
State and Federal Aid	307.0	302.9	(4.1)
Tobacco Settlement	23.6	23.6	-
Other Revenues	<u>739.1</u>	<u>747.7</u>	<u>8.6</u>
 Total Revenues	 <u>2,859.0</u>	 <u>2,853.1</u>	 <u>(5.9)</u>
 Obligations:			
Payroll and Fringe Benefits	1,260.4	1,271.3	(10.9)
Debt Service	299.9	297.4	2.5
Social Services	373.5	362.1	11.4
Other Obligations	<u>925.2</u>	<u>925.8</u>	<u>(0.6)</u>
 Total Obligations	 <u>2,859.0</u>	 <u>2,856.6</u>	 <u>2.4</u>
 Administrative Actions:			
Use of Termination Pay Reserve			7.9
Additional Capital Reserves			<u>1.4</u>
 Projected Surplus after Administrative Actions			 <u><u>\$ 5.8</u></u>

* This forecast includes the following five county funds:
General, Police Headquarters, Police District,
Debt Service, and Fire Prevention, Safety, Communication and Education

Our analysis projects a \$13.8 million shortfall in sales tax revenues. This estimate is based upon growth of 3 percent for the balance of 2007 on top of the 1.9 percent growth experienced in the first six months. The County originally budgeted 3.9 percent growth for the full year. If the growth in sales tax continues at 1.9 percent, it could increase the shortfall and eliminate the potential surplus. We also project that police termination pay will be \$12.9 million over budget, based on the number of officers who have already filed for retirement this year. The administration has provided us with their plan to address the projected shortfalls, should they materialize. The plan is identified as "Administrative Actions" in Table 1.

In 2003 – 2006 the County conservatively used its annual surpluses to establish reserves that it has been drawing on to provide budget relief. We estimate the balance of these reserves will decline from \$214.5 million at the end of 2004 to \$77.7 million at the end of FY 07 (see Chart 2 below).



The 2007 balance of reserves is detailed below:

YEAR END 2007 PROJECTED RESERVE BALANCES	
\$'s Millions	
Pension Savings Reserve	\$ 25.0
Reserve for Future Medical Expense	
Tobacco Settlement Revenues	34.1
Interest earned on Tobacco Settlement Revenues	2.1
Litigation Reserve	3.0
Employee Benefit Reserve	13.5
Total Projected Year End 2007 Reserve Balances	<u>\$ 77.7</u>

The use of each type of reserve is shown on the following table:

TABLE 2					
Reserves - Primary Funds					
Source (Use)					
(\$'s Millions)					
Source of Reserve (Use of Reserve)	2003	2004	2005	2006	2007
<u>Pension Savings Reserve (major funds)</u>		\$ 78.5			
Replenish reserve			\$ 24.8	\$ 16.0	
(Payment of pension expense)			(34.4)	(33.5)	\$ (26.5)
<u>Funds Reserved for Pension Bond Retirement</u>	\$ 18.1				
(Payment of pension bonds)		(9.9)	(8.2)		
<u>Reserve for future medical expense</u>					
Unpledged TSR's and Settlement Interest			0.7	1.6	43.0
Current year Tobacco receipts		23.6	(23.0)	(23.0)	(23.6)
Balance of Tobacco funds available		37.0			
<u>Reserve for payment of debt service</u>		10.0			
(Use of reserve)			(10.0)		
<u>Reserve for bond indebtedness</u>		25.0	0.7		
(Use of reserve)				(10.9)	(14.8)
<u>Reserve for litigation</u>		3.3	3.0		
(Use of reserve)			(3.3)		
<u>Funds set aside for police terminations</u>	38.5				
(Release of reserves to establish Employee Benefit Accrued Liability Reserve Fund)		(28.9)			
(Anticipated 2004 termination costs)		(7.0)			
(Purchase of additional police vehicles)		(2.3)			
(Deficit fund balance)		(0.3)			
<u>Employee Benefit Accrued Liability Reserve Fund</u>		28.9	(7.5)		(7.9)
<u>Transitional reserve</u>					
Reserve for Retirement of Bonds			35.0		
Recovery of 2003 sewer charges			15.0		
Appropriation of Fund Balance					25.0
Use of Fund Balance for Property Tax Refunds					(25.0)
(Use of reserve)				(50.0)	
Total source	\$ 56.6	\$ 206.3	\$ 79.2	\$ 17.6	\$ 68.0
Total use	-	(48.4)	(86.4)	(117.4)	(97.8)
Balance	\$ 56.6	\$ 214.5	\$ 207.3	\$ 107.5	\$ 77.7

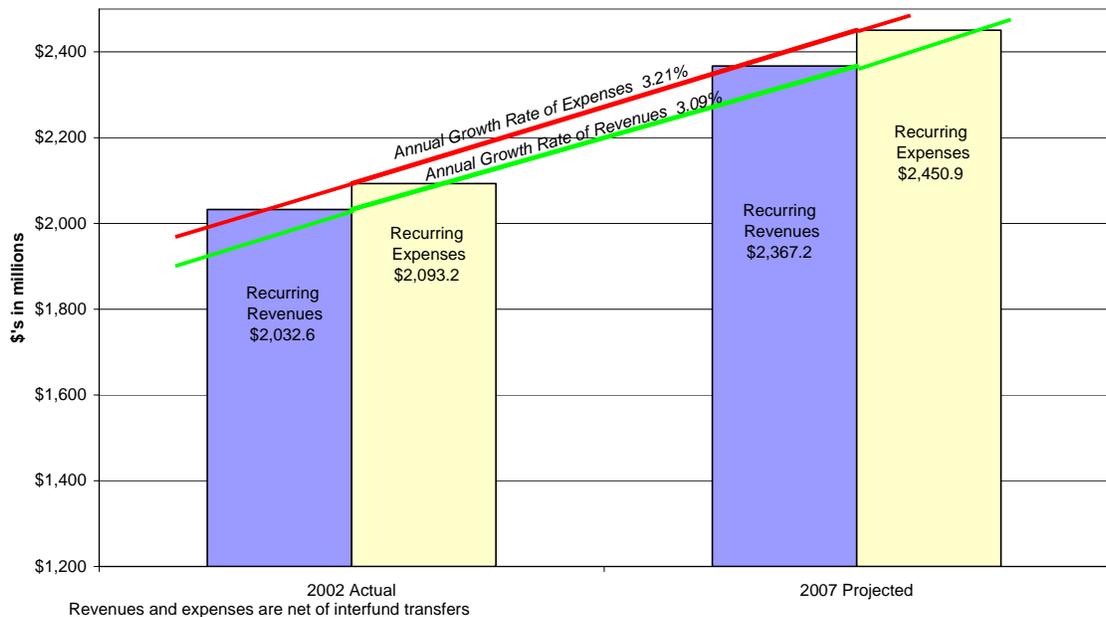
The 2008 budget will create challenges for the administration and Legislature. Sales tax receipts have softened, and economic forecasts do not anticipate a more robust local economy in 2008. The lower than anticipated increase in sales tax receipts in 2007 also provides a lower baseline for future years.

We project FY 07 police termination pay will be over budget, and will require further depletion of available reserves. Police retirements are likely to increase again in 2008 because of the impact of the Police Benevolent Association (PBA) arbitration award's capping of termination pay at two times salary, which takes effect in 2009. It is likely that the Police Headquarters reserve will be exhausted in 2007, putting increased pressure on the 2008 budget to fund Headquarters termination expense.

The PBA award achieved targeted first year savings in 2007 when contingency reserves are taken into account. However, the Updated Multi-Year Plan does not include these contingency reserves and achieving targeted labor savings will be more difficult in 2008 and thereafter.

The County does not generate enough recurring revenue to cover its recurring expenses. Since 2002, the Suozzi administration faced with double digit growth in pension, Medicaid and employee health benefit costs, still managed to keep annual County expenditures to a compounded growth rate of only 3.21 percent. Even at this rate of increase, however, expenses have grown faster than the County's recurring revenues, which, as shown in Chart 3, grew at 3.09 percent.

CHART 3 ANALYSIS OF GROWTH OF RECURRING REVENUE & EXPENSES 2002 - 2007
(000's omitted)



In addition, since 2004, the County has incurred two major recurring expenditures for which no permanent revenue sources were provided: an increase of approximately \$100 million per year to our pension contribution beginning in 2005; and the inclusion in the operating budget of \$50 million in real estate tax refunds that were previously bonded, starting in 2006. The County has used reserves to help fund these cost increases. Since the current reserves dedicated to pension and real estate tax refund payments will

be depleted at the end of FY07, new sources of recurring revenues must be identified. The administration had supported various initiatives at the State level that would have had the effect of increasing recurring revenues and closing the structural gap in 2008, including an increase in the cigarette tax, a unified filing fee for county clerks and red light cameras. Because the State Legislature has not yet enacted any of the proposals into law, the structural gap has not improved. Without State legislative assistance, the County will find it difficult to fund all the services it currently provides in the 2008 budget.

SIGNIFICANT VARIANCES - Revenues

Tax Revenues

Sales Tax

Gross sales tax receipts are projected to total \$1.016 billion, which is \$13.8 million less than the \$1.0298 billion adopted budget. (For presentation purposes we do not include the deferred portion of the part county sales tax of \$1.1 million which is included in budgeted total sales tax). Growth in sales tax receipts is lower than the 3.9 per cent rate assumed in the 2007 budget, rising 1.9 percent over 2006 receipts in the first six months of the year. Our \$1.016 billion forecast is based on 3 percent sales tax growth during the second half of 2007.

The Multi-Year Financial Plan Update Fiscal 2007 - 2010 includes a revised 2007 sales tax projection of \$1.0258 billion, which represents a decrease from the adopted budget of \$5.1 million, and revised future estimates calculated using this new base. Total sales tax growth in 2007 through 2010 is projected at approximately 3.5 percent. The actual outcome of this assumption will have to be monitored. The County will always be vulnerable to a potential sales tax shortfall, since sales tax, at 42 percent of budgeted revenues net of inter-fund transfers, is the County's largest revenue source and actual results are subject to uncontrollable economic factors.

SALES TAX			
(\$'s in millions)			
	JULY 1 YTD Sales Tax Collected	% July 1 YTD vs total collected/projected	GROSS ANNUAL Sales Tax Collected/Projected*
	(\$'s in millions)		(\$'s in millions)
2001	\$351.9	42.3%	\$831.9
2002	358.0	41.4%	865.5
2003	362.2	40.4%	895.5
2004	392.0	41.7%	939.9
2005	392.1	41.1%	953.8
2006	415.6	41.9%	991.2
2007	423.5	41.7%	1,016.0

* 2007 projected is net of the deferred part county sales tax of \$1 million

Property Tax

Property tax revenue is projected to be \$3.4 million more than the \$758.4 million adopted budget. The amount over budget has been generated primarily by the expiration of assessment exemptions upon sale of properties.

PROPERTY TAX				
(EXCLUDING SEWER DISTRICT FUND)				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$739.6	\$758.4	\$761.8	\$761.8	\$3.4

Although the value of the assessment roll has increased, total property tax revenues for all funds including the county-wide sewer and storm water district have not increased since 2003.

Non-Tax Revenues

Investment Income

The County typically invests available funds in interest bearing checking accounts and bank certificates of deposit. Because the Federal Funds Rate has risen and the County has more available cash to invest, the County and the Nassau Interim Finance Authority have had higher interest earnings. We forecast investment income will be \$7.1 million over the \$19.8 million budget.

INVESTMENT INCOME				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$25.2	\$19.8	\$8.3	\$26.9	\$7.1

State Aid

In total, state aid is projected to be \$2.8 million under the FY 07 adopted budget of \$195.5 million.

\$4.1 million of budgeted reimbursement for Fashion Institute of Technology payments will not be received since it was not included in the current New York State budget. In addition, we estimate reimbursements for social services direct assistance will be \$2 million under budget resulting from decreases in the number of Temporary Assistance for Families (TANF) cases and static daycare cases, which were budgeted to increase.

These shortfalls will be partially offset by reimbursements for Department of Health preschool special education programs, which we estimate will be \$3 million over budget. As discussed in the Early Intervention / Pre-School Special Education section

below, related expenses are projected to be over budget, as a result of rate increases for center based programs.

STATE AID INCOME (\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$187.8	\$195.5	\$41.1	\$192.7	(\$2.8)

Permits and Licenses

For 2007, we project a shortfall of \$2.5 million against the \$13.5 million budget for permits and licenses revenue. This is due to lack of State legislative approval for a licensing program for plumbers and electricians.

PERMITS AND LICENSES (\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$10.5	\$13.5	\$5.7	\$11.0	(\$2.5)

Departmental Revenue

We project that departmental revenue in the County Parks Department will be \$4.7 million under budget. The budget included aggressive estimates in addition to revenues from fee increases which have not been adopted by the County Legislature. We estimate that this shortfall will be partially offset by several factors. Based on 2006 and year-to-date 2007 Police Headquarters ambulance fee receipts, we project ambulance fees will exceed the budget by approximately \$900 thousand. We also project that Civil Service Commission fees will be \$900 thousand over budget as a result of the large turnout for the test for police officer candidates, in addition to smaller amounts over budget in several other County departments.

DEPARTMENTAL REVENUE (\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$84.4	\$88.0	\$40.5	\$86.4	(\$1.6)

Federal Aid

Federal Aid is projected to be \$1.3 million under the \$111.5 million adopted budget. We estimate reimbursements for social services direct assistance will be \$3.1 million under budget as a result of a reduction in associated costs resulting from decreases in the number of Temporary Assistance for Families (TANF) recipients. We project that this will be partially offset by \$2.7 million for unbudgeted reimbursement at the County corrections facility from the State Criminal Alien Assistance Program.

FEDERAL AID INCOME				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$115.2	\$111.5	\$10.6	\$110.2	(\$1.3)

SIGNIFICANT VARIANCES - Obligations

Labor Costs

In total, payroll and fringe benefit expenditures are projected to be approximately \$10.9 million over the adopted \$1.3 billion FY 07 budget. This estimated shortfall is comprised primarily of police termination pay, projected to be \$12.9 million over budget. The 2007 budget projected 84 police retirements. As of mid July, 99 police officers have filed for retirement. The administration has informed us that if this trend continues, they plan to utilize \$7.9 million of available termination pay reserves as follows: \$5.6 million in the Police Headquarters Fund, which fully exhausts the reserve, and \$2.3 million in the Police District Fund, which leaves a balance of \$13.5 million. The use of these reserves requires legislative approval.

The Police Benevolent Association labor contract, which expired December 31, 2006, has been resolved by an arbitration award. Our analysis includes projected budget savings from this award. Although all of the salary savings included in the FY 07 budget will not be achieved, the difference will be covered by contingency reserves contained in the fringe benefit budget.

The labor contract with the Detectives Association Inc. (DAI) expired on December 31, 2006. We project that a DAI arbitration award will parallel the PBA award. A tentative collective bargaining agreement for the period 2005 through 2010 has not yet been reached with the Sheriffs Officers Association (ShOA). The current contract expired on December 31, 2004. Negotiations for a new ShOA contract are currently at an impasse. However, our projection for ShOA salaries includes a 3.5% half year raise for 2005, 3.7% for 2006 and 3.6% for 2007, based upon the proposed memorandum of agreement rejected by the legislature. Labor costs for the Civil Service Employees Association and Superior Officers Association are based on the current collective bargaining agreements, which expire on December 31, 2007.

SALARIES and FRINGES (\$'s in millions)					
	2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
Salaries	\$801.6	\$827.0	\$417.0	\$856.1	(\$29.1)
Fringes	<u>379.1</u>	<u>433.4</u>	<u>261.3</u>	<u>415.2</u>	<u>18.2</u>
Total Salaries and Fringes	<u>\$1,180.7</u>	<u>\$1,260.4</u>	<u>\$678.3</u>	<u>\$1,271.3</u>	<u>(\$10.9)</u>

POLICE TERMINATION					
(\$'s in millions)					
	2006 Actual	2007 Budget	2007 filed as of June	2007 Forecast	Variance
Termination Pay					
Police District	\$5.2	\$9.5	\$8.7	\$11.8	(\$2.3)
Police Headquarters	18.1	10.1	13.8	20.7	(10.6)
Total Termination Pay	<u>\$23.3</u>	<u>\$19.6</u>	<u>\$22.5</u>	<u>\$32.5</u>	<u>(\$12.9)</u>
Officers Retired					
Police District	21	42	38	51	(9)
Police Headquarters	51	42	55	79	(37)
Total Officers Retired	<u>72</u>	<u>84</u>	<u>93</u>	<u>130</u>	<u>(46)</u>

Overtime

Overtime costs for the Police Department and the Correctional Center total \$23.2 million through the end of June 2007. Overtime for these two departments is projected to be over the \$60.9 million adopted budget by \$3.1 million. This shortfall is comprised of \$3.6 million in the Police Headquarters Fund, and \$1.3 million in the Correctional Center, partially offset by Police District Fund overtime projected to be \$1.8 million under budget. (These overtime estimates are included in the total salary amounts presented above.)

OVERTIME					
(\$'s in millions)					
	2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
Police District	\$21.4	\$22.5	\$6.3	\$20.7	\$1.8
Police Headquarters	22.4	17.7	7.1	21.3	(3.6)
Correctional Center	22.6	20.7	9.8	22.0	(1.3)
Total	<u>\$66.4</u>	<u>\$60.9</u>	<u>\$23.2</u>	<u>\$64.0</u>	<u>(\$3.1)</u>

Fringe Benefits

Health Insurance

The FY 07 budget includes an estimated health insurance rate increase over 2006 of 7 percent for active employees and 3.2 percent for retirees. Actual rate increases were approximately 6.4 percent for active employees and 2 percent for retirees. As a result, we project that health costs will be \$3.9 million under budget.

Working in conjunction with the administration, the Comptroller's Office plans to implement Governmental Accounting Standards Board Statement No. 45 – *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than*

Pensions (GASB 45), during 2007. As a result, for the first time, the County’s Comprehensive Annual Financial Report will include a valuation of the total liability for health insurance for retired County workers, calculated based on the estimated lives of current and projected new retirees. While this amount will have no direct budgetary impact, it will highlight the increasing annual payments for retiree health benefits and bring attention to the cost of providing this fringe benefit.

We were pleased to see that the recent PBA arbitration award eliminated duplicate health insurance coverage as recommended in our report “*Dual Health Insurance Family Coverage for County / NHCC Employees*”.² Additional options for savings are presented in the Comptroller’s Audit Advisory Committee report “*Providing Affordable Health Benefits for County Employees and Retirees*”.³

HEALTH INSURANCE EXPENSE (\$'s in millions)					
	2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
Active employees	\$101.5	\$111.9	\$54.3	\$108.0	\$3.9
Retired employees	78.2	80.4	39.7	79.7	0.7
NHCC retired employees	17.9	17.6	7.2	18.3	(0.7)
Total	\$197.6	\$209.9	\$101.2	\$206.0	\$3.9

Workers’ Compensation

Expenditures for workers’ compensation are projected to be \$21.7 million, \$1.7 million over the \$20 million adopted budget. Our estimate is based on the first half of 2007, during which medical bill payments have been higher than estimated in the budget.

WORKERS' COMPENSATION EXPENSE (\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$21.2	\$20.0	\$6.9	\$21.7	(\$1.7)

² <http://www.nassaucountyny.gov/agencies/Comptroller/NewsRelease/2006/06-05-06.html>

³ http://www.nassaucountyny.gov/agencies/Comptroller/Docs/PDF/Cost_Saving_Initiatives121306.pdf

Social Services

Medicaid

The County is currently operating under the new State Medicaid Cap, which became effective in 2006. After 2008, the County has an option of paying an annual Medicaid increase of 3% per year. In lieu of this option, the County could elect to provide the State with a calculated percentage of sales tax revenue. This second option would prove financially desirable only if future sales tax revenue increased at less than 3 percent per year.

MEDICAID EXPENSE (\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$212.6	\$218.0	\$124.0	\$218.0	\$0.0

Early Intervention / Pre-School Special Education

The early intervention / pre-school special education programs administered by the Department of Health are projected to be over budget by approximately \$5.5 million. This is primarily the result of higher than budgeted rate increases, granted by New York State, for center based programs. The rate increases were set after the County's budget was adopted. The increase in this expense will be partially offset by approximately \$3 million of state aid.

EARLY INTERVENTION / PRE-SCHOOL EDUCATION (\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$154.9	\$153.5	\$146.3	\$159.0	(\$5.5)

Direct Assistance

We project that direct assistance programs administered by the Department of Social Services will be \$11.4 million under the \$155.5 million budget. Our estimate is based on a 7 percent reduction in the Temporary Assistance for Families (TANF) caseload and a static number of daycare cases which were budgeted to increase, partially offset by a 5 percent increase in Safety Net cases.

DIRECT ASSISTANCE					
(\$'s in millions)					
	2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
Recipient Grants	\$ 50.0	\$ 53.7	\$ 24.5	\$ 48.2	\$ 5.5
Purchased Services	42.0	47.9	32.4	42.0	5.9
Vendor Payments	51.3	53.9	40.6	53.9	-
Total Direct Assistance	\$ 143.3	\$ 155.5	\$ 97.5	\$ 144.1	\$ 11.4

Other Obligations

Our analysis indicates that other obligations will be \$13.3 million under the adopted budget, resulting primarily from contingency reserves which will be transferred to cover shortfalls elsewhere in the budget.

OTHER OBLIGATIONS				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$42.8	\$43.7	\$22.5	\$30.4	\$13.3

Utilities

We estimate that utility costs will be close to budget. The budget included General Fund expenses and reimbursements for Community College electricity costs. The college however, began paying for electric bills directly, resulting in offsetting utility and interfund revenue budget variances, which have no impact on the County's bottom line.

UTILITY COSTS				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$39.2	\$42.2	\$20.8	\$38.4	\$3.8

Debt Service

After the FY 07 budget was adopted, OMB's calculations used to charge NIFA issued debt to County funds were modified, resulting in a \$2.5 million variance in both

interfund revenues and debt service expenditures. This change had no impact on the County's bottom line since the resulting budget variances are offsetting.

Interest on bond anticipation notes is projected to be \$440 thousand over budget, as a result of the timing and sizing of the FY 07 BAN borrowing varying from estimates included in the adopted budget.

DEBT SERVICE				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$290.6	\$299.9	\$68.8	\$297.4	\$2.5

Contractual Obligations

Contractual obligations are projected to be \$4 million more than the \$133.6 million adopted budget. Contributing to this variance are unbudgeted contracts or extensions in the amount of \$2.7 million for medical care for inmates at the correctional center due to an increase in the number of inmates treated and the mix of services provided, \$700 thousand for the third party administrator for workers compensation, \$600 thousand for financial advisors, Public Financial Management and \$300 thousand for the law firm of Manatt, Phelps & Phillips, the consultant on matters relating to health care,.

CONTRACTUAL EXPENSE				
(\$'s in millions)				
2006 Actual	2007 Budget	2007 YTD June	2007 Forecast	Variance
\$134.5	\$133.6	\$68.8	\$137.6	(\$4.0)

Property Tax Refunds

The 2007 budget included \$50 million to pay real property tax refunds. At the end of 2006, the County accrued \$19.5 million for the current portion of unpaid refund claims. The expense for 2007 will be comprised of the amount actually paid out during the year adjusted by the changes in the year-end accrual. The County has paid out \$29.7 million for the first seven months of 2007. The administration has advised that due to the existence on the court calendar of cases involving large potential refunds and increased efficiencies in processing refund payments, it is possible the County may incur more expenses than the \$50 million included in the FY 07 budget.

