SAVING TAX DOLLARS ON CAPITAL SPENDING AND ECONOMIC DEVELOPMENT PROGRAMS IN NEW YORK STATE

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Thank you Ericka and thank you EJ, for making this event possible.

Since leaving state government a little over a year ago I have had the great pleasure of consulting for the New York City Partnership. Kathy Wylde and her organization have given me the opportunity to continue working on a lot of the ideas I cared about when working for government. So, I want to thank her publicly for that chance.

I agreed to be part of this event today because I am, like most of you, worried. For over the past twenty years my work has been to support all of the major forms of spending on education, health, environment, public assistance, affordable housing, the state workforce and economic development..

After you spend sometime in the Comptroller's office if you are alert to it, you realize most of these worthy efforts have become captives of mission drift.

Once good ideas, a lot of the spending deemed as important to progressive government have become wasteful, insulated and impervious to change.

I have two topics today, but they are really the same – I am to address how money can be saved as we spend on capital projects --- and what could be done to save money on the state's economic development programs.

Each issue addresses a different way that state expenditures interact with the private economy.

So, let's get to the capital spending side of the discussion.

Some numbers are useful to start:

- DOB projects annual capital outlays of just over $9 billion between now and 2013 -- that is $56 billion – about $24 billion will be financed with pay as you go contributions, and the rest by debt.
- The MTA Capital budget anticipates spending at $8 billion per year… local governments $1.6 billion annually…. NYC - $3 billion annually and IDA's approximately $700 million annually.

Not all debt goes to capital expenditures. These admittedly crude and incomplete numbers place spending at upward of $24 billion annually.

If we review the many reports from state and local government school districts and public authorities, this capital spending supports an impressive set of projects. For the most part, these projects are not only evidence that government is working to improve communities, the level and type of projects also stimulate our economy –for the construction trades and the financial services industry. -

But, let me be blunt: there is far too much waste in the way we spend these dollars. Ironically, most of the waste is created by rules and regulations we have adopted to protect against waste.

Unfortunately, I only have ten minutes, but if you want to know why we have the government contracting rules we have today – you can start with Kenneth Ackerman's recent biography of Boss Tweed.

The basic theory of government contracting assumes that through competitive bidding, based on objective design specifications – the state receives a market price from a credible vendor. It is a good idea. When I served at the Comptroller's Office we saw a large part of our work as helping the state determine if it had in fact received a market price for a given product or service.

However, the rules have grown too cumbersome over the years to handle a new, dynamic economy. Consequently, on major capital projects there are too few bidders. Last week I read in the papers where a huge water system project in New York City had skyrocketed in cost, in part, because there were too few bidders. The rules have been around so long that anyone who plays the game has figured out how to abuse them.?

Large private sector builders are now global in their reach. They can forego New York's large, but not large enough capital program --- and they do. What that means is that the State is not getting a market price. It is getting the price that those who wish to bid will charge. The system is broken.

Our state contracting officials know this, the contracting community knows this, our political leaders know this --- and nothing changes. Last week I attended an AIA conference that put the waste factor at somewhere between 2% and 15% . The meeting was held in a small room that was only half full up the street at Rockefeller College. None of the major contracting agencies were there.

We do not need another study. New York State and New York City pay more than the rest of the country for heavy capital projects and that is unacceptable.

If the state has the appetite for real change, and it should, it could adopt the American Bar Associations 2007 Model Code for Public Infrastructure Procurement. There are many practices outlined in this code that would save money. It would also take some getting used to by state procurement professionals. But the effort is worth it.

If the state decides it must study this code and waste more time, than there are other smaller ways to reform the system in the short term.

1. A few years ago the Comptroller asked for a new flexibility in the state's procurement rules. Make those changes. This would at least allow for some experimentation with some of the procurement models that are contained in the model code.

2. Pay construction vendors on a timely basis. …Agree to risk sharing and reduce bond insurance costs. …the end of the bid process should be the beginning of construction, not an expensive, long drawn out contract process that adds no value. These changes can be instituted without legislative action.

During any study period, the state should realize that it already has experience with a variety of procurement models.

Ask the Dormitory Authority to produce a report on the varied procurement and bidding processes it uses because of the large variety of clients it serves. Those clients are governed by different contract laws, but also by a number of different procurement models that boards of directors of their client organizations have adopted over the years. The experiential base is there but everyone acts as if changes in state finance law or relevant municipal law that would save dollars on contracting are somehow a foreign concept.

On the construction side, we know the problems, the solutions are there --- it is a crime against the taxpayers that we continue to use 19th century contracting ideas in the 21 st century.

One word on the other side of the coin ---- getting good debt deals. One anecdote will suffice. The Comptroller signs off on debt issuances. In 2005 the state's Bridge and Highway Fund went into the market for $2.9 billion to fund the system. The bond deal did not meet the Comptroller's prudency standards, so questions were raised. To make a very long story short, the questions produced almost $1 billion in savings over the 20 year life of the bond deal. Lesson to state and local government --- now more than ever – scrutinize any bond deal for fat and waste – it is there. Put pressure on every bond deal – on the structure of the deal and the size of payments to investment banks, lawyers and underwriters.

When the state spends money to put construction workers to work it should not waste money on high interest payments and large payouts to underwriters and lawyers.

Another way in which the state government interacts with the private sector is with the provision of a series of payments to businesses that locate in the state or remain in the state and meet certain regulations. We know these programs by their alphabet soup names --- but they fall most commonly under the name of Empire Zone – and a host of loan and grant programs that are passed by the legislature on a regular basis.

The performance of Empire Zone programs are fundamentally flawed. For the $500+ million the state now spends on the program it does not receive measurable numbers of jobs, nor can anyone tell if the companies the state invests with are healthier because of the business incentives. Laying this out chapter and verse would take too long --- review the work of the Comptroller's Office, State Assemblymembers Richard Brodsky and Joe Morelle – and the work of the state's newspapers. Most of the major papers in the state have looked at how these programs have played out in local communities.

This year, let's eliminate the Empire zones program. First year savings would be at least $50 million. That would occur if we simply stopped it in its tracks. Because of the long term liabilities involved, the numbers increase over time. The savings is more if the state acts aggressively to enforce compliance of program rules, and less if it chooses to accept the status quo.

Some new policies must be developed to improve New York's business climate, but the state has had periods in the past where there were no "economic development programs" – the sky did not fall. And, we are in a recession, now is the time to plan for better programs so that when investment starts up again, New York can take advantage of it.

We can argue about what goes in it place. There are a number of good ideas in circulation.

On the various loans and grants programs I would argue that they too need to be frozen. No more, until the state adopts a business strategy that has a chance of succeeding and the funding is aligned with that plan.

My recommendation extends to any of ESDC's named programs --- and also to the host of economic development initiatives that are annually funded through member items. Freeze them this year and work out a program that is something more than a legislator responding to a constituent request for money.

If the state adopted some of the suggestions I have made today it would save millions. Adopt more and you save billions. Adopt them all and you begin to put the state on the right track toward ---- more capital projects funded for the same or less dollars, and a new economic development climate where job creation and healthy companies are the priority.