Review of the Financial Plan of the City of New York

March 2009

Report 9-2009

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I. Executive Summary

Just a few years ago, New York City posted record budget surpluses, but now the City is facing its greatest fiscal challenge in decades. Tax revenues are projected to fall by $5 billion over a two-year period as a result of the rapid deterioration in the national and local economies, particularly on Wall Street, the City's economic engine. These events are transforming the securities industry—which in prior years accounted for up to 20 percent of New York State tax revenue and 12 percent of City tax revenue—and the transformation will have long-term implications for both the State and the City. Moreover, the recession will likely deepen in the months ahead and may last longer than anticipated in the City's four-year financial plan.

Wall Street lost an estimated $47 billion in 2008 and may lose another $10 billion in 2009 before profitability returns in 2010. Job losses in the City are accelerating and could reach 294,000 by the second quarter of 2010, a loss of 7.8 percent. The national slowdown in the residential real estate market has reached New York City and the surrounding suburbs, and the commercial market is weakening. Since the beginning of the current fiscal year, New York City has reduced its tax revenue forecasts by $1.1 billion in FY 2009 and by about $3 billion annually in subsequent years. These revisions diminish, but do not eliminate, the downside revenue risks.

The economic crisis gripping the nation is also taking a toll on the investments of the City's pension systems. Last year the systems lost 5 percent, and while the City's January 2009 Financial Plan (the "January Plan") assumes a 20 percent loss in FY 2009, actual losses so far this year have been greater. Pension contributions, which averaged $1.5 billion annually during most of the 1990s, are now projected to reach $7.7 billion by 2013, reflecting investment shortfalls and benefit enhancements enacted in past years.

Since just the beginning of the current fiscal year, these developments widened the projected budget gaps by about $3.5 billion annually to $7.7 billion in FY 2010 and about $10.5 billion in subsequent years. The City, however, has been proactive, and has already taken steps to reduce these gaps and has proposed other actions that will help close the remaining budget gap projected for FY 2010 (see Figure 1).

In November 2008, the City began implementing an aggressive agency cost-reduction program, which was expanded in January. The program is expected to generate about $2 billion annually beginning in FY 2010. Most of the cuts are concentrated in the Department of Education and the Police Department, but every agency will be affected. In addition, the City plans to curtail the capital program by half in an effort to bring the growth in debt service in line with the projected growth in revenues.

In December 2008, the City Council rescinded, at the Mayor's request, the 7 percent real property tax cut that was enacted at the beginning of FY 2008. Although the City Council preserved the $400 real property tax rebate program for the current year, the rebate has been eliminated for future years. These actions will generate an estimated $576 million in the current year and about $1.5 billion annually thereafter.

The Governor released his proposed budget in December—one month sooner than required—for the State fiscal year that begins on April 1, 2009. The January Plan reflects the potential impact of the Governor's proposals to balance the State budget, which could have a net adverse impact of $1 billion on the City. Most of this impact would come from curtailing planned increases in education aid and the elimination of revenue-sharing payments to the City, which the City hopes will be rescinded.

Many of the initiatives proposed by the Mayor to balance the FY 2010 budget require the approval of the State and the municipal unions. The Mayor has endorsed the Governor's proposals to broaden the coverage of the sales tax, but he also has asked that the State increase the City sales tax rate by 0.25 percent (to reach 4.25 percent), and that the State eliminate the sales tax exemption on clothing and footwear that cost less than $110. These actions would generate $900 million in FY 2010 alone.

The Mayor and the Governor have both made proposals to reduce the cost of employee fringe benefits. The Mayor has proposed that active employees and retirees shoulder a greater share of the cost of their health insurance so the City can realize annual savings of about $600 million. The Governor has proposed less costly pension plans for new State and local civilian employees and, at the Mayor's request, for new uniformed employees that work for the City, which could generate substantial savings during the financial plan period.

Our review concludes that New York City will end the current fiscal year in balance given its substantial reserves, and that considerable progress has been made in closing the FY 2010 budget gap. The January Plan, however, includes $2.1 billion in budget risks for FY 2010 (see Figure 2) and the FY 2011 budget gap remains formidable at $6 billion (by our estimation). In the months ahead, the City's four-year financial plan is likely to undergo significant changes after the State adopts a new budget and acts on the City's budget proposals, the benefits of the federal economic stimulus bill are taken into account, and the City addresses known budget risks.

The federal stimulus bill recently signed into law by the President will help New York State and New York City balance their budgets and will offset cuts in State education aid proposed by the Governor. While the federal stimulus bill will provide relief over the next two years from a deepening recession, the need for governmental reform has not been diminished given the long-term trends.

Figure 1
New York City Financial Plan
(in millions)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
REVENUES					
Taxes					
General Property Tax	$ 14,357	$ 16,246	$ 17,178	$ 17,767	$ 18,155
Other Taxes	19,869	17,232	19,102	20,633	22,141
Discretionary Transfers [1,2]	546	546	- - -	- - -	- - -
Debt Defeasance [4]	362	382	- - -	- - -	- - -
Tax Audit Revenue	680	596	596	595	594
Sales Tax Increase Program	77	894	920	972	1,023
Subtotal - Taxes	**35,891**	**35,896**	**37,796**	**39,967**	**41,913**
Miscellaneous Revenue	5,945	5,739	5,908	5,976	5,992
Unrestricted Intergovernmental Aid	254	254	254	254	254
Less: Intra-City Revenues	(1,631)	(1,462)	(1,462)	(1,462)	(1,462)
Disallowances against Categorical Grants	(15)	(15)	(15)	(15)	(15)
Subtotal - City Funds	**$ 40,444**	**$ 40,412**	**$ 42,481**	**$ 44,720**	**$ 46,682**
Other Categorical Grants	1,104	1,021	1,023	1,026	1,025
Inter-Fund Revenues	477	445	437	434	433
Total City Funds, Capital IFA and Other Categorical Grants	**$ 42,025**	**$ 41,878**	**$ 43,941**	**$ 46,180**	**$ 48,140**
Federal Categorical Grants	6,037	5,326	5,323	5.334	5,334
State Categorical Grants	12,031	11,629	12,127	12,390	12,833
Total Revenues	**$ 60,093**	**$ 58,833**	**$ 61,391**	**$ 63,904**	**$ 66,307**
EXPENDITURES					
Personal Service					
Salaries and Wages	$ 22,019	$ 21,817	$ 22,980	$ 23,203	$ 23,472
Pensions	6,383	6,502	7,031	7,280	7,554
Fringe Benefits [1]	6,774	6,451	6,504	6,767	7,711
Subtotal - Personal Service	**$ 35,176**	**$ 34,770**	**$ 36,515**	**$ 37,250**	**$ 38,737**
Other Than Personal Service					
Medical Assistance	$ 5,644	$ 4,756	$ 4,916	$ 6,089	$ 6,270
Public Assistance	1,313	1,299	1,299	1,299	1,299
All Other [1,2]	18,477	17,787	18,601	19,256	19,834
Subtotal - Other Than Personal Service	**$ 25,434**	**$ 23,842**	**$ 24,816**	**$ 26,644**	**$ 27,403**
General Obligation and Lease Debt Service [1,2,3]	3,829	4,353	4,783	5,211	5,496
General Obligation and TFA Debt Defeasances [4]	(279)	(2,313)			
FY 2008 Budget Stabilization & Discretionary Transfers [1]	(4,089)	- - -	- - -	- - -	- - -
FY 2009 Budget Stabilization & Discretionary Transfers [2]	1,553	(1,007)	- - -	- - -	- - -
FY 2010 Budget Stabilization [3]	- - -	350	(350)	- - -	- - -
General Reserve	100	300	300	300	300
Subtotal	**$61,724**	**$60,295**	**$66,064**	**$69,405**	**$71,936**
Less: Intra-City Expenses	(1,631)	(1,462)	(1,462)	(1,462)	(1,462)
Total Expenditures	**$ 60,093**	**$ 58,833**	**$ 64,602**	**$ 67,943**	**$ 70,474**
Gap To Be Closed	**$ - - -**	**$ - - -**	**$ (3,211)**	**$ (4,039)**	**$ (4,167)**

1) Fiscal Year 2008 Budget Stabilization and Discretionary Transfers total $4.635 billion, including prepayments of subsidies of $500 million, Retiree Health Benefits of $460 million, lease debt service of $46 million, net equity contribution in bond refunding of $10 million, Budget Stabilization of $3.073 billion, and a TFA grant which increases FY 2009 revenues by $546 million.
2) Fiscal Year 2009 Budget Stabilization and Discretionary Transfers total $1.553 billion, including Budget Stabilization of $1.007 billion, and a TFA grant which increases FY 2010 revenues by $546 million.
3) Fiscal Year 2010 Budget Stabilization totals $350 million.
4) FY 2007 GO Debt Defeasance of $536 million reduced debt service by $27 million, $279 million, and $277 million in FY 2008 through FY 2010, respectively. FY 2008 GO Debt Defeasance of $1.986 billion reduced debt service by $2.036 billion in FY 2010. FY 2007 TFA Debt Defeasance of $718 million increase revenues by $33 million, $362 million, and $382 million in FY 2008 through FY 2010, respectively.

Source: NYC Office of Management and Budget

Figure 2
OSDC Risk Assessment of the NYC Financial Plan

(in millions)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
			Better/(Worse)		
Surplus/(Gaps) per January Plan	**$ - - -**	**$ - - -**	**$ (3,211)**	**$ (4,039)**	**$ (4,167)**
Actions Outside the Mayor's Direct Control:					
Rescind Proposed Cut in State Revenue-Sharing	(242)	(242)	(242)	(242)	(242)
Raise NYC Sales Tax Rate	(25)	(302)	(304)	(316)	(332)
Eliminate Sales Tax Exemption on Clothing	(36)	(394)	(409)	(439)	(462)
Broaden Sales Tax Coverage	(16)	(198)	(207)	(217)	(229)
Restructure Employee Health Insurance Costs	- - -	(557)	(586)	(618)	(653)
Enact Lower-Cost Pension Plans for New Employees	- - -	(200)	(200)	(200)	(200)
Enact 5-Cent Fee on Plastic Bags	- - -	(100)	(160)	(140)	(140)
Receipt of Additional Federal Medicaid Assistance	- - -	(50)	(50)	- - -	- - -
Agency Actions	(4)	(58)	(58)	(64)	(64)
Subtotal	**(323)**	**(2,101)**	**(2,216)**	**(2,236)**	**(2,322)**
Estimation:					
Higher Overtime Costs	- - -	(50)	(50)	(50)	(50)
Implementation of GASB 49 for Budgetary Purposes	- - -	- - -	(500)	(500)	(500)
Subtotal	**- - -**	**(50)**	**(550)**	**(550)**	**(550)**
OSDC Risk Assessment	**(323)**	**(2,151)**	**(2,766)**	**(2,786)**	**(2,872)**
Remaining Gap to be Closed Per OSDC [1]	**$ (323)**	**$ (2,151)**	**$ (5,977)**	**$ (6,825)**	**$ (7,039)**
Additional Risks and Offsets					
Pension Contributions [2]	- - -	- - -	(180)	(326)	(453)
Wage Increases at the Projected Inflation Rate	- - -	- - -	(190)	(481)	(868)

[1] The January Plan includes an annual general reserve of $100 million in FY 2009 and $300 million in each of fiscal years 2010 through 2013.

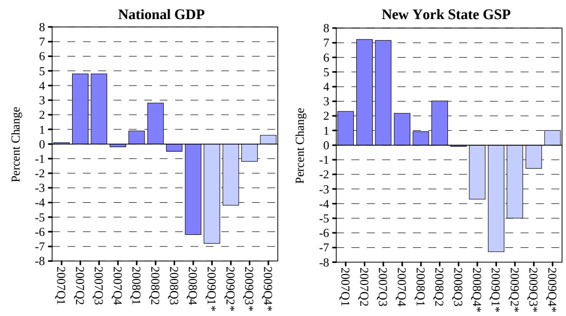
[2] These estimates assume that pension fund investment performance will not improve between February 27, 2009, and the end of the fiscal year.

II. Economic Trends

In the fourth quarter of 2008, the Real Gross Domestic Product (GDP) declined at an annual rate of 6.2 percent, the largest contraction since the first quarter of 1982. According to the March 2009 forecast by IHS Global Insight, the national economy will contract at an annual rate of 6.8 percent during the first quarter of 2009 and will not begin to recover until the fourth quarter (see Figure 3). On an annual basis, the GDP is forecast to contract by 2.5 percent in 2009 but then grow by 2.2 percent in 2010.

Figure 3

Economic Growth

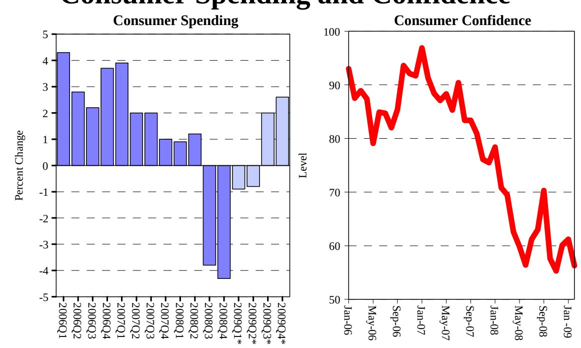


* Forecast by IHS Global Insight

Source: Bureau of Economic Analysis

Figure 4

Consumer Spending and Confidence

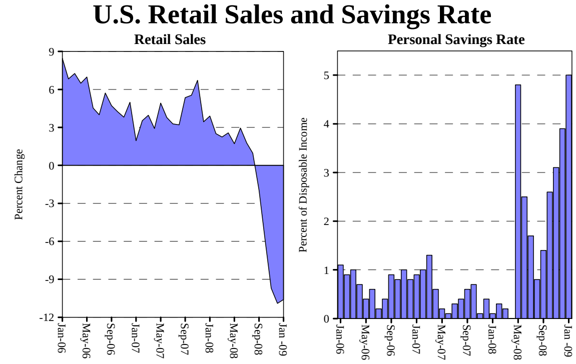


* Forecast by IHS Global Insight

Sources: Bureau of Economic Analysis; University of Michigan

Figure 5

U.S. Retail Sales and Savings Rate



Sources: U.S. Census Bureau; U.S. Bureau of Economic Analysis

In New York State, IHS Global Insight estimates that, while the Real Gross State Product (GSP) contracted at an annual rate of 3.7 percent during the fourth quarter of 2008, the State's economy will contract by 7.3 percent during the first quarter of 2009—considerably more than the national estimate (see Figure 3). While IHS Global Insight predicts that the State's overall economy will also begin to recover during the fourth quarter, the growth in the State will be weaker than in the nation.

Consumption, which accounts for two thirds of the GDP, has been constrained by diminished home values, falling personal financial wealth, and job losses. Consumer spending fell at an annual rate of about 4 percent during the second half of 2008 (see Figure 4). The falloff in consumer spending reflects the collapse in consumer confidence. The University of Michigan's index of consumer sentiment plunged in the second half of 2008 and remains near record lows.

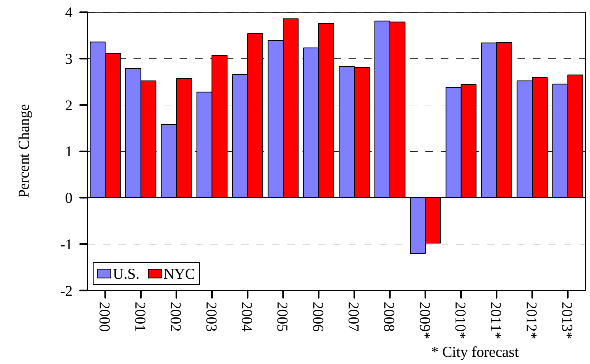
A further manifestation of the decline in consumer confidence and spending is the sharp decline in retail sales. Retail sales slowed during the first half of 2008 but began to decline late last summer (see Figure 5). As consumers spend less, they are saving more (and paying down debt)—some forecasters contend that consumer psychology is changing, which could reduce consumption for years.

The decline in energy prices has helped consumers, but not enough to offset the retrenchment in consumer spending. Recessionary pressures, including the collapse in energy prices, will cause prices to decline (i.e., deflation) for the first time in 70 years. The January Plan assumes that prices will decline by 1.2 percent in 2009 at the national level and by 1 percent in the City, after a rise of 3.8 percent in 2008, which was a 16-year high (see Figure 6).

Weak consumption and tight credit have forced many businesses into bankruptcies and layoffs. The Institute for Supply Management's non-manufacturing index fell to a new low (since the beginning of the series in 2004) in November 2008, and the manufacturing index fell to a 29-year low in December 2008 (see Figure 7).

Figure 6

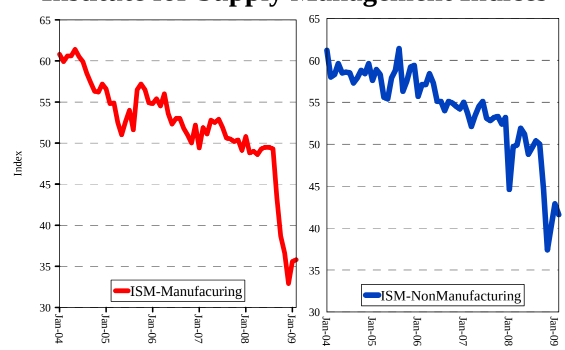
Annual Inflation Rates



Source: U.S. Bureau of Labor Statistics

Figure 7

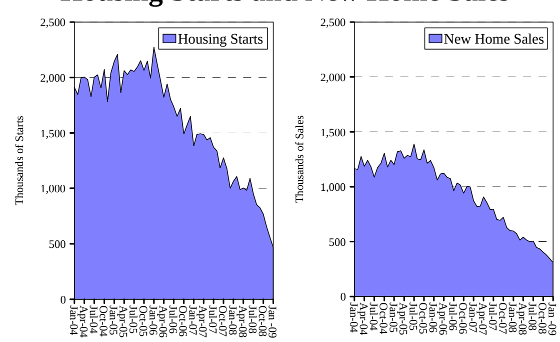
Institute for Supply Management Indices



Sources: Institute for Supply Management; OSDC analysis

Figure 8

Housing Starts and New Home Sales



Source: U.S. Census Bureau

Housing markets remain distressed. According to the U.S. Census Bureau, both new home starts and new home sales reached record lows in January 2009 (see Figure 8). The S&P/Case-Shiller Home Price Index shows that between June 2006 and December 2008, average national home prices fell by nearly 27 percent. The metropolitan areas with the sharpest price declines during the period were in the western and southern United States, where mortgage foreclosures and defaults skyrocketed. During the same time period, home prices in the New York City metropolitan area fell by 15.2 percent (see Figure 9).

The economies of both New York State and New York City have joined the nation in recession. According to the Federal Reserve Bank of New York's Coincident Index, which measures the current strength of the economy, the economic expansion peaked in the nation in November 2007, but growth continued in New York State until March 2008, and in New York City until August 2008 (see Figure 10).

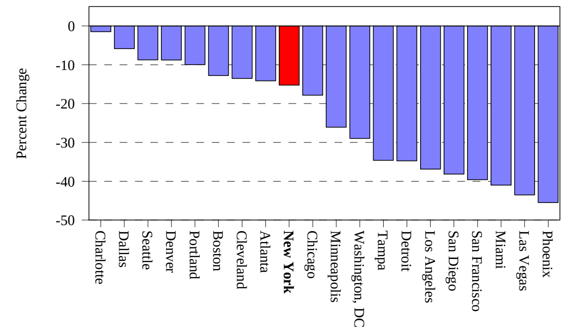
Between December 2007 and February 2009, the nation lost 4.4 million jobs, with more than half of the job losses occurring since October 2008 (see Figure 11). In December 2008 job losses totaled 681,000, the worst monthly loss since September 1945. IHS Global Insight forecasts that total job losses will exceed 7 million before a recovery begins in the second quarter of 2010, when the national unemployment rate will exceed 10 percent.

Between August 2008 and January 2009, New York City lost 86,200 jobs. The job losses recorded in November and December were the worst two-consecutive-month losses since September and October 2001.

Figure 9

Changes in Home Values

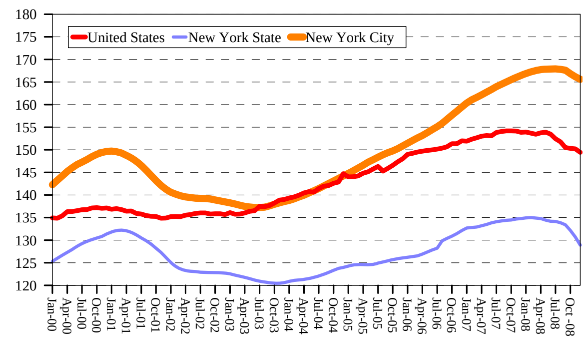
June 2006 to December 2008



Sources: Moody's Economy.com; S&P/Case-Shiller Home Price Index

Figure 10

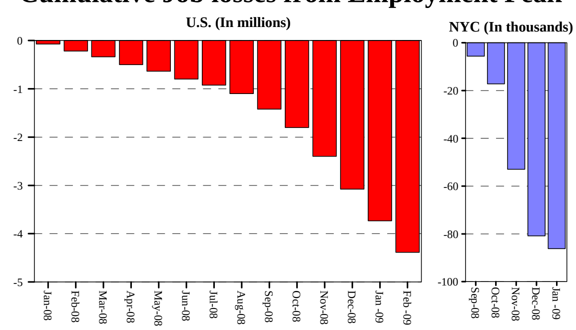
Coincident Index



Sources: Federal Reserve Bank of NY; Economic Cycle Research Institute

Figure 11

Cumulative Job losses from Employment Peak



* Seasonally adjusted statistics

Sources: U.S. Bureau of Labor Statistics; NYS Department of Labor

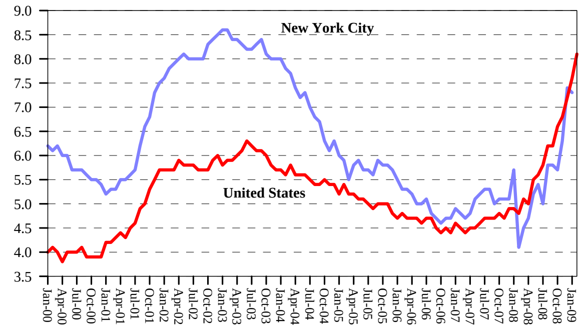
The unemployment rates in both the nation and the City were approaching 8 percent in January 2009, compared with less than 6 percent in July 2008 (see Figure 12). Initial claims for unemployment insurance benefits soared to 670,000 in the nation in the week ending February 21, 2009—a 26-year high—and rose to 34,000 in New York State by the end of 2008—a 25-year high (see Figure 13).

The securities industry in New York City has lost 19,200 jobs since employment peaked in September 2007. Through multiplier effects these losses have spread into the rest of the City's economy, just as the national recession has resulted in other local job losses. The January Plan assumes that the City will lose 294,000 jobs in all industries (including 46,000 securities industry jobs) over a seven-quarter period ending in the second quarter of 2010 (see Figure 14).

By comparison, in the recession of the early 1990s the City lost more than 350,000 jobs over 11 quarters, and in the recession of the early 2000s it lost 230,000 jobs over 10 quarters. The City believes that in the current recession employers are moving more quickly to eliminate jobs, which will cause a shorter but more intense period of job losses. While this position is not unreasonable, the recession could be deeper and longer than the City assumes in the January Plan, resulting in even greater job losses.

Figure 12

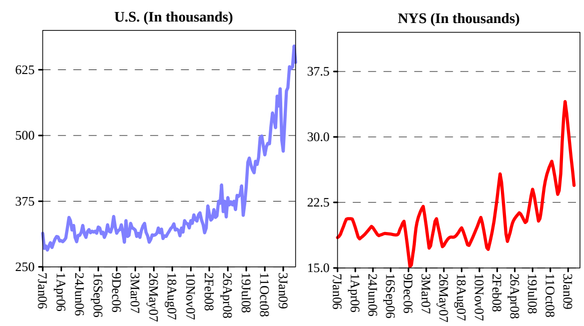
Unemployment Rate



Sources: U.S. Bureau of Labor Statistics; NYS Department of Labor

Figure 13

Initial Claims for Unemployment Insurance



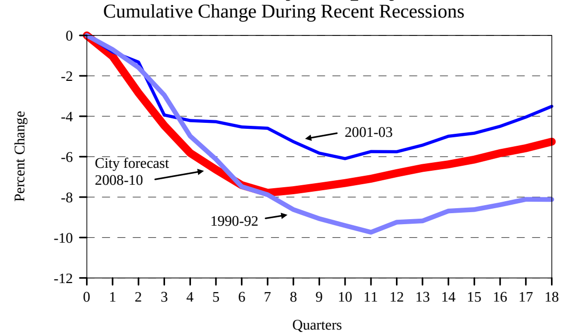
* Seasonally adjusted statistics

Sources: Bureau of Labor Statistics; Moody's Economy.com; OSDC analysis

Figure 14

New York City Employment

Cumulative Change During Recent Recessions



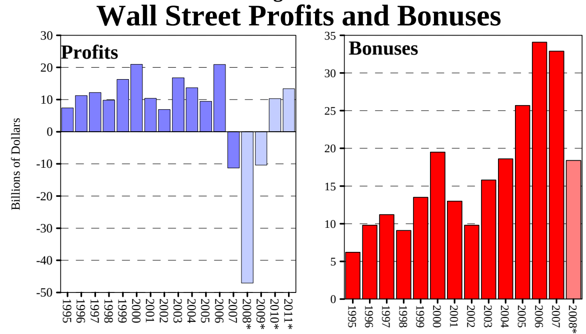
Sources: NYC Office of Management and Budget; NYS Department of Labor; OSDC analysis

Wall Street continues to post record losses and is in the midst of a historic period of transformation. Among the City's major financial firms, Lehman Brothers collapsed, Bear Stearns and Merrill Lynch were sold, and Goldman Sachs and Morgan Stanley were forced to restructure. Wall Street is being transformed from a highly leveraged investment business model to a better-capitalized commercial banking model.

Wall Street's profits have plummeted as write-offs continue to accumulate and credit markets remain unsettled. The City estimates that after an $11.3 billion loss in 2007, Wall Street lost another $47.2 billion in 2008—a new record, driven by losses in trading and lower revenues in underwriting and other businesses, such as mergers and acquisitions (see Figure 15). The January Plan assumes that Wall Street will lose $10.4 billion in 2009, but that the industry will recover and realize profits just above $10 billion in 2010.

Figure 15

Wall Street Profits and Bonuses



* Profits forecasts are City forecasts; bonuses are OSDC estimates.
Note: Profits are for broker/dealer operations of NYSE member firms.
Sources: NYS Department of Labor; New York Stock Exchange; Securities Industry and Financial Markets Association; OSDC analysis

The State Comptroller has estimated that Wall Street bonuses declined by 44 percent to $18.4 billion in 2008, the lowest level since 2003 (see Figure 15). Wall Street's compensation is expected to be lower in future years, as the industry has been fundamentally changed. It is anticipated that the Wall Street downturn will contribute to a total wage decline of 11.8 percent in 2009—the largest decline since data first became available in 1985. In addition, restrictions on executive compensation for firms that receive funds from the U.S. Treasury's financial rescue programs could also lower future wage growth.

The recession has begun to affect the market for condominium and cooperative apartments in the City. Prudential Douglas Elliman reported that in the fourth quarter of 2008, compared with the same period one year earlier, the listed inventory of available apartments increased by 39.3 percent; the number of days that apartments were on the market increased by 21.3 percent; and the volume of sales fell by 9.4 percent. In the same period, the median sales price rose by 5.9 percent, but this reflects sales of new developments that were contracted more than one year ago, and thus does not reflect current market conditions.

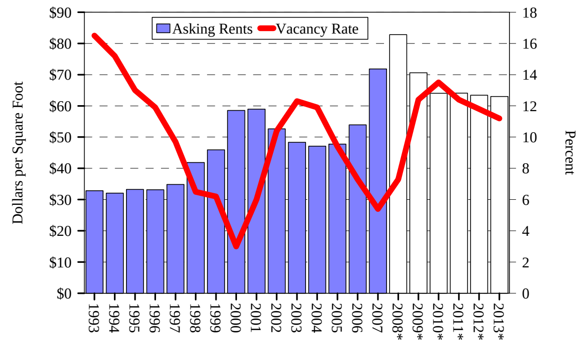
During the same period, the sales volume and median price of resale apartments fell by 35.5 percent and 3.6 percent, respectively. The January Plan projects that the volume of apartment sales will drop by 15 percent annually through 2010, while prices will fall by more than 35 percent by 2010. The January Plan also projects that single-family home prices in the City will decline by 25 percent between the third quarter of 2007 and the fourth quarter of 2009, and that sales are estimated to fall by 33 percent in 2008 and 5 percent in 2009.

Retrenchment and failures among financial firms, law firms, and media firms have precipitated the falloff of office leasing activity. According to Colliers ABR, between the first quarter and the fourth quarter of 2008, the average asking rent in the primary office market (Class A) in Manhattan declined by 13.1 percent from the record high of $87.40 per square foot, to $76.00 per square foot. Meanwhile, the vacancy rate rose from 5.7 percent to 9.1 percent.

The January Plan assumes that the average rent in Manhattan's primary office market will decline by 14.8 percent in 2009 and by another 9.3 percent in 2010, after averaging a record $82.80 per square foot in 2008 (see Figure 16). It also assumes that the vacancy rate will more than double, from 5.4 percent in 2007 to 13.5 percent in 2010. In subsequent years, the market should stabilize as the City's economy starts to create jobs. Overall, the City expects that the lack of overbuilding in recent years will limit available inventory and thus limit the depth of the commercial market downturn.

Figure 16

Manhattan Commercial Property



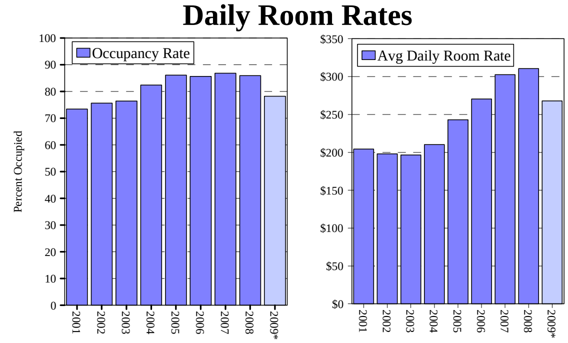
* City forecast

Sources: NYC Office of Management and Budget; Cushman & Wakefield

The once-booming tourism sector is faltering. In 2008, a record 47 million tourists visited the City, including 9.8 million international tourists. Tourists spent an estimated $30 billion in the City, with international tourists outspending domestic visitors by a multiple of four, on average. The January Plan projects that the number of tourists will decline by 5 percent in 2009—the sharpest decline in decades. In response to fewer tourists and an increase in the hotel tax rate, the average daily room rate for hotels in New York City is expected to fall from a record high of $311 for all of 2008 to $268 in 2009, while the occupancy rate is expected to decline from 86 percent in 2008 to 78 percent in 2009 (see Figure 17).

Figure 17

New York City Hotel Occupancy and Daily Room Rates



* City forecast

Source: PKF Consulting

The federal government and the Federal Reserve have committed trillions of dollars to efforts to revive the financial system and stimulate the economy, but results thus far have been limited. While the new administration in Washington, D.C., has been aggressive on many fronts, both fiscal and monetary stimulus will take time to affect the economy, and may not be able to mitigate the deepest part of the recession in the first half of 2009.

III. Fiscal Year 2009

Since the current budget was adopted, the City has significantly revised its forecasts for FY 2009 in response to a succession of unprecedented events stemming from the global financial crisis and the continued deterioration in the economy. Since the beginning of the fiscal year, the size of the FY 2009 surplus has declined by $668 million to $144 million, and the projected budget gaps have grown by about $3.6 billion annually (see Figure 18).

Most of the adverse impact comes from a sharp decline in projected tax revenues and higher future pension contributions due to investment shortfalls. As a result of these developments, the City is taking steps to close budget gaps that total an estimated $7.7 billion in FY 2010 and $10.6 billion in each of fiscal years 2011 and 2012.

Compared with the estimates in the June 2008 Financial Plan, tax collections are now projected to be lower by $1.1 billion in FY 2009, $3.3 billion in FY 2010, and about $3 billion annually in fiscal years 2011 and 2012. This change reflects a significant downward revision in the City’s economic forecast for jobs and Wall Street—which has reduced the City’s forecasts for personal and business income taxes.

The economic crisis continues to take its toll on the investments of the City’s pension systems. The systems are required by law to assume an 8 percent annual return on investments, but last year the systems lost 5 percent. The January Plan assumes a 20 percent loss for all of FY 2009, but the pension systems have lost about 30 percent through February 27, 2009. Pension contributions, which averaged $1.5 billion annually during most of the 1990s, are now projected to reach $7.7 billion by 2013, reflecting shortfalls in investment earnings and benefit enhancements.

Energy costs were lower than expected as a result of the collapse in oil prices last fall. The City also realized budgetary benefits from drawing down reserves. Public assistance and health insurance rates, however, grew more quickly than anticipated by the City in the June Plan.

Figure 18
Financial Plan Reconciliation
June 2008 Plan vs. January 2009 Plan

(in millions)

	Better/(Worse)			
	FY 2009	**FY 2010**	**FY 2011**	**FY 2012**
Surplus/(Gap) per June 2008 Plan [3]	**$ 812**	**$ (4,229)**	**$ (7,006)**	**$ (6,667)**
Revenues				
Real Estate Transaction Tax	(427)	(724)	(614)	(648)
Personal Income Tax	(407)	(1,327)	(958)	(872)
Business Taxes	(319)	(678)	(696)	(563)
Sales Tax	(111)	(529)	(498)	(527)
Real Property Tax	(1)	30	(52)	(271)
All Other Taxes	58	(117)	(154)	(186)
Subtotal	**(1,207)**	**(3,346)**	**(2,972)**	**(3,067)**
Tax Audits	100	8	8	7
Non-Tax Revenues	70	(87)	(56)	(26)
Total	**(1,037)**	**(3,425)**	**(3,020)**	**(3,086)**
Expenditures				
Pension Contributions	(87)	(80)	(345)	(612)
Public Assistance	(55)	(57)	(57)	(57)
HIP Rate Increase	(3)	(53)	(58)	(65)
Debt Service	11	3	(11)	49
Energy	97	137	56	13
Other	43	13	32	33
Total	**6**	**(36)**	**(382)**	**(638)**
Drawdown of Reserves				
General Reserve	200	- - -	- - -	- - -
Prior Years' Expenses	500	- - -	- - -	- - -
Pension Audit Reserve	- - -	200	- - -	- - -
Total	**700**	**200**	**- - -**	**- - -**
Potential State Budget Impact	**(338)**	**(234)**	**(198)**	**(150)**
Net Change During FY 2009	**(668)**	**(3,495)**	**(3,600)**	**(3,874)**
Baseline Surplus/(Gap) as of January 2009	**$ 144**	**$ (7,724)**	**$ (10,606)**	**$ (10,541)**

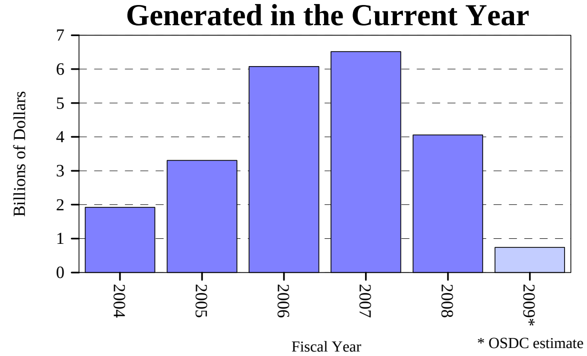
Note: Totals may not add due to rounding.
Sources: NYC Office of Management and Budget; OSDC analysis

[3] These estimates exclude the impact of the Mayor's proposal to increase real property taxes, which was approved by the City Council in December 2008, and savings anticipated from restructuring the municipal health insurance program, which requires the approval of the municipal unions.

IV. Current-Year Operating Results

In recent years, surging Wall Street profits and rising real estate values and transactions, combined with conservative revenue forecasts, resulted in large amounts of unanticipated resources during the fiscal year. As shown in Figure 19, these resources peaked at $6.5 billion in FY 2007 and are expected to decline sharply in FY 2009 to $741 million, reflecting the rapid deterioration in the local economy. The City will transfer these surplus resources, together with resources generated in prior years, to narrow future budget gaps.

Figure 19
Surplus Resources Generated in the Current Year

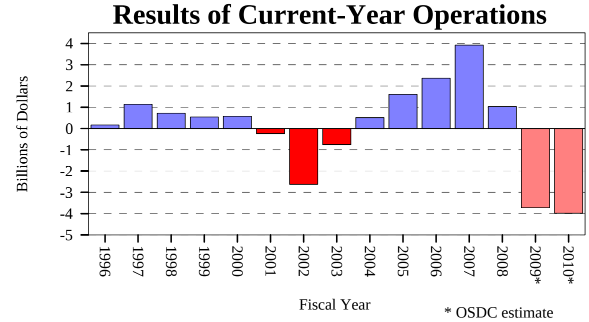


Sources: NYC Office of Management and Budget; OSDC analysis

This transfer of resources between years masks the relationship between recurring revenues and expenditures. A clearer picture of the City's fiscal condition can be obtained by examining the results of current-year operations—the difference between revenues and expenditures in the current year. This entails adjusting for surplus transfers and other factors that impede transparency, such as discretionary actions.

As shown in Figure 20, the size of the current-year surplus grew each year after the end of the last recession, and peaked in FY 2007 at $3.9 billion. The current-year surplus declined sharply in FY 2008 because spending increased rapidly, despite the beginning of the economic slowdown. Spending is projected to exceed current-year resources by $3.7 billion in FY 2009**,** and the FY 2009 budget will be balanced using surplus resources accumulated in prior years. The City is on track for a $4 billion current-year deficit in FY 2010, reflecting the impact of the recession. This estimate assumes full implementation of the City's proposed gap-closing program, which appears unlikely.

Figure 20
Results of Current-Year Operations



Note: Adjusted for surplus transfers, TFA, TSASC, and discretionary actions. Includes benefit of proposed and enacted gap-closing actions.
Sources: NYC Office of Management and Budget; NYC Comptroller; OSDC analysis

V. Potential Impact of the State Budget

In December 2008, the Governor projected a budget gap of $1.6 billion for the remainder of the current State fiscal year, which ends on March 31, 2009, and gaps of $13.7 billion for State fiscal year (SFY) 2009-2010, $17.1 billion for SFY 2010-2011, and $18.6 billion for SFY 2011-2012. The Governor proposed a series of actions to balance the budget for this year and next, and to narrow the out-year State budget gaps. The State recently took actions to ensure that the current State fiscal year ends in balance, but it also lowered its tax revenue forecast for next year by $1 billion.

Some of the gap-closing initiatives proposed by the Governor and recently implemented by the State would adversely affect New York City's budget. The net adverse impact, which could total as much as $307 million in FY 2009 and $799 million in FY 2010, has been reasonably reflected in the January Plan. As shown in Figure 21, most of the impact would come from curtailing a planned increase in education aid for next year and eliminating assistance to the City under the Aid and Incentives to Municipalities program (AIM), which would take effect this year.

The impact of these two actions could be lessened by other initiatives proposed by the Governor, such as broadening the City's sales tax base and mandate relief. In addition, the allocation of resources from the federal economic stimulus bill may offset the impact of the proposed cut in State education aid.

Figure 21
Potential Impact of the Governor's Proposed Budget on New York City's Financial Plan
(in millions)

	FY 2009	FY 2010	FY 2011	FY 2012
School Aid	$ - - -	$ (766)	$ (1,163)	$ (1,259)
Aid and Incentives to Municipalities	(328)	(328)	(328)	(328)
Social Services	(18)	(67)	(83)	(100)
Revenue Enhancements	55	357	416	464
Other	(17)	5	42	77
Total [4,5]	**$ (307)**	**$ (799)**	**$ (1,116)**	**$ (1,146)**

Sources: NYS Division of the Budget; NYC Office of Management and Budget; OSDC analysis

[4] These estimates do not reflect the Governor's proposal to allow the Battery Park City Authority to securitize a revenue stream currently dedicated to affordable housing. This would raise an estimated $540 million, which would be split evenly between the State and the City. The proposal requires the approval of the Mayor and the City Comptroller.

[5] The City continues to benefit from actions taken by the State in past years that capped the growth in the local share of Medicaid costs at 3 percent and assumed the local cost of the Family Health Plus program. Together, these actions generate an estimated $500 million in recurring savings for New York City.

The major initiatives proposed by the Governor in December include the following.

State Education Aid: Reduce planned increases in State education aid by $668 million for FY 2010 and by nearly $1 billion for FY 2011 compared with the estimates in the November Plan. Despite these cutbacks, the Governor remains committed to increasing education aid to New York City in accordance with the resolution of the Campaign for Fiscal Equity lawsuit, but would extend the phase-in of increased State aid by two years until the 2012-2013 school year. The Governor also would reduce the State's share of the cost of preschool special education by $97 million in FY 2010, and by more than $100 million annually in subsequent years. The receipt of federal economic stimulus funds will likely offset the impact of these proposed budget cuts.

Aid and Incentives to Municipalities (AIM) Program: Eliminate assistance to New York City under the AIM program, which would have a budgetary impact beginning in the current year.

Social Services: Increase the local share of administering social services programs ($40 million); raise the public assistance grant by 10 percent annually over a three-year period beginning in January 2010 ($40 million by FY 2012); and eliminate funding for certain optional child welfare services ($12 million).

Revenue Enhancements: Broaden the sales tax to cover cable and satellite television and radio, digital products, entertainment, and transportation, and place limits on exemptions for capital improvements. The Governor also proposed expanding the red-light camera program; reducing itemized deductions for high-income earners; and increasing local fees for birth and death certificates and marriage licenses. Although the Governor excluded New York City from his proposal to eliminate the sales tax exemption on clothing and footwear that cost less than $110 per item, the Mayor recommends that the State eliminate the exemption in New York City as well as increase the local sales tax rate.

Mandate Relief: Create a new pension plan for future State and local civilian employees that would require employees to contribute 3 percent of their wages for the duration of employment, compared with ten years for employees in Tiers III and IV; increase the minimum retirement age from 55 to 62; and increase the amount of time needed to vest from five years to ten years. At the request of the Mayor, the Governor also proposed a new plan for City uniformed employees that would raise the retirement age to 50 with 25 years of service; base benefits on the average salary of the final three years of service; and require higher employee contributions than are currently mandated.

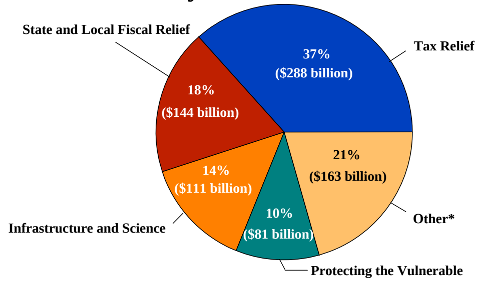
The Governor also proposed that the State allow the Transitional Finance Authority (TFA) to issue additional debt as long as the total of TFA and general obligation debt remains within the State constitutional debt limit. This would allow the City to realize savings from diversifying its financing vehicles ($5 million). In addition, the Governor proposed granting the City greater flexibility in the issuance of bond anticipation notes ($10 million); and raising the Wicks Law threshold from $3 million to $10 million, which would generate savings to the capital program.

City-Related Entities: Raise tuition for the City University of New York and reduce State operating aid to community colleges. The City University has already approved a tuition increase equivalent to the increase proposed by the Governor, and is negotiating with the State to mitigate the impact of $20 million in other reductions. The Governor also has proposed actions that would reduce Medicaid reimbursements to the Health and Hospitals Corporation (HHC) by about $130 million annually; HHC has sufficient resources in the short term to offset the impact.

VI. The Federal Stimulus Bill

In February 2009, Congress approved and the President signed into law the American Recovery and Reinvestment Act of 2009 (i.e., the federal economic stimulus bill), which is designed to reinvigorate the economy by creating jobs, preventing layoffs, providing tax relief, and offering fiscal relief to state and local governments. The Act is valued at $787 billion and allocates $288 billion for tax relief; $163 billion for education, energy, and health care initiatives; $144 billion in fiscal relief to state and local governments; and $111 billion for infrastructure and science initiatives (see Figure 22).

Figure 22
Allocation of Funds Under the American Recovery and Reinvestment Act



Note: Other includes Health Care, Education, Workforce Training, and Energy
Sources: White House (http://www.recovery.gov); OSDC analysis

The City expects to receive $4.5 billion in federal funding over the next two years (see Figure 23). Of this amount, the City anticipates $2 billion in additional Medicaid funding (which the January Plan includes in the gap-closing program), and $1.9 billion in education aid, which will offset the impact of proposed cuts in State education aid. (The State recently announced that the City will receive an estimated $1.9 billion in additional federal Medicaid aid.) The total amount of federal assistance could be even higher if the City were to successfully apply for competitive grants, which could be used to fund new initiatives in education, public safety, and other areas.

Figure 23
Potential Impact of the Federal Economic Stimulus Funds on New York City
(in millions)

Temporary Federal Medicaid Increase	$ 2,000
Fiscal Stabilization Education Restoration	1,070
Education Initiatives	820
Social Services	231
Energy Efficiency and Conservation	140
Housing	142
Workforce Investment	63
Public Safety	41
Total	**$ 4,508**

Source: New York City Office of the Mayor

VII. Program to Eliminate the Gap

Since the beginning of the fiscal year, the City has taken (or plans to take) a number of actions to balance the FY 2010 budget. In total, we estimate that these actions are valued at nearly $1.6 billion in FY 2009 and more than $6.5 billion in each subsequent year (see Figure 24). Some of these actions are within the City's control to implement, such as raising the property tax rate, while others require the cooperation of the State and federal governments or the municipal unions.

Figure 24
Budget-Balancing Actions
(in millions)

	FY 2009	FY 2010	FY 2011	FY 2012
Increase Real Property Taxes by 7 Percent	$ 576	$ 1,223	$ 1,298	$ 1,359
Implement Agency Actions	499	2,001	2,058	2,080
Rescind Proposed Cut in State Revenue-Sharing	242	242	242	242
FY 2009 Projected Surplus	144	- - -	- - -	- - -
Increase Sales Tax Revenues	77	894	920	972
Raise Hotel Tax Rate	15	62	66	35
Obtain Higher Federal Medicaid Reimbursement	- - -	1,000	1,000	- - -
Restructure Employee Health Insurance Costs	- - -	557	586	618
Eliminate $400 Property Tax Rebate	- - -	256	256	256
Enact Lower-Cost Pension Plans for New Employees	- - -	200	200	200
Draw Down Retiree Health Benefits Trust	- - -	82	395	672
Curtail Planned Capital Commitments by 30 Percent	- - -	4	24	67
Total	**1,553**	**6,521**	**7,045**	**6,502**
Surplus Roll	(1,553)	1,203	350	- - -
Available Resources	**$ - - -**	**$ 7,724**	**$ 7,395**	**$ 6,502**

Note: Totals may not add due to rounding.
Sources: NYC Office of Management and Budget; OSDC analysis

Real Property Taxes: In December 2008, the City Council approved the Mayor's proposal to rescind, effective January 1, 2009, the 7 percent real property tax cut that was enacted at the beginning of FY 2008. This action will generate $576 million in FY 2009 and about $1.3 billion annually thereafter. Raising the tax rate automatically eliminated the $400 property tax rebate beginning in FY 2010, which will raise an additional $256 million annually beginning that year.

Hotel Tax: In December 2008, the City Council also enacted a temporary increase in the hotel tax rate, from 5 percent to 5.875 percent, which will generate $15 million in FY 2009, more than $60 million in each of fiscal years 2010 and 2011, and $35 million in FY 2012 (the provision expires in November 2011).

Federal Medicaid Match: The January Plan assumes that the federal economic stimulus bill will provide the City with $2 billion in additional Medicaid aid. The State recently announced that the City will receive an estimated $1.9 billion, less than the $2.1 billion estimated by the City. The actual amount of aid could fall to $1.6 billion under some scenarios.

State Revenue-Sharing: The Mayor is requesting that the Governor rescind his proposal to eliminate revenue-sharing payments to the City, and instead maintain payments at the 2008 level. This issue will be resolved with the State budget.

Increase Sales Tax Revenues: The Mayor has endorsed the Governor's proposal to broaden the sales tax to include cable and satellite television and radio, digital products, transportation, and entertainment, which collectively could increase sales tax collections by $200 million annually beginning in FY 2010; and has proposed that the State raise the City's portion of the sales tax by 0.25 percent to reach 4.25 percent, effective June 1, 2009 (valued at about $300 million annually), and eliminate the sales tax exemption on clothing and footwear items that cost less than $110. (The Governor has already proposed eliminating this exemption outside of New York City.) Eliminating the exemption would raise about $400 million annually. All of these initiatives require State approval, which remains uncertain.

Restructure Employee Health Insurance Costs: The City has proposed that municipal employees and retirees shoulder a greater share of health insurance costs so as to reduce the City's costs by about $600 million annually beginning in FY 2010. For example, the Mayor has proposed that municipal employees and retirees pay 10 percent of the cost of their health insurance premiums—about $850 per year for current employees and about $580 per year for retirees. These initiatives will require the approval of the municipal unions.

Pension Plan: The Governor and the Mayor have proposed less costly pension plans for new State and City civilian employees, and City uniformed employees. New civilian employees would be required to contribute 3 percent of their salaries for the length of their service instead of for just ten years, and the minimum retirement age would increase from 55 to 62. Uniformed employees would be eligible to retire at age 50 with 25 years of service, instead of no age minimum with 20 years of service. The unions have opposed such changes in the past, and the State is requiring a home rule message from the City in support of these changes.

Drawdown From Retiree Health Benefits Trust (RHBT): The Mayor has proposed using, over a three-year period, $1.1 billion of the $2.5 billion deposited in the RHBT to offset an increase in future pension contributions arising from poor pension fund investment performance. While using the RHBT to help balance the operating budget is within the City's discretion, it represents a setback in the City's efforts to fund health insurance costs for retirees, and shifts the burden to future taxpayers.

Agency Actions: The Mayor proposed agency actions in November 2008 and in January 2009 that would generate $499 million in the current year and about $2 billion annually thereafter (see Figure 25). About 45 percent of the resources would come from the Department of Education and the Police Department. Most of the resources would come from actions that are within the City's control to implement, but a number of initiatives require State approval, while others will require close monitoring because they are not fully developed or are based on optimistic assumptions.

Figure 25
Agency Program
(in millions)

	FY 2009	FY 2010	FY 2011	FY 2012
Department of Education	$ 176.1	$ 691.4	$ 691.4	$ 691.4
Police Department	37.7	259.9	277.5	222.7
Fire Department	31.7	100.5	107.1	110.4
Sanitation	25.0	85.9	50.9	35.4
Admin. for Children's Services	19.1	83.7	93.0	95.2
Social Services	26.9	75.2	66.5	66.7
Transportation	20.8	53.1	51.1	49.8
Information Technology	17.4	29.8	28.8	28.2
Citywide Admin. Services	16.5	14.8	11.8	18.1
Health & Mental Hygiene	10.3	43.5	46.4	46.5
Correction	9.7	49.3	50.2	56.3
Libraries	8.0	35.3	35.3	35.3
Homeless Services	7.9	35.2	35.3	35.4
Finance	7.6	23.5	25.9	25.9
Parks	6.7	31.2	29.6	29.8
Elected Officials	6.6	4.0	4.0	4.0
Youth	4.6	21.3	21.3	21.3
Cultural Affairs	3.8	16.8	16.8	16.8
District Attorneys & Prosecutors	3.0	10.8	27.1	27.4
CUNY	0.8	22.2	22.2	22.2
Fleet Reduction	- - -	20.0	2.0	2.0
Procurement Savings	- - -	55.5	55.5	55.5
5-Cent Plastic Bag Fee	- - -	100.0	160.0	140.0
Pension Contributions	- - -	- - -	6.7	123.4
Other	58.8	138.0	141.4	120.7
Total	**$ 499.0**	**$ 2,000.9**	**$ 2,057.8**	**$ 2,080.4**

Source: NYC Office of Management and Budget

The following initiatives, with a value of $158 million in FY 2010 and more than $200 million in subsequent years, require State approval.

- The City has proposed charging consumers $0.05 per plastic bag. While this initiative has strong environmental benefits, it requires State approval. The initiative would generate $100 million in FY 2010, $160 million in FY 2011, and $140 million annually thereafter.

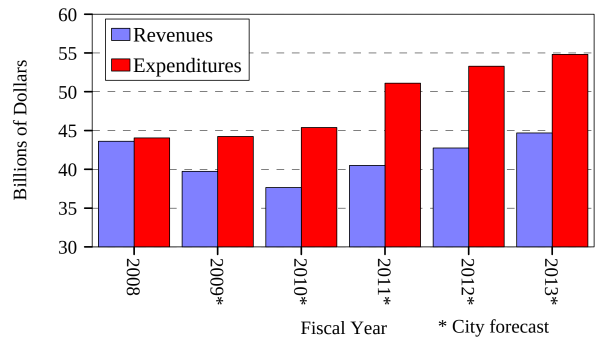
- The Fire Department has proposed increasing the tax on fire insurance premiums from 2 percent to 4 percent, which would generate $21 million annually beginning in FY 2010.
- The Department of Correction plans to transfer City detainees to State jails, which would save the City $3 million in FY 2009, $19 million in each of FY 2010 and FY 2011, and $25 million annually in subsequent years. The department also seeks to develop programs to reduce the time spent by inmates in custody, expedite the bail process, increase supervised releases for low-risk defendants, and substitute videoconferencing for the physical transport of prisoners; these would reduce costs by $18 million annually beginning in FY 2010.

VIII. Revenue and Expenditure Trends

The January Plan assumes that City fund revenues will decline in fiscal years 2009 and 2010 as the economic recession takes its toll on collections, before growth resumes in FY 2011. During the same period, spending is expected to grow steadily (see Figure 26). Overall, City fund revenues are projected to grow at an average annual rate of 0.5 percent during fiscal years 2009 through 2013, while spending is expected to grow at an average annual rate of 5.5 percent, resulting in large baseline budget gaps.

Figure 26

Revenue and Expenditure Trends



Note: Adjusted for surplus transfers, PIT-backed TFA, and TSASC.
Excludes proposed tax increases, the proposed agency program, and other gap-closing actions.
Sources: NYC Office of Management and Budget; NYC Comptroller; OSDC analysis

A. Revenue Trends

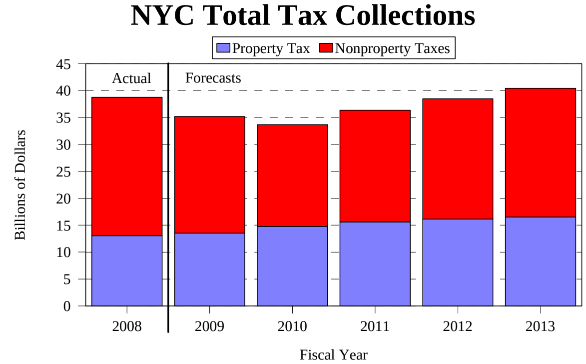
In recent months, the economy has deteriorated at a more rapid rate than was anticipated in the November 2008 Financial Plan. Job losses have accelerated, Wall Street losses have grown, and the real estate slowdown has reached Manhattan residential properties. Since the budget was adopted in June 2008, the City has reduced its forecast of tax revenues by $1.1 billion in FY 2009 and about $3 billion annually in fiscal years 2010 through 2012. Much of that change—more than $800 million in FY 2009 and nearly $2 billion annually over the rest of the plan period—has occurred since November.

The City now projects that total tax collections will decline from a peak of $38.8 billion in FY 2008 to $33.7 billion in FY 2010—a drop of $5.1 billion, or 13.1 percent. This decline will occur primarily in the personal and business income taxes and the real estate transaction taxes (see Figure 27).

To offset part of the projected decline in tax revenue, the City enacted a mid–fiscal year increase in the property tax rate; eliminated the $400 home owner property tax rebate beginning in FY 2010; and enacted a temporary increase in the hotel tax rate. The January Plan also includes proposals to increase sales tax collections by nearly $1 billion annually.

Figure 27

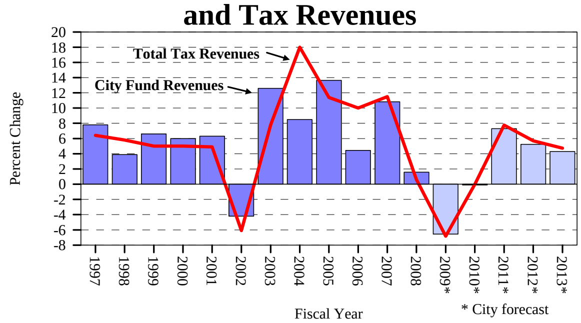
NYC Total Tax Collections



Note: Excludes enacted and proposed tax increases.
Sources: New York City Comptroller's Office; New York City Office of Management and Budget

Even assuming implementation of these and other gap-closing actions, City fund revenues are forecast to decline by nearly $2.9 billion, or 6.6 percent, in FY 2009 (see Figure 28). This would be only the third time since FY 1981 (when the City's budget was first balanced according to Generally Accepted Accounting Principles) that revenues would decline—but both the amount and rate of the projected drop would be the largest recorded during the period. The January Plan forecasts that total City fund revenues will remain unchanged in FY 2010; without the gap-closing actions, these revenues would decline 5.3 percent.

Figure 28
Annual Change in City Fund Revenues and Tax Revenues



Note: Includes proposed tax changes and gap-closing program. Adjusted for debt service on TFA and tobacco bonds, receipt of TFA BARB revenue, and the transfer of TSASC revenues.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

During fiscal years 2011 through 2013, City fund revenues (including the benefit of the tax increases and other gap-closing initiatives) will grow at an average annual rate of 5.6 percent (see Figure 29). In FY 2013, collections from business and personal income taxes and real estate transaction taxes are expected to remain below FY 2008 levels, while other nonproperty tax collections will be only slightly higher.

Figure 29
City Fund Revenues
(in millions)

	FY 2009	FY 2010	Annual Growth	FY 2011	FY 2012	FY 2013	Average Three-Year Growth Rate
Taxes							
Property Tax	$ 13,781	$ 14,767	7.2%	$ 15,624	$ 16,152	$ 16,540	3.9%
Personal Income Tax	7,169	5,707	-20.4%	6,749	7,352	7,851	11.2%
Sales Tax	4,555	4,139	-9.1%	4,341	4,637	4,979	6.4%
Business Taxes	4,619	4,232	-8.4%	4,632	5,181	5,549	9.5%
Real Estate Transaction Taxes	1,507	1,159	-23.1%	1,246	1,320	1,513	9.3%
Other Taxes	3,137	3,077	-1.9%	3,182	3,266	3,411	3.5%
Audits	677	586	-13.5%	586	585	584	-0.1%
Subtotal	**35,445**	**33,667**	**-5.0%**	**36,360**	**38,493**	**40,427**	**6.3%**
Miscellaneous Revenues	4,302	3,992	-7.2%	4,142	4,258	4,276	2.3%
Unrestricted Intergovernmental Aid	12	12	N.A.	12	12	12	N.A.
Grant Disallowances	(15)	(15)	N.A.	(15)	(15)	(15)	N.A.
Total	**$ 39,744**	**$ 37,656**	**-5.3%**	**$ 40,499**	**$ 42,748**	**$ 44,700**	**5.9%**
Revenue Enhancement Initiatives							
Property Tax Increase (enacted)	576	1,479	N.A.	1,554	1,615	1,615	3.0%
Hotel Tax Increase (enacted)	15	62	N.A.	66	35	0	N.A.
Increase Sales Tax Collections	77	894	N.A.	920	972	1,023	4.6%
Restore Revenue-Sharing Payments	242	242	N.A.	242	242	242	N.A.
Agency Actions	103	384	N.A.	404	358	356	-2.5%
Total	**$ 40,757**	**$ 40,717**	**-0.1%**	**$ 43,685**	**$ 45,969**	**$ 47,936**	**5.6%**

Note: Personal income tax includes the portion of those revenues used to pay debt service on bonds issued by the TFA.
Sources: NYC Office of Management and Budget; OSDC analysis

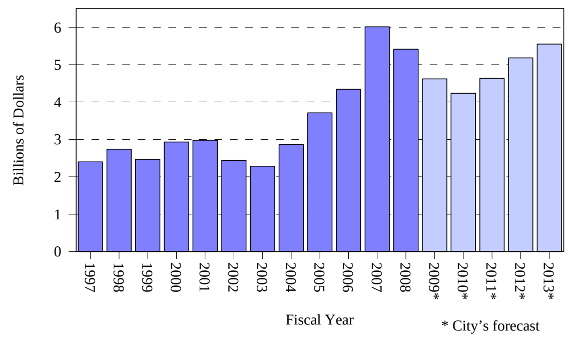
Details of the City's revenue trends are discussed below and shown in Figure 29.

1. Business Taxes

After rising rapidly for four consecutive years, business tax collections declined in FY 2008, falling by 10 percent (see Figure 30). This reflects the surge in Wall Street profits followed by a record loss of $11.3 billion in 2007 as firms began to write off mortgage-backed securities, in particular those associated with subprime mortgages. The City estimates that losses reached $47.1 billion in 2008. Business taxes are now forecast to fall by 14.7 percent ($794 million) in FY 2009 and another 8.4 percent ($387 million) in FY 2010.

Figure 30

Business Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

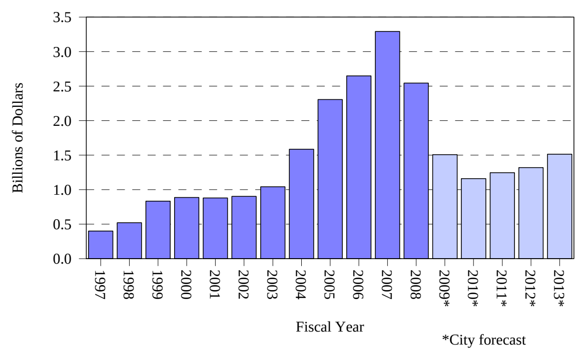
Business tax collections will be held down in the next few years because businesses are applying tax credits owed from prior overpayments against future tax liabilities. Many firms are requesting refunds to improve their cash positions, which is exacerbating the current decline in business tax collections—but will allow collections to recover more rapidly when the economy improves. As a result, when the economy begins its expected recovery during the second half of 2009, the City projects business taxes will rebound with strong gains of 9.5 percent in FY 2011, 11.9 percent in FY 2012, and 7.1 percent in FY 2013.

2. Real Estate Transaction Taxes

Collections from the mortgage recording tax and the real property transfer tax depend on transaction activity and sale prices. Both components are in decline as a result of declining personal income, difficulty obtaining financing, weaker demand for office space, and a falloff in foreign investment. The January Plan assumes that collections from these taxes will fall by 40.8 percent in FY 2009 and by another 23 percent in FY 2010. The City does not expect conditions to stabilize until FY 2010 when collections are expected to return to levels experienced at the beginning of the decade (see Figure 31). Although the January Plan forecasts slow growth beginning in FY 2011, collections are expected to be $1.8 billion lower in FY 2013 than at their peak in FY 2007.

Figure 31

Real Estate Transaction Taxes

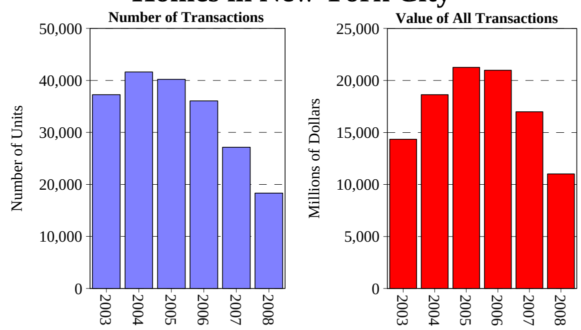


Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

According to the S&P/Case-Shiller Home Price Index, home values in the New York City metropolitan area have declined less than in many areas of the country, and transaction data from the City's Department of Finance show median sales prices declined only modestly beginning in 2008. The number of local transactions involving one-, two-, and three-family homes, however, began to decline in 2005 (see Figure 32), but it was not until FY 2007 that the falling level of transactions began to push down the value of transactions.

Figure 32

Sales of One-, Two-, and Three-Family Homes in New York City



Source: NYC Department of Finance; OSDC analysis

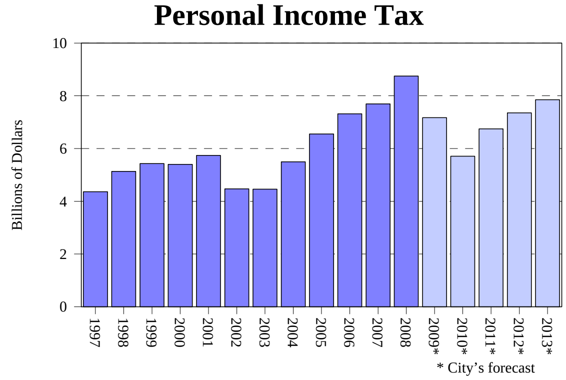
Another factor that supported real estate transaction tax growth in prior years was the strong demand for condominiums and cooperative apartments in Manhattan, but sales of these properties are now beginning to decline. In 2008, the number of transactions for Manhattan apartments declined by 6 percent and the total value of these transactions fell by 13.1 percent. In addition, the number of transactions for Manhattan office properties declined steeply in 2008, and this has had an adverse impact on revenues. In 2007, the 257 transactions for Manhattan offices had a value of $25.7 billion—25.5 percent of the value of all real estate transactions in the City that year. In 2008, the number of transactions for Manhattan commercial real estate declined to 132, and had a value of $8.1 billion—or 13.3 percent of the total value of all transactions. For the Manhattan office properties valued at $50 million or more, the number of transactions fell from 66 in 2007 to 27 in 2008.

3. Personal Income Tax

Personal income tax collections have been most affected by the recession—the City now expects FY 2010 collections to be $1.3 billion lower than forecast in the June 2008 Financial Plan. Overall, collections are projected to drop by nearly $3 billion or 34.8 percent between fiscal years 2008 and 2010 (see Figure 33). The decline reflects a sharp reduction in Wall Street bonuses and a steep drop in employment. The City now expects the local economy to lose

Figure 33

Personal Income Tax



Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

294,000 jobs between the third quarter of 2008 and the second quarter of 2010. Unfavorable financial market conditions also led the City to forecast a 56 percent decline in capital gains realizations in 2008, with another 14 percent decline in 2009.

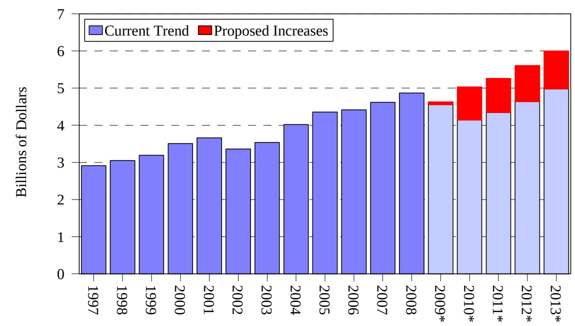
When employment and wages recover, the City expects a strong surge in personal income tax collections, with increases of 18.3 percent in FY 2011, 8.9 percent in FY 2012, and 6.8 percent in FY 2013. The sharp rebound, however, is not expected to be fueled by wage growth, but by a surge in capital gains and other taxpayer behavioral responses to the end of tax cuts implemented by the Bush Administration. The size and source of the sharp projected increase in FY 2011 collections may not materialize if the tax code changes, if job losses become more severe, or if the economy takes more time to recover.

4. Sales Tax

At the beginning of FY 2009, it appeared that tourism would cushion sales tax collections during the recession, but with the retrenchment in domestic consumer spending, sales tax collections are now forecast to fall by $729 million during fiscal years 2009 and 2010 (see Figure 34). As the economy recovers, growth is expected to resume with gains of 4.9 percent in FY 2011, 6.8 percent in FY 2012, and 7.4 percent in FY 2013. Collections would be higher by about $900 million annually beginning in FY 2010 if the Governor's and Mayor's sales tax proposals are approved by the State Legislature.

Figure 34

Sales Tax



* City's forecast

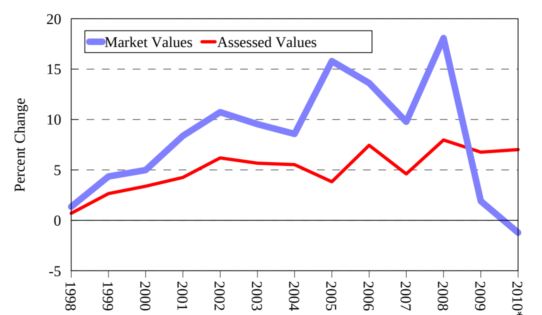
Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

5. Real Property Tax

The real property tax, even excluding the rate increase that became effective in January 2008, is the only major tax that is forecast to grow during each year of the financial plan period. Despite the easing of property values in recent years, revenues will still rise as the result of provisions of State law that phase in the impact of large market value changes on assessments. Large increases from previous years are still being phased in. The tentative tax roll for FY 2010 shows that although market values have declined by 1.2 percent, assessed values will increase by 7 percent (see Figure 35).

Figure 35

Annual Change in Property Values



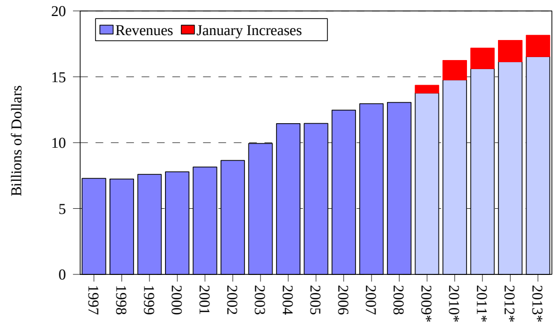
*Tentative

Source: NYC Department of Finance

During the previous recession, the City increased real property tax rates by 18 percent in order to close its projected budget gaps. As economic conditions improved, the City provided home owners with a rebate of $400 beginning in FY 2005 and then cut the average real property tax rate by 7 percent in FY 2008. Faced with declining nonproperty tax revenues, the City rescinded the average tax rate cut beginning in the second half of FY 2009, and rescinded the rebate beginning in FY 2010. These revenue increases raised the average annual growth rate for property taxes between fiscal years 2008 and 2013 from 4.8 percent to 6.8 percent (see Figure 36). As a result of the combination of the growth in real property taxes and the decline in nonproperty taxes, the property tax is expected to comprise 43.2 percent of all City tax revenues in FY 2013 (excluding proposed sales tax increases), compared to 33.7 percent in FY 2008.

Figure 36

Real Property Tax Revenues



*City forecast

Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

6. Tax Initiatives

The City has enacted or proposed a number of actions that would increase tax collections by more than $2.5 billion annually beginning in FY 2010 (see Figure 37). In December 2008, the City raised real property taxes and the hotel tax. The January Plan assumes increases in sales tax collections that will come from increasing the rate, broadening the coverage, and eliminating the exemption for clothing and footwear items that cost less than $110.

Figure 37
Tax Initiatives
(in millions)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Enacted					
Increase Real Property Tax Rate	$ 576	$ 1,223	$ 1,298	$ 1,359	$ 1,359
Increase Hotel Tax Rate	15	62	66	35	- - -
Eliminate Property Tax Rebate	- - -	256	256	256	256
Subtotal	**591**	**1,541**	**1,620**	**1,650**	**1,615**
Proposed					
Repeal Clothing Sales Tax Exemption	36	394	409	439	462
Increase Sales Tax Rate	25	302	304	316	332
Broaden Sales Tax Base	16	198	207	217	229
Subtotal	**77**	**894**	**920**	**972**	**1,023**
Total Tax Initiatives	**$ 668**	**$ 2,435**	**$ 2,540**	**$ 2,622**	**$ 2,638**

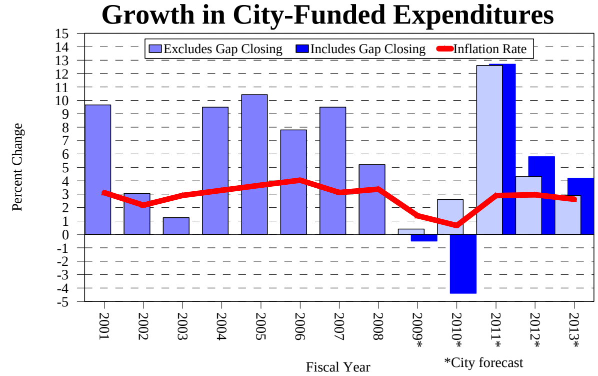
Sources: NYC Office of Management and Budget; OSDC analysis

B. Expenditure Trends

City-funded expenditures grew at average annual rates of nearly 10 percent during fiscal years 2004 and 2005, and 8.6 percent during fiscal years 2006 and 2007 (see Figure 38).[6] Most of the growth was due to the rising cost of debt service, Medicaid, and employee fringe benefits. The City also contributed $2.5 billion to the Retiree Health Benefits Trust ($1 billion in FY 2006 and $1.5 billion in FY 2007), and retired nearly $1.3 billion in outstanding debt in FY 2007 that was due in fiscal years 2009 and 2010. Excluding these discretionary actions, spending would have grown more slowly (by 2.5 percent in FY 2006 and by 7.4 percent in FY 2007).

Figure 38

Growth in City-Funded Expenditures



Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

In FY 2008, expenditures increased by 5.2 percent, including amounts set aside by the City to pre-fund $2 billion of FY 2010 debt service. Spending is projected to decline by 0.5 percent during FY 2009 and by another 4.4 percent during FY 2010, reflecting the benefit of discretionary actions taken in prior years and actions taken to help balance the FY 2010 budget. Without these gap-closing actions, spending would grow by 2.6 percent in FY 2010 (see Figure 38).

In FY 2011, spending will accelerate because of the expiration of the benefit of discretionary actions to reduce debt service costs in FY 2010; the impact of collective bargaining agreements; and higher pension fund contributions necessitated by investment losses in fiscal years 2008 and 2009. City-funded spending will grow more slowly during fiscal years 2012 and 2013 (at an average annual rate of 5.0 percent), but still faster than the local projected inflation rate for those years.

Nondiscretionary spending (i.e., debt service, pension contributions, Medicaid, and employee health insurance costs) is projected to consume more than 57 percent of City fund revenues by FY 2013, but the burden would be reduced to 51 percent with the successful implementation of the Mayor's proposals to implement less costly pension plans for new employees, shift a greater share of health insurance costs to active employees and retirees, and scale back the capital program. In addition, Medicaid would have continued to consume a greater share of City fund revenues if not for steps taken by the State in January 2006 to cap the growth in the local share of Medicaid to 3 percent annually.

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6 Adjusted for surplus transfers and for debt service on PIT-backed bonds issued by the Transitional Finance Authority and by TSASC.

The January Plan is premised on the assumptions shown in Figure 39; these and other trends in the expenditure budget are discussed below.

Figure 39
Estimated City-Funded Expenditures
(Adjusted for Surplus Transfers)
(in millions)

	FY 2009	FY 2010	Annual Growth	FY 2011	FY 2012	FY 2013	Average Three-Year Growth Rate
Salaries and Wages	$12,554	$13,197	5.1 %	$14,126	$14,199	$14,239	2.6%
Debt Service	4,314	2,756	-36.0%	5,874	6,392	6,740	34.7%
Medicaid	5,492	5,643	2.8%	5,803	5,977	6,157	2.9%
Pension Contributions	6,215	6,525	5.0%	7,057	7,422	7,695	5.7%
Health Insurance	3,236	3,796	17.3%	4,250	4,817	5,109	10.4 %
Other Fringe Benefits	2,602	2,457	-5.6%	2,382	2,402	2,446	-0.1%
Judgments and Claims	638	675	5.8%	732	793	856	8.3%
Public Assistance	489	490	0.1%	490	490	490	0.0%
General Reserve	100	300	200%	300	300	300	0.0%
Energy	820	853	4.0%	942	985	1,021	6.2%
Other	7,776	8,688	11.7%	9,153	9,527	9,802	4.1%
Total	**44,235**	**45,380**	**2.6%**	**51,109**	**53,304**	**54,857**	**6.5%**
Proposed Cost-Reduction Initiatives							
Reduce Capital Commitments by 30 Percent	- - -	(4)	**NA**	(28)	(83)	(158)	**NA**
Draw from Retiree Health Benefits Trust	- - -	(82)	**NA**	(395)	(672)	- - -	**NA**
Less Costly Pension Plans for New Workers	- - -	(200)	**NA**	(200)	(200)	(200)	**NA**
Restructure Health Insurance Costs	- - -	(557)	**NA**	(586)	(618)	(653)	**NA**
Receipt of Additional Federal Medicaid Aid	- - -	(1,000)	**NA**	(1,000)	- - -	- - -	**NA**
Implement Agency Actions	(396)	(1,617)	**NA**	(1,654)	(1,723)	(1,743)	**NA**
Total Including Gap-Closing	**$43,839**	**$41,920**	**-4.4%**	**$47,246**	**$50,008**	**$52,103**	**7.5%**

Notes: Components above exclude the impact of the agency expense program and other gap-closing measures. Totals may not add due to rounding. Debt service includes bonds issued by the Transitional Finance Authority backed by the City's personal income tax and bonds issued by TSASC and backed by the City's share of anticipated revenues from a legal settlement with cigarette companies. The City's financial plan does not include these items, so the presentation of revenues and expenditures in this report is adjusted to include them.
Sources: NYC Office of Management and Budget; OSDC analysis

1. Salaries and Wages

Salaries and wages costs, including overtime, are projected to grow from $12.6 billion in FY 2009 to $14.2 billion in FY 2013, an increase of $1.7 billion, or 3.2 percent annually. The growth reflects the cost of actual and anticipated labor agreements (see Figure 40); and the May 2008 arbitration award for the Patrolmen's Benevolent Association (PBA), which has been extended to all other uniformed employees.

The January Plan also assumes that wages will increase by 1.25 percent in each of fiscal years 2011, 2012, and 2013 for all employees. If wages were to rise at the projected inflation rate instead, the City would incur additional costs of $190 million in FY 2011, $481 million in FY 2012, and $868 million in FY 2013.

Figure 40
Wage Increase Patterns
(Percent Change)

	Civilian	Uniformed
2005	3.00	4.50
2006	3.15	5.00
2007	2.00	4.00
2008	4.00	4.00
2009	4.00	4.00
2010	4.00	4.00
2011	1.25	1.25
2012	1.25	1.25
2013	1.25	1.25

Source: NYC Office of Management and Budget

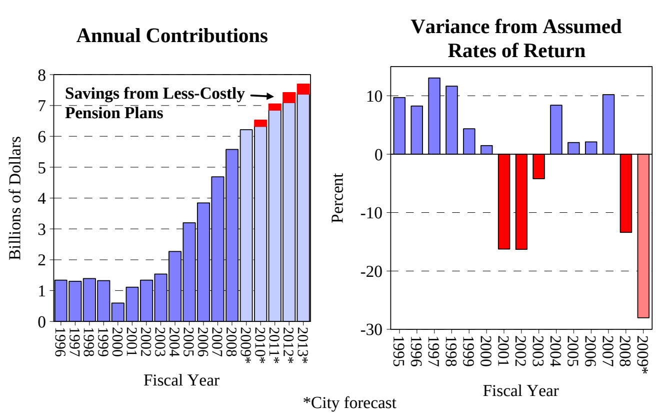
2. Overtime

Between fiscal years 2003 and 2008, overtime for both uniformed and civilian employees grew from $839 million to more than $1 billion. During these years, most of the growth was concentrated in the Police, Fire, Transportation, and Environmental Protection departments. In FY 2010, overtime is projected to decline by $64 million to $843 million. The January Plan assumes that overtime costs will remain at about $860 million in subsequent years. Our analysis indicates that overtime costs could be higher by $145 million during the financial plan period. Most of the cost, however, will be covered by capital funds and federal and State grants, leaving a City-funded risk of $50 million annually.

3. Pension Contributions

City contributions to the five actuarial pension systems have grown from about $1.5 billion in the late 1990s to $6.2 billion in FY 2009, reflecting the impact of poor investment performance, benefit enhancements, and labor settlements. Contributions are projected to total $6.5 billion in FY 2010 and then rise to $7.7 billion by FY 2013, which is due largely to pension fund investment shortfalls during fiscal years 2008 and 2009. Annual contributions could be reduced by an estimated $200 million beginning in FY 2010 if the Governor's and Mayor's proposals to enact less costly pension plans for new State and City workers are enacted into law (see Figure 41).

Figure 41



Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

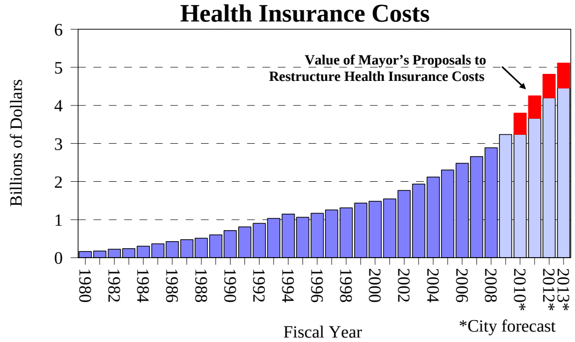
Current State law requires the actuarial pension systems to assume an 8 percent annual rate of return on investments. As shown in Figure 41, the pension systems earned significantly more than the assumed rates of return that were in effect during the second half of the 1990s, but then fell far short of expectations during fiscal years 2001 through 2003 as a recession took hold. Investment returns exceeded the actuarial rate of return during fiscal years 2004 through 2007 with strong growth in the equity and real estate markets, but the pension funds lost 5.4 percent during FY 2008—a shortfall of 13.4 percentage points from the expected rate of return.

During FY 2009 the equity and real estate markets declined sharply. The January Plan assumes that for FY 2009 the pension funds will lose 20 percent of their value.[7] Our analysis indicates that pension fund investments have lost about 30 percent through February 27, 2009. If this trend continues through the end of the fiscal year, future City contributions to the pension funds could increase by $180 million in FY 2011, $326 million in FY 2012, and $453 million in FY 2013.

4. Health Insurance

Health insurance costs for active employees and retirees are projected to grow from $3.2 billion in FY 2009 to $5.1 billion in FY 2013—an increase of 58 percent (see Figure 42).[8] The growth is based on the assumption that health insurance premiums will increase by 9.4 percent in FY 2009, 9.7 percent in FY 2010, and by 8 percent annually in subsequent years. These costs could be reduced by about $600 million annually beginning in FY 2010 if the municipal unions accept the Mayor's proposals to shift a greater share of the cost to employees and retirees. In the past, the City and the unions have agreed to draw down resources from the Health Stabilization Account, which currently has a balance in excess of $700 million.

Figure 42
Estimated City-Funded Health Insurance Costs



Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

7 The November Plan assumed that the City would use $1.1 billion of the resources in the Retiree Health Benefits Trust ($82 million in FY 2010, $395 million in FY 2011, and $672 million in FY 2012) to fund higher pension contributions from an 8 percent pension fund investment loss in FY 2009, and to help fund the higher contributions that arose from the 5.4 percent loss in FY 2008. The January Plan now assumes a higher investment loss in FY 2009, but it does not plan to use any additional resources from the RHBT.

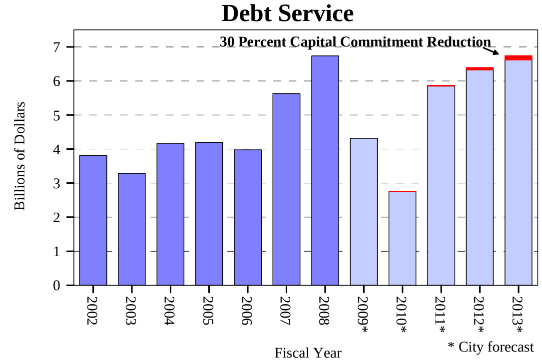
8 These estimates exclude savings anticipated from two mayoral proposals to reduce the City's health insurance costs. A May 2008 plan to restructure the municipal health insurance program is expected to generate annual savings of $200 million beginning in FY 2010. A January 2009 plan to require active employees and retirees to contribute 10 percent of the costs of their premiums would reduce the City's costs by over $350 million annually beginning in FY 2010. The estimates have also been adjusted to exclude a drawdown from the RHBT to help fund the cost of health insurance for retirees during fiscal years 2010 through 2012.

The cost of municipal health insurance also could be affected by the outcome of the State's review of a proposed conversion of the not-for-profit health insurers Health Insurance Plan of New York (HIP) and Group Health Incorporated (GHI) to a single, for-profit entity. Together, HIP and GHI cover 93 percent of the municipal workforce. While the Mayor opposes the conversion on the premise that a for-profit entity would drive up the cost of health insurance premiums and lower the quality and extent of coverage for municipal employees, he had previously stated that the City should receive some of the proceeds from any conversion. The conversion requires the approval of the Superintendent of the New York State Insurance Department, who is still reviewing comments from stakeholders. The State's financial plan assumes a conversion would generate $1.2 billion for the State over a four-year period; this is half the amount anticipated before the economic slowdown.

5. Debt Service

Debt service in fiscal years 2009 and 2010 has been reduced primarily through the use (in FY 2007) of $1.3 billion in surplus resources to pay down debt, and the use (in FY 2008) of $2 billion in surplus resources to pre-fund FY 2010 debt service. Although the Mayor intends to reduce planned capital commitments by 30 percent, in addition to the 20 percent cut implemented in the fall, debt service will grow by 56 percent from $4.3 billion in FY 2009 to $6.7 billion in FY 2013 (see Figure 43).[9] The debt service burden (i.e., debt service as a percent of City fund revenues) will rise from 10.7 percent in FY 2009 to 14.4 percent in FY 2013. These estimates reflect the City's intention to reenter the short-term borrowing market in FY 2010 after meeting its cash needs during the past five years with extraordinary revenues from the economic expansion.

Figure 43
Debt Service



Note: Debt service amounts are adjusted for prepayments.
Sources: NYC Office of Management and Budget; NYC Comptroller; OSDC analysis

6. Judgments and Claims

Judgments and claims costs are projected to grow from $675 million in FY 2010 to $856 million by FY 2013. The growth reflects an increase in the average cost and number of settlements, including those that cost more than $1 million. Expenditures for FY 2009 include a $31 million settlement to four plaintiffs in the Staten Island Ferry crash of October 15, 2003, and four other settlements totaling $7 million.

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9 We estimate that the Mayor's plan to curtail City-funded capital commitments will save $382 million during the financial plan period and $4 billion cumulatively through FY 2020.

7. Medicaid

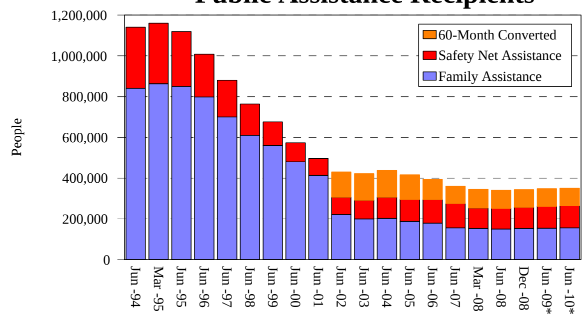
City-funded Medicaid expenditures are projected to grow from $5.6 billion in FY 2010 to $6.2 billion by FY 2013, an average annual rate of only 2.9 percent. The low rate of growth reflects steps taken by the State in January 2006 to cap the annual growth in the local share of Medicaid at 3 percent. In contrast, the State's share of the Medicaid program is projected to grow much more rapidly over the next three years, reflecting the rising cost of health care, higher enrollment, and increased utilization.

8. Public Assistance

Between March 1995 and June 2002, the public assistance caseload declined by more than half. The caseload rose by 16,000 people during the 2000-2003 recession (see Figure 44), and although the caseload resumed its decline beginning in FY 2005, it rose by 8,815 individuals during the second quarter of FY 2009 as the current recession deepened. The January Plan assumes that the caseload will rise by another 8,308 individuals by December 2009, and then remain at that level.

Figure 44

Public Assistance Recipients



Sources: NYC Human Resources Administration; NYC Office of Management and Budget; OSDC analysis

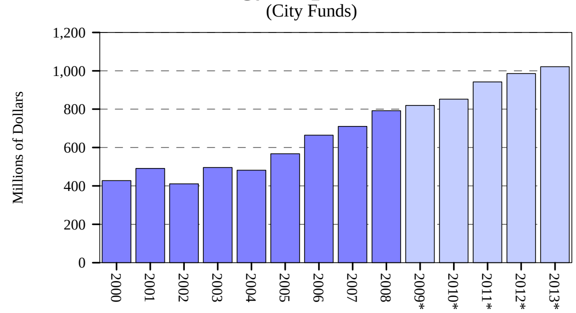
9. Energy Costs

Energy costs are projected to reach $1 billion by FY 2013 (see Figure 45), which is much lower than previous estimates due to the steep drop in oil prices. The price of oil has fallen from a record high of $147.27 per barrel in July 2008 to $40.15 per barrel as of March 2, 2009, and the January Plan assumes that oil will average $42.75 per barrel during fiscal years 2010 through 2013, which is consistent with the latest forecast from IHS Global Insight. In September 2008, Con Edison requested a 19.3 percent increase in the amount it charges customers for the transmission and delivery of electricity, which could push up City energy costs if approved.

Figure 45

Energy Expenditures

(City Funds)



Sources: NYC Comprehensive Annual Financial Report; NYC Office of Management and Budget; OSDC analysis

IX. Semi-Autonomous Agencies

The following public authorities and other entities have a financial relationship with the City that could affect the City during the financial plan period.

A. Department of Education

In response to the recession, both the Mayor and the Governor have scaled back planned increases for education as contemplated for part of the resolution of the Campaign for Fiscal Equity (CFE) litigation. In 2007, the City agreed to increase funding for education by $2.3 billion and the State agreed to increase aid to the City's public schools by $3.2 billion, both by the 2010-2011 school year.

The City is on track to keep its CFE commitment, even though it cut projected funding for educational programs by almost $1 billion annually, because it allocated additional funding for pension contributions, debt service, and collective bargaining costs. In December 2008, the Governor proposed reducing education aid to localities, including New York City, and delaying full implementation of the planned $3.2 billion increase in education aid by two years until the 2012-2013 school year.

While the January Plan assumes that State education aid will fall short of the levels previously anticipated by $766 million in FY 2010 and by about $1.2 billion annually in later years, which the Mayor has said could lead to layoffs of 13,930 pedagogical employees (mostly teachers), it now appears likely that the Governor will be able to effectively rescind most of the planned cuts because the federal economic stimulus bill has been signed into law. The stimulus bill will provide New York State with $4.6 billion in education aid (excluding competitive grants) over a two-year period. Of this amount, New York City can expect to receive $1.9 billion, assuming the existing distribution formula will apply, and possibly even more if it applies for certain grants that are allocated on a competitive basis.

The legislation that granted the Mayor greater control over the Board of Education will terminate on June 30, 2009, unless it is reauthorized. The Mayor and the Chancellor advocate reauthorization, as they believe the law has improved accountability and performance. While support for mayoral control is widespread, changes are under consideration that would enhance the role of parents and improve transparency.

B. Metropolitan Transportation Authority

In November 2008, the Metropolitan Transportation Authority (MTA) released a revised four-year financial plan that showed that projected budget gaps had grown by about $300 million in 2009, $500 million in 2010, and about $600 million annually thereafter. The gaps increased largely because the State lowered its forecast of dedicated transit taxes, and real estate transaction tax collections weakened more than expected as a result of the economic slowdown and difficulties in obtaining financing. The budget gaps totaled $1.4 billion in 2009 and reached $3 billion by 2012.

In December, the MTA adopted a 2009 budget that includes a mid-year hike in fares and tolls that would raise revenues by 23 percent and impose deep cuts to customer services. The MTA also plans to raise fares and tolls again in January 2011 to increase revenues by another 5 percent. Even with two fare increases and substantial cuts in services, the MTA's financial plan forecasts gaps of $266 million in 2010, $454 million in 2011, and $608 million in 2012.

In addition to the large operating budget gaps, the MTA's capital program has a large funding gap. The MTA has said that its upcoming 2010-2014 capital plan will require $22 billion to maintain the transit system, $5 billion to complete the first phase of the Second Avenue Subway and East Side Access projects, and $1 billion for regional projects such as bringing Metro-North Railroad into Pennsylvania Station. The next five-year capital plan could have a funding gap of up to $15 billion.

The Governor appointed a commission, chaired by former MTA Chairman Richard Ravitch, to identify new sources of funding for the MTA's operating and capital budgets for the next ten years. The commission's report, which was issued on December 4, 2008, makes a number of recommendations. The Governor and the Mayor have expressed their support, but the recommendations require the approval of the State Legislature and perhaps the City Council.

The commission recommends imposing a payroll tax on employers within the 12-county MTA region, which would raise an estimated $1.5 billion per year and would cost employers an average of $330 per $100,000 of payroll. The resources would be used in the first year to "support the operating needs of the Authority and its funding partners."[10] The commission also recommends that the MTA use these resources to reduce the proposed fare and toll increase from 23 percent to 8 percent, and to rescind the proposed cuts in services. In the second year of the payroll tax, the resources would be transferred to a new MTA subsidiary, the MTA Capital Finance Authority, and the proceeds would be dedicated to funding capital improvements.

10 The commission's report does not indicate whether any of these resources would supplant State or City subsidies.

The commission also recommends imposing tolls on the bridges over the East River (at the same level as tolls on the major MTA bridges and tunnels) and on the bridges over the Harlem River (at a level to match the cost of a single subway ride). This would raise an estimated $1 billion each year, of which $600 million would be used to improve mass transit, such as expanding bus service. The remainder would be used to maintain the bridges and to fund the costs of installing an electronic toll system. A number of issues, including ownership of the bridges, still need to be resolved. More recently, the Speaker of the State Assembly proposed linking the tolls over both rivers to the value of a single subway ride.

Revenue collections over the past few months have reflected the impact of the deepening recession. Collections from real estate–related taxes during the first two months of the calendar year were $75 million less than anticipated. In addition, weekday subway ridership was down by 2 percent in January 2009, compared with one year earlier—the first decline since 2003 (excluding bad weather or holidays). In addition, bridge and tunnel crossings were also down compared to last year, and dedicated State taxes could also be adversely affected. The MTA estimates that, if these trends continue, revenues could be as much as $650 million less than projected for calendar year 2009, further exacerbating an already difficult situation.

The MTA expects to receive $1.1 billion from the federal economic stimulus bill. The MTA plans to use $497 million to complete the Fulton Street Transit Center, and to use the remainder to start work on various projects, including many that were cut from the 2005-2009 capital plan when costs increased more than expected. These projects include subway station rehabilitations, repairing the Long Island Rail Road viaduct at Atlantic Avenue, and constructing a new Harmon Shop for Metro-North.

C. City University of New York

The City University of New York (CUNY) is the largest urban public university in the nation, and serves 244,253 degree-earning students as well as 272,000 students in adult and continuing education programs. CUNY consists of eleven senior colleges and six community colleges, and enrollment is at its highest in nearly four decades. City-funded expenditures for CUNY are projected to total $416 million in FY 2010.

The Governor has proposed tuition increases for public universities and colleges, and the CUNY Board of Trustees has already approved increases of up to $200 per semester for resident full-time community college students; up to $300 per semester for full-time resident senior college students; and larger amounts for graduate students. These increases will generate at least $110 million annually beginning in FY 2010, which would offset proposed cuts in State and City support and enable CUNY to offer new services. The Governor has also proposed increasing State funding for the Tuition Assistance Program and creating a new student loan program.

CUNY also could benefit from the federal economic stimulus bill with funding for research and development programs and to modernize facilities. In addition, the stimulus program provides an additional $200 million for the college work-study program for students nationwide; an additional $17.1 billion for Pell Grants; and $13.8 billion for a higher education tax credit that has been made partially refundable, so that more low-income parents may benefit.

D. New York City Housing Authority

The New York City Housing Authority (NYCHA) projects a $172 million budget gap for calendar year 2009. In recent years, NYCHA has relied heavily on reserves and federal capital grants to balance its operating budget. NYCHA expects to receive $423 million in capital financing from the federal economic stimulus package, allowing it to complete deferred capital projects.

E. Health and Hospitals Corporation

The Health and Hospitals Corporation (HHC) suffers from a fundamental structural imbalance between recurring revenues and expenditures, but it ended FY 2008 with a cash balance of $880 million due to nonrecurring supplemental Medicaid payments. While the Governor's proposed budget includes a number of initiatives that would adversely affect the HHC, the Governor has also proposed raising outpatient care reimbursement rates and creating a new indigent care pool to subsidize care to the uninsured or underinsured that would benefit the HHC. On a net basis, these proposals would have a net adverse impact of $130 million in FY 2010. The HHC could benefit from the federal economic stimulus bill with funding for health information technology and capital funding for clinics.

F. West Side Development

As part of the City's effort to redevelop the far West Side of Manhattan, the City created the Hudson Yards Infrastructure Corporation (HYIC). The HYIC is authorized to issue up to $3.5 billion in bonds to finance the extension of the No. 7 subway line and other improvements on the far West Side. The HYIC issued $2 billion in bonds in December 2006, with interest payments beginning in FY 2008. In the near term, development within the Hudson Yards Special District is not expected to generate sufficient revenues to cover both principal and interest payments, and thus the City Council has agreed to support, subject to annual appropriation, the interest costs on up to $3 billion of HYIC bonds to the extent that project revenues are insufficient to cover principal and interest costs.

In FY 2008 and so far in FY 2009, payments from the City have not been needed because enough revenue has been generated—from the investment earnings on unused bond proceeds, the receipt of tax equivalency payments (i.e., the property tax generated by improvements to residential properties), and the sale of development rights—to fully fund the interest payments on the HYIC bonds. Revenues are currently sufficient enough that the City expects its interest liability to be reduced to $74 million from $85 million in FY 2010, but the January Plan assumes that the City will fund the full interest cost in subsequent years.

On May 22, 2008, the MTA, the Long Island Rail Road, and a joint development venture of Related Companies and Goldman Sachs Group signed an agreement that stated that a contract would be signed by November 3, 2008, regarding development over the eastern and western rail yards located at the southern end of the Hudson Yards Special District. As a result of the financial crisis, however, the MTA and Related have agreed to delay the contract signing until January 31, 2010, for the eastern rail yard and January 31, 2011, for the western rail yard, which still must be rezoned. The two parties are working on instituting economic milestones, and if the economy improves the contract signing could be accelerated.

The MTA is constructing the $2 billion extension of the No. 7 subway line from its existing terminus at 41st Street and 8th Avenue to 34th Street and 11th Avenue. A planned station at 41st Street and 10th Avenue is not currently funded but could be included in the final project if funding is made available. Currently, no agreement exists regarding whether the MTA, the HYIC, or the City would fund any cost overruns on the extension if they were to occur.

G. Lower Manhattan Redevelopment

In October 2008, the Port Authority of New York and New Jersey released a major reassessment of rebuilding at the World Trade Center (WTC). The reassessment was designed to make the rebuilding effort more transparent and realistic, and to resolve several fundamental issues that had stifled the rebuilding effort for years. The report also extended completion deadlines and raised project cost estimates for most projects to better conform with construction reality.

Since the report was released, the real estate and financial markets have collapsed, raising new concerns that the commercial development on the site (Towers 2, 3, and 4) will be further delayed due to market conditions. Specific updates of the major WTC projects are discussed below.

- One World Trade Center (i.e., the Freedom Tower) is expected to be completed during the fourth quarter of 2013 at an estimated cost of $3.18 billion. Preliminary lease commitments have been made on approximately half of the tower, with State and federal agencies occupying approximately 1 million square feet and the China Center, the first private tenant in the Freedom Tower, occupying slightly less than 200,000 square feet. The Freedom Tower is currently 105 feet above street level—the height of a seven-story building.

- The WTC Transportation Hub (the third-largest transportation hub in the City) is expected to be completed during the fourth quarter of 2014 at an estimated cost of $3.25 billion. The Port Authority undertook a redesign that considerably simplified the original plan and reduced costs. The Transportation Hub will devote more than half of its 800,000 square feet to retail space and will serve 200,000 commuters per day, connecting PATH service, 13 different subway lines, and the Battery Park City ferry terminal, as well as other locations on and around the WTC site.

During the recent assessment, the Port Authority made extensive changes to the rebuilding program to ensure that the Memorial Plaza will be open to the public by the tenth anniversary of the terrorist attacks. Since the rest of the site will still be under construction, the Plaza will be open to the public on a limited basis as final work on the Plaza progresses and the Visitor's Center is completed. The Memorial's museum is scheduled to open in 2013. The Port Authority's share of this project is $195 million, with the balance to be paid by the September 11th Memorial Foundation. The Vehicular Security and Tour Bus Parking Facility (VSC) is scheduled to be completed during the third quarter of 2012 at an estimated cost of $633 million.

In addition to the public projects underway, the Port Authority's master plan includes space for Tower 5 to be located at 130 Liberty Street, the site of the former Deutsche Bank building, which the Lower Manhattan Development Corporation is in charge of deconstructing. In mid-2008, delays in the deconstruction of the Deutsche Bank building and JPMorgan Chase's acquisition of Midtown office space with its purchase of Bear Stearns led to the termination of discussions between the Port Authority and JPMorgan Chase regarding the development of Tower 5 to house JPMorgan Chase's financial headquarters. The delay in the deconstruction of the building could also affect construction of the VSC.

Also according to the master site plan, Silverstein Properties is to construct three office towers (Towers 2, 3, and 4) on the easternmost portion of the site. The financing and construction of all three of the planned office towers will be challenged by the deteriorating real estate and financial markets. Silverstein Properties is currently in discussions with the Port Authority on a new timeline for development and alternative financing options to better reflect market conditions.

X. Other Issues

The following issues could have a significant impact on the City's financial plan.

A. Other Post-Employment Benefits

In June 2004, the Governmental Accounting Standards Board (GASB) issued Statement No. 45, which establishes standards for measuring and reporting the expense and related liabilities of other post-employment benefits (OPEBs), such as health insurance, on an actuarial basis. Although GASB does not require entities to fund these costs on an actuarial basis, entities could realize significant long-term savings if they did.

In September 2008, the City reported that its accrued liability for past OPEB services was $63.3 billion, and estimated that the present value of its future OPEB obligations was $41 billion. Overall, the present value of projected OPEB benefits totaled $104.3 billion, an increase of $2.3 billion from the FY 2006 level. The "normal cost," or the portion of the present value of future obligations that is attributed (on an actuarial basis) to services received in the current year, was estimated at $3.1 billion, about $130 million less than estimated in 2006 due to lower forecasts of health insurance costs.

To address the growing cost of OPEBs, the City created its own Retiree Health Benefits Trust (RHBT) in 2006, setting aside surplus resources to help fund future costs. These resources are invested, and any earnings will reduce future costs to City taxpayers. The City contributed $2.5 billion to the RHBT during fiscal years 2006 and 2007 when the local economy was booming. The Mayor, however, now proposes to use $1.1 billion of these resources over a three-year period to pay a portion of the City's retiree health care expenses in order to help balance the operating budget.

B. Governmental Accounting Standards Board Statement No. 49

GASB has issued Statement No. 49, which requires certain pollution remediation costs to be accounted for as expense items. Pursuant to the Financial Emergency Act (FEA), such costs may not be included in the City's capital budget or financed through the issuance of bonds, absent action by the Financial Control Board.

The City was required to begin compliance with GASB 49 as of the start of FY 2009 (i.e., July 1, 2008). The City estimated that immediate compliance with GASB 49 for budgeting purposes would increase expense budget costs by up to $500 million annually, because certain environmental remediation costs would no longer be eligible for capital reimbursement.[11] These costs would have hit the expense budget at the same time that the City was dealing with the revenue losses anticipated from the economic slowdown and the Wall Street credit crunch. In addition, the City had difficulty identifying the environmental remediation component of larger capital projects, such as school renovations. Pursuant to the FEA, the City would have been unable to move forward with these capital projects until the environmental remediation costs were identified. (The City hired KPMG to assist in this effort.)

While the City has complied fully with GASB 49 for financial reporting purposes, it has sought additional time to comply with GASB 49 for budgeting purposes as required by the FEA. (The FEA authorizes the Financial Control Board to phase in the implementation of new accounting standards when immediate implementation would have a substantial adverse impact on the delivery of essential services.) Given the potential adverse impact on the budget and the technical challenge of identifying the environmental remediation component of larger capital projects, the Financial Control Board approved a resolution on April 30, 2008, which defers the City's implementation of GASB 49 for budgeting purposes until July 1, 2010. The resolution requires the City to report twice each year on its progress in complying with GASB 49 for budgeting purposes. The City issued its first report in December 2008, which indicated that the City was making progress estimating the budgetary impact and that a final estimate would be completed by the end of calendar year 2009.

C. Financial Emergency Act

The Financial Emergency Act (FEA) was scheduled to terminate on July 1, 2008, but was effectively extended until 2033 when the State assumed responsibility (in 2003) for the outstanding 1970s fiscal crisis debt of the Municipal Assistance Corporation. Even though the Financial Control Board's authority to impose a control period terminated on July 1, 2008, it still annually reviews the five conditions that have been identified in the FEA as indications of serious fiscal stress for New York City that could jeopardize the orderly functioning of the City's fiscal affairs. One of those conditions relates to access to the credit markets. Although the City's credit rating remains high, it has had to reduce the size of planned debt issuances in response to a lack of liquidity in the financial markets. Although demand has recently improved, it has gone to the market more frequently to satisfy its cash needs. The Governor, at the City's request, has proposed changes to the FEA to permit the City to issue bond anticipation notes for one year rather than the current limit of six months, to provide greater flexibility given current limitations in the municipal credit market. The City previously proposed legislation that would restore the Financial Control Board's

[11] The City now states that compliance with GASB 49 for budgeting purposes would result in "significant increased costs to the City's expense budget."

authority to impose a control period and grant additional discretionary authority to waive new accounting regulations (such as GASB 49 for budgeting purposes).

D. New York City's Credit Rating

Since the summer of 2007, the City's credit ratings have been the highest in at least 70 years ("AA" from Standard & Poor's, "Aa3" from Moody's Investors Service, and "AA-" from Fitch Ratings). The ratings reflect the City's comprehensive financial planning process and the proactive steps the City has taken to address risks to its budget. Although the current credit outlook remains stable, the rating agencies continue to express concern about the recession; liquidity problems in the municipal credit markets; the City's heavy reliance on Wall Street; the rising cost of debt service and pension contributions; post-employment benefits other than pensions; and the size of the projected budget gaps for New York State.

E. Litigation

The City and its contractors face more than 11,000 claims that allege injuries ensuing from rescue and cleanup work at the World Trade Center (WTC) site. The January Plan assumes that no liability will arise from these claims. In 2004, the WTC Captive Insurance Company was formed to cover these kinds of claims, using $1 billion in federal aid—but the City cannot assure that the insurance will be sufficient to cover all the liability that could arise. The Mayor and members of Congress have previously proposed legislation that would mitigate the City's liability.

In March 2008, the U.S. Court of Appeals rejected the City's appeal to cap its liability from the Staten Island Ferry crash of October 15, 2003, because the City was found to be negligent in enforcing safety rules. The City has agreed to pay $64.9 million to settle 142 lawsuits (including all 11 death claims), out of a total of 172 lawsuits filed. In the single case tried in court thus far, a judge awarded $18.3 million to a plaintiff who was paralyzed in the crash.

As of February 11, 2009, 126 claims have been filed against the City and other parties related to two separate incidents of construction crane collapse, on East 51st Street and East 91st Street in Manhattan. Of these claims, 30 are currently in litigation—and the City's liability has not yet been established.

Appendix
City-Funded Staffing Levels

Between fiscal years 2003 and 2008, the size of the municipal workforce increased by 22,822, to reach 269,598 full-time and full-time-equivalent employees. More than half of the growth occurred in the Department of Education and in the Police Department, with significant additions in the Parks Department, the Department of Social Services, and the Department of Health and Mental Hygiene.

As of December 31, 2008, City-funded staffing totaled 268,839. The January Plan forecasts that City-funded staffing will decline by 22,623 by the end of June 2010 (see Figure 46), but most of the job losses, especially in education, will be restored with federal economic stimulus funds. Social services, housing, and general government agencies are below the levels planned for the end of the current fiscal year, and it is expected that most positions in these agencies will remain unfilled.

- The Police Department will reduce staffing by 3,162 employees (2,591 officers and 571 civilians) by the end of June 2010. The police force is projected to decline to 33,217 officers by the end of FY 2010—the lowest level since FY 1990.
- The Department of Education will reduce staffing by 16,352 employees (15,869 pedagogues and 483 non-pedagogues) by the end of June 2010, mostly through 13,930 teacher layoffs. If the City receives sufficient offsetting funds from either the State or the federal government, most of these job cuts could be averted. The other positions would be eliminated through attrition.
- The City University of New York will reduce staffing by 876 pedagogues and 410 non-pedagogues by the end of June 2010.
- The Fire Department will reduce the number of firefighters by 906, through attrition, and the number of civilians by 28, in a series of three layoffs, by the end of June 2010.
- The Department of Correction will reduce uniformed staffing by 908 employees and will add 167 civilian employees by the end of June 2010.
- The Department of Sanitation will eliminate 372 uniformed positions and will add 72 civilian employees by the end of June 2010.
- The Administration for Children’s Services will reduce staffing by 906 employees (including 608 layoffs) by June 2010.
- The City’s district attorneys and prosecutors will reduce staffing by 315 employees by the end of June 2009.

Figure 46
City-Funded Staffing Levels
(Full-Time and Full-Time-Equivalents)

Increase/(Decrease)

		Actual				Projected		Dec. 2008 to June 2010
		FY 2006	FY 2007	FY 2008	Dec. 2008	FY 2009	FY 2010	Change
Public Safety		**81,764**	**82,879**	**83,016**	**83,726**	**82,691**	**78,802**	**(4,924)**
Police Dept.	Uniformed	35,773	35,548	35,405	35,808	35,128	33,217	(2,591)
	Civilians	15,365	16,331	16,467	16,503	16,441	15,932	(571)
Fire Dept.	Uniformed	11,633	11,513	11,578	11,677	11,222	10,771	(906)
	Civilians	4,484	4,670	4,770	4,726	4,897	4,698	(28)
Correction	Uniformed	8,451	8,466	8,413	8,657	8,646	7,749	(908)
	Civilians	1,293	1,323	1,411	1,387	1,476	1,554	167
District Attys. & Prosecutors		3,428	3,544	3,582	3,607	3,292	3,292	(315)
Probation Department		850	1,019	931	902	925	943	41
Other		487	465	459	459	664	646	187
Health and Welfare		**24,307**	**24,718**	**25,208**	**24,926**	**26,118**	**24,647**	**(279)**
Social Services		10,982	11,003	10,478	10,272	11,347	10,891	619
Children's Services		6,319	6,605	7,101	6,930	6,760	6,024	(906)
Health and Mental Hygiene		4,516	4,797	5,298	5,229	5,385	5,354	125
Homeless Services		2,194	2,042	2,055	2,066	2,227	1,992	(74)
Other		296	271	276	429	399	386	(43)
Environment & Infrastructure		**19,051**	**19,759**	**19,736**	**17,882**	**18,743**	**18,052**	**170**
Sanitation	Uniformed	7,581	7,605	7,556	7,606	7,452	7,234	(372)
	Civilians	1,836	1,898	1,943	1,937	2,032	2,009	72
Dept. of Transportation		2,218	2,307	2,345	2,379	2,321	2,344	(35)
Parks & Recreation		6,968	7,489	7,417	5,753	6,658	6,230	477
Other		448	460	475	207	280	235	28
General Government		**8,556**	**8,824**	**9,167**	**9,349**	**9,443**	**9,293**	**(56)**
Finance		2,229	2,199	2,203	2,092	2,208	2,208	116
Law Department		1,352	1,370	1,370	1,365	1,317	1,314	(51)
Citywide Admin. Services		1,277	1,335	1,387	1,662	1,608	1,713	51
Taxi & Limo. Commission		445	422	422	426	466	462	36
Investigations		245	265	241	235	271	240	5
Board of Elections		421	415	550	617	377	377	(240)
Info. Technology & Telecomm.		866	978	1,057	1,078	1,171	1,087	9
Other		1,721	1,840	1,937	1,874	2,025	1,892	18
Housing		**1,744**	**1,873**	**1,937**	**1,925**	**2,114**	**2,039**	**114**
Buildings		1,093	1,181	1,240	1,246	1,355	1,339	93
Housing Preservation		651	692	697	679	759	700	21
Department of Education		**113,454**	**116,240**	**121,083**	**121,069**	**119,743**	**104,717**	**(16,352)**
Pedagogues		89,369	92,491	97,189	97,763	96,921	81,894	(15,869)
Non-Pedagogues		24,085	23,749	23,894	23,306	22,822	22,823	(483)
City University of New York		**6,436**	**6,600**	**6,931**	**7,497**	**6,504**	**6,211**	**(1,286)**
Pedagogues		4,052	4,154	4,406	4,925	4,126	4,049	(876)
Non-Pedagogues		2,384	2,446	2,525	2,572	2,378	2,162	(410)
Elected Officials		**2,441**	**2,513**	**2,520**	**2,465**	**2,568**	**2,455**	**(10)**
Total		**257,753**	**263,406**	**269,598**	**268,839**	**267,924**	**246,216**	**(22,623)**

Sources: NYC Office of Management and Budget; OSDC analysis