Review of the Financial Plan of the City of New York

June 2013

Report 2-2014

New York State
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I. Executive Summary

On May 2, 2013, the Mayor released his executive budget for FY 2014 and the associated four-year financial plan ("the May Plan"). The May Plan (see Figure 1) reflects the estimated impact of federal sequestration, the cost of Superstorm Sandy and the enacted State budget. Although the May Plan projects modest budget gaps beginning in FY 2015, the City has yet to reach new labor agreements with its unions.

The May Plan assumes that New York City's economic recovery will continue, though at a slower pace than in recent years. Since the economic recovery began in 2009, the City has added jobs at a much faster pace than the nation and has regained nearly twice as many jobs as were lost during the recession. About two-thirds of the new jobs, however, have been in sectors that pay less than the citywide average salary.

Unlike past economic recoveries, the securities industry has not significantly contributed to the City's job gains. Despite strong profits, the industry has regained only 19.5 percent of the jobs it lost during the recession. Last year, the industry earned \$23.9 billion from its broker/dealer operations, making 2012 among the most profitable years on record.

Wall Street got off to another strong start in 2013, with first-quarter profits of \$6.6 billion—half of the City's forecast for the entire year. However, industry profitability has been volatile in recent years as the industry works through the fallout from the financial crisis. Regulatory reforms and the European sovereign debt crisis could also hold down profitability in subsequent quarters. Nonetheless, the first quarter is a positive development for the City's budget.

For the first time, the May Plan reflects the impact of federal sequestration, which the City estimates will reduce federal funding by a total of \$148 million over the course of fiscal years 2013 and 2014. The City intends to offset the impact on education and debt service, but funding for some social service programs will be cut. The May Plan does not reflect the impact of federal budget cuts that are scheduled to take effect in federal fiscal year 2014.

Superstorm Sandy caused serious damage to public infrastructure, and hardship for thousands of New York City residents and businesses. The City estimates that storm preparations, emergency repairs, cleanup and damages totaled \$4.5 billion. The May Plan assumes that federal funds will cover most of the costs incurred by the City, although a portion of the funding could be lost to sequestration. The City was recently awarded an additional \$1.8 billion in federal grants to be used to help home owners and businesses, and to begin mitigation projects against the impact of future storms.

The enacted State budget benefits the City by $381 million in FY 2014, mostly from an increase in education aid. The additional aid is contingent, as it was last year, on the implementation of a new teacher evaluation system. The City's failure to reach agreement with the teachers' union by the January 2013 deadline may have cost the City $250 million in FY 2013, but the loss will depend on the outcome of ongoing litigation. The State recently established a new teacher evaluation program for the City, because the City and the teachers' union were unable to reach an agreement on their own. The City has until September 1, 2013, to implement the new teacher evaluation program or risk the loss of $364 million in education aid in FY 2014.

The City developed a surplus of more than $2 billion during FY 2013, mostly from higher revenue ($1.5 billion) and a drawdown in reserves. Nearly half of the unanticipated revenue resulted from taxpayers shifting income into calendar year 2012 to avoid higher federal income tax rates that took effect on January 1, 2013. The City intends to transfer most of the surplus to FY 2014, but a small amount would be transferred to FY 2015 to help narrow the budget gap projected for that year.

The New York City real estate market continues to improve, especially for commercial and large residential properties such as apartment buildings, cooperatives and condominiums. The May Plan assumes that real property tax collections will be nearly $3 billion higher during the financial plan period than the forecast in June 2012.

The May Plan shows a balanced budget for FY 2014, but out-year budget gaps of $2.2 billion in FY 2015, $1.9 billion in FY 2016 and $1.4 billion in 2017. These gaps result in large part from the City's reliance on nonrecurring resources ($3.9 billion) to balance the FY 2014 budget (see Appendix A).

While revenue collections could be stronger than forecast by the City in the short run, the City faces some significant budget risks, including further delays in the sale of taxi medallions and the potential cost of new labor agreements (see Figure 2). The May Plan also includes cuts to municipal services (e.g., libraries, cultural institutions, after-school programs and fire companies) that have been proposed by the Mayor but rescinded during the budget adoption process in prior years.

New York City projects a significant surplus in FY 2013 and a balanced budget for FY 2014 based on reasonable assumptions. Overall, the City has recovered from the Great Recession faster than most municipalities, but our review finds that the City still faces a number of challenges.

Figure 1
New York City Financial Plan
(in millions)

	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
REVENUES					
Taxes					
General Property Tax	$ 18,561	$ 19,486	$ 20,328	$ 21,259	$ 22,026
Other Taxes	25,707	25,044	26,810	27,834	29,003
Tax Audit Revenue	1,060	709	709	709	709
Subtotal: Taxes	$ 45,328	$ 45,239	$ 47,847	$ 49,802	$ 51,738
Miscellaneous Revenues	6,359	6,562	6,612	6,619	6,730
Unrestricted Intergovernmental Aid	- - -	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(1,732)	(1,563)	(1,561)	(1,565)	(1,566)
Disallowances Against Categorical Grants	(15)	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 49,940	$ 50,223	$ 52,883	$ 54,841	$ 56,887
Other Categorical Grants	996	888	893	881	877
Inter-Fund Revenues	560	535	516	515	515
Federal Categorical Grants	9,005	6,429	6,312	6,295	6,292
State Categorical Grants	11,344	11,701	12,037	12,519	13,033
Total Revenues	**$ 71,845**	**$ 69,776**	**$ 72,641**	**$ 75,051**	**$ 77,604**
EXPENDITURES					
Personal Service					
Salaries and Wages	$22,083	$ 22,032	$ 22,158	$ 22,429	$ 22,785
Pensions	8,185	8,317	8,326	8,524	8,778
Fringe Benefits	8,553	8,827	9,447	10,148	10,913
Retiree Health Benefits Trust	(1,000)	(1,000)	- - -	- - -	- - -
Subtotal: Personal Service	$37,821	$ 38,176	$ 39,931	$ 41,101	$ 42,476
Other Than Personal Service					
Medical Assistance	$ 6,335	$ 6,366	$ 6,447	$ 6,415	$ 6,415
Public Assistance	1,378	1,387	1,385	1,385	1,391
All Other[1,2]	22,279	20,765	21,295	21,804	22,273
Subtotal: Other Than Personal Service	$ 29,992	$ 28,518	$ 29,127	$ 29,604	$ 30,079
General Obligation, Lease and TFA Debt Service[1,2,3]	$ 5,994	$ 6,245	$ 7,179	$ 7,510	$ 7,732
FY 2012 Budget Stabilization & Discretionary Transfers[1]	(2,431)	(31)	- - -	- - -	- - -
FY 2013 Budget Stabilization[2]	2,161	(2,161)	- - -	- - -	- - -
FY 2014 Budget Stabilization[3]	- - -	142	(142)	- - -	- - -
General Reserve	40	450	300	300	300
Subtotal	$73,577	$ 71,339	$ 76,395	$ 78,515	$ 80,587
Less: Intra-City Expenses	(1,732)	(1,563)	(1,561)	(1,565)	(1,566)
Total Expenditures	**$71,845**	**$ 69,776**	**$ 74,834**	**$ 76,950**	**$ 79,021**
Gap To Be Closed	**- - -**	**- - -**	**$ (2,193)**	**$ (1,899)**	**$ (1,417)**

Source: New York City Office of Management and Budget

1 Fiscal Year 2012 Budget Stabilization and Discretionary Transfers total $2.462 billion, including GO of $1.340 billion, TFA of $879 million, lease debt service of $156 million, net equity contribution in bond refunding of $23 million and subsidies of $64 million.

2 Fiscal Year 2013 Budget Stabilization totals $2.161 billion, including GO of $2.097 billion and subsidies of $64 million.

3 Fiscal Year 2014 Budget Stabilization totals $142 million.

Figure 2
OSDC Risk Assessment of the City Financial Plan
(in millions)

	Better/(Worse)				
	FY 2013	**FY 2014**	**FY 2015**	**FY 2016**	**FY 2017**
Surplus/(Gaps) per May Plan	**$ - - -**	**$ - - -**	**$ (2,193)**	**$ (1,899)**	**$ (1,417)**
Tax Revenue	- - -	300	200	200	200
Debt Service	150	- - -	100	- - -	- - -
Agency Actions	(59)	(137)	(125)	(125)	(125)
Taxi Medallion Sale	- - -	(300)	(400)	(360)	(400)
OSDC Risk Assessment	**91**	**(137)**	**(225)**	**(285)**	**(325)**
Surplus/(Gaps) per OSDC[4]	**$ 91**	**$ (137)**	**$ (2,418)**	**$ (2,184)**	**$ (1,742)**
Additional Risks and Offsets [5, 6]					
Federal Budget Reductions[7]	- - -	(150)	(200)	(200)	(200)

4 The May Plan includes a general reserve of $40 million in FY 2013, $450 million in FY 2014 and $300 million in each of fiscal years 2015 through 2017. The City also has a reserve of nearly $1 billion for disallowances of federal and State aid, which, if not needed for that purpose, could be used to help balance the budget.

5 The May Plan assumes that the 14 percent personal income tax surcharge (valued at more than $1 billion annually), which is scheduled to expire on December 31, 2014, will be extended as it has been every two to three years since it was enacted in 1991.

6 The City imposed a three-year wage freeze on City employees during the recession, but the City has not yet reached new labor agreements covering that period or subsequent years. The May Plan assumes that municipal employees will not be compensated for the wage freeze and will agree to annual wage increases of 1.25 percent during the plan period, which is less than the projected inflation rate. In addition, the City still has not reached a labor settlement with the United Federation of Teachers and the Council of School Supervisors and Administrators for the round of collective bargaining covering calendar years 2009 and 2010 (see Section VII, "Expenditure Trends," page 22, for further discussion of collective bargaining).

7 While the City's financial plan now reflects the impact of the federal sequestration in federal fiscal year 2013, it still does not reflect the potential impact of budget cuts scheduled to take effect in federal fiscal year 2014.

II. Economic Trends

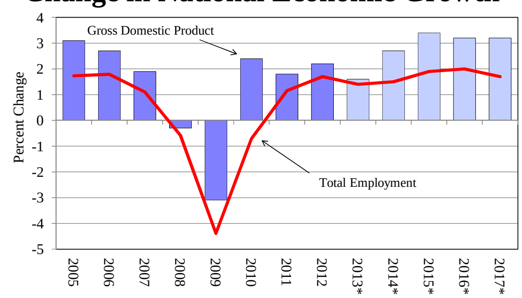
In the three years since the end of the Great Recession, annual growth in the nation's economy has not surpassed the modest rate of 2.5 percent. A weak global economy (especially in Europe), domestic fiscal tightening (due to tax increases and budget cuts) and uncertainty surrounding efforts to reduce the federal deficit continue to weigh down consumer and business spending. Nevertheless, a housing recovery has begun to contribute to economic growth, creating jobs in the construction and home-related industries and lifting home values and the number of home sales.

Because the federal government did not reach agreement on a long-term deficit reduction program, automatic spending cuts took effect on March 1, 2013, and many economists believe these will lower the nation's economic growth. With the deadline to set a new debt limit approaching, continued delay or inaction in resolving this issue or in reaching agreement on next year's budget could further reduce economic growth. IHS Global Insight and many other economists assume that an agreement on the debt limit will be reached and that more targeted tax increases and spending cuts aimed at reducing the federal budget deficit will replace the automatic cuts by the end of 2013. The May Plan, however, assumes the negotiation process will last into 2014.

Gross Domestic Product (GDP) rose by 2.2 percent in 2012, boosted by the steepest growth in consumer spending in more than two years. The May Plan assumes that GDP growth will slow to 1.6 percent in 2013 as the full effects of the federal tax increases and spending cuts begin to weigh on the economy. Growth is projected to gradually strengthen to more than 3 percent by 2015 (see Figure 3).

Figure 3

Change in National Economic Growth



*City forecast

Sources: U.S. Bureau of Economic Analysis; NYC Office of Management and Budget

Since the end of the recent recession, the United States has added 6.2 million jobs (a gain of 4.8 percent), recovering 70 percent of the jobs lost during the recession. The private sector has added 6.8 million jobs, while government has continued to shed jobs (626,000). While job growth is expected to slow from the 2012 rate, employment is projected to increase enough to bring the unemployment rate down from 8.1 percent in 2012 to below 7 percent by 2015, at which point the Federal Reserve is expected to begin raising interest rates.

Economic growth has been much stronger in New York City than in the nation, but the May Plan assumes that economic growth in the City will lag behind the nation throughout the financial plan period. During the first four months of 2013, the rate of job growth in the City still exceeded the national rate.

Recent employment revisions reveal that the City gained more jobs than originally reported. Additionally, the level of total employment surpassed the previous peak set in 1969 and set new records in both 2011 and 2012, when it reached 3.9 million. The pace of job creation (2.3 percent in 2011 and 2.1 percent in 2012) was the strongest in any two consecutive years since 1999 and 2000. The City has recovered nearly twice as many jobs as it lost during the recession.

Job recovery has been uneven across the City's employment sectors. As of April 2013, neither the finance sector nor the construction sector had recovered all the jobs lost during the recession, and manufacturing and government continued to shed jobs. Nevertheless, each of the sectors of trade, information, business services, tourism and personal services had regained more jobs than were lost.

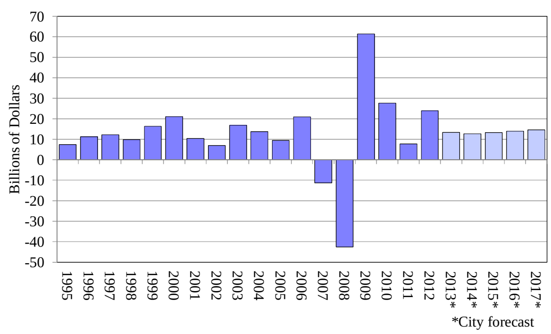
The mix of job gains has shifted toward lower-paying sectors. The sectors with gains since the recession have an average annual salary of $70,000, while the jobs lost during the recession had an annual average of $118,000. In some sectors, low average pay is also a function of a large number of workers who work part-time (e.g., in retail trade, restaurants and many tourism-related businesses). In 2012, the citywide average salary fell by 1.1 percent (the first decline since the recession), reflecting more jobs in lower-paying industries coupled with lower Wall Street bonuses for performance in 2011 that were paid in the first quarter of 2012.

The May Plan assumes that the pace of job growth will slow to 1.4 percent in 2013, and then average 1.2 percent between 2014 and 2017, compared to a national average of 1.8 percent. The May Plan assumes that wage gains will accelerate to 3.5 percent in 2013 from 1 percent in 2012, and then stay at a similar pace between 2014 and 2017. However, the City expects that more than one-third of the jobs added in 2013 and 2014 will be in the lower-paying sectors of health and social services, and tourism.

Wall Street continues to work its way through the fallout from the financial crisis and a new regulatory environment. Profits at the broker/dealer operations of New York Stock Exchange member firms tripled to $23.9 billion in 2012, driven primarily by trading gains. The Office of the State Comptroller (OSC) estimated that the industry's cash bonuses for the 2012 bonus season grew by 8 percent, driven in part by bonuses deferred from prior years.

Figure 4

Wall Street Profits



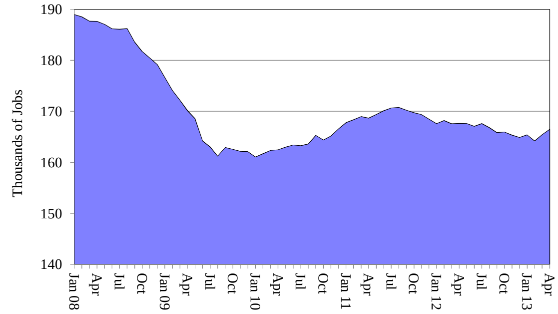
Sources: NYSE Euronext; Securities Industry and Financial Markets Association; NYC Office of Management and Budget

Wall Street got off to another strong start in 2013, with first-quarter profits of $6.6 billion, and equity markets recently surpassed the previous record highs set in 2007. The City assumes, however, that industry profits will fall to $13.4 billion in 2013 (see Figure 4) and then remain at this level in subsequent years as a result of financial industry reforms and the ongoing European debt crisis.

Unlike in previous recoveries, Wall Street has not significantly contributed to the City's job gains. Wall Street has accounted for less than 2 percent of the jobs created in the City's private sector, only a small fraction of the industry's average at this point in either of the last two recoveries. OSC estimates that Wall Street has recovered 19.5 percent of the jobs lost during the recent recession. The securities industry gained jobs between January 2010 and August 2011 (see Figure 5), but since then it has lost jobs again (4,300 jobs through April 2013). The May Plan assumes the industry will cut 1,000 jobs in 2013 and grow modestly for the remainder of the financial plan period.

Figure 5

Securities Employment in New York City



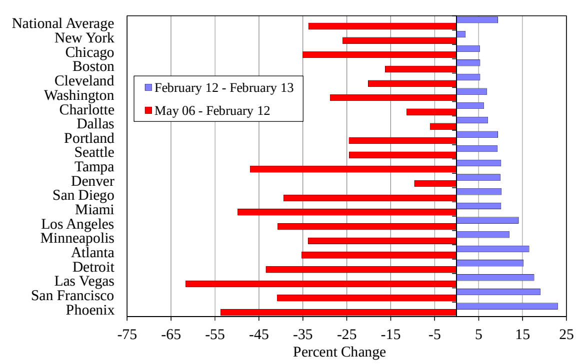
Note: Data have been seasonally adjusted.

Sources: NYS Department of Labor; OSC analysis

Tourism, which is a significant component of the City's recovery, continues to grow despite the impact of recessions in Europe and a stronger dollar. NYC & Company, the City's tourism agency, estimates that the number of visitors (52 million) and their spending ($36.9 billion) reached record levels in 2012. The City estimates that the number of tourists will reach 55 million by 2015. The number of foreign tourists reached a record 11 million, increasing the City's share of foreign tourists to 33 percent from 28 percent in 2006. Hotel occupancy rose to nearly 88 percent in 2012, and the average daily room rate rose to $284.

Figure 6

S&P/Case-Shiller Home Price Index



Source: S&P/Case-Shiller Home Price Index

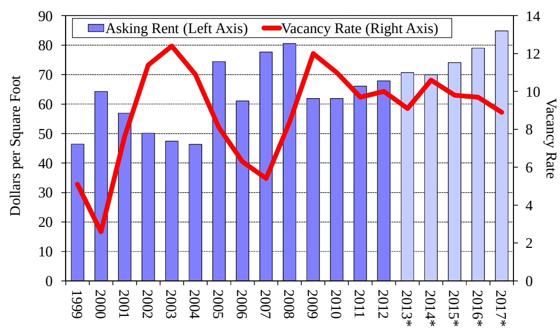
The City's housing recovery appears to be underway. The S&P/Case-Shiller Home Price Index shows that after declining by 26 percent from May 2006 to February 2012, home prices in the New York metropolitan area rose by 2 percent through February 2013 (see Figure 6). Although the growth in home values in the metropolitan area was lower than growth in all U.S. metropolitan areas (9 percent), the decline was also smaller than for the nation (34 percent).

According to Douglas Elliman, the median sales price of Manhattan apartments rose by nearly 6 percent during the first quarter of 2013, to $820,555 (the strongest pace since the third quarter of 2010). Listing inventory fell by 34 percent (the steepest decline in 12 years) to one of the lowest levels on record, as sellers looked to complete transactions ahead of changes in the federal tax laws. Sales of Manhattan apartments grew by more than 6 percent. Limited inventory, coupled with strong demand, has lifted sales prices for homes in many parts of the City.

The City's commercial real estate market continues to show improvement. Building sales remain strong, and new projects are moving forward in many parts of the central business district. The vacancy rate in Manhattan's primary office market edged up slightly in 2012, finishing the year at 10 percent, although rents continued to rise. The May Plan assumes that the vacancy rate in Manhattan's primary office market will fall to 9.1 percent by the end of 2013, and that average asking rents will rise to $70.75 per square foot (see Figure 7). The upcoming completion of towers one and four at the World Trade Center will add more than 4 million square feet of office space to the primary office market, which is expected to raise the vacancy rate to 10.6 percent by the end of 2014.

Figure 7

Manhattan Commercial Real Estate



*City forecast

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

III. Changes Since the June 2012 Plan

In June 2012, the City projected a balanced budget for FY 2013 and budget gaps of $2.5 billion in FY 2014 and about $3 billion in each of fiscal years 2015 and 2016. Since then, the City has increased its tax revenue forecast; delayed the proceeds anticipated from the sale of additional taxi medallions; proposed additional agency actions; drawn down reserves; and recognized other expenditure changes (see Figure 8). The City now projects a surplus of $2 billion in FY 2013, a balanced budget for FY 2014 and smaller out-year gaps ($2.2 billion in FY 2015 and $1.9 billion in FY 2016).

Figure 8

Financial Plan Reconciliation–City Funds
May 2013 Plan vs. June 2012 Plan

(in millions)

		Better/(Worse)		
	FY 2013	**FY 2014**	**FY 2015**	**FY 2016**
Gaps Per June 2012 Plan	**$ - - -**	**$ (2,508)**	**$ (3,117)**	**$ (3,070)**
Revenue Reestimates				
Personal Income Tax	639	(384)	(84)	(100)
Business Taxes	276	(100)	(37)	(210)
Real Estate Transaction Taxes	254	92	153	145
Real Property Tax	136	525	709	1,002
Other Taxes	30	(17)	(33)	(40)
Audits	335	- - -	- - -	- - -
All Other	(142)	(20)	(28)	(81)
Total	**1,528**	**96**	**680**	**716**
Taxi Medallion Sale	**(635)**	**(65)**	**(60)**	**360**
Agency Actions	**507**	**819**	**560**	**573**
Drawdown of Reserves				
Prior Payables	500	- - -	- - -	- - -
General Reserve	260	(150)	- - -	- - -
Total	**760**	**(150)**	- - -	- - -
Expenditure Reestimates				
Energy	109	140	155	202
Debt Service	94	435	8	(43)
Health Insurance	11	191	210	232
Social Services	(150)	(178)	(146)	(154)
Pension Contribution	(124)	(203)	(320)	(420)
Uniformed Agencies	(71)	(142)	(106)	(106)
Other	8	(330)	(199)	(189)
Total	**(123)**	**(87)**	**(398)**	**(478)**
Surplus/(Gap)	**2,037**	**(1,895)**	**$ (2,335)**	**$ (1,899)**
Surplus Roll	**(2,037)**	**1,895**	**142**	- - -
Gaps Per May 2013 Plan	**$ - - -**	**$ - - -**	**$ (2,193)**	**$ (1,899)**

Sources: NYC Office of Management and Budget; OSC analysis

The $2 billion surplus for FY 2013 is largely the result of unanticipated revenues ($1.5 billion) and a drawdown in reserves ($760 million). Tax collections were $1.3 billion higher than initially projected, with half of the revenue coming from transactions that were completed in 2012 to avoid higher federal tax rates that took effect in 2013. The City intends to use the surplus to help balance the FY 2014 budget ($1.9 billion) and to reduce the FY 2015 budget gap ($142 million).[8]

Legal challenges continue to delay the sale of 2,000 additional taxi medallions, which the City's June 2012 financial plan assumed would generate $1.5 billion over three years beginning in FY 2013. In November 2012, the City acknowledged that it would not realize any proceeds in the current fiscal year, and proposed additional agency cost-reduction actions (discussed in greater detail in Section IV, "The Agency Program") to mitigate the loss and help narrow the out-year budget gaps. The City now expects the sale proceeds to be spread out over four years beginning in FY 2014.

The City drew down $760 million in reserves in FY 2013, but increased the general reserve in FY 2014 by $150 million (for a total of $450 million) to offset potential risks to the financial plan, such as disallowances of federal aid for Superstorm Sandy.

Savings are expected from lower-than-planned energy costs and from health insurance premiums rising more slowly than anticipated because the State approved a 5.2 percent rate increase for the Health Insurance Plan of Greater New York for active employees, slightly more than half the increase assumed in the June 2012 financial plan (9.5 percent). Additionally, the City's capital plan has benefited from historically low interest rates. The City realized savings of $94 million in FY 2013 and $435 million in FY 2014 from refinancing outstanding debt and from lower-than-expected interest rates on new debt issuances and variable rate debt.

The effects of the federal sequester are reflected in the City's financial plan for the first time. The May Plan estimates that the sequester will reduce federal funds by a total of $148 million during fiscal years 2013 and 2014 combined. The City will offset the cuts to education with State funds and to subsidies for municipal bonds with City funds, and will use other federal funds to offset cuts in housing programs. Other cuts are expected to be implemented, affecting programs such as Head Start, meals for senior citizens, and services for people with HIV/AIDS (for more detail see Section VIII, "Other Issues").

Over the past year, the City also raised its expenditure forecasts for social services programs, mostly homeless shelters; pension contributions, mostly due to a shortfall in FY 2012 investment earnings and other reestimates; the uniformed services; and other agency programs.

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8 The May Plan projects a surplus of nearly $2.2 billion in FY 2013. Of this amount, $2 billion was generated in FY 2013 and the remaining surplus funds were transferred from FY 2012 into FY 2013.

IV. The Agency Program

The FY 2014 agency program was first proposed by the Mayor in November 2012, and was slightly modified in the preliminary and executive budgets. The program is expected to generate cumulative resources of $3 billion during the financial plan period, and would reduce planned staffing by 1,327 positions by the end of FY 2014 (see Figure 9). Most of the resources would come from actions that are not expected to affect services (e.g., cost reestimates, management initiatives and cost-shifts to other levels of government), but some initiatives would reduce services (e.g., cuts to mental health and school health programs) and raise fees.

The May Plan still includes a number of cost-reduction initiatives that have been proposed by the Mayor in prior years but rescinded by the City Council during the annual budget adoption process. These initiatives have an estimated value of $230 million in FY 2014, including a 36 percent reduction in funding to libraries and cultural programs, the closure of 20 fire companies, the loss of more than 20,000 after-school slots and the closure of seven school-based community centers. It is likely that the City Council will again seek to restore funding for these programs during the budget adoption process for FY 2014.

Figure 9
Agency Program
(in millions)

	Positions	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
Health and Social Services	491	$ 144.5	$ 140.3	$ 84.1	$ 101.5	$ 103.9
Dept. of Education	- - -	122.3	298.0	266.0	266.0	266.0
Uniformed Agencies						
Correction	393	28.1	41.4	16.4	16.6	16.9
Police	- - -	22.3	21.3	- - -	- - -	- - -
Fire	(24)	13.8	9.7	5.0	5.0	2.3
Sanitation	124	0.9	75.7	- - -	- - -	- - -
Transportation	144	25.5	41.9	30.0	26.3	26.3
Law	- - -	17.7	1.0	- - -	- - -	- - -
Dept. of Citywide Admin. Svcs.	75	17.1	16.6	2.7	2.7	2.7
Finance	- - -	16.7	19.1	20.1	21.2	21.7
Mayoralty	23	15.4	2.2	2.2	2.2	2.3
Dept. of Information Tech.	21	15.3	23.4	9.9	7.8	7.8
Fin. Information Svcs. Agency	- - -	11.3	2.2	1.8	1.8	1.8
Cultural Institutions	- - -	6.0	8.1	8.1	8.1	8.1
Libraries	- - -	4.1	16.7	16.7	16.7	16.7
All Other Agencies	80	46.3	45.8	41.8	41.2	41.0
Procurement Savings	- - -	- - -	55.5	55.5	55.5	55.5
Total	**1,327**	**$ 507.3**	**$ 818.9**	**$ 560.3**	**$ 572.6**	**$ 573.0**

Note: Excludes debt service savings.
Sources: NYC Office of Management and Budget; OSC analysis

The May Plan assumes that the Department of Education (DOE) will reduce planned spending by a total of $1.2 billion during the financial plan period. This represents 40 percent of the total value of the agency program, which is greater than the DOE's share of the City-funded budget. The majority of the savings would come from reestimates of the cost of special education ($672 million) and from non-classroom efficiencies ($368 million). The DOE also intends to raise the price of school lunches by $1.00 for students whose families' incomes exceed 185 percent of the poverty level.

Savings from agencies that provide health and social services would generate 19 percent of the total value of the agency program, or nearly $600 million. By our estimate, 40 percent of the resources would come from efficiencies, such as expanding the web-based application process for social services, that will eliminate the need for more than 1,000 employees by FY 2016. The City intends to maximize federal reimbursements ($154 million), but some of these initiatives may be jeopardized in the current federal budget environment. The Mayor has also proposed cuts ($81 million) to child care, mental hygiene and school health programs.

Savings in the uniformed agencies would generate $275 million by FY 2017, but the proposed actions are not expected to affect basic municipal services. The Department of Correction would reduce planned spending by canceling the reopening of the Queens Detention Center Complex, eliminating funding for 100 vacant civilian positions and revising inmate recreation and visitation schedules, an action that requires approval from the New York City Board of Correction. The Department of Sanitation has identified surplus funds in its waste export program, as well as savings due to delays in opening its marine transfer stations.

The agency program also includes some revenue-enhancement initiatives. The Department of Finance would generate about $100 million during the financial plan period by reviewing commercial and not-for-profit tax exemptions, and by increasing audit and collection efforts. The Department of Transportation would raise $62 million from new and increased parking and permit fees.

Our review of the May Plan has identified agency initiatives that may not achieve their targets because they have failed in the past or require outside approval that may not be forthcoming; these are valued at $59 million in FY 2013, $137 million in FY 2014 and $125 million in each subsequent year. For example, the City anticipates annual savings of $50 million in police overtime as well as additional federal Medicaid reimbursement for special education services ($50 million annually beginning in FY 2015), but similar initiatives in the past have failed to meet their targets.

V. State Budget Impact

The City's financial plan reflects the New York State Enacted Budget for State Fiscal Year (SFY) 2013-2014 and associated financial plan, which benefits New York City by $381 million in FY 2014, $645 million in FY 2015 and $947 million in FY 2016. The increase is largely due to planned annual increases in education aid, which averages $321 million over the next three years (see Figure 10).[9] Future increases in education aid are tied to the growth in personal income and dependent on the implementation of a teacher evaluation system.

Figure 10
Impact of the Enacted Budget for SFY 2013-2014 on New York City's Financial Plan
(in millions)

	FY 2014	FY 2015	FY 2016
Annual Increases in Education Aid			
SFY 2013-14	$ 364.0	$ 364.0	$ 364.0
SFY 2014-15	- - -	278.0	278.0
SFY 2015-16	- - -	- - -	320.0
All Other Actions	16.5	2.9	(14.6)
Total Impact	**$ 380.5**	**$ 644.9**	**$ 947.4**

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

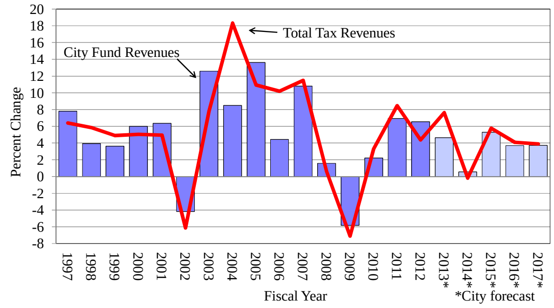
The City and the United Federation of Teachers (UFT) were unable to reach agreement on a new teacher evaluation system by January 17, 2013, the deadline required in last year's enacted State budget to ensure the City would receive $250 million in additional State education aid beginning in FY 2013. The enacted State budget restored the funding for future years, and the New York State Supreme Court has issued a preliminary injunction that prevents the State from withholding the aid for FY 2013, pending the resolution of a lawsuit challenging the constitutionality of the teacher evaluations. The State Education Commissioner recently established a new teacher evaluation program for the City, because the City and the UFT failed to reach an agreement on their own. The City has until September 1, 2013, to implement the new evaluation program or risk the loss of $364 million in education aid in FY 2014.

9 The enacted budget also includes $125 million in education grants for which the City may apply.

VI. Revenue Trends

The May Plan assumes that the growth in City fund revenues will slow to less than 1 percent in FY 2014, down from 4.6 percent in FY 2013 (see Figure 11). The slower rate of growth reflects the effects of a temporary change in taxpayer behavior, caused by higher federal income tax rates (including those on capital gains) that took effect on January 1, 2013. Some upper-income taxpayers acted to avoid the increase by accelerating income into calendar year 2012 from 2013 and later years. Based on actual tax receipts, the City estimates that $650 million in tax revenue was shifted into FY 2013 from subsequent years, primarily FY 2014. After adjusting for this shift, City fund revenues are forecast to grow by 3.2 percent in FY 2014, after a gain of 3.3 percent in FY 2013.[10]

Figure 11
Annual Changes in City Fund Revenues and Tax Revenues



Note: Adjusted for debt service on TFA and Tobacco Bonds, and the transfer of TSASC revenues.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

Growth in tax revenues, the largest component of City fund revenues, is forecast to slow to 2.7 percent in FY 2014, from 6.1 percent in FY 2013, after adjusting for the tax revenue shift.[11] This slowdown reflects the City's assumption that the pace of economic growth will moderate and that Wall Street profits will decline.

The May Plan expects that the sale of new taxi medallions will generate $1.5 billion in revenue over four years beginning in FY 2014, although litigation may delay or prevent receipt of these resources. The May Plan projects the sale will yield $300 million in FY 2014, which offsets a portion of the tax revenue slowdown.

Growth in City fund revenues is expected to rise in subsequent years as the economy strengthens and taxpayers adjust to the new rates.

Details of the City's revenue forecast are shown in Figure 12 and discussed below. Our analysis suggests that tax revenues could be greater than the City forecast by $300 million in FY 2014 and $200 million in each of fiscal years 2015 through 2017. This primarily reflects our projection of additional strength in personal income and sales tax collections. In addition, real estate transaction activity has remained strong in the first few months of 2013, and this will boost real estate transaction tax collections in the near term.

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[10] Although this revenue was shifted into FY 2013, the City intends to transfer these resources back into FY 2014 to help balance that year's budget.

[11] The May Plan shows the impact of the shift, forecasting that tax revenues would decline by less than 1 percent in FY 2014 after a gain of 7.6 percent in FY 2013.

Figure 12
City Fund Revenues
(in millions)

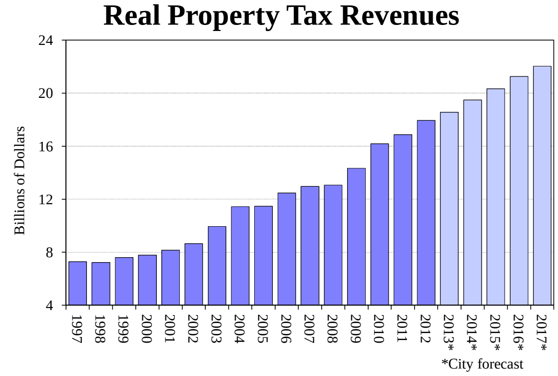
	FY 2013	FY 2014	Annual Growth	FY 2015	FY 2016	FY 2017	Average Three-Year Growth Rate
Taxes							
Real Property Tax	$ 18,560	$ 19,486	5.0%	$ 20,328	$ 21,259	$ 22,026	4.2%
Personal Income Tax	9,115	8,169	-10.4%	9,045	9,397	9,723	6.0%
Sales Tax	6,071	6,323	4.2%	6,590	6,829	7,092	3.9%
Business Taxes	5,762	5,726	-0.6%	5,990	6,153	6,454	4.1%
Real Estate Transaction Taxes	1,801	1,833	1.8%	2,094	2,293	2,515	11.1%
Other Taxes	2,959	2,993	1.2%	3,091	3,162	3,219	2.4%
Audits	1,060	709	-33.1%	709	709	709	0.0%
Subtotal	**45,328**	**45,239**	**-0.2%**	**47,847**	**49,802**	**51.738**	**4.6%**
Miscellaneous Revenues	4,702	5,073	7.9%	5,126	5,128	5,238	1.1%
Grant Disallowances	(15)	(15)	NA	(15)	(15)	(15)	NA
Total	**$ 50,015**	**$ 50,297**	**0.6%**	**$ 52,958**	**$ 54,915**	**$ 56,961**	**4.2%**

Note: Miscellaneous revenues include debt service on tobacco bonds.
Sources: NYC Office of Management and Budget; OSC analysis

1. Real Property Taxes

In January 2013, the City released its tentative real property tax roll for FY 2014, which showed that total market value for all properties rose by 4.3 percent, driven by strong gains for commercial properties and moderate gains for large residential properties (apartment buildings, cooperatives and condominiums). Market values for one-, two- and three-family homes grew by less than 1 percent.

Figure 13
Real Property Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

The May Plan assumes that assessed values, which are the basis for property tax calculations, will rise by 7 percent in FY 2014 as gains from prior years are phased in pursuant to State law, but that damage from Superstorm Sandy and taxpayer challenges to assessments will hold down the increase to slightly more than 5 percent. The final roll, which was released on May 28, 2013, was consistent with the City's assumptions.

Consequently, the May Plan assumes that real property tax collections will grow by 5 percent in FY 2014 (from 3.4 percent in FY 2013) to $19.5 billion (see Figure 13). In subsequent years, property tax revenues are projected to grow at a slightly lower rate of 4.2 percent annually, with weaker market value growth supplemented by the continued phase-in of increases from prior years. The strong growth in the FY 2014 tax roll will lift the tax base throughout the financial plan period, generating an additional $2.7 billion in revenue through FY 2017 over what was originally forecast in the June 2012 financial plan.

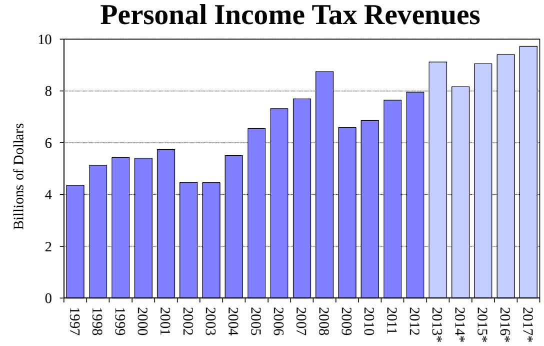
Commercial properties have driven the growth in assessed values and revenues in recent years. Between FY 2009 and FY 2013, commercial properties have accounted for 56 percent of the growth in citywide assessments. Apartment buildings, cooperatives and condominiums contributed about one-third of the growth in total assessments. One-, two- and three-family homes, which constitute more than two-thirds of all properties in the City, have accounted for about 6 percent of the growth in total assessments.

2. Personal Income Taxes

While the May Plan shows that personal income tax collections are projected to decline by more than 10 percent in FY 2014, the decline is due to changes in taxpayer behavior, as some upper-income taxpayers acted to avoid higher federal income tax rates (including on capital gains) that took effect January 1, 2013. As a result, revenue that would have been received in FY 2014 (and later years) was instead shifted into FY 2013. After adjusting for this shift, personal income tax collections are forecast to rise by 1.6 percent in FY 2014 after a gain of 7.8 percent in FY 2013.

Figure 14

Personal Income Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

Receipts in FY 2014 are expected to be constrained by a slowdown in job growth, and the May Plan's forecast of lower Wall Street profits in 2013 is expected to result in slower wage growth. While job growth is forecast to remain subdued in subsequent years, wage growth is projected to rise slightly as Wall Street profits improve. As a result, the expected growth in personal income tax collections averages 3.7 percent annually in each of fiscal years 2015 through 2017 (after adjusting for the income shift). Collections are expected to reach $9.7 billion by FY 2017 (see Figure 14).

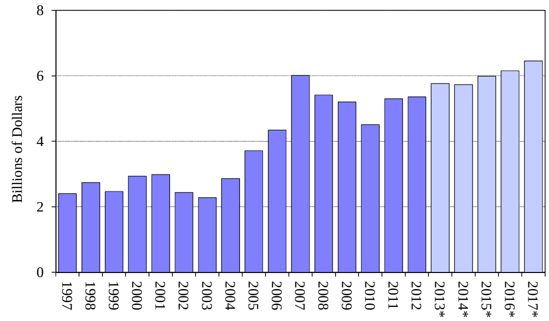
3. Business Taxes

After growing by an estimated 7.5 percent in FY 2013, business tax collections are forecast to decline slightly (by 0.6 percent) to $5.7 billion in FY 2014, the first decline since FY 2010 (see Figure 15). Forecasts are based on the City's assumptions of an overall slowdown in economic growth and a sharp decline in Wall Street profits.

The May Plan assumes that Wall Street profits will decline from $23.9 billion in 2012 to $13.4 billion in 2013, and will decline again to $12.6 billion in 2014 before rising to $14.6 billion in 2017. As profits begin to rise and economic conditions improve, the May Plan forecasts growth in the business taxes to average 4.1 percent annually from fiscal years 2015 through 2017. Collections are not expected to exceed prerecession levels until FY 2016.

Figure 15

Business Tax Revenues



*City forecast

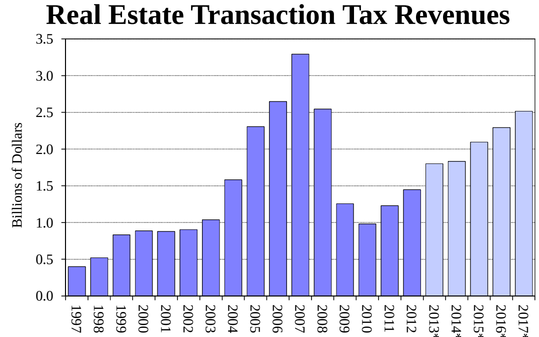
Sources: NYC Comptroller; NYC Office of Management and Budget

4. Real Estate Transaction Taxes

The May Plan forecasts that collections from the real estate transaction taxes will rise by 1.8 percent in FY 2014, much less than the 24.3 percent gain in FY 2013. As with the personal income tax, the increase in federal capital gains tax rates on January 1, 2013, led some investors to close on real estate transactions before the end of 2012. This shifted some transaction revenue out of FY 2014 and into FY 2013. Although collections in FY 2014 are expected to reach more than $1.8 billion, that level is only slightly more than half the peak reached before the recession (see Figure 16).

Figure 16

Real Estate Transaction Tax Revenues



*City forecast

Sources: NYC Comptroller; NYC Office of Management and Budget

The acceleration of closings is also reflected in transaction activity (including for large commercial deals), which has been strong during the first nine months of FY 2013. Refinancing activity has also been strong, helped by low interest rates.

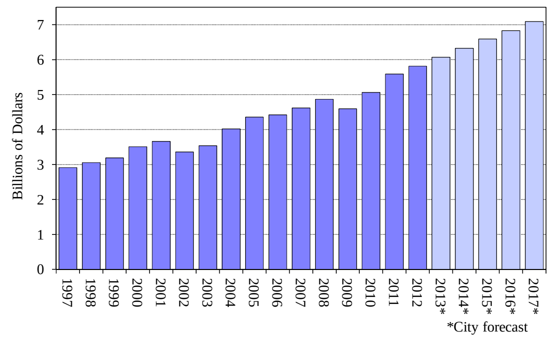
Given the continued improvement in the real estate markets, real estate transactions are forecast to grow at an average annual rate of 10 percent in subsequent years.

5. Sales Tax

Throughout the economic recovery, sales tax revenues have been bolstered by strength in the City's tourism sector, even as consumers have been cautious with their spending and as wages have shown only modest growth. In FY 2014, sales tax collections are expected to increase by 4.2 percent, reaching $6.3 billion (see Figure 17). This is comparable with the rate of growth in fiscal years 2012 and 2013, which averaged 4.3 percent annually.

Figure 17

Sales Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

For fiscal years 2015 through 2017, the May Plan forecasts sales tax collections to increase at an average annual rate of 3.9 percent, as wage growth continues to remain modest and tourism remains strong.

Unlike the personal income and real estate transaction taxes, the sales tax is not expected to be affected by the changes in the federal tax code. While Superstorm Sandy did disrupt spending patterns, it also led consumers and businesses to purchase alternate goods and services during the storm and its aftermath, and has since generated spending for reconstruction.

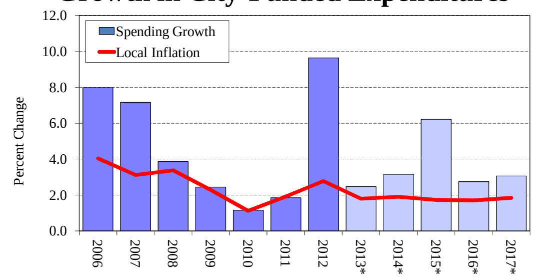
VII. Expenditure Trends

City-funded expenditures[12] are projected to grow by 4.1 percent ($2.1 billion) to $52.3 billion in FY 2014 (see Figure 18), driven primarily by continued increases in the cost of employee fringe benefits and debt service. In recent years, the City has diverted resources from the Retiree Health Benefits Trust to help balance the budget. This held down the growth in City-funded spending during those years, but the trust will be virtually depleted by the end of FY 2014. As a result, the rate of expenditure growth is expected to pick up in FY 2015.

The City's financial plan assumes that no financial liability will arise from wage freezes imposed on municipal workers during the recession, even though the City has not reached new labor agreements that cover this period. While the May Plan includes a reserve for collective bargaining for fiscal years 2013 through 2017, the amounts set aside are sufficient to fund annual wage increases of only 1.25 percent beginning in FY 2013.

Figure 18

Growth in City-Funded Expenditures



Note: City-funded expenditures grew by 9.6 percent in FY 2012 because the City replaced expiring federal stimulus aid ($1.8 billion) and a cut in State education aid ($812 million) with City funds.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

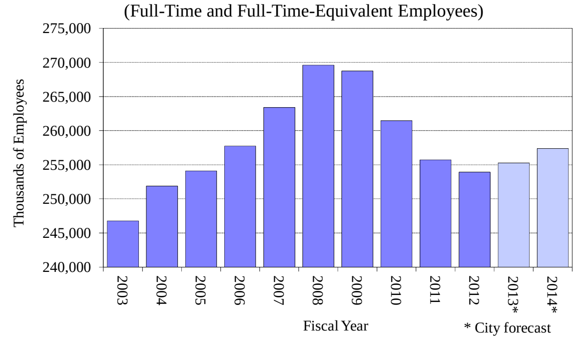
Although City-funded spending is projected to exceed City fund revenues by $2.1 billion in FY 2014, the budget will be balanced with resources from prior years. By our estimate, the FY 2014 budget includes $3.9 billion in nonrecurring resources, $1.6 billion more than the FY 2013 budget (for more information, see Appendix A).

The City-funded workforce grew between fiscal years 2003 and 2008 (see Figure 19) as the economy expanded, but since then it has contracted by nearly 6 percent as budget cuts were imposed by the City to help weather the recent recession. Although the May Plan assumes that staffing will rise in fiscal years 2013 and 2014, many positions are likely to remain vacant because the Mayor has imposed a hiring freeze (for more information, see Appendix B).

Figure 19

City-Funded Staffing Levels

(Full-Time and Full-Time-Equivalent Employees)



Note: Staffing levels are as of June 30 of each fiscal year.
Sources: NYC Office of Management and Budget; OSC analysis

[12] Adjusted for surplus transfers and including debt service on bonds issued by TSASC.

The May Plan is based on the trends shown in Figure 20 and discussed below.

Figure 20
Estimated City-Funded Expenditures
(Adjusted for Surplus Transfers and TSASC)
(in millions)

	FY 2013	FY 2014	Annual Growth	FY 2015	FY 2016	FY 2017	Average Three-Year Growth Rate
Salaries and Wages	$ 12,773	$ 13,215	3.5%	$ 13,618	$ 13,784	$ 13,892	1.7%
Pension Contributions	8,029	8,160	1.6%	8,170	8,367	8,621	1.8%
Medicaid	6,190	6,272	1.3%	6,353	6,322	6,322	0.3%
Debt Service	5,705	6,090	6.7%	6,961	7,293	7,519	7.3%
Health Insurance	4,599	4,857	5.6%	5,478	6,078	6,746	11.6%
Other Fringe Benefits	2,778	2,941	5.9%	3,025	3,124	3,219	3.1%
Energy	897	935	4.2%	950	937	947	0.4%
Judgments and Claims	735	768	4.5%	779	815	851	3.5%
Public Assistance	574	586	2.1%	584	584	588	0.1%
General Reserve	40	450	NA	300	300	300	NA
Drawdown Retiree Health Benefits Trust	(1,000)	(1,000)	NA	- - -	- - -	- - -	NA
Prior Year's Expenses	(500)	- - -	NA	- - -	- - -	- - -	NA
Other	9,460	9,073	-4.1%	9,074	9,210	9,372	1.1%
Total	**$50,280**	**$52,347**	**4.1%**	**$55,292**	**$56,814**	**$58,377**	**3.7%**

Sources: NYC Office of Management and Budget; OSC analysis

1. Collective Bargaining

All of the labor agreements with the unions that represent the municipal workforce have expired. Most of the agreements expired more than three years ago, making this period among the longest that many City employees have worked without an agreement since the fiscal crisis of the 1970s. The May Plan assumes that the municipal unions will agree to annual wage increases of 1.25 percent during fiscal years 2013 through 2017, which is lower than the projected inflation rate, following a three-year period in which the City effectively imposed a unilateral wage freeze through FY 2012. Each annual percentage-point increase in wages above the wage rates assumed in the May Plan would raise costs by $300 million annually.[13] The City's financial plan makes no provision for retroactive wage increases.

In addition, the City still has not reached a labor settlement with the United Federation of Teachers (UFT) and the Council of School Supervisors and Administrators for the prior round of collective bargaining covering calendar years 2009 and 2010. In early 2010, the State Public Employment Relations Board (PERB)

[13] If wages were to rise at the projected inflation rate without any offsetting savings, costs would increase by $13 million in FY 2013, $81 million in FY 2014, $219 million in FY 2015, $398 million in FY 2016 and $606 million in FY 2017.

found that contract negotiations between the City and the UFT had reached an impasse, and appointed a mediator to facilitate negotiations between the two parties, but the mediation was unsuccessful. In the fall of 2012, the PERB established a fact-finding panel to determine the underlying causes of the impasse. Although panel recommendations are nonbinding, they could serve as a framework for a new labor agreement. An agreement similar to those negotiated by the City's other unions for those years would increase costs by $900 million annually beginning in FY 2013, excluding any retroactive costs.

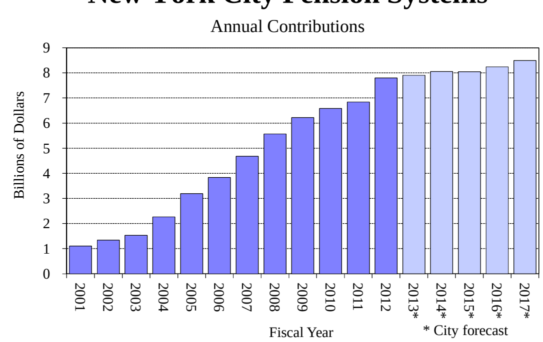
The City is preparing a solicitation to engage the services of new insurance carriers to provide the city workforce with a new health care plan, which the Mayor estimates could realize savings of up to $400 million annually. Any changes to the fringe benefits of City workers would require agreements between the City and its unions before they could be implemented.

2. Pension Contributions

After rising rapidly over the past decade, City-funded pension contributions are expected to rise more slowly during the financial plan period (see Figure 21). The May Plan assumes that pension contributions will average about $8 billion during fiscal years 2012 through 2014 before rising to $8.6 billion by FY 2017. These estimates reflect recent changes in the assumptions and methodologies used to calculate City pension contributions, which were recommended by the City Actuary and approved by the boards of trustees of the City's five pension systems and the State. The changes were fully implemented in January 2013.

Figure 21

New York City Pension Systems



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

The changes include a reduction in the investment earnings assumption from 8 percent to 7 percent; a different cost methodology to determine the projected cost of future pension benefits; and a longer amortization period, which will help free up resources during the financial plan period but also will result in higher costs in the longer term.[14] The City has engaged the services of an independent actuarial consultant to conduct two consecutive charter-mandated biennial audits of the pension systems. The results of these audits are expected to be released during FY 2014.

[14] The staff of the New York State Financial Control Board estimates that the longer amortization period deferred the payment of $1.7 billion in pension contributions planned for FY 2012.

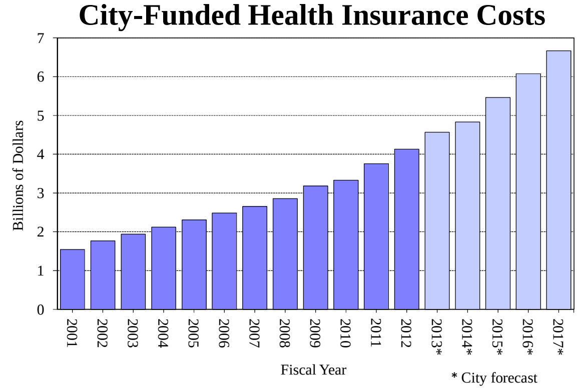
Although the City's pension systems fell short of their investment earnings target last year, the funds are on track to exceed the target in FY 2013. We estimate that, as of May 31, 2013, the pension systems have gained 13.6 percent on their investments compared to an expected annual return of 7 percent.

3. Health Insurance

City-funded health insurance costs are projected to rise by 5.6 percent in FY 2014 to $4.9 billion (see Figure 22), despite the smallest increase in health insurance premiums for active City employees in 15 years.[15] The May Plan assumes that health insurance costs will grow more rapidly over the balance of the financial plan period, from $4.9 billion in FY 2014 to $6.7 billion by FY 2017, an average of 11.6 percent annually. The greater pace of growth in these years reflects the City's expectation that the cost of health insurance premiums for active employees will resume growth at 9 percent annually. (Premiums for Medicare-eligible retirees are expected to grow by 8 percent annually during the financial plan period.)

Figure 22

City-Funded Health Insurance Costs



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

The Congressional Budget Office, the Kaiser Family Foundation, and others have noted that the growth in health care costs has begun to slow across the nation. Recent studies, while inconclusive, have found that the last recession and slow economic growth are linked to a temporary reduction in consumer health care spending, but that recently implemented cost controls could have a lasting impact.

4. Uniformed Agencies

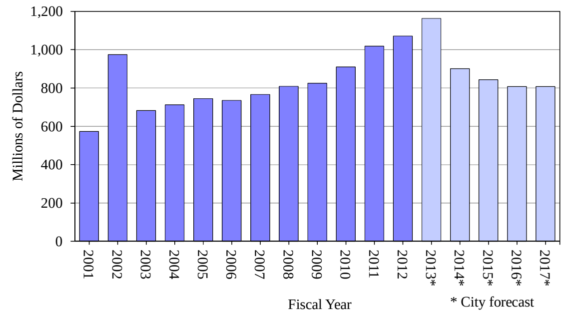
Overtime in the uniformed agencies (the Police, Fire, Correction and Sanitation departments) has grown by 18 percent since FY 2010 as a result of staff shortages in the Fire and Correction departments, along with the effects of severe weather. The May Plan assumes that overtime will total nearly $1.2 billion in FY 2013 (see Figure 23), including $150 million in overtime associated with Superstorm Sandy. Excluding these one-time costs, overtime is projected to decline by $112 million to $901 million in FY 2014.

[15] Last fall, the State Department of Financial Services (DFS) rejected an application from the Health Insurance Plan of Greater New York to increase premiums for active City employees by 10.1 percent in FY 2014 because of concerns regarding management practices. The DFS instead approved a premium increase of 5.2 percent.

The City believes overtime will be lower in FY 2014 because the federal court order banning the City from hiring firefighters has been lifted.[16] In addition, the Department of Correction is scheduled to add 109 officers by the end of FY 2014. The City estimates that the Police Department will implement cost-reduction initiatives for annual savings of $50 million, although such actions have failed in the past.

Figure 23

Uniformed Agencies Overtime Spending



Sources: NYC Office of Management and Budget; OSC analysis

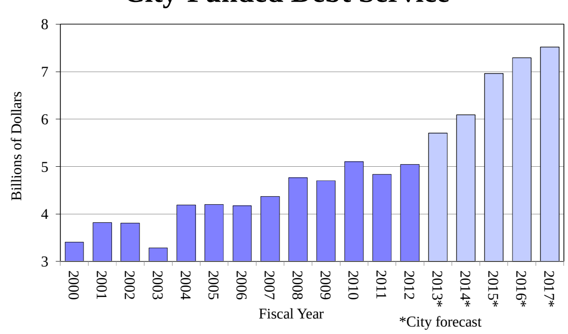
5. Debt Service

In recent years, the City has been taking advantage of historically low interest rates by refinancing outstanding debt. Since FY 2008, the City has refinanced more than $17 billion in debt (about one-quarter of all bonds outstanding) for cumulative savings of $1.5 billion through FY 2014. For example, during fiscal years 2013 and 2014 the City will realize nearly $900 million in savings from refinancing debt. The City will realize an additional $100 million in savings in FY 2015 from a recent refinancing that has not yet been reflected in the City's financial plan. In the past several years, the City has also realized significant savings from lower-than-expected interest rates on new debt issuances and variable rate debt. In fact, our analysis suggests that the City will likely realize an additional $150 million in savings in FY 2013 on variable rate debt, and could realize a similar amount in FY 2014 if interest rates remain low.

The May Plan assumes that City-funded debt service (adjusted for defeasances and surplus transfers) will increase from $5.7 billion in FY 2013 to $7.5 billion by FY 2017 (see Figure 24), an increase of 32 percent over four years. These estimates, however, do not anticipate any future debt refinancings and are based on relatively high interest rates given current Federal Reserve policies.

Figure 24

City-Funded Debt Service



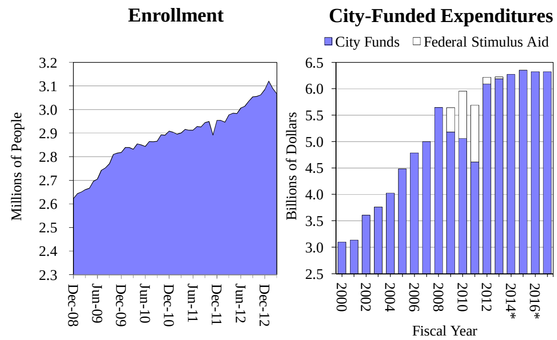
Note: Debt service amounts are adjusted for prepayments and debt defeasances.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

[16] In 2010 the federal court found that the City's hiring practices were biased against certain minorities, but the court recently approved revised hiring practices.

6. Medicaid

Over the past four years, enrollment in the Medicaid program grew by 15 percent to more than 3 million people as of March 2013 (see Figure 25), about one of every three New York City residents. Enrollment growth is largely attributed to the recent recession and is expected to continue with the enactment of federal health reform legislation, which will extend Medicaid eligibility. Despite the expected growth in enrollment, the City-funded cost of Medicaid will remain flat because of actions taken by the State.

Figure 25
Medicaid



*City forecast

Sources: NYC Human Resources Administration; OSC analysis

Medicaid expenditures have posed significant challenges to local budgets (including New York City) as a result of program expansions and the relatively rapid growth in the cost of medical care. During fiscal years 2000 through 2006, the City-funded cost of this program grew at an average annual rate of 7.5 percent to $4.8 billion in FY 2006. In 2005, the State assumed full financial responsibility for the Family Health Plus program (a Medicaid expansion program), and in January 2006 the State capped the growth in the local share of Medicaid to about 3 percent annually.[17]

The City-funded cost of this program reached $5.6 billion in FY 2008, and then declined to $4.6 billion in FY 2011 as a result of temporary federal stimulus aid (see Figure 25). The City's share of Medicaid reached $6.1 billion in FY 2012 (after the expiration of most federal aid). The May Plan assumes that it will reach $6.3 billion in FY 2014 and then remain at that level because last year the State agreed to assume all of the growth in the local share of Medicaid, to be phased in over a three-year period.

7. Homeless Services

The May Plan estimates that the City-funded cost of providing services to the City's homeless people will total $564 million in FY 2014, which is $40 million less than in the current fiscal year.[18] These estimates assume that the City Council will approve an initiative to shelter homeless families with fewer than four members in shared living units (for a savings of $9 million annually beginning in FY 2014), but the City

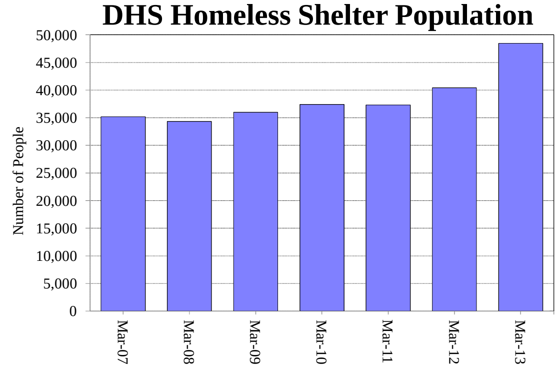
[17] The cap on the local share of Medicaid costs does not include the additional City-funded support provided to the Health and Hospitals Corporation (HHC) in order to leverage Medicaid supplemental payments for the care that the HHC provides to uninsured and Medicaid patients. These supplemental City-funded payments have averaged $650 million annually since FY 2006.

[18] The Department of Homeless Services, which shelters homeless families and single adults in more than 200 City facilities, accounts for 80 percent of these costs.

Council has rejected similar initiatives in the past. In addition, City funding for runaway and homeless youth programs are expected to decline by $7 million; however, in the past these funds have been restored at the urging of the City Council during the budget adoption process.

As shown in Figure 26, the shelter population managed by the Department of Homeless Services (DHS) reached 48,481 (including 20,654 children) in March 2013, which was 20 percent higher than one year earlier. The DHS also provides funding for short-term housing and overnight shelters, which are operated by community-based and faith-based organizations, for about 1,500 single adults in special needs populations.

Figure 26



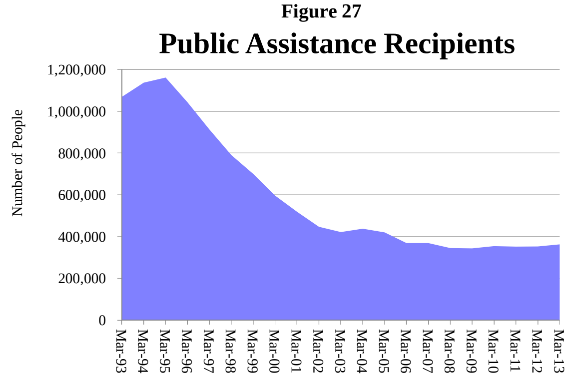
Source: NYC Department of Homeless Services; OSC analysis

The Human Resources Administration shelters more than 2,500 people in facilities for victims of domestic violence and another 2,000 people in facilities for homeless people with HIV/AIDS. The Department of Housing Preservation and Development provides emergency housing to about 2,000 people who have become homeless as a result of extraordinary circumstances, such as fires. The City also provides funding for 250 shelter beds operated by community-based and faith-based organizations for runaway and homeless youth aged 16 to 21.

8. Public Assistance

The public assistance caseload has grown by 6 percent over the past four years to 362,454 recipients in March 2013 (see Figure 27), even though the recent recession was the deepest of the postwar era.[19] In 2011 (the most recent year for which data are available), about one in every five New York City residents received public assistance or food stamps. City-funded expenditures for public assistance will total $586 million in FY 2014 (largely unchanged from the prior year) and remain relatively steady through FY 2017.

Figure 27



Sources: NYC Human Resources Administration; OSC analysis

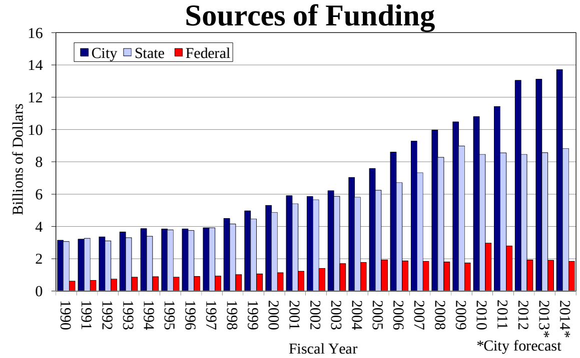
[19] The March 2013 caseload is 800,000 lower than the peak in March 1995, largely as a result of federal welfare reform measures implemented in the late 1990s that enforced work requirements.

VIII. Other Issues

1. Department of Education

Over the past decade, City funding for education has more than doubled, rising from $6.2 billion in FY 2003 to $13.2 billion in FY 2013 (see Figure 28). State education aid grew by less than half during the same period, rising from $5.9 billion to $8.6 billion.

Figure 28
Department of Education Sources of Funding



Sources: NYC Office of Management and Budget; OSC analysis

In FY 2014, total funding for education is projected to increase by nearly $1 billion to $24.8 billion. Of this amount, the Department of Education (DOE) intends to use $626 million to fund a variety of programmatic needs such as hiring additional teachers, opening new schools and expanding universal prekindergarten. The balance of the increase is scheduled to fund fringe benefits and debt service costs.

The State budget increases education aid to the City by $364 million in FY 2014, but like last year the aid is contingent on the implementation of a teacher evaluation program.[20] The State Education Commissioner recently established a new teacher evaluation program for the City, because the City and the teachers' union were unable to reach agreement on their own. The City has until September 1, 2013, to implement the new evaluation program or risk the loss of aid in FY 2014.

2. Metropolitan Transportation Authority

The February 2013 financial plan of the Metropolitan Transportation Authority (MTA) shows a budget surplus of $48 million in 2013 and relatively small budget gaps of $77 million in 2014, $21 million in 2015 and $227 million in 2016. These estimates assume fare and toll increases of about 7 percent in 2013 (which took effect in March 2013) and in 2015, as well as continued implementation of the MTA's cost-reduction program and the receipt of federal aid and insurance proceeds to cover most of the costs associated with Superstorm Sandy. The MTA's financial plan does not include the MTA's share of any storm mitigation projects.

[20] The City failed to reach an agreement with the United Federation of Teachers (UFT) on a new teacher evaluation program by the January 17, 2013, deadline for the receipt of additional State education aid in FY 2013. The City's financial plan reflects the loss of this aid in FY 2013, although there is a possibility that the aid could be restored. The New York State Supreme Court has issued a preliminary injunction preventing the State from withholding the aid pending the resolution of a lawsuit challenging the constitutionality of the teacher evaluation requirements.

The State's enacted budget for State Fiscal Year 2013-14 appropriated $40 million more than the amount assumed in the MTA's financial plan, and thus the MTA is exploring the possibility of increasing service with the additional funding. While real estate transaction tax receipts are significantly better than forecast through May 2013, collections from other taxes are lagging, although some of this variance may be due to timing. In addition, debt service is effectively $37 million lower than forecast through April 2013. Despite these positive developments, the MTA is facing other fiscal challenges including the outcome of labor negotiations, the pace of the economic recovery, and a court decision regarding the constitutionality of the payroll mobility tax, which generates about $1.6 billion annually.

3. Health and Hospitals Corporation

The Health and Hospitals Corporation (HHC) is the largest municipal hospital system in the country and the single-largest provider of health care to uninsured New York City residents. The HHC receives most of its patient revenue from public health plans, of which 65 percent comes from Medicaid.[21] The heavy reliance on Medicaid makes the HHC vulnerable to actions taken by the State and federal governments to reduce Medicaid reimbursements.

In FY 2007, the HHC ended its fiscal year with a cash balance of more than $1 billion (its highest closing balance ever) as it benefited from large, prior-year, nonrecurring Medicaid reimbursements. Because of a structural imbalance between recurring revenues and expenditures, the HHC has been drawing on these reserves to balance its budget. In January, the HHC estimated that it would end FY 2013 with a deficit of $43 million if it failed to recover $183 million in lost revenue related to Superstorm Sandy. Since the HHC does not expect to receive any federal aid to cover these operational costs before FY 2014, the City has provided financial assistance.

The City has agreed that the HHC may delay payments to the City totaling $389 million (largely to reimburse the City for medical malpractice and debt service costs) until FY 2014. Thus the HHC expects to end FY 2013 with a cash balance of $358 million, but it still needs to address the underlying structural imbalance.

In spite of recent efforts to reduce costs and increase revenues, the HHC projects large gaps beginning in FY 2014. To close these gaps the HHC plans to develop additional cost-containment actions that are expected to generate $100 million in FY 2014 and $300 million annually thereafter; however, these actions have yet to be identified. The HHC is also counting on the receipt of $500 million in additional Medicaid and Medicare revenue starting in FY 2014, but the likelihood of such additional funding is uncertain given current budgetary constraints.

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21 Including supplemental Medicaid payments for providing care to uninsured and Medicaid patients, the HHC realizes approximately 75 percent of its patient revenues from Medicaid.

4. New York City Housing Authority

For years, the New York City Housing Authority (NYCHA), which is dependent on aid from the federal government and rental payments from its low-income residents, has had difficulty balancing its budget and maintaining its housing assets in a state of good repair. While capital resources are limited, a consultant hired by the agency has identified opportunities to reduce costs and improve management practices that would increase the effectiveness of the available capital resources.

The NYCHA's current budget includes a variety of cost-reduction and revenue-generating initiatives. These include plans to raise rents on the 47,000 households that devote less than 30 percent of their household income to rent, increase resident parking fees, and lease parking lots and playfields surrounding its housing developments to private developers. Despite these actions, the NYCHA faces an estimated operating budget deficit of $192 million in calendar year 2013 because its budget does not yet reflect the impact of federal funding cuts. With less than seven months before the end of the year, the NYCHA has not identified actions to close a budget gap of this magnitude.

5. Sale of Taxi Medallions

The City's financial plan had initially assumed the City would realize $1 billion in FY 2013 from legislation authorizing the sale of additional taxi medallions, but since then the City has modified its expectations four times in response to legal challenges and other considerations that have delayed the proposed sale. While the City no longer expects any proceeds in FY 2013, the May Plan assumes that the sale will generate nearly $1.5 billion over four years beginning in FY 2014 ($300 million in FY 2014, $400 million in FY 2015, $360 million in FY 2016 and $400 million in FY 2017).

On August 17, 2012, a ruling by the New York State Supreme Court effectively invalidated the legislation, which authorized the sale of 2,000 additional taxi medallions and also allowed the creation of 18,000 new hail licenses that would allow livery drivers to pick up street hails in some parts of the City. The court ruled that several aspects of the legislation were unconstitutional. Specifically, the court found that the State could not authorize the sale without a home rule message from the City, which requires approval from the City Council.

In September 2012, the City appealed directly to the New York State Court of Appeals, the highest court in the State. Oral arguments were heard on April 24, 2013, and the Court is expected to issue a ruling in early June 2013. If the ruling is in the City's favor, the first sale of taxi medallions is planned for the fall of 2013. In the event of an adverse ruling, the City could seek a home rule message from the City Council authorizing the sale.

6. The Federal Budget

In January 2013, as part of an effort to reduce the federal deficit, Congress increased taxes on individuals who earn more than $400,000 and couples who earn more than $450,000, and permitted the expiration of a temporary reduction (of two percentage points) in the Social Security payroll tax. The bill also delayed, for two months, the implementation of automatic federal deficit reduction spending cuts (i.e., the sequester) of $85 billion in federal fiscal year 2013, with the cuts divided equally between federal defense and non-defense programs.

The May Plan estimates that the sequester will result in decreased federal funding to the City totaling $148 million during fiscal years 2013 and 2014, largely reflecting automatic cuts to discretionary programs in federal fiscal year 2013. The City will offset the cuts to education with State funds and will offset the cuts to subsidies for municipal bonds with City funds, and will use other federal funds to offset cuts in housing programs. Other cuts are still scheduled to take effect; these are concentrated in Head Start programs, meal programs for senior citizens and services for people with HIV/AIDS.[22]

Starting in federal fiscal year 2014, reduced discretionary spending will be achieved through lower caps on spending and not through direct cuts to programs. The City has not reflected any impact in the May Plan. OSC estimates that these cuts could reduce federal discretionary spending to the City by an additional $150 million in FY 2014 and $200 million annually in subsequent years.

The United States will likely reach its debt limit later in the year, and if the debt ceiling is not raised the federal government will be unable to borrow money to pay its financial obligations. During this process the President and congressional leaders may negotiate further spending cuts and revenue actions to reduce the annual federal budget deficit. They may also adopt alternative actions for the cuts imposed via the sequester.

[22] These estimates do not include the impact on programs outside of the City's financial plan, such as those at the New York City Housing Authority, the Metropolitan Transportation Authority and other organizations that receive federal funding.

7. Superstorm Sandy

Superstorm Sandy, which struck on October 29, 2012, resulted in an estimated $4.5 billion in costs to the City, including $3 billion in capital needs and $1.5 billion in emergency operating expenses. Federal assistance provided through the Federal Emergency Management Agency (FEMA) is expected to cover up to 90 percent of eligible costs, with the remainder funded by non-City sources.[23] The City is exploring the use of other federal relief assistance to cover the local share.

The $1.5 billion in storm-related operating expenses includes emergency repairs, debris removal and overtime. Rather than funding these costs with City funds, the City has set up a receivable line item for federal funds in its revenue budget, with corresponding budget codes in its expense budget. The largest cost is for the NYC Rapid Repairs program, which provided emergency repairs at no cost to private home owners ($577 million). The City's uniformed agencies spent an estimated $333 million (including fringe benefits), of which $150 million is for overtime (mostly in the Police and Sanitation Departments). The City's estimate also includes storm preparation and restoration costs for public hospitals ($104 million), parks ($76 million), public schools ($57 million), and roads and bridges ($52 million).

The City estimates that it will incur capital costs of $3 billion to make permanent repairs to damaged infrastructure, including parks and beaches ($785 million), roads and bridges ($775 million), hospitals ($712 million) and schools ($400 million). The City is in the process of developing scopes of work (i.e., the plan for repair and remediation) for each capital project, which will require approval from FEMA. The City expects that federal reimbursements from FEMA and other non-City sources will cover and match the flow of capital expenditures, but the amount and timing of reimbursements will ultimately be determined by the federal government. To this end, the May Plan includes a $300 million reserve for City-funded borrowing, which would increase debt service by about $20 million annually starting in FY 2016.

In addition, the City has been awarded an initial allocation of $1.77 billion in Community Development Block Grant Disaster Recovery (CDBG-DR) funds. The City intends to use these funds largely to provide assistance to home owners and businesses ($941 million), help fund the local share of recovery costs not covered by FEMA ($360 million), and study and begin implementing resiliency measures to protect against future storms ($294 million). The City's Special Initiative for Rebuilding and Resiliency is expected to release a report shortly that identifies strategies to strengthen infrastructure, communications, housing and other areas.

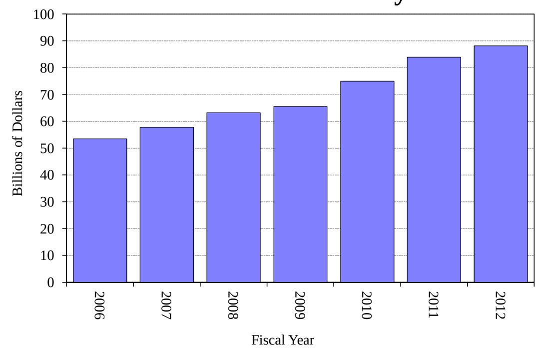
[23] Federal sequestration may reduce the total amount of federal relief expected to benefit the City by $500 million, including approximately $75 million that would benefit the operating budget.

8. 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 45 does not require entities to fund these costs on an actuarial basis, entities could realize significant long-term savings if they did so. As shown in Figure 29, the City's accrued OPEB liability for past employee service reached $88.2 billion as of FY 2012, an increase of $34.7 billion since FY 2006 (the first OPEB valuation year reported by the City), and $4.3 billion more than in the prior year.

Figure 29

Accrued OPEB Liability



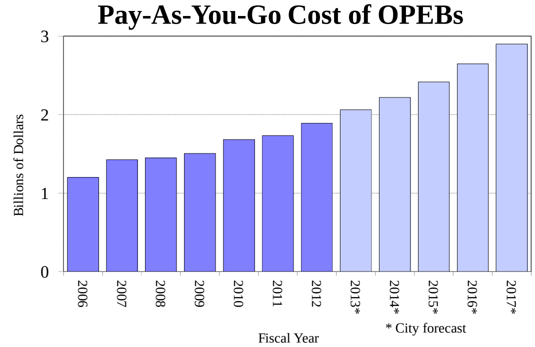
Sources: NYC Actuary; OSC analysis

Although the City is required to fund pension costs on an actuarial basis to ensure that current taxpayers pay their fair share of services, the City is not required to fund OPEBs on a similar basis. The City, like many employers, pays the annual cost of benefits provided to current retirees on a pay-as-you-go (PAYGO) basis.

In FY 2012, the City paid half of the present value of obligations ($2.8 billion) that is attributed, on an actuarial basis, to services received that fiscal year, deferring nearly $1.4 billion to future taxpayers. OPEB costs, on a PAYGO basis, are projected to rise from $1.9 billion in FY 2012 to $2.9 billion in FY 2017 (see Figure 30), an increase of 53.2 percent in five years.

Figure 30

Pay-As-You-Go Cost of OPEBs



Sources: NYC Actuary; NYC Office of Management and Budget; OSC analysis

The City deposited $2.5 billion in the Retiree Health Benefits Trust during the last economic expansion to help fund these costs. In recent years, however, the City has been drawing on these resources to help balance the budget, leaving future taxpayers to fund the full cost of services provided in past years. The City drew down $1.1 billion during fiscal years 2010 through 2012, and intends to draw down $1 billion in each of fiscal years 2013 and 2014 (a total of $3.1 billion including interest). OSC estimates that remaining funds in the trust at the end of FY 2014 could total $116 million.

Appendix A:
Nonrecurring Resources

Nonrecurring resources totaling an estimated $2.3 billion in FY 2013 and $3.9 billion in FY 2014 will be used to balance the City's budget in those years (see Figure 31).

Figure 31
Nonrecurring Resources
(in millions)

	FY 2013	**FY 2014**
Surplus Transfers - Net[24]	$ 270	$ 2,050
Retiree Health Benefits Trust	1,000	1,000
Debt Refinancings - Net	326	532
Taxi Medallion Sales	- - -	300
Educational Construction Fund	- - -	32
Prior-Year Payables	500	- - -
State Building Aid	143	- - -
Federal Medicaid Assistance	32	- - -
Total	**$ 2,271**	**$ 3,914**

Sources: NYC Office of Management and Budget; OSC analysis

- Surplus resources accumulated in prior years will be transferred to help balance the budget in fiscal years 2013 and 2014.
- The City plans to nearly deplete the balance of the Retiree Health Benefits Trust by drawing down $1 billion in each of fiscal years 2013 and 2014.
- Debt refinancings during fiscal years 2012 and 2013 will reduce debt service by $326 million in FY 2013 and $532 million in FY 2014, but will produce minimal savings in future years.
- The May Plan anticipates $1.5 billion from the sale of additional taxi medallions over a four-year period beginning in FY 2014.
- The Educational Construction Fund will transfer $32 million in surplus funds to the Department of Education in FY 2014.
- The City expects to save $500 million in FY 2013 from overestimating prior years' expenses, but the May Plan does not anticipate any future savings.
- The release of excess State building aid by the Transitional Finance Authority will benefit the City's budget by $143 million in FY 2013.
- Federal stimulus budget relief for Medicaid totals $32 million in FY 2013.

24 The City transferred FY 2012 surplus resources of $2.4 billion to FY 2013 and $31 million to FY 2014. The May Plan assumes the City will transfer surplus resources of $2.2 billion from FY 2013 to FY 2014, and that a $142 million surplus in FY 2014 would be transferred to FY 2015.

Appendix B: Staffing Levels

Between June 2008 and June 2012, the City's workforce (full-time and full-time-equivalent employees) declined by 15,666 positions (5.8 percent) to 253,932, reflecting the impact of agency cost-cutting actions. While the May Plan assumes that the workforce will increase by 1,339 positions during FY 2013 (see Figure 32), many of these positions are likely to remain vacant because the Mayor has imposed a hiring freeze. The May Plan also assumes staffing levels will continue to rise in FY 2014 (by 2,101 positions), primarily reflecting the addition of teachers at the Department of Education. These and other changes are discussed below.

- The Department of Education intends to add a net of 2,587 pedagogues next year, largely to restore previously planned cuts.
- The size of the police force is projected to hold steady during the financial plan period at about 34,500 officers, which is one of the lowest annual levels in the past 21 years. Despite the relatively small size of the police force, serious crime continues to decline.
- The Fire Department is expected to maintain uniformed staffing at about 10,300 positions during the financial plan period. Future hiring is planned only to offset anticipated attrition.
- The Department of Correction is expected to increase its uniformed staffing by 109 positions through the end of FY 2014 to fill posts previously staffed through overtime.
- The Department of Parks and Recreation plans to reduce staffing to 4,784 employees by June 2014, which would be 1,308 fewer than at the end of FY 2012.

Figure 32

City-funded Staffing Levels

(Full-Time and Full-Time-Equivalent Employees)

Additions/(Reductions)

		Actual		City Forecast		Variance		
		June 2012	March 2013	June 2013	June 2014	June 2012 to March 2013	June 2012 to June 2013	June 2013 to June 2014
Public Safety		**79,883**	**80,729**	**79,828**	**79,672**	**846**	**(55)**	**(156)**
Police	Uniformed	34,406	35,064	34,379	34,483	658	(27)	104
	Civilian	15,679	15,533	15,773	15,610	(146)	94	(163)
Fire	Uniformed	10,254	10,299	10,274	10,274	45	20	0
	Civilian	5,110	5,113	4,982	4,972	3	(128)	(10)
Correction	Uniformed	8,519	8,760	8,942	8,869	241	423	(73)
	Civilian	1,447	1,395	1,624	1,603	(52)	177	(21)
District Attys. & Prosecutors		3,690	3,817	3,130	3,137	127	(560)	7
Probation		766	736	707	707	(30)	(59)	0
Board of Correction		12	12	17	17	0	5	0
Health & Welfare		**22,598**	**22,420**	**23,940**	**23,532**	**(178)**	**1,342**	**(408)**
Social Services		10,090	10,096	10,570	10,135	6	480	(435)
Children's Services		6,097	6,022	6,398	6,463	(75)	301	65
Health & Mental Hygiene		4,268	4,199	4,701	4,567	(69)	433	(134)
Homeless Services		1,762	1,735	1,861	1,960	(27)	99	99
Other		381	368	410	407	(13)	29	(3)
Environment & Infrastructure		**17,085**	**14,906**	**16,964**	**16,278**	**(2,179)**	**(121)**	**(686)**
Sanitation	Uniformed	6,882	7,116	7,064	7,194	234	182	130
	Civilian	1,888	1,847	2,027	2,112	(41)	139	85
Transportation		2,005	1,874	1,864	1,968	(131)	(141)	104
Parks & Recreation		6,092	3,859	5,786	4,784	(2,233)	(306)	(1,002)
Other		218	210	223	220	(8)	5	(3)
General Government		**9,148**	**9,080**	**10,505**	**10,863**	**(68)**	**1,357**	**358**
Finance		1,814	1,819	1,951	1,976	5	137	25
Law		1,348	1,316	1,389	1,379	(32)	41	(10)
Citywide Admin. Services		1,397	1,281	1,409	1,426	(116)	12	17
Taxi & Limo. Commission		461	517	617	642	56	156	25
Investigations		192	202	230	228	10	38	(2)
Board of Elections		768	682	1,150	1,361	(86)	382	211
Info. Tech. & Telecomm.		963	961	1,093	1,162	(2)	130	69
Other		2,205	2,302	2,666	2,689	97	461	23
Housing		**1,522**	**1,486**	**1,610**	**1,639**	**(36)**	**88**	**29**
Buildings		1,067	1,026	1,140	1,162	(41)	73	22
Housing Preservation		455	460	470	477	5	15	7
Department of Education		**113,584**	**113,941**	**112,403**	**115,335**	**357**	**(1,181)**	**2,932**
	Pedagogues	91,841	92,530	90,775	93,362	689	(1,066)	2,587
	Non-Pedagogues	21,743	21,411	21,628	21,973	(332)	(115)	345
City University of New York		**7,815**	**9,550**	**7,635**	**7,768**	**1,735**	**(180)**	**133**
	Pedagogues	5,048	6,488	5,013	5,028	1,440	(35)	15
	Non-Pedagogues	2,767	3,062	2,622	2,740	295	(145)	118
Elected Officials		**2,297**	**2,264**	**2,386**	**2,285**	**(33)**	**89**	**(101)**
Total		**253,932**	**254,376**	**255,271**	**257,372**	**444**	**1,339**	**2,101**

Sources: NYC Office of Management and Budget; OSC analysis