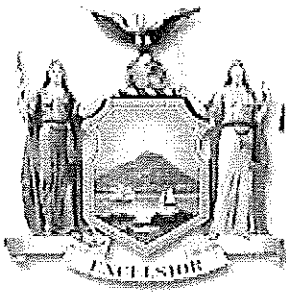


Staff Report

**REVIEW OF FYs 2011-2014  
FINANCIAL PLAN**

July 22, 2010



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## I. Overview

The city has adopted a balanced budget of \$63.2 billion for FY 2011. It was able to accomplish this task by prepaying \$3.6 billion of FY 2011 expenses with surplus resources from FY 2010. The budget assumes total revenue will decline by \$643 million in FY 2011 compared with the prior year, because of a projected drop in categorical aid from the federal and state governments. However, with the economy in the early stages of a gradual recovery, city-fund revenue increases by \$1.1 billion in FY 2011 due to the assumption of stronger tax collections. The city expects FY 2011 nonproperty taxes to grow by six percent, a rate that is consistent with a weak and unsteady economic recovery. In addition, the city has expanded the program to eliminate budget gaps and changed its labor policy to freeze all wages over the next two years, in response to growing expenditures, particularly in areas such as pensions, healthcare and debt service.

The city's four-year financial plan projects that the nation's economic recovery will be slow and unsteady. Given that view, the city assumes moderate revenue growth consistent with its forecast of a gradual economic recovery, moderating securities industry profits, and the winding down of federal stimulus programs. A moderate gain in employment for the nation and the city indicates that the long-awaited economic recovery is taking hold. The recession may have been less severe than was originally feared for the city because federal stimulus programs effectively channeled resources into job creation, infrastructure improvement, the housing and financial markets, and state and local government support. With the federal government stepping back from these support programs, the next challenge is for the economy to demonstrate staying power in the absence of stimulus spending.

Meanwhile, the growth in expenditures is outpacing the growth in revenues over the financial plan years. While the assumption for tax revenue growth is moderate, expenditure areas such as pension, healthcare, and debt service costs seem to be growing uncontrollably. For example, debt service costs are growing 55 percent over the life of the plan. This burgeoning cost is being generated largely by existing contract liabilities, making the expense mostly nondiscretionary. In FY 2014, when debt service at \$6.8 billion is projected to consume over 15 percent of the city's tax revenues, only 10 percent of the cost is derived from borrowing for capital commitments scheduled to be undertaken in FYs 2011-14, while 90 percent is derived from borrowing for prior-years capital contracts, which limits flexibility for substantial reductions during the plan years.

Despite over \$3 billion in agency reductions over the last two years, with total expenditures still outgrowing total revenues, the city projects budget shortfalls of \$3.3 billion in FY 2012, \$4.1 billion in FY 2013 and \$4.8 billion in FY 2014. Adding to the increased pressure of rising expenditures are the potential risks, mainly of state and federal aid, to the city's financial plan. We estimate these risks to add \$596 million in FY 2011, \$1.5 billion in FY 2012, \$1.6 billion in FY 2013 and \$1.3 billion in FY 2014 to the city's projected multi-billion dollar budget gaps. Our additional risks bring the city's projected budget imbalance to \$596 million in FY 2011, \$4.8 billion in FY 2012, \$5.7 billion in FY 2013 and \$6.1 billion in FY 2014.



The city, as it has effectively done in the past, must manage FY 2011 in a way that will build up the Budget Stabilization Account to help balance FY 2012. This is more important due to the fact that the outyear budget gaps, projected by the city, may be understated since there is no funding for any future labor contracts. In addition, given the fiscal condition of the state, the likelihood of further reductions in state aid, including education aid, is high. This would be on top of the likely loss of \$850 million in federal stimulus aid for education.



**JULY FINANCIAL PLAN:  
THE CITY'S OPERATING PROJECTIONS FOR  
FISCAL YEARS 2011-2014**

TABLE 1

(\$ in millions)

	FY 2011	FY 2012	FY 2013	FY 2014
<b><u>Revenues</u></b>				
Taxes:				
General Property	\$16,740	\$17,383	\$17,652	\$17,789
Other Taxes	21,504	22,766	24,012	25,204
Tax Audit Revenue	622	621	620	620
Anticipated Tax Program	--	--	--	--
Sale of Property Tax Liens	40	40	40	40
Miscellaneous Revenues	7,147	6,880	6,908	6,956
Unrestricted Intergovernmental Aid	14	314	314	314
Interfund Revenues	558	493	493	493
Less: Intracity Revenues	(1,616)	(1,498)	(1,502)	(1,502)
Disallowances	(15)	(15)	(15)	(15)
Total City Funds	\$44,994	\$46,984	\$48,522	\$49,899
Federal Categorical Grants	6,813	5,747	5,674	5,667
State Categorical Grants	11,352	12,274	12,487	12,903
<b>Total Revenues</b>	<b><u>\$63,159</u></b>	<b><u>\$65,005</u></b>	<b><u>\$66,683</u></b>	<b><u>\$68,469</u></b>
<b><u>Expenditures</u></b>				
Personal Service	\$36,462	\$36,303	\$37,721	\$38,878
Other Than Personal Service	26,167	26,863	27,617	28,769
General Obligation, Lease & TFA Debt Service	5,351	6,294	6,602	6,859
Budget Stabilization & Prepayments	(3,642)	--	--	--
General Reserve	437	300	300	300
Subtotal	\$64,775	\$69,760	\$72,240	\$74,806
Less: Intracity Expenditures	(1,616)	(1,498)	(1,502)	(1,502)
<b>Total Expenditures</b>	<b><u>\$63,159</u></b>	<b><u>\$68,262</u></b>	<b><u>\$70,738</u></b>	<b><u>\$73,304</u></b>
<b><u>Gap To Be Closed</u></b>	<b><u>\$0</u></b>	<b><u>(\$3,257)</u></b>	<b><u>(\$4,055)</u></b>	<b><u>(\$4,835)</u></b>



**CHANGES TO THE CITY'S OPERATING PROJECTIONS FOR  
FISCAL YEARS 2011-2014  
JULY FINANCIAL PLAN COMPARED TO JANUARY MODIFICATION**

TABLE 2

(\$ in millions)

	FY 2011	FY 2012	FY 2013	FY 2014
<b><u>Revenues</u></b>				
Taxes:				
General Property	(\$107)	(\$113)	(\$54)	(\$53)
Other Taxes	236	141	4	(54)
Tax Audit Revenue	10	10	10	10
Anticipated Tax Program	(219)	(241)	(262)	(284)
Sale of Property Tax Liens	(30)	0	0	0
Miscellaneous Revenues	154	(128)	(141)	(113)
Unrestricted Intergovernmental Aid	(326)	(26)	(26)	(26)
Interfund Revenues	87	43	43	43
Less: Intracity Revenues	(71)	49	50	50
Disallowances	0	0	0	0
Total City Funds	(\$266)	(\$265)	(\$376)	(\$427)
Federal Categorical Grants	199	27	(6)	(12)
State Categorical Grants	(414)	(133)	(570)	(292)
<b>Total Revenues</b>	<b><u>(\$481)</u></b>	<b><u>(\$371)</u></b>	<b><u>(\$952)</u></b>	<b><u>(\$731)</u></b>
<b><u>Expenditures</u></b>				
Personal Service	\$272	\$7	(\$327)	\$46
Other Than Personal Service	125	(338)	(308)	115
General Obligation, Lease & TFA Debt Service	(185)	8	23	44
Budget Stabilization & Prepayments	(759)	--	--	--
General Reserve	137	0	0	0
Subtotal	(\$410)	(\$323)	(\$612)	\$205
Less: Intracity Expenditures	(71)	49	50	50
<b>Total Expenditures</b>	<b><u>(\$481)</u></b>	<b><u>(\$274)</u></b>	<b><u>(\$562)</u></b>	<b><u>\$255</u></b>
<b><u>Gap To Be Closed</u></b>	<b><u>\$0</u></b>	<b><u>(\$97)</u></b>	<b><u>(\$390)</u></b>	<b><u>(\$986)</u></b>





TABLE 3

**RISKS TO THE FINANCIAL PLAN**

(\$ in millions, positive numbers are offsets to risks)

	FY 2011	FY 2012	FY 2013	FY 2014
<b>Stated Financial Plan Gap</b>	<b>\$0</b>	<b>(\$3,257)</b>	<b>(\$4,055)</b>	<b>(\$4,835)</b>
<b>Estimation</b>				
Property Taxes	\$0	(\$150)	(\$100)	(\$50)
Miscellaneous Revenue	25	50	75	100
Uniformed Services Overtime	(140)	(187)	(184)	(184)
<b>Subtotal</b>	<b>(\$115)</b>	<b>(\$287)</b>	<b>(\$209)</b>	<b>(\$134)</b>
<b>Not in Mayor's Control</b>				
Aid and Incentives to Municipalities	\$0	(\$302)	(\$302)	(\$302)
Accrual of State Education Aid	(202)	0	0	0
Federal Medicaid Assistance*	(279)	(61)	(269)	0
Federal Stimulus Aid for Education	0	(850)	(850)	(850)
<b>Subtotal</b>	<b>(\$481)</b>	<b>(\$1,213)</b>	<b>(\$1,421)</b>	<b>(\$1,152)</b>
<b>Risk Total</b>	<b>(\$596)</b>	<b>(\$1,500)</b>	<b>(\$1,630)</b>	<b>(\$1,286)</b>
<b>Total FCB Estimated Surplus/(Gap)</b>	<b>(\$596)</b>	<b>(\$4,757)</b>	<b>(\$5,685)</b>	<b>(\$6,121)</b>
*Note: The city has increased the \$300 million General Reserve by \$137 million in FY 2011 to partially offset the possible loss of FMAP funding.				



## II. Balancing the FY 2011 Budget

The city has adopted a balanced budget of \$63.2 billion for FY 2011. It was able to accomplish this task by prepaying \$3.6 billion of certain current-year expenses with surplus resources from FY 2010. In so doing, the city has fully depleted its Budget Stabilization Account and is left with no more funds to facilitate future-year budget balance.

The budget assumes total revenue will decline by \$643 million in FY 2011 compared with the prior year, because of a projected drop in categorical aid from the federal and state governments. However, with the economy in the early stages of a gradual recovery, city-fund revenue increases by \$1.1 billion in FY 2011 due to the assumption of stronger tax collections. The city expects FY 2011 nonproperty taxes to grow by six percent, a rate that is consistent with a weak and unsteady economic recovery.

The city's adopted budget for FY 2011 also reduces spending by \$643 million from FY 2010. The fact that \$3.6 billion of FY 2011 spending was prepaid in FY 2010 masks increasing expenditures in such areas as pension and debt service costs. In attempting to rein in spending, the city has expanded the program to eliminate its budget gaps and changed its labor policy to freeze all wages over the next two years.

### **TAXES LEAD THE RECOVERY IN CITY-FUND REVENUES**

City funds increase by \$1.1 billion in FY 2011, from the previous year, to \$43.2 billion. City funds, which include taxes, intergovernmental aid and miscellaneous revenue, are higher due to a \$1.8 billion upturn in tax collections. Despite this impressive tax growth, total revenue declines by \$643 million in FY 2011, to \$63.2 billion, due to a projected drop in categorical aid.

As shown in the figure to the right, the real property tax increases by \$623 million, to \$16.8 billion in FY 2011. The city expects that property tax growth will weaken even as the nonproperty taxes gain strength in the coming economic recovery. The nonproperty taxes grow by \$1.2 billion to \$20.6 billion in FY 2011, starting to recover from the recession-induced declines of the previous two years.

There are no major tax program initiatives in the city's financial plan. The city estimates that a state cigarette tax increase will have a negative impact on city revenues. The city has therefore included a negative \$19 million tax program to account for the drop in its own sales and cigarette tax revenues that could result from a state cigarette tax increase. The state approved an increase of \$1.60 per pack and pledged increased enforcement initiatives, which if effective could mitigate the negative effects on the city's tax

<b>FY 2011 City-Fund Revenues Increase by \$1.1 Billion (\$ in millions)</b>	
Property Tax	\$623
Nonproperty Taxes	1,208
Audits	(268)
Tax Program	(19)
STAR Aid	39
Miscellaneous Revenue	(112)
Nonrecurring Revenue	(320)
Intergovernmental Aid	(22)
<b>City Funds</b>	<b>\$1,128</b>
Categorical Aid	(1,747)
Interfund Revenue	(25)
<b>Total Change in Revenues</b>	<b>(\$643)</b>
Note: Numbers may not add due to rounding.	

collections.

The city's tax audit program declines by \$268 million in FY 2011, to \$622 million, following a five-year run of strong audit collections. Audits, which used to produce about \$500 to \$600 million annually, have moved into the \$800 million to \$1.1 billion range over the last five years. With the recession having weakened profits for many business tax payers, it is possible that audit collections could decline. However, even if audit collections slow down, the success of the audit program may be measured in improved taxpayer compliance and enhanced baseline tax revenues.

The city's share of the state's School Tax Relief (STAR) program is up \$39 million to \$943 million in FY 2011. Despite this increase since the previous year, the STAR program has been scaled back due to state budget cuts from the peak aid of about \$1.2 billion that was paid out in each of FYs 2008 and 2009. Also because of state budget cuts, Intergovernmental Aid (IGA) is down \$157 million in the city's plan for FY 2011.

The city's FY 2011 miscellaneous revenue projection of \$4.3 billion represents, on a year-over-year basis, a decline of \$432 million largely because, at this early point in FY 2011, the city anticipates generating and using \$320 million less nonrecurring resources. On a closer inspection of the city's miscellaneous revenue forecast, most of the areas that sponsor recurring revenue growth, such as fees, interest, fines, rent, and licenses, are projected to show a net increase of \$49 million over the prior year.

Categorical aid declines by \$1.7 billion to \$19.4 billion. The largest aid reductions are to federal grant programs, which fell by \$1.4 billion, reflecting the winding down of stimulus aid.

### **Property Tax**

The city expects the real property tax to yield \$16.8 billion in FY 2011, an amount that is \$623 million, or 3.9 percent, higher than the previous year. This lackluster growth represents a significant weakening from the 12 percent growth surge in FY 2010, when revenue growth was buoyed by the elimination of rebate and tax cut programs. Even so, the slowdown of billable tax base growth to 4.2 percent in FY 2011, from the near-seven percent growth rate recorded in both FYs 2009 and 2010, indicates that the city's property tax is entering a period of slower growth, possibly leading to stagnation.

The slowing of property tax revenue is a delayed after-effect of the flattening of market values over the past four years. Market values on the city's tax rolls have remained stagnant at the \$800 billion level from FYs 2008 through 2011. State rules, designed to limit excessive assessment growth in strong real estate markets, have resulted in a lagged response of property tax revenue to shifts in the real estate market. These state regulations, consisting of a system of assessment caps and phase-ins, tend to prop up growth in the early years of a downturn at the cost of prolonging the period of weakness beyond the end of the downturn. Property tax revenue growth is likely to weaken in the outyears because of stagnant market values, because of long assessment lags and because further tax increases are not planned.

The city is preparing for a collections slowdown by raising its property tax contingency reserves. The city has set aside \$1.6 billion in reserves for FY 2011, an amount that is \$112 million higher than the reserves that were needed in FY 2010. The reserve for delinquency, or nonpayment of tax bills, increased by \$54 million in FY 2011 to \$375 million. In order to prepare for a possible surge in assessment complaints, the city enlarged its refund reserve by \$126 million to \$394 million.

The city kept property tax rates steady in FY 2011 at an average rate of \$12.283 per \$100 assessed value, which was fixed in December 2008 when tax rates were increased in the middle of FY 2009. This is the same average tax rate that had been in effect in FYs 2004-2007, prior to the FY 2008 seven percent rate cut. As a temporary measure, the previous year's class tax rates were used for the initial billing of FY 2011, since new tax rates had not yet been fixed when the bills were sent out.

The new tax rates that were enacted for FY 2011 would have caused individual class tax rates to have shifted by as much as four percent, favoring the commercial property classes to the dismay of residential property owners, even though the overall average tax rate would remain stationary. The city is therefore seeking legislative approval for a cap to ameliorate the swings in class tax rates. Given the legislative support for this measure both in the city and the state, it may be assumed that the property tax rates for FY 2011 will be adjusted retroactively, later in the fiscal year.

Once these adjustments are implemented, the new property tax rates would result in relatively small increases in residential tax rates and a small decrease in the commercial tax rate. Owners of private homes will see their tax rate go up by 1.6 percent, to \$17.364, while the rate for residential apartment buildings increases by 0.9 percent, to \$13.353. Offsetting these increases is a decline for the utility property tax rate of 0.9 percent, to \$12.631, and a 1.1 percent rate reduction for commercial properties to \$10.312.

### **Nonproperty Taxes**

With the national job market having shown positive growth for five out of the first six months of calendar year (CY) 2010, the nation appears to be at the start of an economic recovery. At present, the recovery appears to be weak and unsteady, as evidenced by the drop in the June job count and by the weakness of private sector hiring since the start of the upturn. The city's nonproperty tax growth targets are consequently modest. The nonproperty taxes increase by \$1.2 billion in FY 2011, to \$20.6 billion. This projected 6.2 percent growth represents a first step upward toward recovering from the two-year 17 percent slide in nonproperty tax collections.

The personal income tax improves by \$680 million, or 10 percent, in FY 2011 following a severe 25 percent revenue loss in FY 2009 and a weak four percent upturn in FY 2010. The business income taxes increase by \$332 million, or seven percent. The business taxes are finally beginning to recover from a three-year downturn during which collections fell by 24 percent. The real property transfer and the mortgage recording taxes are scheduled to increase by about \$101 million or 10 percent, which would signal the start of a gradual recovery for this group of taxes. These recession-battered property transaction taxes had fallen by 70 percent over the previous three

years. The city sales tax, following along with this broad-based revenue upturn, grows by \$133 million, an increase of three percent.

### **EXPENDITURE HIGHLIGHTS IN FY 2011**

In the July financial plan, the city projects increased spending in FY 2011 on pension, fringe benefits and debt service costs as compared to FY 2010. Still, total-funded expenditures in FY 2011 decreased from FY 2010 by a net \$643 million due to the use of FY 2010 surplus funds to prepay FY 2011 expenses. The city also applied savings produced from reduced labor costs, agency actions and the drawdown of the Retiree Health Benefits Trust (RHBT). The adopted budget estimates total-funded expenditures for FY 2011 to be about \$63.2 billion verses \$63.8 billion in FY 2010.

The city's pension costs are projected to grow by \$852 million to \$7.6 billion in FY 2011 from almost \$6.8 billion in FY 2010. The majority of the increase reflects the addition of \$400 million in reserve funds, which will address expected changes in the pension systems' actuarial assumptions and methods. Also, after eliminating a proposed plan to create a Tier 5 in the pension systems for new employees, the city has added back \$200 million of planned pension savings to the budget. Fringe benefits such as health insurance, worker's compensation, employment insurance, and social security contributions have also risen and are projected to grow by almost \$341 million from FY 2010. The city also expects debt service costs to rise by \$914 million in FY 2011 over FY 2010. Additionally, the city has also increased its General Reserve by \$137 million to \$437 million.

### **FY 2011 Program to Eliminate the Gap**

For FY 2011, the city will proceed to take gap-closing actions to reduce agency expenditures. In building upon actions taken since January 2008, which total nearly \$3 billion (includes revenues and restorations) as of FY 2010, city agencies were expected to produce an additional \$1.2 billion of new spending reductions and \$87 million of higher revenues in FY 2011, for a total Program to Eliminate the Gap (PEG) of close to \$1.3 billion as stated in the FY 2011 Executive Budget. For the FY 2011 Adopted Budget, the City Council has restored close to \$111 million of those new PEGs, which will reduce targeted savings in FY 2011 to about \$1.2 billion (total expense and revenue PEGs). Also the city, in preparation of substantial cuts in state aid for the 2010-2011 school year proposed in the state's executive budget, has budgeted to lower school spending in the Department of Education (DOE) by \$493 million in FY 2011 from a combination of headcount reductions through attrition and labor actions. The expected loss of the school funding will bring total citywide agency savings close to \$1.7 billion, as shown in Table 4.

# FY 2011 PROGRAM TO ELIMINATE THE GAP

TABLE 4

(\$ in thousands)

Agency Categories:	January PEG	May PEG	PEG Subtotal	Adopted Restorations	Total FY 11 PEG
<b>Uniformed Services</b>					
Police	(\$128,038)	\$81,263	(\$46,775)	\$0	(\$46,775)
Fire	(17,282)	(9,880)	(27,162)	5,587	(21,575)
Correction	(51,885)	(19,376)	(71,261)	0	(71,261)
Sanitation	(62,729)	(25,876)	(88,605)	0	(88,605)
<b>Health and Welfare</b>					
Children Services	(51,867)	(31,307)	(83,174)	16,181	(66,993)
Social Services	(55,800)	(19,359)	(75,159)	7,993	(67,166)
Homeless	(22,068)	(2,449)	(24,517)	1,600	(22,917)
Health & Mental Hyg.	(33,601)	(15,430)	(49,031)	1,247	(47,784)
<b>Other Mayoral</b>					
Housing Preservation	(1,514)	(2,522)	(4,036)	0	(4,036)
Finance	(5,528)	(740)	(6,268)	0	(6,268)
Transportation	(27,337)	(16,655)	(43,992)	1	(43,991)
Parks and Recreation	(33,816)	(11,185)	(45,001)	9,305	(35,696)
Libraries	(22,066)	(9,102)	(31,168)	31,016	(152)
Cultural Affairs	(10,512)	(4,336)	(14,848)	14,848	0
Citywide Admin.	(7,088)	(7,681)	(14,769)	0	(14,769)
All Other Agencies	(107,496)	(73,400)	(180,896)	22,680	(158,216)
<b>Major Organizations</b>					
Education	(316,824)	(300)	(317,124)	0	(317,124)
CUNY	(15,416)	(6,359)	(21,775)	0	(21,775)
HHC	0	(3,445)	(3,445)	400	(3,045)
<b>Other</b>					
Procurement Savings	(55,519)	0	(55,519)	0	(55,519)
<b>Total PEGs</b>	<b>(\$1,026,386)</b>	<b>(\$178,139)</b>	<b>(\$1,204,525)</b>	<b>\$110,858</b>	<b>(\$1,093,667)</b>
School Funding Loss					(492,920)
Revenue PEG					(86,681)
<b>Total FY 2011 PEG</b>					<b>(\$1,673,268)</b>
(Negative) numbers decrease the gap. Numbers may not add due to rounding.					

For the FY 2011 Adopted Budget, the City Council has also restored more than \$234 million of prior-year PEGs that were identified in previous financial plans.<sup>1</sup> One of the more prominent funding restorations took place in the Fire Department with restored funding of nearly \$32 million to reverse the planned closure of 20 engine companies. Also the city restored more than \$21 million to the City University of New York and almost \$16 million to the Department of Cultural Affairs. This brings total FY 2011 restorations to more than \$345 million. Also, the City Council has allocated funding to cover nearly \$50 million of discretionary spending for dedicated districts across the city.

Of targeted PEG savings, about a third of projected expenditure reductions of \$1.1 billion will be centralized in the city's major organizations, with the bulk of the savings projected to come from the DOE with \$317 million in reductions. The savings in the DOE stem from an anticipated decrease in collective bargaining expenses, which

<sup>1</sup> Agency savings are identified in each year of the city's financial plan and restorations to a particular year's planned savings are addressed at the time of that year's budget adoption.

eliminates wage increases for members of the United Federation of Teachers (UFT) and the Council of School Supervisors and Administrators (CSA).

About 21 percent, or \$228 million, of expenditure savings are focused in the city's uniformed services. Most of the savings from uniformed services are centered in the Departments of Sanitation and Correction, with savings of \$89 million and \$71 million, respectively. Separate from restorations, the city has removed \$81 million of planned savings to the Police Department's budget. The bulk of that reduction was targeted to lower overtime expenditures by \$50 million in FY 2011, but due to a delayed implementation of that initiative, the savings have been budgeted to begin in FY 2012.

Also, other mayoral agencies collectively will reduce spending by \$263 million. Some of the more prominent savings in this area will come from the Department of Transportation, which projects nearly \$44 million in reduced spending, and Parks and Recreation that plans to save \$36 million. A large chunk of the restorations added back money to libraries and cultural organizations, whose budgets were replenished by \$31 million and \$15 million, respectively.

#### FY 2011 HEADCOUNT REDUCTION

TABLE 5

Agency Categories:	FY 2011 Executive Budget			FY 2011 Adopted Budget		
	Layoffs	Attrition	Total	Layoffs	Attrition	Total
<b>Uniformed Services</b>						
Fire	--	(399)	(399)	--	(299)	(299)
Correction	--	(509)	(509)	--	(509)	(509)
Sanitation	--	(302)	(302)	--	(302)	(302)
<b>Health and Welfare</b>						
Children Services	--	(250)	(250)	--	(53)	(53)
Social Services	--	(407)	(407)	--	(159)	(159)
Homeless	--	(57)	(57)	--	(57)	(57)
Health & Mental Hyg.	(164)	(76)	(240)	(145)	(76)	(221)
<b>Other Mayoral</b>						
Housing Preservation	(15)	(28)	(43)	(15)	(28)	(43)
Environmental	--	(5)	(5)	--	(5)	(5)
Finance	(69)	54	(15)	(69)	54	(15)
Transportation	--	(100)	(100)	--	(100)	(100)
Parks and Recreation	--	(377)	(377)	--	(377)	(377)
Citywide Admin.	(3)	(19)	(22)	(3)	(19)	(22)
All Other Agencies	(188)	(366)	(554)	(188)	(307)	(495)
<b>Major Organizations</b>						
Education						
Pedagogical	(4,419)	(1,995)	(6,414)	(23)	(1,995)	(2,018)
Civilian	(279)	--	(279)	(279)	--	(279)
<b>Covered Agencies</b>						
Libraries	(605)	(135)	(740)	(309)	--	(309)
Cultural Institutions	(284)	--	(284)	(88)	--	(88)
<b>Total Reduction</b>	<b>(6,026)</b>	<b>(4,971)</b>	<b>(10,997)</b>	<b>(1,119)</b>	<b>(4,232)</b>	<b>(5,351)</b>

The city's health and welfare agencies found cost reductions totaling about \$205 million, which is about 19 percent of total agency savings. After \$24 million of restored funding, the Department of Social Services and the Administration for Children Services plan to reduce spending by about \$67 million each. The Departments of Homeless



Services, and Health and Mental Hygiene will reduce their budgets by approximately \$71 million collectively.

The city has also planned to reduce its headcount in FY 2011, with a significant number of those positions coming from attrition and the remaining reductions realized from layoffs. As shown in Table 5, the city had planned in its FY 2011 Executive Budget to reduce headcount by nearly 11,000 positions with 40 percent of those positions identified as pedagogical layoffs. The planned layoffs of more than 4,400 teachers were significantly reduced to just 23 positions in the FY 2011 Adopted Budget in anticipation of a wage freeze in the last round of collective bargaining. This labor action, if realized, along with restorations in other areas like libraries and cultural institutions, will more than cut in half the number of positions targeted for elimination, while at the same time, the city will still recognize savings through headcount attrition.

While headcount reductions are citywide and will affect nearly every agency because the city has taken off the table planned uniformed reductions in the Police Department. In response to the Times Square bomb incident, the city restored in the executive budget for FY 2011 a planned headcount reduction of 1,600 officers in the Department. The Fire Department will also budget for an additional 100 firefighters reducing its planned attrition total.

#### **Labor Actions and Collective Bargaining**

More than half of the collective bargaining agreements with the city's major unions will have expired at the end of FY 2012. The standout is the UFT, whose contract had expired on October 31, 2009. The city has taken a number of actions to reduce expenditures that includes a shift in its labor policy, which assumes all wages will be frozen over the next two years.

Over the course of FY 2010, the city had altered its labor policy for the last round of collective bargaining for UFT and CSA members by reducing an anticipated wage increase to two percent on the first \$70,000 of wages earned, which reflects a change to its previous pattern of giving out four percent annual raises to the city's other major unions. The smaller increase for the UFT and CSA members was expected to produce savings of \$350 million. Later in the fiscal year, due to further budget constraints, the two percent raises were also removed from the budget, which enabled the city to save an additional \$276 million in FY 2011. Also, the city eliminated funding for prospected wage increases of 1.25 percent for all remaining union members that is expected to produce a savings of \$190 million in FY 2011. Lastly, the city's labor actions allowed it to reduce the labor reserve by an additional \$268 million in FY 2011.

The city has taken the position in its labor policy that all wage increases in the last round of collective bargaining will be self-funded. However, the city would like to achieve productivity savings in health insurance and pension costs, even though such proposals have been removed from the budget. The city estimates that a 10 percent health insurance contribution and a Tier 5 in the pension system would yield savings of \$557 million in FY 2011. The source of these productivity savings could be used to fund wage increases in the last round of collective bargaining. Alternatively, to the extent

that a wage increase is not self-funded, we estimate that the cost of a one percent wage increase could be approximately \$335 million.

### **Department of Education**

With student population growing to a year-over-year increase of just above two percent, which represents an enrollment register of over 1.1 million, the city for FY 2011 authorized just under \$18.6 billion in spending to the Department of Education (DOE) for operational purposes. Nonoperational pension and debt service costs, which are accounted for centrally, are not included. This adopted total is an increase of \$285 million, or 1.6 percent, over FY 2010 projection of just over \$18.3 billion.

Federal funds aided by the "stimulus" (American Recovery & Reinvestment Act 2009), provided almost \$2.6 billion for FY 2011 making up a share of almost 14 percent of the department's budget. Although this amount is less than FY 2010 forecasted amount (almost \$3 billion), it is 2.3 percentage points above the average share for FYs 2005-2009. This current reduction stemmed from the state accelerating stimulus funds from FY 2011 to FY 2010 in order to supplement the state's deficit reduction assessment. It should be noted that FY 2011 is the final year for federal stimulus contribution.

In FYs 2005-2009 state funds provided 46 percent of DOE's operational budget and are forecast to equal the city's share distribution at 43 percent. It should be noted that the state's budget for 2010-11 is still pending. This decline in state funding represents a negative rate of 1.3 percent from FY 2010, or a decrease of \$102 million, making its forecasted total contribution for FY 2011 just below \$8 billion.

City funds, including other categorical and intracity, are budgeted at just above \$8 billion. This translates to an annual increase of 10.6 percent, or just over \$768 million more than the forecasted FY 2010. This \$8 billion comprises just over 43 percent of the DOE's total operational budget.

### **FY 2011 Uniformed Agency Overtime**

For the FY 2011 Adopted Budget, the city plans to spend \$722 million on uniformed overtime expenditures, including civilian personnel, which is about \$140 million less than what it had spent in FY 2010. At the end of FY 2010, the city had spent almost \$862 million in overtime for the four uniformed agencies (Police, Fire, Correction, and Sanitation Departments), which is less than the targeted spending amount of \$885 million and under budget by \$23 million. However, because of the postponed implementation of a planned overtime reduction initiative in the Police Department, which was expected to yield \$50 million in reduced spending and negligible overtime savings identified in the other uniformed agencies, we believe that the city will likely exceed its overtime estimates in FY 2011 by \$140 million. A detailed explanation of projected overtime risk over the life of the financial plan is on page 31 in "Uniformed Agency Overtime for FYs 2011-2014."

### **FY 2010 Investment Performance and FY 2011 Pension Cost**

For FY 2011, planned contributions made by the city to its five actuarial pension systems will exceed \$7.6 billion in total funds. The projected pension expense is based on an actuarial valuation that incorporates the impact of investment losses in FYs 2008 and 2009 of 5.4 percent and 18.3 percent, respectively. The city has also put in reserve \$600 million to address forthcoming recommendations by the City Actuary, which can potentially impact pension costs. Also, in estimating the pension cost for FY 2011, the city has reversed a proposed savings of \$200 million that was anticipated from the creation of a Tier 5.

With the close of FY 2010, we project investment performance will yield a return higher than the pension systems' required rate of return or Actuarial Interest Rate (AIR) of eight percent. In the second half of FY 2010, markets retreated from a strong performance in the first half, due to debt troubles in Europe, persistently high U.S. unemployment and lingering uncertainty in the direction of the U.S. economy. The turbulent investment environment in the second half of the fiscal year erased early investment gains projected in the earlier part of the fiscal year, but the expected return on the fund's assets is still projected to land firmly in positive territory. The city estimates that the combined return for the pension systems in FY 2010 will be approximately 13 percent.

### **Debt Service**

At \$5.4 billion, the FY 2011 total fund debt service cost for the city and the New York City Transitional Finance Authority (NYCTFA), net of prepayments, reflects an increase of \$914 million relative to the prior fiscal year. When comparing the debt service costs for the two fiscal years, it is important to note that the amount for FY 2010 includes a reduction of \$659 million that resulted from the use of surplus resources for the early retirement and defeasance of bonds originally scheduled to mature in FY 2010.

After an adjustment for the early retirement and defeasance of FY 2010 bond maturities, the remaining \$255 million year-over-year increase in debt service is attributable in part to the interest expense on the large amount of debt incurred in FY 2010 and projected to be incurred in FY 2011. Specifically, the plan reflects one year more of interest in FY 2011 than FY 2010 on the sale of \$7.0 billion of bonds by the city and the NYCTFA in FY 2010 in combination with the sale of \$6.1 billion of bonds in FY 2011 to support the city's burgeoning capital program. Additionally, there is provision in the plan for the city and the NYCTFA to pay higher interest rates in FY 2011 on variable rate bonds than the extraordinarily low rates that occurred in FY 2010. Also, the plan provides for the city's sale of \$2.4 billion of short-term notes in FY 2011 to meet seasonal cash flow needs after not participating in that market for six years. Finally, the plan reflects payment by the city in FY 2011 of the full interest cost on bonds sold by the Hudson Yards Infrastructure Corporation to finance the extension of the Number 7 subway line, whereas in FY 2010 project revenues were available to cover most of this cost.

Debt service costs will grow from consuming 11.9 percent of tax revenues in FY 2010 to 13.8 percent in FY 2011. The debt service burden is forecasted to rise over the

years covered by the plan to 15.7 percent in FY 2014. We provide a detailed discussion of the city's debt burden in the section of the report titled "Debt Service as a Non-Discretionary Expense" beginning on page 36.

### **III. The FYs 2011-2014 Financial Plan**

The nation's economic recovery appears to be slow and unsteady. The city, benefitting from the revival of its financial sector, is recovering more strongly than the nation. Finance sector compensation, which has remained high even when Wall Street firms faced heavy losses, has helped stabilize the local economy. The city's moderate revenue growth assumptions are consistent with its forecast of a gradual economic recovery, moderating securities industry profits, and the winding down of federal stimulus programs. Uncertainty about the effects of finance industry regulatory reform is another factor that supports the city's conservative revenue projections.

Total revenue, which falls by \$643 million in FY 2011, begins to grow in FY 2012, supported by rising tax receipts and by the assumption that state aid cuts will eventually be restored. Over the four years of the plan, total revenue grows by \$4.7 billion, or 7.3 percent, from \$63.8 billion in FY 2010 to \$68.5 billion in FY 2014. The relatively slow growth of total revenue is largely due to the termination of federal categorical aid linked to the stimulus program. City-fund revenues increase by \$6.2 billion or 15 percent over the city's plan. Most of the revenue growth in the plan comes from the nonproperty taxes, which expand by 25 percent over the next four years. An extended real estate slowdown could weaken the property tax in the outyears of the plan, even as most other taxes are staging a recovery from the recent downturn.

Meanwhile, the growth in expenditures is outpacing the growth in revenues over the financial plan years. The city estimates that total-fund expenditures (excluding intracity expenses and interfund agreements) will increase by 15 percent over the life of the financial plan, climbing almost \$9.6 billion from \$63.2 billion in FY 2010 to \$72.8 billion in FY 2014. The growth in expenditure is being driven largely by a 55 percent growth in debt service costs. In our review of the debt service in the financial plan, we observe that this burgeoning cost is being generated primarily by existing contract liabilities, making the expense mostly nondiscretionary. In FY 2014, when debt service at \$6.8 billion is projected to consume over 15 percent of the city's tax revenues, only 10 percent of the cost is derived from borrowing for capital commitments scheduled to be undertaken in FYs 2011-14, while 90 percent is derived from borrowing for prior-years capital contracts, which limits flexibility for substantial reductions during the plan years.

The city will experience growth in other expenditure areas such as fringe benefits, pension, Medicaid, and other than personal service. With total expenditures outgrowing total revenues, the city projects budget shortfalls of \$3.3 billion in FY 2012, \$4.1 billion in FY 2013 and \$4.8 billion in FY 2014. Adding to the increased pressure of rising expenditures are the potential risks to the city's financial plan. We estimate these risks to add \$596 million in FY 2011, \$1.5 billion in FY 2012, \$1.6 billion in FY 2013 and \$1.3 billion in FY 2014 to the city's projected multi-billion budget gaps. Our additional risks bring the city's projected budget imbalance to \$596 million in FY 2011, \$4.8 billion in FY 2012, \$5.7 billion in FY 2013 and \$6.1 billion in FY 2014.

## THE OUTLOOK FOR REVENUE GROWTH

Total revenue increases by \$4.7 billion or 7.3 percent, over the four years of the plan, from \$63.8 billion in FY 2010 to \$68.5 billion in FY 2014, as shown in Table 6. At the start of the plan, total revenue edges down by one percent in FY 2011 due to weakness in revenues such as audits, miscellaneous revenue, unrestricted aid and categorical grants. Despite this early weakness, total revenue growth improves to about 2.7 percent annually in FYs 2012 through 2014, supported by the moderate growth of tax revenues, and the assumption that some state aid cuts will be restored.

TABLE 6

**CITY FUNDS INCREASE BY \$6.2 BILLION OVER THE NEXT FOUR YEARS**  
(\$ in millions)

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2010-14 % Change	FY 2010-14 \$ Change
Property Tax	\$16,156	\$16,780	\$17,423	\$17,692	\$17,829	10.4%	\$1,673
Nonproperty Taxes	19,373	20,581	21,806	22,975	24,168	24.8	4,795
Tax Program	0	(19)	(18)	(18)	(18)	--	(18)
Audit Revenue	890	622	621	620	620	(30.3)	(270)
Miscellaneous	4,288	4,176	4,223	4,254	4,304	0.4	16
Nonrecurring	440	120	17	13	13	(97.0)	(427)
STAR Aid	904	943	980	1,055	1,055	16.7	151
Unrestricted Aid	21	14	314	314	314	1395.2	293
Disallowances	0	(15)	(15)	(15)	(15)	--	(15)
<b>Total City Funds</b>	<b>\$42,072</b>	<b>\$43,201</b>	<b>\$45,349</b>	<b>\$46,890</b>	<b>\$48,269</b>	<b>14.7%</b>	<b>\$6,197</b>
Categorical Aid	\$21,147	\$19,400	\$19,163	\$19,300	\$19,707	(6.8%)	(\$1,440)
Interfund Revenue	583	558	493	493	493	(15.4)	(90)
<b>Total Funds</b>	<b>\$63,802</b>	<b>\$63,159</b>	<b>\$65,005</b>	<b>\$66,683</b>	<b>\$68,469</b>	<b>7.3%</b>	<b>\$4,667</b>

Notes: Categorical Aid is the sum of state, federal and other categorical grants. Numbers may not add due to rounding.

City-fund revenues increase by \$6.2 billion or 15 percent over the city's plan, from \$42.1 billion in FY 2010 to \$48.3 billion in FY 2014. City fund growth starts out slow with 2.7 percent growth in FY 2011. Growth improves to five percent in FY 2012, but slips back to about three percent by FY 2014. The nonproperty taxes, which recover with 25 percent growth over the four years of the plan, support much of the growth of city funds. Despite this strong recovery, the nonproperty taxes in FY 2014 will only be slightly ahead of where they stood before the recession. A growth slowdown affecting the real property tax, which increases by only 10 percent over the four-year plan, causes city fund growth to weaken after FY 2012.

The nonproperty taxes are the fastest growing major revenue source in the city's plan. These taxes increase by \$4.8 billion or 25 percent from \$19.4 billion in FY 2010 to \$24.2 billion in FY 2014. Previously, revenues had fallen by 17 percent from the pre-recession peak of \$23.4 billion in FY 2008. Thus if collections meet the plan's growth targets, nonproperty tax revenue will not surpass its previous high point until FY 2014.

The city is planning for reduced levels of state aid due to the state's budgetary difficulties. The state reduced the city's share of the school tax relief (STAR) program by \$283 million in FY 2010. Nevertheless, the city expects the state to gradually restore about half of this reduction by FY 2014. Over the plan, STAR aid increases by \$151 million or 17 percent. Also because of state aid cuts, the city does not expect to receive any unrestricted aid from the Aid and Incentives to Municipalities program (AIM) in

FYs 2010 and 2011. Previously, the city's allocation from this source of state aid often exceeded \$300 million per year. The city expects unrestricted aid of \$314 million in each of FYs 2012-2014. Given the state's budgetary difficulties, we are placing \$302 million of state aid at risk.

Categorical aid, which consists of federal, state and private program-specific grants, falls by \$1.4 billion during the plan, a decline of nearly seven percent. Most of this reduction reflects the winding down of federal stimulus aid. For example, federal education grants decline about \$340 million in FY 2011 and by \$850 million in FY 2012. Similarly, health and social support grants fall by about \$170 million in FY 2011 and by \$40 million in FY 2012. Medicaid grants increase by almost \$200 million in FY 2011, on the assumption that Congress will extend this program by two quarters. These grants then fall by \$460 million in FY 2012.

### **Property Tax Growth**

The property tax, which grows by \$1.7 billion or 10 percent over the plan period, produces a diminishing share of the plan's revenue growth. Most of the property tax growth occurs early in the plan, with weak growth occurring in the outyears. Property tax revenue growth declines from 3.9 percent in FY 2011 to 3.8 percent in FY 2012, 1.5 percent in FY 2013, and 0.8 percent in FY 2014. Previously, stronger assessment growth and tax increases had lifted the FY 2010 property tax growth rate by 12 percent.

Property tax revenue growth is ebbing in the city's plan because market values failed to grow on the city's FY 2011 tax roll, remaining stagnant at about \$800 billion for a fourth consecutive year since this level was approached in FY 2008. These weak market value reports stand in sharp contrast to the double-digit growth of market values during the boom years. As for the future, we await evidence that the expiring stimulus homebuyer incentive program will have a lasting effect on the real estate market.

Billable assessments increased 4.2 percent on the final roll for FY 2011, which represents a severe slowdown from the 6.7 percent billable growth in the previous year. The city expects billable assessment growth to slip to 3.5 percent in FY 2012, before dropping to about one percent in the outyears. Given that assessment growth is in the midst of a downtrend and that market values may fail to recover in FY 2012, it is possible that the city's 3.8 percent property tax growth target might not be achieved in FY 2012. We therefore place the property tax at risk for \$150 million in FY 2012, \$100 million in FY 2013 and \$50 million in FY 2014.

Property tax refunds through FY 2010 have remained flat, enabling the city to reduce its refund reserve by about \$50 million to \$268 million at the end of FY 2010. Despite this good fortune, refunds remain a concern because assessment disputes tend to proliferate during real estate downturns. It can take many years for assessment complaints to wind their way through Tax Commission hearings and Law Department reviews before ending up in court and possibly generating large multi-year refund liabilities. Recognizing this risk, the city increased its property tax refund reserve from \$268 million in FY 2010 to \$394 million in FY 2011 and \$409 million in FY 2012.

## **Economic Outlook**

A gradual upturn in employment for the nation and the city indicates that the long-awaited economic recovery is taking hold. The recession may have been less severe than was originally feared because federal stimulus programs effectively channeled resources into job creation, infrastructure improvement, the housing market and state and local government support. With the federal government stepping back from these support programs, the next challenge is for the economy to demonstrate staying power in the absence of federal stimulus spending. The city expects the recovery to be slow and gradual for both the economy and for local tax revenues. In a surprising reversal, a relatively strong upturn in local jobs is placing the city out in front of the nation in this phase of the economic recovery.

Economic output reports indicate that the national recovery has been slow and unsteady. Gross domestic product (GDP) increased at a 2.7 percent rate in the first quarter of calendar year (CY) 2010, decelerating from the 5.6 percent spurt in the fourth quarter of 2009. The city sees GDP recovering with lackluster growth of 2.9 percent in 2010 from the 2.4 percent decline in 2009. Growth increases to 3.7 percent in 2012, before dropping below three percent in 2014. Local output follows a somewhat more volatile growth plan. Gross city product (GCP) spurts by 3.6 percent in 2010 following a steep 4.5 percent decline in 2009. Growth dips near zero percent in 2011, before resuming the recovery with steady growth of two percent annually in the outyears. The more unsteady local growth path apparently reflects the wild swings of the financial services sector, which tend to have a greater impact on the city than the nation.

Employment began to turn around at the start of 2010 for both the nation and the city, but the city's recovery is considerably more robust than the nation's. The nation has added 882,000 jobs through June, whereas the city has produced 63,000 new jobs in the first six months of the year. While the nation has recovered about 11 percent of the 8.4 million jobs that were lost in the recession, the city has recovered about 30 percent of the nearly 200,000 jobs that were lost in the recession. Another difference is that temporary census jobs dominated hiring and firing at the national level; but this was less of a factor for the city where 52,000 of the new local jobs were in the private sector.

From January through June, local private jobs expanded at a seasonally adjusted annual rate of 2.1 percent, while national private hiring through June increased at the more subdued growth rate of 1.3 percent. Similarly, the local seasonally adjusted unemployment rate steadily declined to 9.5 percent in June from 10.4 percent in January, while national unemployment has moved down more slowly to 9.5 percent in June from 9.7 percent in January. The employment data show that the city is leading the nation in the recovery from the recession. These job reports reflect a very early view of how the recovery is proceeding and the trends could shift in the months ahead.

The relatively more robust local improvement may reflect the revival of Wall Street profits, and the brisk upturn of the local tourist industry. New York Stock Exchange member firms earned \$10.3 billion in the first quarter of 2010. These strong profits continue the trend that was set in 2009 when \$61.4 billion was earned for the year. Previously, Wall Street firms had accumulated two years of losses totaling \$54



billion. Similarly, tourist spending in the city is on track to recover fully from a 15 percent decline in 2009.

### **Nonproperty Taxes**

The city expects the nonproperty taxes to increase by \$4.8 billion, or 25 percent, over the next four years, from \$19.4 billion in FY 2010 to \$24.2 billion in FY 2014, as shown in Table 6 on page 17. However, because collections had fallen sharply during the recession, nonproperty tax revenues will be only three percent higher in FY 2014 than they were in FY 2008 before the recession had brought down collections. The plan anticipates that these taxes will recover fairly steadily through the plan, with only slight slippage in the outyear growth rates.

Among the fastest growing taxes are the mortgage recording tax which has a four-year increase of nearly 100 percent, and the general corporation tax which expands by almost 60 percent. The personal income tax, which increases by \$1.8 billion or 26 percent, yields the most additional revenue. Also growing strongly are the unincorporated business tax, the sales tax and the real property transfer tax. Not all of the city's taxes participate in the growth surge. The bank tax, which climbed 75 percent in FY 2009, is expected to weaken by six percent over the plan. Similarly, the commercial rent tax, the hotel tax and the cigarette tax fail to recover and decline slightly over the plan.

**Property Transactions Taxes.** With the transactions taxes badly weakened by a severe three year downturn, this revenue source could be nearing its low point. The city expects the two property transactions taxes (the real property transfer tax and the mortgage recording tax) to increase by more than \$570 million, from \$1.0 billion in FY 2010 to \$1.6 billion in FY 2014. These taxes recover with 10 percent growth in FY 2011, after which growth accelerates to 15 percent in FY 2012. Towards the end of the plan, growth drops back to 12 percent in FY 2013 and 11 percent in FY 2014. Previously, revenue had fallen by a staggering \$2.3 billion, or 70 percent, from a peak level of \$3.3 billion in FY 2007 to \$1.0 billion in FY 2010.

Improved affordability for homes, low mortgage rates and stimulus tax credits for homebuyers might have sparked some home sales in FY 2010. It remains to be seen whether the incipient real estate recovery will continue without tax credits. However, even if the residential market starts to improve, the stalled commercial market would have to revive before tax collections can recover strongly. The city's plan for the commercial rent tax reflects its long term view that commercial real estate may not yet be poised for recovery. Revenue from this tax on commercial renters is scheduled to fall moderately in FYs 2011-2012, with no recovery in sight before FY 2013.

**Business Taxes.** The city's three business income taxes (the general corporation tax, the banking corporation tax and the unincorporated business tax) is another tax group that is recovering after three years of decline. The plan calls for revenues to climb seven percent in FY 2011, with growth reaching 10 percent in FY 2012. Outyear growth then slips to seven percent in FY 2013 and five percent in FY 2014. Previously, revenues had fallen by \$1.4 billion from the peak \$6 billion collected in FY 2007 to \$4.6 billion

estimated for FY 2010. With the moderate recovery in the revenue plan, business tax collections will not surpass the pre-recession high point until FY 2014.

The city's business taxes had fallen over the previous three years because national pretax corporate profits and securities industry profits had severe setbacks in the recession. Corporate profits are recovering from a three-year 22 percent slide, during which profits had fallen from \$1.823 trillion earned in CY 2006 to \$1.428 trillion in 2009. Profits soared to \$1.847 trillion in the first quarter of 2010, surging by 48 percent compared with the depressed profit levels in the first quarter of 2009. The city's economic outlook sees corporate profits growing 16 percent in 2010, 10 percent in 2011, after which growth drops near zero percent in the outyears. The securities industry, which reported losses totaling \$54 billion in CYs 2007 and 2008, are recovering strongly. Securities firms earned record profits of \$61 billion in 2009 and they earned \$10 billion in the first quarter of 2010.

These strong results for corporate profits and for Wall Street firms could mean that a very strong recovery for business taxes could be at hand. We are reluctant to add upside potential to business tax collections because the economic recovery still appears to be weak and unsteady.

**Sales Tax.** In its latest plan, the city estimates that sales tax revenue will increase by 2.7 percent over the prior year to \$5.1 billion in FY 2011.<sup>2</sup> On a common rate and base, which removes the yield from last year's tax increase package, sales tax collections are projected to rise modestly by 0.3 percent in FY 2011, 4.3 percent in FY 2012, 5.8 percent in FY 2013, and 5.2 percent in FY 2014.<sup>3</sup> Besides tourist-based spending to support the sales tax base, local consumption is expected to rise over the plan period as households become less pessimistic and hesitant due to evidence of consistent income and job growth.

In the city's view, FY 2011 marks a transition point from two years of negative sales tax growth in FYs 2009 and 2010 due to the national and local recessions, to job gains taking hold by the second half of FY 2011. In fact, an improvement in employment might be starting a little earlier than the city estimates since on a year-over-year basis, private employment increased by 6,100 jobs in June, which represents the first year-to-year job gains since November 2008. It only took 10 months from the peak of job losses in August 2009 on a year-over-year basis for the city's economy to generate jobs, as

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<sup>2</sup> The city's sales tax forecast does not reflect changes to the exemption for clothing and footwear purchases priced under \$110 that has been proposed by the state legislature after the city budget was adopted. The Governor and the state legislature agreed to: (1) remove the state sales tax exemption on purchases of clothing and footwear priced under \$110 from October 1, 2010 through March 31, 2011; (2) return the state exemption on clothing and footwear purchases priced under \$55 from April 1, 2011 through March 31, 2012, with an opt-in provision for local governments; and (3) restore the original state exemption at \$110 on April 1, 2012.

<sup>3</sup> "On a continuing base" or "on a common rate and base" refers to tax collections that have been adjusted to remove the effects of tax programs and other technical changes to focus on the influence of the economy.

opposed to 26 months during the previous recession for the city to post the first positive over-the-year job numbers.<sup>4</sup>

Supporting the sales tax base are the city's assumptions that employment and wages will start to recover by the end of 2010 and pick up momentum in 2011. From peak-to-trough, total local employment losses are estimated to reach 188,000 from the fourth quarter of 2008 to the third quarter of 2010, where the financial sector loses 54,000 jobs from the first quarter of 2008 to the third quarter of 2010.<sup>5</sup> While it was almost certain that finance sector compensation in 2010 would improve significantly from the prior year due to the extreme profitability of the securities industry in 2009, wages in the non-finance sector of the economy are also expected to show modest improvement of 1.9 percent in 2010 before moving closer to trend growth of 3.7 percent in 2011 to \$201.7 billion.

Yet, sales tax collections in the near-term may be constrained by the cautiousness of households as they continue to grapple with high levels of home foreclosures and personal debt, frequent volatility in the stock market, sluggish wage growth, and tight credit conditions. In addition, tourist-based consumption, which has helped to propel sales tax collections thus far, might temporarily fall off because of the steep drop in the value of the euro compared to the dollar.

**Personal Income Tax.** From FY 2011 through FY 2014, the city expects a recovery that began on Wall Street in 2009 to spread to other sectors of the economy in terms of job and income gains, which will drive personal income tax collections (on a continuing base) by 8.4 percent in FY 2011, 4.7 percent in FY 2012, 3.8 percent in FY 2013, and 4.8 percent in FY 2014. A rebound in the national economy with 2.2 million jobs added in 2011 and an appreciation in stock prices are also anticipated by the city to support the personal income tax (PIT) base. However, certain regulatory changes that are part of the financial industry reform legislation, known as the Dodd-Frank Act, have the potential to hurt earnings, and to a lesser degree, employee compensation, in the short run.

Judging by New York Stock Exchange (NYSE) member firms' profits of \$61.4 billion in 2009 and \$10.3 billion for the first quarter of 2010, and double-digit growth in bonus payouts in 2009, it is clear that the finance sector has recovered from two prior years of losses in 2007 and 2008. The city expects another year of improvement in the bonus payout on 2010 NYSE member firms' earnings even though it assumes that securities industry profits will fall on a year-to-year basis by \$40.8 billion to \$20.6 billion in 2010. In the city's view, seen in Chart 1 on page 23, securities industry profits will fall further in 2011 and remain at the \$11 billion level from 2011 through 2013, but increase by \$1.7 billion to \$13 billion in 2014. Historically speaking, the city's forecast for

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<sup>4</sup> Daniel Massey, "NYC's Jobless Rate Keeps Falling," Crain's New York Business.com June 17, 2010.

<sup>5</sup> The city assumes that the securities industry, part of the financial sector, will have shed 35,000 jobs peak-to-trough from the second quarter of 2008 to the third quarter of 2010.

securities industry profits is reasonable given that from 1996 to 2006, Wall Street earned at least \$10 billion annually in eight out of the 11 years, and was only above \$20 billion twice, in 2000 and 2006.

### FINANCE SECTOR COMPENSATION REMAINS HIGH DESPITE FALLING SECURITIES INDUSTRY PROFITS

CHART 1

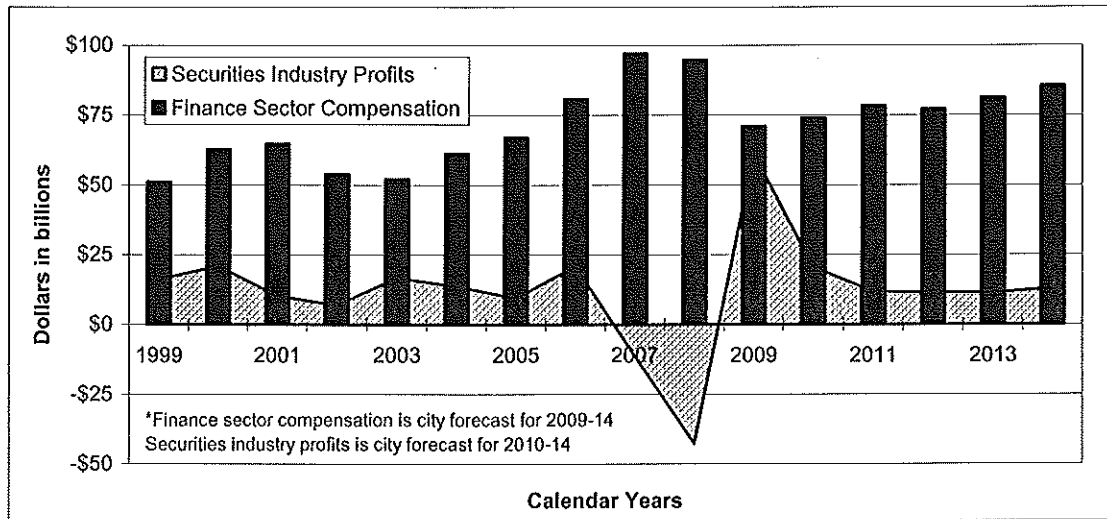


Chart 1 also shows the high threshold of annual finance sector compensation--exceeded \$50 billion from 1999 to 2005, surpassed \$80 billion from 2006 to 2008, and may range from \$70 billion to \$80 billion from 2009 to 2014--despite year-to-year gains or declines in industry profitability, or outright losses during the same periods.<sup>6</sup> Compensation reached a new summit of over \$90 billion in both 2007 and 2008, at the same time that NYSE member firms lost \$11.3 billion and \$42.6 billion, respectively, because of derivatives whose value was based on subprime mortgages that were in default. As a result, banks and bank holding companies had to write-down the value of mortgage- and other asset-backed debt and increase reserves for real estate (residential and commercial) and consumer loans.

Financial services firms may opt to maintain a certain level of compensation to attract and retain particular employees, and comply with provisions of employee contracts. Recently, the amount and structure of employee earnings, particularly among executives and other highly-paid finance professionals, have changed to align payments with the long-term profitability and risks undertaken by firms. Between salaries, cash bonuses, stocks and options, there is now a greater emphasis on higher base salaries and bonuses comprised mostly of stock that vests over longer-time periods. With less cash and more stock in the annual bonus payout, there will likely be less growth in withholding revenue during January through March than in prior years.

<sup>6</sup> The city's forecast of finance sector earnings is composed of salaries, cash bonuses and other forms of (stock) compensation where the tax is prepaid via withholding revenue.

Meanwhile, the local labor market is in transition and the city expects the local economy to generate jobs by the second half of FY 2011. After two years of job losses in 2009 and 2010, job gains (on a year-to-year basis) are projected to number 12,000 in 2011 and more than triple to about 40,000 in both 2012 and 2013 before slowing slightly to 31,000 in 2014. Besides the expectation of a large Wall Street bonus payout on 2010 earnings, it is also salaries from additional jobs in the finance and non-finance sectors of the economy that will support annual withholding growth of 1.4 percent in FY 2011 and over four percent by FY 2014. Nonwage income, from a variety of sources, is expected to significantly improve in 2010, primarily due to the shifting of capital gains realizations from 2011 into 2010 because of a rise in the federal capital gains tax rate in 2011. Despite this one-time event, capital gains realizations are likely to fall after 2010 until the housing and equity markets stabilize and appreciate in value.

Even with the hoped-for recovery in employment and income, there are risks to the city's PIT forecast that are out of the city's control and relate to stock market volatility and provisions in the Dodd-Frank Act. The sharp swings and downward pressure on stock prices that occurred in the second quarter of 2010 may continue into the rest of the year or until traders feel more sanguine about sovereign debt in the euro zone, and the domestic housing and labor markets. If the volatility continues at its current pace, it may be harder to achieve the city's estimates of 2010 securities industry profits and capital gains realizations, and overall PIT revenue in FY 2011.

To ensure that another financial crisis does not occur, the President and Congress have proposed more regulations and regulators for the financial industry rather than restructure or split up large financial services companies. While regulators will be developing new rules and standards for the Dodd-Frank Act, there are provisions in the law that may reduce the profits of larger banks and bank holding companies in the short term, which include:

- an end to propriety trading although banks may make a limited investment in hedge, private equity, and real estate funds.
- the use of affiliates for swap trading desks and higher capital requirements based on value of derivative contracts cleared through a third party and traded on an exchange.<sup>7</sup>
- federal oversight of credit and debit card fees, and mortgage lending.
- new capital requirements based on the size and risk profile of banks.

An illustration of the importance of selling derivatives for larger financial institutions is that commercial banks nationwide held derivatives with a notional value of \$212.8 trillion in the fourth quarter, where JPMorgan Chase, Citigroup, Bank of America, Goldman Sachs, and Morgan Stanley held 97 percent of that total.<sup>8</sup> As the

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<sup>7</sup> Companies would still be able to trade derivative contracts related to interest rates, currencies, and gold and silver swaps.

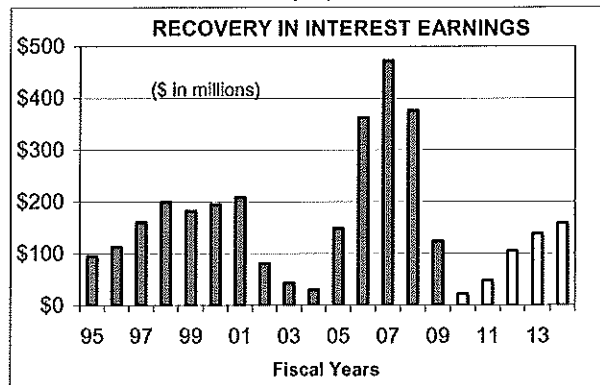
<sup>8</sup> Phil Mattingly and Robert Schmidt, "Goldman Sachs, Morgan Stanley Would Be Least Affected by Swaps Proposal," [Bloomberg.com](http://Bloomberg.com) June 23, 2010.

financial industry and other interested parties pore over the legislation, it will take time for federal regulators to fill in the details and set appropriate capital, risk, and compensation limits depending on the size of the financial services firms. Meanwhile, the Federal Reserve and other federal banking regulators are continuing the process of requiring banks to examine their compensation and risk policies. For example, the 25 biggest banks were ordered to develop and submit plans to the federal monitors to show how their estimate of compensation (i.e. structure, timing) does not encourage short-term risk taking, but is instead linked to the long-term performance of their company.

### **Miscellaneous Revenue**

From FY 2010 to FY 2014, the city projects miscellaneous revenue (including nonrecurring resources) will fall by 8.7 percent or \$411.4 million to \$4.3 billion. If we exclude specific revenue sources that do not exhibit recurring growth and instead focus on the remaining core categories, there is a projected net increase of 5.6 percent or \$141.9 million to nearly \$2.7 billion by FY 2014.<sup>9</sup> One of the main reasons for the significant difference in the plan variances is that fewer nonrecurring actions are expected to be generated and used in FY 2014. However, at the present time, it is too early in the financial plan process to determine if this will actually occur.

Over the plan period, core category revenue advances largely from a resurgence in interest income for two reasons. The city expects higher short-term interest rates sponsored by the Federal Reserve, and to a lesser extent, a modest recovery in nonproperty taxes that could supply cash for investment.<sup>10</sup> The figure to the right shows that after interest income reached a historic low of \$22 million in FY 2010, which was even less than the interest earned in FYs 2003 and 2004, interest income is forecast to grow steadily to \$158.7 million by FY 2014.



The primary reason for the comparatively low returns earned by the city on available cash balances has been the expansionary monetary policy of the Federal Reserve, which has kept the target range for the federal funds rate at 0 to 0.25 percent since December 2008. While the Federal Reserve's accommodative stance was needed to

<sup>9</sup> Core category revenue consists of: licenses, fees or charges, interest, rent, fines, and a miscellaneous category that is stripped of major nonrecurring actions, tobacco proceeds, housing revenue, and Health and Hospitals Corporation payments. Since water and sewer charges are dedicated to programmatic expenditures and therefore unavailable for gap-closing assistance, they are also excluded from the definition of core category revenue.

<sup>10</sup> Over the past six years, the city built up cash balances (in part from strong nonproperty tax collections) to the degree that short-term borrowing was not undertaken in FY 2005 through FY 2010. However, the city plans to sell \$2.4 billion of short-term notes in FY 2011 to meet peak seasonal needs.

supply liquidity to the credit markets and foster borrowing by businesses and households, it also severely lowered the yield on investments. Based on a model, the city projects that short-term interest rates will rise steadily through FY 2011 and average under one percent, and average 2.7 percent in FY 2012, 3.5 percent in FY 2013, and just over four percent in FY 2014. While it is not certain when the Federal Reserve will raise short-term interest rates and adopt other means to drain excess reserves from the financial system, it is clear that over the plan period the federal funds rate will start to return to a more "normal" range. Based on historical patterns of growth and the city's practice of developing new initiatives, the city's miscellaneous revenue forecast could be higher by \$25 million in FY 2011, \$50 million in FY 2012, \$75 million in FY 2013, and \$100 million in FY 2014.

### **SOURCES OF EXPENDITURE GROWTH IN THE FINANCIAL PLAN**

The city's expenses between FYs 2010 and 2014 are expected to rise by almost \$9.6 billion, or 15 percent, with total spending reaching \$72.8 billion in the final year of the financial plan from \$63.2 billion in FY 2010, as shown in Table 7 on page 27. While total spending is projected to rise annually over the life of the financial plan, the city projects expenditures (excluding intracity expenses and interfund agreements) to fall by one percent, or \$618 million, between FYs 2010 and 2011. The decrease in expenditures is primarily due to a significantly large prepayment of FY 2011 expenditures and to a lesser extent a reduction in wage expense. These reductions have been offset by growth in other budgetary areas like fringe benefits, pension, Medicaid and debt service costs.

It should be noted that the city has obtained state legislative approval to exclude pollution remediation costs from its expense budget and instead use bond proceeds to fund these costs. The city estimated that these costs would total \$150 million in each of FYs 2011 and 2012, and \$200 million in each of FYs 2013 and 2014. Prior to passage of the legislation, the city was required by the Financial Emergency Act (FEA) to fund pollution remediation projects from current resources because under Statement 49 of the Government Accounting Standards Board (GASB) these expenses are accounted for in the operating budget. With enactment of the legislation, the amended FEA continues to prohibit the city from issuing bonds to pay operating expenses, but now provides the limited exception of GASB 49 pollution remediation costs. All other localities in the state are permitted to sell bonds for operating purposes. The financial plan reflects this change. In selling bonds for pollution remediation, the city will increase its debt service costs by small increments over an extended number of years.

# PROJECTED EXPENDITURE GROWTH IN FYs 2010-2014

TABLE 7 (yr/yr percent change, \$ in millions)

	FYs 2010-11	FYs 2011-12	FYs 2012-13	FYs 2013-14	FYs 2010-14	Level in FY 2010	Level in FY 2014
<b>Total Expenditures</b>	(1.0%)	8.3%	3.7%	3.7%	15.2%	\$63,219	\$72,812
<b>Total PS</b>	1.3%	(0.3%)	4.0%	3.1%	8.3%	\$35,103	\$38,021
Salaries and Wages	(3.1%)	(2.4%)	1.5%	2.7%	(1.4%)	21,446	21,143
Fringe Benefits	3.6%	1.9%	13.4%	6.0%	27.0%	7,021	8,917
Pensions	12.8%	3.5%	1.4%	1.3%	20.0%	6,636	7,962
<b>Total OTPS</b>	(3.8%)	19.5%	3.3%	4.2%	23.7%	\$28,116	\$34,790
Public Assistance	0.4%	2.5%	(0.7%)	0.0%	2.2%	1,580	1,614
Medicaid	0.5%	15.1%	3.8%	9.8%	31.9%	5,140	6,778
Debt Service	20.6%	17.6%	4.9%	3.9%	54.6%	4,437	6,859
Other OTPS	(11.8%)	23.4%	2.9%	2.9%	15.2%	16,960	19,539

Note: Includes city, state, and federal funds. Excludes intracity expenses and interfund agreements. Numbers may not add due to rounding.

As shown in Table 7, personal service (PS) increases by eight percent from FY 2010 to FY 2014 driven by a 27 percent climb in fringe benefits and an increase of 20 percent in pension costs. However, that increase is mitigated with an expected reduction in salary and wage expense of 1.4 percent, assuming a wage freeze, and headcount reduction materialize. The savings are expected to bring down the city's wage expense by nearly \$304 million over the life of the financial plan.

The shift in city labor policy, which assumes all wages will be frozen over the next two years, is expected to produce significant results. Over the course of FY 2010, the city had eliminated a wage increase of 1.25 percent for most city unions, with expected savings of \$190 million in FY 2011, \$448 million in FY 2012, \$660 million in FY 2013 and \$798 million in FY 2014. Also, the city eliminated a four percent hike for teachers and administrators in the last round of collective bargaining that will be expected to save \$272 million in FY 2010 and \$626 million in FY 2011. This action follows an earlier measure that capped the Department of Education (DOE) wage increase to two percent. The city projects the savings from that earlier labor action could amount to \$462 million in FY 2012, \$515 million in FY 2013 and \$518 million in FY 2014. Also, the city's actions have allowed it to reduce its labor reserve by \$268 million in FY 2011, \$336 million in FY 2012, \$266 million in FY 2013 and \$164 million in FY 2014.

On the other hand, the city would like to achieve productivity savings that could be used by city employees to self-fund a wage increase in the last round of collective bargaining. The savings from health insurance and pension costs, which have been removed from the budget, could be a source of the funding. The city estimates that a 10 percent health insurance contribution and a Tier 5 in the pension system would yield savings of \$557 million in FY 2011, \$586 million in FY 2012, \$618 million in FY 2013 and \$651 million in FY 2014.

Other than personal service (OTPS) expenditures are expected to increase by almost 24 percent from FY 2010 to FY 2014. The primary cause of the growth in this area is debt service, which is projected to increase by almost 55 percent, and Medicaid expenditures, which are expected to grow by almost 32 percent. However, the bulk of the increases in Medicaid and debt service are the result of lower costs in FY 2010 related



to the phasing out of stimulus funds, and the exhaustion of savings realized from the defeasance and early retirement of outstanding bonds, respectively.

PS expenditures are being driven up by the rising costs in fringe benefits and pensions. Between FYs 2010 and 2014, fringe benefits expense increases 27 percent from \$7 billion to \$8.9 billion. Fringe benefits grow particularly fast between FYs 2012 and 2013, a jump of more than \$994 million, or 13.4 percent. While growth in the cost of employee healthcare is expected to continue to push up the city's spending on fringe benefits over the years of the financial plan and beyond, the increase from FY 2012 to FY 2013 mostly reflects a technical adjustment for the restoration of a planned drawdown of the Retiree Healthcare Benefits Trust in FY 2013 to help fund pension system losses.

The city's annual pension cost will increase from \$6.6 billion in FY 2010 to almost \$8 billion in FY 2014, which equates to an increase of more than \$1.3 billion. The pension systems suffered losses in the billions of dollars in FYs 2008 and 2009 and those losses are being funded at increasing annual percentages over the course of the financial plan. Also contributing to the increase is the city's funding of a reserve to address higher costs that may occur upon completion of an experience study currently being performed by the City Actuary. The additional funding of the reserve will amount to \$400 million in FY 2011 and \$150 million in each of FYs 2012 to 2014. The city has also eliminated a planned savings of \$200 million annually related to the creation of a Tier 5.

The city expects that public assistance costs will remain flat for the entirety of the financial plan at about \$1.6 billion; however medical assistance spending will increase by 32 percent, or around \$1.6 billion as seen in Table 7. The increase mainly reflects the winding down of the Federal Medical Assistance Percentages (FMAP) rate reduction enacted through the federal stimulus package. The federal aid enabled the city to reduce expenditures for Medicaid by \$1.6 billion from October 2008 to December 2010 and is budgeted to be extended by two quarters thereafter adding \$600 million in savings. Also, in addition to the extension of FMAP, the city will realize further savings from the healthcare reform legislation recently signed into law. In total, the city anticipates about \$2.8 billion in savings to be realized over a five-year period from FY 2009 to FY 2013 from the FMAP totaling \$2.2 billion and the healthcare reform totaling \$600 million.

Unfortunately, the passage of the FMAP extension remains highly uncertain. The U.S. Senate has pushed the legislation aside due to an impasse on how it would be financed and failure to pass the legislation has also occurred in the U.S. House of Representatives even after the program was scaled back by billions of dollars. Still, the city has budgeted to receive the extension of \$600 million and has reduced spending on Medicaid expenditures reflecting savings of \$279 million in FY 2011, \$61 million in FY 2012 and \$269 million in FY 2013. With the FMAP extension, the city has included budget relief of \$663 million in FY 2010, \$856 million in FY 2011, \$395 million in FY 2012 and \$422 million in FY 2013, in anticipation of the funding. The city has already realized savings of \$459 million in FY 2009.

If the FMAP is not extended, the city will have to remove the \$600 million of planned savings, which we hold at risk, but the city will have still realized \$2.2 billion of spending reductions by FY 2013. Subsequently, to address the possibility that the \$600

million of FMAP funding will be lost, the city has funded the General Reserve by an additional \$137 million bringing the reserve total to \$437 million in FY 2011.

Expenditures that fall under Other OTPS, which includes the impact of prepaid expenses but excludes public assistance, Medicaid and debt service costs, are expected to rise by 15 percent after a nearly 12 percent decrease between FYs 2010 and 2011, as shown in Table 7 on page 27. The decline between FYs 2010 and 2011 occurs as a consequence of a prepayment of FY 2011 expenses. The increase of almost \$2.6 billion from FY 2010 to FY 2014 is driven primarily by a jump in expenditures between FYs 2011 and 2012 of nearly 24 percent. Some areas affecting the increase between FYs 2011 and 2012 are libraries, the DOE, the Health and Hospitals Corporation (HHC), uniformed services, other miscellaneous areas and adjustments. .

Elsewhere in expenditures, the city has allocated funding to help address a shortfall in the operating budget for HHC. For many years, HHC has functioned as a self-sustained operation, but the health of its finances has suffered in the recession with a large number of uninsured patients having sought treatment at its facilities. In response, the city will give financial support to HHC's operations over the life of the financial plan. The city has budgeted annual funding of \$349 million in FY 2010, \$82 million in FY 2011, \$229 million in FY 2012 and \$300 million in each of FYs 2013 and 2014.

#### **Program to Eliminate the Gap for FYs 2012-2014**

The city has implemented a number of gap-closing actions to reduce agency expenditures on a citywide basis over the course of the financial plan. As discussed on page 9, the city's agency program or Program to Eliminate the Gap (PEG) is expected to produce expenditure savings in FY 2011 of \$1.1 billion. As shown in Table 8, the city expects the PEGs to reduce expenditures by more than \$1.2 billion in each of FYs 2012-2014. Additionally, the city expects to be able to expand the PEGs with additional revenue collections of nearly \$38 million in each of FYs 2012 and 2013 and almost \$33 million in FY 2014.

TABLE 8

<b>AGENCY PEG PROGRAM FOR FYs 2012-2014</b>			
(\$ in thousands)			
<b>Agency Category</b>	<b>FY 2012</b>	<b>FY 2013</b>	<b>FY 2014</b>
Uniformed Services	(\$309,345)	(\$311,421)	(\$258,573)
Health and Welfare	(217,653)	(215,630)	(216,436)
Mayoral	(298,810)	(287,121)	(287,835)
Major Organizations	(341,434)	(341,434)	(341,434)
Elected Officials	(16,611)	(16,648)	(16,695)
All Other	(61,727)	(81,118)	(91,953)
<b>Total Expense PEG</b>	<b>(\$1,245,580)</b>	<b>(\$1,253,372)</b>	<b>(\$1,212,926)</b>
<b>Total Revenue PEG</b>	<b>(37,567)</b>	<b>(37,866)</b>	<b>(32,564)</b>
<b>Total Program</b>	<b>(\$1,283,147)</b>	<b>(\$1,291,238)</b>	<b>(\$1,245,490)</b>
(Negative) numbers decrease the gap.			

Most of the departmental reductions are spread over the city's many agencies, with DOE expecting to contribute nearly a quarter of the PEG savings. The DOE plans to achieve more than \$300 million in annual savings as a result of labor actions that are

expected to freeze the wages of teachers and administrators over the last round of collective bargaining.

In other areas, the city's mayoral agencies, such as the Cultural Affairs, Departments of Aging, Transportation, Finance and Environmental Protection, comprise the majority of the PEG actions in this category, which totals almost \$300 million in FY 2012 and about \$287 million in each of FYs 2013 and 2014. The city's uniformed agencies, representing the Police, Fire, Correction and Sanitation Departments, expect to produce savings totaling more than \$300 million in each of FYs 2012 and 2013, but that figure will fall by about \$50 million in FY 2014. The bulk of the savings will come from Correction and Sanitation with various reduction proposals. As part of its PEG actions, the Police Department budgeted to reduce its overtime spending by \$50 million annually starting in FY 2012. Lastly, the city's health and welfare agencies, which are comprised of the Administration of Children Services and the Departments of Social Services, Homeless and Health and Mental Hygiene, will reduce their spending by about \$218 million in FY 2012 and only slightly less in each of FYs 2013 and 2014.

### **Department of Education**

The Department of Education's (DOE) budget is projected to grow over FYs 2010-2014, but at a more moderate pace relative to FYs 2005-2009. In the most recent past, FYs 2005 through 2009, the average percentage growth for the total DOE budget was 6.4 percent. By comparison, the five-year projection for FYs 2010 through 2014 has an average percentage growth of 1.7 percent.

Over the years the city's funding share remains rather constant. In FYs 2005-2009, city funding (including other categorical and intracity) averaged \$6.7 billion, or an average of 42.2 percent of DOE's budget. From FYs 2010-2014, it is projected to average \$8 billion, for an average share of 42.6 percent of the department's total. The average growth rate for FYs 2005-2009 was 6.3 percent; whereas going forward, FYs 2010-2014, the average growth is estimated to be 2.6 percent, with city funding for FY 2014 forecast at almost \$8.5 billion.

The effects of the state's budget austerity on education funding begin to show in FYs 2012 through 2014. Between FYs 2005-2009, state funding provided an average contribution of almost \$7.4 billion, or an average of 46.3 percent of the department total operational budget. From FYs 2010 through 2014, aid from the state is forecast to average just over \$8.6 billion, or on average of 45.9 percent of the total budget. However, in FYs 2010-2014, the average growth rate falls in comparison to the prior five years. In FYs 2005-2009, the average actual growth rate stood at 8.3 percent, whereas in FYs 2010 through 2014, it is projected to be 1.6 percent. State funding for FY 2014 is currently forecast at just below \$9.3 billion.

With a contribution of just under \$2.6 billion, federal funds made up almost 14 percent of the department's total budget in FY 2011. In the recent past, the share hovered around 12 percent. For example, between FYs 2005-2009, its average contribution annually was just above \$1.8 billion, or 11.5 percent of total share, which translated into a negative growth rate of 0.4 percent over the same period. But with the surge in funding in FYs 2010 and 2011 stemming from the stimulus aid, the average

growth rate for FYs 2010 through 2014 soars to almost five percent, even though projections for FYs 2012-2014 are showing very conservative estimates, just over \$1.7 billion per year, resulting in the average proportion remaining stable at 11.4 percent between FYs 2010-2014.

#### **Uniformed Agency Overtime for FYs 2011-2014**

As mentioned in "FY 2011 Uniformed Agency Overtime" on page 13, the city had spent \$862 million on uniformed agency overtime expenditures in FY 2010. The amount of money appropriated to this budgetary area has been on the rise for the last several years and has remained elevated at above \$700 million since the September 11<sup>th</sup> attacks. The increase in spending has been most prevalent in the Police Department, which has increased spending each year. The other agencies, Fire, Correction and Sanitation, have needed additional funding as well, but not on a regular basis.

The Police Department must continue to fund programs that are paid for with overtime dollars such as Operation Impact. The Department must also handle unscheduled events or occurrences that could require numerous overtime hours. The city has recognized that steps must be taken to rein in the high cost of overtime spending in the Department and has devised a plan that will focus on overtime spending, not at the Department level but at the precinct level. The idea is to control overtime where it is mostly created, which will provide savings centrally. The city expects to save \$50 million annually in its overtime budget. However, we remain cautious that the savings will fully materialize given that the plan's initiation has been moved to FY 2012 from an original start date of FY 2010 due to logistical concerns.

In the July financial plan, the city projects uniformed agency overtime spending will not exceed the \$800 million threshold as it did in FY 2010. As shown in Table 9, the city expects to spend \$722 million in FY 2011 and stay under \$700 million in FYs 2012 through 2014. These projections may hold if the Police Department is able to enact spending discipline according to its plan. Additionally, the Department of Correction has identified efficiencies that will restrain it from spending above its allocated budget. However, overtime spending in the Fire Department may be elevated due to the Department operating with fewer firefighters than budgeted (a pending court decision pertaining to a bias issue may inhibit the Department's ability to hire) and the elimination of savings that was related to the closure of 20 fire companies, which has been reversed by the City Council restorations.

**PROJECTED RISK TO UNIFORMED OVERTIME BUDGET FOR FYs 2011-2014**

TABLE 9

(\$ in millions)

<b>Agency</b>	<b>FY 2011</b>	<b>FY 2012</b>	<b>FY 2013</b>	<b>FY 2014</b>
Police Department	\$413	\$367	\$366	\$366
Fire Department	174	168	171	171
Department of Correction	76	76	76	76
Department of Sanitation	59	64	65	65
<b>City Budgeted Overtime</b>	<b>\$722</b>	<b>\$675</b>	<b>\$678</b>	<b>\$678</b>
FCB Projected Overtime	862	862	862	862
<b>Projected Risk</b>	<b>(\$140)</b>	<b>(\$187)</b>	<b>(\$184)</b>	<b>(\$184)</b>

Based on an analysis of actual overtime spending by the four agencies, for both uniform and civilian personnel, for FY 2010 we are anticipating risks to the overtime budget in the outyears of the financial plan. We project an increased level of spending in all years of the financial plan with \$140 million more in FY 2011, \$187 million in FY 2012, and \$184 million in each of FYs 2013 and 2014, as shown in Table 9. The city historically underestimates its overtime budget at the beginning of each fiscal year and increases it with each budget modification based on the current level of spending. As this action occurs, the risk to the city's budget is mitigated.

### **Pension Costs in FYs 2011-2014**

As shown in Table 10, pension costs for FYs 2011 to FY 2014 are projected to rise by about \$474 million from \$7.6 billion in FY 2011 to almost \$8.1 billion in FY 2014. Year-to-year growth is \$264 million from FY 2011 to FY 2012 and more than \$100 million between each of FYs 2012 and 2013, and FYs 2013 and 2014. For the July financial plan, the overall growth in the city's annual pension contribution of 20 percent over the plan reflects earlier adjustments that required the city to fund massive investment losses. Had the city not taken such early prudent actions to deal with back-to-back years of negative investment returns, the city would be facing significantly higher costs. Still, the city's pension cost continues to climb each fiscal year and is contributing to the growth in overall city expenses over the financial plan.

TABLE 10

**PROJECTED PENSION CONTRIBUTIONS IN FYs 2011-2014**  
(\$ in millions)

Funding Source	FY 2011	FY 2012	FY 2013	FY 2014
City	\$7,447	\$7,710	\$7,815	\$7,918
State	38	39	41	41
Federal	3	3	3	3
Intracity	124	124	124	124
<b>Total Contributions</b>	<b>\$7,612</b>	<b>\$7,876</b>	<b>\$7,983</b>	<b>\$8,086</b>

The city's pension contribution covers contributions made to five primary systems and an additional number of noncity and nonactuarial systems, as shown in Table 11. The New York City Retirement Systems (NYCRS) is comprised of the New York City Employees' Retirement System (NYCERS), the Teachers' Retirement System of the City of New York (TRS), the New York City Police Pension Fund, the New York City Fire Department Pension Fund, and the New York City Board of Education Retirement System (BERS).

TABLE 11

**RECONCILIATION OF PROJECTED CONTRIBUTIONS IN FYs 2011-2014**  
(\$ in millions)

Plan Adjustments	FY 2011	FY 2012	FY 2013	FY 2014
NYCERS	\$1,304	\$1,376	\$1,436	\$1,503
TRS	2,429	2,562	2,680	2,779
Police	2,084	2,167	2,181	2,118
Fire	891	920	904	893
BERS	171	182	186	196
Noncity Systems	81	92	103	115
Nonactuarial Systems	50	51	53	53
Financial Plan Adjustments	603	527	440	430
<b>Total Pension Contributions</b>	<b>\$7,612</b>	<b>\$7,876</b>	<b>\$7,983</b>	<b>\$8,086</b>
Note: Numbers may not add due to rounding.				

Every fiscal year, the city makes a required contribution to its pension systems. As shown in Table 11 on page 32, the city's annual contribution is comprised of separate contributions to each pension system, noncity systems and nonactuarial systems. The contribution to each of those systems represents the present value of the future benefits earned by active city employees each year. The benefits rise with salary increases, overtime pay, and other added compensation and benefits.

In addition, the city often makes financial plan adjustments to its budgeted projections. When necessary, the pension systems need additional funding to meet obligations, such as in the case of funding investment losses. The city has funded losses suffered in FYs 2008 and 2009 in prior plans. To provide these resources, the city is reducing the funding allocated to the Retiree Health Benefits Trust (RHBT) used to pay annual healthcare insurance for current and retired city workers. It plans to reduce the RHBT by \$395 million in FY 2011 and \$672 million in FY 2012, to offset the phase-in of pension losses in those fiscal years, and has already used \$82 million in FY 2010. The city had planned to drawdown an additional \$957 million in FY 2013; however those plans have been reversed and deemed unnecessary.

In this plan, the city is also recognizing adjustments for additional reserves to address higher costs related to an upcoming actuarial recommendation, a valuation update that incorporates investment losses, headcount adjustments and reversal of a Tier 5 proposal. Also, the city is recognizing savings from labor actions that will reduce pension costs by \$43 million in FY 2012 and \$87 million in each of FYs 2013 and 2014. As shown in Table 11, in its July financial plan, the city expects to make financial plan adjustments to its FY 2011 projected pension cost of \$603 million, \$527 million in FY 2012, \$440 million in FY 2013, and \$430 million in FY 2014.

#### **Other Postemployment Benefits**

The New York City Health Benefits Program provides Other Postemployment Benefits (OPEB) to eligible retirees and beneficiaries. OPEB is comprised of Pre-Medicare and Medicare payments, Medicare Part B reimbursements and welfare fund contributions. Prior to a change in reporting standards (Statement No. 45) by the Governmental Accounting Standards Board (GASB) that requires governments to report their promised OPEB expenses as a liability, the city reported its annual OPEB expense on a pay-as-you-go basis and financial statements did not reflect the effects of these costs until paid.

Starting in FY 2006 and based on a FY 2005 actuarial valuation, the city began to recognize the actuarial present value of promised OPEB benefits for active city workers. Those promised benefits are known as the Unfunded Actuarial Accrued Liability (UAAL). As stated in GASB Statement No. 45, governments are not required to fund their OPEB liability but they are to report it on their financial statements. Nonetheless, the city took the initiative to form and fund the RHBT with an initial funding of \$1 billion in FY 2006 and followed with another payment in FY 2007 of \$1.5 billion. As of June 2009, trust fund assets have grown to more than \$3.1 billion.

The UAAL was initially calculated at \$50.5 billion and represents the amount needed to fully fund the RHBT. The liability continues to grow each fiscal year at an

average annual rate of 6.7 percent and remains significantly underfunded. As of FY 2009, the UAAL is estimated to be \$65.5 billion, which is \$15 billion, or nearly 30 percent, higher than the FY 2005 valuation. As reported in the city's financial statements for FY 2009, the OPEB obligation represents the city's largest long-term liability and accounts for 45 percent of total liabilities of \$146 billion. At this rate of growth, we estimate that the city's OPEB obligation will top \$90 billion by FY 2014. The growth could be accelerated further by higher anticipated spending on city healthcare benefits. The city's pay-as-you-go annual healthcare expense for retirees is expected to almost double over a nine-year period from about \$1.2 billion in FY 2005 to \$2.3 billion in FY 2014. Since FY 2005, on average, healthcare expenses for retirees have increased by more than eight percent annually, based on projected costs through FY 2014. The city currently estimates \$4.2 billion will be added to active employee healthcare expenses, increasing to almost \$6.5 billion in FY 2014.

It is obvious that the OPEB liability is likely to grow higher beyond FY 2014. Regardless, the city has budgeted for no additional funding of the RHBT and has in fact budgeted to tap into the RHBT to cover pension fund losses, reducing the trust fund by a projected \$1.1 billion including \$82 million, which has already been used in FY 2010. Also, the city has eliminated from the plan a proposal to collect a 10 percent premium health insurance contribution starting in FY 2011 that was expected to save \$357 million annually. Subsequently, the city and the Municipal Labor Committee have agreed to charge covered employees and retirees co-payments for certain medical services. Those savings have materialized, producing savings of \$200 million in FY 2010 and are expected to produce savings of \$200 million in FY 2011 and recurring annual savings of \$150 million thereafter.

## **RISKS AND OFFSETS**

Our risk evaluation of the city's financial plan is shown in Table 3 on page 5. Based on our evaluation, we estimate that the city could have risks to the budget ranging from \$596 million to \$1.6 billion in FYs 2011-2014. When we add our risks to the budget gaps stated in the financial plan, we conclude that the budget shortfalls facing the city will total \$596 million in FY 2011, \$4.8 billion in FY 2012, \$5.7 billion in FY 2013 and \$6.1 billion in FY 2014.

Property tax assessments increased 4.2 percent on the final roll for FY 2011, which represents a severe slowdown from the 6.7 percent billable growth in the previous year. The city expects billable assessment growth to slip to 3.5 percent in FY 2012, before dropping to about one percent in the outyears. Given that assessment growth is in the midst of a downtrend and that market values may fail to recover in FY 2012, it is possible that the city might not achieve its property tax growth target in FY 2012. We therefore place the property tax at risk for \$150 million in FY 2012, \$100 million in FY 2013 and \$50 million in FY 2014.

Based on historical patterns of growth and the city's practice of developing new initiatives, the city's miscellaneous revenue forecast could be higher by \$25 million in FY 2011, \$50 million in FY 2012, \$75 million in FY 2013, and \$100 million in FY 2014. We estimate that uniformed services overtime, based on our analysis and historical growth

rates, will exceed what the city has budgeted by \$140 million in FY 2011, \$187 million in FY 2012 and \$184 million in each of FYs 2013 and 2014.

Our projected risks to the city's budget, which are not in the Mayor's control, include anticipated state funding for the Aid and Incentives for Municipalities (AIM) program and education aid. Although the state financial plan assumes AIM funding of \$302 million in each of FYs 2012-2014, we have chosen to risk this amount. In the state's annual budget negotiation process the provision of these funds is sometimes reduced. As a consequence of the large gaps in this year's state budget, the entire amount was removed. Given the likelihood of state's continued fiscal stress, we believe the appropriation of these funds is uncertain. In addition, there is a potential risk of \$202 million in FY 2011 related to the accrual of state lottery funding for education. Since FY 2003, the city has been allowed to recognize future education aid in the current fiscal year in the amount of \$202 million. This authorization has been removed from the state's budget, due to the Governor's veto of the Article VII legislation for education aid. It is likely to be restored later in the fiscal year. Until the state legislature approves these funds as part of its budget, we hold this amount at risk.

The city is relying on the passage of an extension of the Federal Medical Assistance Percentages (FMAP) stimulus that will reduce Medicaid spending by an additional \$600 million from FY 2011 through FY 2013. The city has budgeted to receive \$279 million in FY 2011, \$61 million in FY 2012 and \$269 million in FY 2013. The city is already slated to save \$2.2 billion from the combination of the FMAP and federal healthcare reform, which will cover the period of FY 2009 through FY 2013. The additional \$600 million FMAP funding remains highly uncertain at this point with both the U.S. Senate and the U.S. House of Representatives having put aside the legislation due to an impasse on the issue of how it would be financed. Given this uncertainty, we hold at risk the receipt of the funding.<sup>11</sup>

Federal stimulus funds, made available by the American Recovery and Reinvestment Act, continued throughout FYs 2010 and 2011 to provide an offset to reduction in state aid. The city claims that over this same period 14,190 pedagogical positions were financed by these appropriations. The education stimulus funds are scheduled to expire at the beginning of FY 2012. If there is no extension of the stimulus and or additional state aid, the city will have to provide \$850 million of city funds or reduce expenditures by an equal amount.

## **DEBT SERVICE AS A NON-DISCRETIONARY EXPENSE**

Debt service cost, one of the more sizeable areas of the budget, has a significant impact on the city's finances. Driven by the cost of financing capital spending on schools, transportation, public buildings, correctional facilities, libraries, park facilities, housing, and more, debt service is arguably an indispensable expense. In addressing its budgetary challenges, the city has sought to reduce debt service by stretching out its

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<sup>11</sup> The city has funded the General Reserve in FY 2011 by an additional \$137 million, for a total reserve of \$437 million, in the event that the FMAP extension funding is not received.



capital plan, diversifying its borrowing program, refunding higher coupon bonds with lower coupon bonds, and maximizing its receipt of interest subsidies. However, as we will show, the vast majority of the burgeoning debt service cost in the financial plan is being generated by existing contract liabilities, making the expense largely nondiscretionary. In FY 2014, when debt service at \$6.8 billion is projected to consume over 15 percent of the city's tax revenues, only 10 percent of the cost is derived from capital commitments scheduled to be undertaken in FYs 2011-14.

### **Capital Spending**

In the financial plan that was released with the Executive Budget in May, the city projects entering into a total of \$30.1 billion of capital commitments during FYs 2011-14 and spending in total a higher \$35.4 billion. Commitments in the financial plan represent the total contractual amounts entered into for individual projects, while spending reflects scheduled contractual payments. Typically, the city enters into multi-million dollar contracts for individual projects that would be paid for over a number of years as the work is undertaken. Commitments and spending are generally not equal because the annual allocation for spending is a function of prior commitments as well as present and future commitments. Table 12 reflects the capital commitment and spending projections contained in the financial plan.

### **CAPITAL SPENDING IS PROJECTED TO EXCEED COMMITMENTS DURING THE OUTYEARS OF THE PLAN**

TABLE 12

(\$ in millions)

	FY 2011	FY 2012	FY 2013	FY 2014	Total
<b><u>CAPITAL COMMITMENTS</u></b>					
GO & NYCTFA Revenue	\$6,548	\$4,353	\$4,209	\$3,565	\$18,675
DEP	1,705	876	1,117	1,237	4,935
NonCity	<u>1,834</u>	<u>1,664</u>	<u>1,311</u>	<u>1,634</u>	<u>6,443</u>
Total	\$10,087	\$6,893	\$6,637	\$6,436	\$30,053
<b><u>CAPITAL SPENDING</u></b>					
GO & NYCTFA Revenue	\$6,048	\$5,441	\$4,941	\$4,873	\$21,303
DEP	2,085	1,936	1,693	1,581	7,295
NonCity	<u>1,409</u>	<u>1,716</u>	<u>1,852</u>	<u>1,784</u>	<u>6,761</u>
Total	\$9,542	\$9,093	\$8,486	\$8,238	\$35,359

Of the total amount of capital commitments in the plan, \$18.7 billion will be supported with proceeds from the sale of city general obligation (g.o.) bonds and the New York City Transitional Finance Authority (NYCTFA) revenue bonds. Correspondingly, the city reveals that it plans to spend a higher \$21.3 billion of city g.o. and NYCTFA revenue bond proceeds on its capital program during FYs 2011-14, as there are existing contract liabilities on which payments have to be made. The sale of city g.o. and NYCTFA revenue bonds generates the vast majority of debt service cost in the financial plan, which is supported by tax revenues. In addition to city tax revenue supported commitments, the plan contains \$4.9 billion of contracts that are backed by proceeds from the sale of Water Authority revenue bonds, which are repaid from user fees, and \$6.4 billion of contracts that are noncity funded. For capital spending, the plan

includes \$7.3 billion that are funded with Water Authority bond proceeds and \$6.8 billion that are noncity funded.

As can be seen in Table 12 on page 36, spending begins to exceed commitments from FY 2012. It was not common in past years for capital spending to exceed commitments.<sup>12</sup> Annual capital spending can be higher than commitments when there is a large accumulation of prior-year contracts that have yet to be liquidated, as is the case in the current financial plan. At the end of FY 2010, there were \$11.2 billion of existing contracts scheduled to be paid for in coming years. The existing contract liability at the end of FY 2010 is comprised of unpaid commitments from the three years with the highest capital contracts. These commitments totaled \$6.0 billion in FY 2008, followed by \$5.1 billion in FY 2009, and a yet to be confirmed \$7.5 billion in FY 2010.

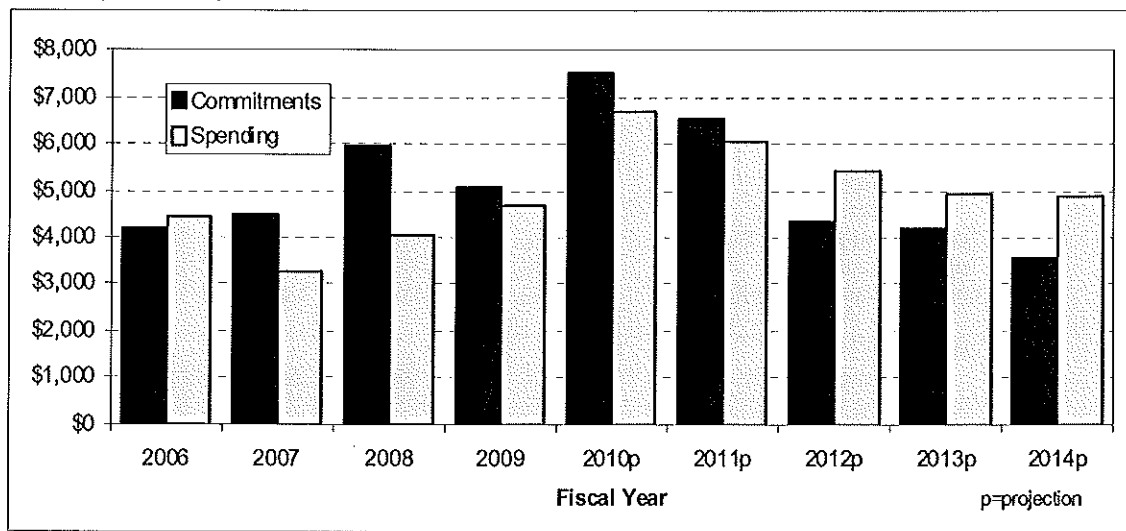
The cash flow rate on commitments varies for some areas. For the Department of Education, which accounts for 24 percent of the g.o. and NYCTFA capital commitments in the plan, it is assumed that 40 percent of current-year commitments is paid for in the first year, 38 percent in the second year, 13 percent in the third year, eight percent in the fourth year and the remaining one percent in the fifth year. Meanwhile, a relatively small amount of commitments, between \$367 million and \$386 million in each of FYs 2011-14, is spent annually to pay capital financing costs and in-house salaries related to capital projects. However, for the vast majority of departments, only about 18 percent of the current-year commitments is assumed to be paid for in the first year; a higher 24 percent in the second year; and decreasing amounts of 19 percent in the third year, 12 percent in the fourth year and eight percent in the fifth year. Payment of the remaining 19 percent is spread over the following five years. With high levels of commitments having yet to be paid for, capital spending is now projected to exceed planned contracts starting in FY 2012, as illustrated in Chart 2.

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<sup>12</sup> On occasions, annual capital contracts and spending were adjusted in large lump sums to reflect particular circumstances, which skewed the reported totals and may have resulted in spending exceeding commitments.

CHART 2

**A BUILD UP OF COMMITMENTS IN PRIOR YEARS IS DRIVING  
THE COMPARATIVELY HIGH CAPITAL SPENDING IN THE OUTYEARS**  
(\$ in millions)



Interestingly, the financial plan assumes that both city g.o.- and NYCTFA-funded capital commitments and spending would peak in FY 2010, decreasing thereafter in each year through FY 2014. For commitments and spending to recede, the city would have to restrain from expanding its capital program beyond the levels in the plan. Given historical patterns where annual commitments and spending have trended upward, reflecting both the growing scope of work undertaken and escalating costs of construction, it would pose a tremendous challenge to the city to keep the two from climbing in the outer years.

### **Debt Levels**

The amount of long-term borrowing scheduled to be undertaken by the city and NYCTFA to support the capital program is commensurate with the levels of capital spending. The financial plan assumes that in FYs 2011-14 the city and NYCTFA will each sell equal amounts of bonds to support the general capital program, for a combined \$21.3 billion. Of this four-year total, \$8.9 billion will fund contracts that had already been entered into and \$12.4 billion will fund future commitments.

For a comprehensive analysis of the debt resulting from the city's capital program, we use the framework of the annual Statement of Debt Affordability that was provided by the city. The Statement of Debt Affordability presents the aggregate debt and debt service levels for bonds backed by tax revenues, as well as city lease expenses. As can be seen in Table 13 on page 39, debt service is projected to climb from \$5.5 billion in FY 2011 to \$6.8 billion in FY 2014, for an average annual growth rate of 7.7 percent.<sup>13</sup>

<sup>13</sup> Debt service projections are based on long-term financing assumptions in the executive budget and are net of prepayments. Debt service estimates based on assumptions in the adopted budget amount to \$5.351 billion in FY 2011, \$6.294 billion in FY 2012, \$6.602 billion in FY 2013 and \$6.859 billion in FY 2014, for an average annual growth rate of 8.6 percent.

TABLE 13

**DEBT SERVICE AND OUTSTANDING DEBT BURDENS ARE HIGH**  
(\$ in millions, except per capita)

	FY 2011	FY 2012	FY 2013	FY 2014	Average Annual Growth
City & NYCTFA Debt Service	\$ 5,462	\$ 6,273	\$ 6,576	\$ 6,817	7.7%
Debt Service Per Capita	682	783	821	851	
<b>Debt Service as Percentage of:</b>					
Tax Revenues	14.0%	15.4%	15.5%	15.6%	
Total Revenues	8.7%	9.7%	9.9%	10.0%	
Local Personal Income	1.3%	1.4%	1.4%	1.4%	
City & NYCTFA Outstanding Debt	\$ 61,185	\$ 63,868	\$ 65,892	\$ 67,761	3.5%
Outstanding Debt Per Capita	7,640	7,975	8,228	8,461	
<b>Outstanding Debt as Percentage of:</b>					
Local Personal Income	14.1%	14.3%	14.1%	13.8%	
Tax Revenues	\$ 38,892	\$ 40,817	\$ 42,330	\$ 43,659	3.9%
Total Revenue	62,938	64,549	66,248	68,027	2.6%
Local Personal Income	433,780	447,620	467,570	489,270	4.1%

The rising debt service costs will require an increase in per capita spending from \$682 in FY 2011 to \$851 in FY 2014. Furthermore, debt service payments are projected to consume larger shares of tax and total revenues, as well as local personal income. Debt service is projected to rise from 14.0 percent in FY 2011 to 15.6 percent in FY 2014 as a percentage of tax revenues; 8.7 percent in FY 2011 to 10.0 percent in FY 2014 as a percentage of total revenues; and 1.3 percent in FY 2011 to 1.4 percent in FY 2014 as a percentage of local personal income. At the outyear levels, the projected debt service burdens hover around the upper range that has existed since the city emerged from the financial crisis of the 1970s. At 7.7 percent, the average annual rate of growth for the combined debt service is outstripping the rates for tax revenues at 3.9 percent, total revenues at 2.6 percent, and local personal income at 4.1 percent.

Debt service has often been referred to as a nondiscretionary expense. The debate of whether debt service is a discretionary or nondiscretionary cost rests on how much flexibility exists in issuing the associated debt. The fact that the vast majority of projected city and NYCTFA debt service is generated by bonding for commitments that have been already entered into makes a case for classifying city and NYCTFA debt service as nondiscretionary. The discretionary portion of debt service – the cost associated with borrowing for commitments to be entered into during the ensuing four years – totals \$25 million in FY 2011, \$151 million in FY 2012, \$391 million in FY 2013 and \$685 million in FY 2014. As a percentage of total debt service, the discretionary share is less than one percent in FY 2011, and reaches 10 percent by FY 2014.

Table 13 also reveals that the combined outstanding debt is forecasted to grow from \$61.2 billion at the end of FY 2011 to \$67.8 billion at the end of FY 2014, for an average annual growth rate of 3.5 percent. While this growth rate may not seem relatively fast, the outstanding debt value for the base year is high. Outstanding debt per capita is expected to rise from \$7,640 in FY 2011 to \$8,461 in FY 2014, which in FY 2014 is over one-third greater than the highest debt per capita since the 1980s. Meanwhile, the debt to income ratio is forecasted to range from a high of 14.3 percent in FY 2012 to a low of 13.8 percent in FY 2014, where the highest debt to income ratio since the 1980s was 14.2 percent.

## **Glossary of Acronyms**

<b>AIM</b>	Aid and Incentives for Municipalities
<b>AIR</b>	Actuarial Interest Rate
<b>ARRA</b>	American Recovery and Reinvestment Act
<b>BERS</b>	Board of Education Retirement System
<b>BSA</b>	Budget Stabilization Account
<b>CSA</b>	Council of School Supervisors and Administrators
<b>CUNY</b>	City University of New York
<b>CY</b>	Calendar Year
<b>DEP</b>	Department of Environmental Protection
<b>DOE</b>	Department of Education
<b>FCB</b>	Financial Control Board
<b>FEA</b>	Financial Emergency Act
<b>FMAP</b>	Federal Medical Assistance Percentages
<b>FY</b>	Fiscal Year
<b>GASB</b>	Government Accounting Standards Board
<b>GCP</b>	Gross City Product
<b>GDP</b>	Gross Domestic Product
<b>G.O. Bonds</b>	General Obligation Bonds
<b>HHC</b>	Health and Hospitals Corporation
<b>IGA</b>	Intergovernmental Aid
<b>NYCERS</b>	New York City Employees' Retirement System
<b>NYCRS</b>	New York City Retirement Systems
<b>NYCTFA</b>	New York City Transitional Finance Authority
<b>NYSE</b>	New York Stock Exchange
<b>OPEB</b>	Other Postemployment Benefits
<b>OT</b>	Overtime
<b>OTPS</b>	Other than Personal Service

PEG	Program to Eliminate the Gap
PIT	Personal Income Tax
PS	Personal Service
RHBT	Retiree Health Benefits Trust
STAR	School Tax Relief program
TRS	Teachers' Retirement System of the City of New York
UAAL	Unfunded Actuarial Accrued Liability
UBT	Unincorporated Business Tax
UFT	United Federation of Teachers

