Review of the Financial Plan of the City of New York

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Contents

I. Executive Summary

On April 26, 2007, the Mayor of New York City released his Executive Budget for FY 2008 and a revised four-year financial plan (the "April Plan"). The April Plan shows that, since the beginning of the fiscal year, New York City has realized $8.9 billion in unanticipated resources for fiscal years 2007 and 2008, even after addressing funding needs that were not contemplated at the start of the fiscal year. As it did last year, the City has used these resources to improve its long-term financial position.

Tax collections have exceeded the City's initial forecast for FY 2007 by $5 billion because of unexpected strength in the local economy. A total of 62,200 jobs were created in calendar year 2006—8,000 more than originally reported and the sixth-best annual gain since the 1970s fiscal crisis. Wall Street profits surged in the last quarter of calendar year 2006 to reach $20.9 billion for the year—just short of the record set in 2000—resulting in record year-end bonuses and the fastest job growth in the industry in 12 years. The City continued to add jobs at a brisk pace during the first quarter of 2007, and Wall Street profits have remained strong.

Overall, the City realized a net benefit of $5.6 billion during FY 2007. Of that amount, the City allocated more than $1.2 billion to retire outstanding debt due in fiscal years 2009 and 2010. This will generate interest savings of $113 million over the next three years and will provide debt relief in the years the City had been forecasting large budget gaps. The relief is short-term, however, and debt service will reach $6.1 billion in FY 2011; this will be 60 percent higher than the level in FY 2006. The City plans to use the remaining net surplus of $4.4 billion—the largest on record—to prepay future expenses, thus narrowing projected budget gaps.

The City also plans to contribute $500 million in FY 2008 to the Retiree Health Benefits Trust Fund, which the City created to help pay down a $50 billion unfunded liability for post-employment benefits. (The City contributed $1 billion in each of fiscal years 2006 and 2007.) In addition, the Mayor has proposed a tax reduction program, worth more than $1.3 billion in FY 2008, which will stimulate economic activity and improve the City's competitiveness with surrounding jurisdictions. The State still has to approve certain elements of the proposed program, which have a value of nearly $600 million in FY 2008 and more than $900 million by FY 2011.

The City also provided additional financial aid to the Health and Hospitals Corporation so the Corporation can continue to obtain supplemental Medicaid funding from the federal government. Although this action could stabilize the Corporation's finances through FY 2009, the federal government is contemplating the restriction of such supplemental payments. The New York City Housing Authority and the Off-Track Betting Corporation still face serious financial difficulties in the current year.

The City has reached new labor agreements with most of the municipal unions for the 2000-2008 rounds of collective bargaining. The Patrolmen's Benevolent Association is seeking larger wage increases through arbitration than the City has been prepared to grant through negotiation. The April Plan includes a substantial increase in education funding over the next four years; sets aside monies to fund PlaNYC 2030, a mayoral initiative to improve the environment and the City's infrastructure; and reflects the impact of the State budget.

The recently enacted State budget increases education aid to the City's public schools by an unprecedented $714 million, but reduces aid to other parts of the City's budget by a net of $366 million during fiscal years 2007 and 2008. Most of the adverse impact comes from the elimination of unrestricted revenue sharing payments for one year, although future payments can no longer be taken for granted. The April Plan reflects the commitments of the Mayor and the Governor to increase funding to the City's public schools by a cumulative total of $5.5 billion over the next four years as part of the resolution of the Campaign for Fiscal Equity lawsuit. The additional funding is an important step toward providing New York City's children with the educational services they will need to effectively compete for well-paying jobs.

Unanticipated revenues, combined with prudent budgeting, have helped close a $3.8 billion budget gap that was projected for FY 2008 and have reduced the FY 2009 budget gap from $4.6 billion to $1.6 billion, a reduction of 66 percent. While the FY 2010 budget gap has been reduced to $3.3 billion, the FY 2011 remains formidable at $4.3 billion. These gap estimates anticipate an economic slowdown beginning later in 2007, which will result in a 4.9 percent decline in nonproperty tax collections during FY 2008. The April Plan assumes that Wall Street profits will decline by 60 percent over the next two years, resulting in lower year-end bonuses and fewer new jobs. While tax revenues may not decline as sharply as anticipated in the April Plan, the City's forecasts are appropriately conservative given its heavy reliance on Wall Street and the volatility of international financial markets.

Figure 1
New York City Financial Plan
(in millions)

	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
REVENUES					
Taxes					
General Property Tax	$12,976	$14,220	$ 15,363	$ 16,485	$ 17,431
Other Taxes	23,498	22,652	22,231	23,040	23,882
Discretionary Transfer FY07 TFA Debt Service	- - -	548	- - -	- - -	- - -
Tax Audit Revenue	959	559	559	560	560
Tax Reduction Program	- - -	(1,331)	(1,607)	(1,735)	(1,846)
Miscellaneous Revenue	5,526	5,912	5,071	5,087	5,121
Unrestricted Intergovernmental Aid	33	340	340	340	340
Less: Intra-City Revenues	(1,401)	(1,369)	(1,364)	(1,365)	(1,365)
Grant Disallowances	(15)	(15)	(15)	(15)	(15)
Subtotal: City Funds	**$ 41,576**	**$ 41,516**	**$ 40,578**	**$ 42,397**	**$ 44,108**
Other Categorical Grants	1,104	1,002	1,003	1,012	1,014
Inter-Fund Revenues	418	428	404	396	391
Total City & Inter-Fund Revenues	**$ 43,098**	**$ 42,946**	**$ 41,985**	**$ 43,805**	**$ 45,513**
Federal Categorical Grants	5,906	5,302	5,384	5,369	5,362
State Categorical Grants	10,259	10,790	11,408	12,272	12,715
Total Revenues	**$ 59,263**	**$ 59,038**	**$ 58,777**	**$ 61,446**	**$ 63,590**
EXPENDITURES					
Personal Services					
Salaries and Wages	$19,668	$ 21,021	$ 22,060	$ 23,463	$ 24,586
Pensions	4,861	5,728	6,390	6,461	6,461
Fringe Benefits	7,018	6,928	6,716	6,997	7,316
Subtotal: Personal Services	**$ 31,547**	**$ 33,677**	**$ 35,166**	**$ 36,921**	**$ 38,363**
Other Than Personal Services					
Medical Assistance	$5,194	$ 5,714	$ 5,603	$ 5,756	$ 6,076
Public Assistance	1,203	1,187	1,187	1,187	1,187
Pay-As-You-Go Capital	200	200	200	200	200
All Other	17,474	17,033	17,352	17,814	18,065
Subtotal: Other Than Personal Services	**$ 24,071**	**$ 24,134**	**$ 24,342**	**$ 24,957**	**$ 25,528**
General Obligation, Lease, and MAC Debt Service	4,327	3,773	3,896	4,244	5,053
FY 2006 Budget Stabilization & Discretionary Transfers	(3,751)	- - -	- - -	- - -	- - -
FY 2007 Budget Stabilization & Discretionary Transfers	4,385	(3,837)	- - -	- - -	- - -
FY 2008 Budget Stabilization & Discretionary Transfers	- - -	2,360	(2,360)	- - -	- - -
FY 2009 Budget Stabilization & Discretionary Transfers	- - -	- - -	350	(350)	- - -
General Reserve	85	300	300	300	300
Subtotal: Expenditures	**$ 60,664**	**$ 60,407**	**$ 61,694**	**$66,072**	**$69,244**
Less: Intra-City Expenses	(1,401)	(1,369)	(1,364)	(1,365)	(1,365)
Total Expenditures	**$59,263**	**$59,038**	**$ 60,330**	**$64,707**	**$67,879**
Gap To Be Closed	**$ ----**	**$ ----**	**$ (1,553)**	**$ (3,261)**	**$ (4,289)**

Source: NYC Office of Management and Budget

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

	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
			Better/(Worse)		
Gaps Per April 2007 Plan	**$ - - -**	**$ - - -**	**$ (1,553)**	**$ (3,261)**	**$ (4,289)**
Tax Revenues	275	500	500	200	200
Uniformed Agency Overtime	- - -	(100)	(100)	(100)	(100)
OSDC Risk Assessment	**$ 275**	**$ 400**	**$ 400**	**$ 100**	**$ 100**
Surplus/(Gaps) to be Closed[1]	**$ 275**	**$ 400**	**$ (1,153)**	**$ (3,161)**	**$ (4,189)**
Additional Risks and Offsets					
Tax Cuts That Require State Approval	- - -	581	797	867	929
State AIM Payments (Revenue Sharing)	- - -	(327)	(327)	(327)	(327)
Wage Increases at Projected Inflation Rate	- - -	- - -	(175)	(450)	(795)

[1] The April Plan includes a general reserve of $85 million in FY 2007 and $300 million annually in fiscal years 2008 through 2011.

II. Economic Overview

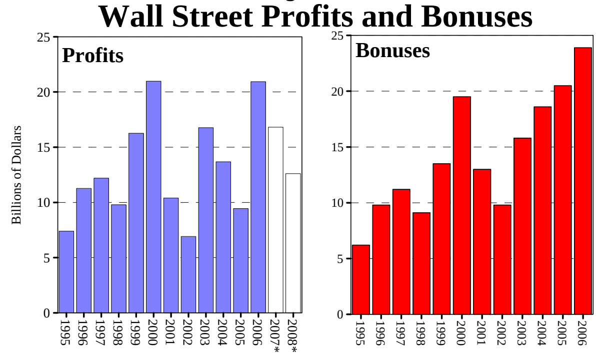
Recent data have revealed that the City's economy was much stronger during 2006 than was initially reported, and that strength has continued into 2007. The City added 62,200 jobs during 2006—the largest increase in six years—and Wall Street profits approached record levels. During the first quarter of 2007 the City continued to add jobs at a brisk pace and Wall Street profits have remained strong. The commercial real estate market also remains strong and the easing in the residential market has been much milder than elsewhere in the nation. Despite the strength of the local economy, the April Plan assumes that economic growth will slow in calendar year 2007 as the slowdown in the national economy takes its toll on the local economy.

Clear signs indicate that the national economy has begun to slow. Preliminary data show that the gross domestic product grew by only 1.3 percent during the first quarter of 2007, which is the weakest performance since the first quarter of 2003. Home construction declined by double-digits for the fourth consecutive quarter, and nonresidential investment slowed sharply during the past two quarters. Consumer spending, however, has remained robust as job and wage gains have more than offset the impact of diminishing home values. While inflation has eased, it remains above the Federal Reserve's target; in addition, rising gasoline prices will put upward pressure on inflation and could adversely affect consumer spending, which accounts for two thirds of the national economy.

The City's economy has demonstrated considerable resiliency, and the slowdown in the national economy has not yet had a significant impact on the City. Wall Street profits more than doubled in 2006 to a near-record of $20.9 billion (see Figure 3), including gains of $7.6 billion in the fourth quarter—the best quarter since the first quarter of 2000. As a result, Wall Street had record year-end bonuses and the fastest job growth in 12 years (5.6 percent). Preliminary reports show that mergers and acquisitions and trading continued to generate strong profits in the first quarter of 2007. Profits at the seven largest financial firms headquartered in the City increased by 54.8 percent in the first quarter of 2007 compared to the first quarter of 2006.

Figure 3

Wall Street Profits and Bonuses



* City forecasts for 2007 & 2008

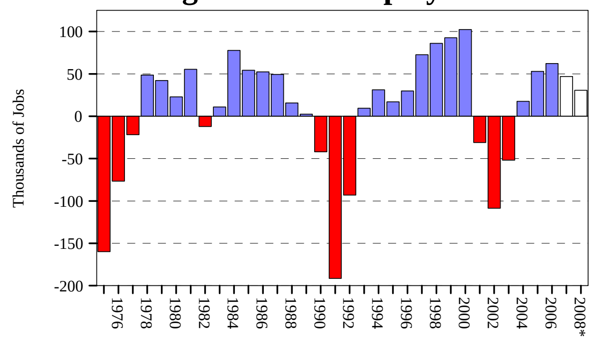
Notes: Bonuses are OSDC estimates. Profits are for broker/dealer operations of NYSE member firms.

Sources: NYS Department of Labor; New York Stock Exchange; Securities Industry and Financial Markets Association; OSDC analysis

The strong performance on Wall Street helped lift job growth in other industries, including professional and business services, information, retail trade, and other financial industries. Manufacturing was the only major sector that lost jobs.

The City's overall gain of 62,200 jobs in 2006 was 8,000 more jobs than originally reported and the sixth-best gain since the fiscal crisis of the 1970s (see Figure 4). Strong job growth pushed the City's unemployment rate down to a record low of 4.9 percent during 2006, and the unemployment rate has averaged 4.7 percent during the first four months of 2007.

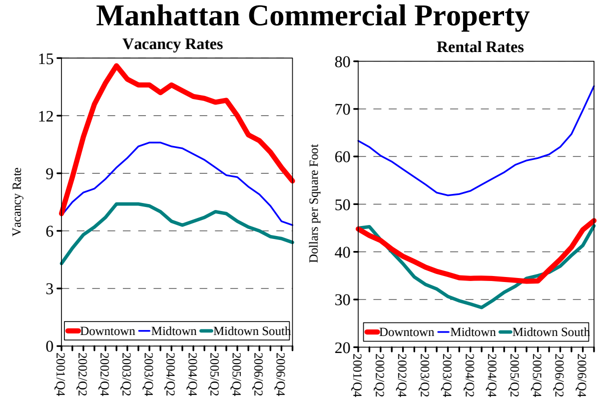
Figure 4
Annual Change in Total Employment in NY



* City's forecasts for 2007 & 2008
Sources: NYS Department of Labor; OSDC analysis

The commercial real estate market is thriving and has almost returned to pre-recession levels. Rental rates for prime commercial properties in each of the three Manhattan submarkets have continued to rise in response to lower vacancy rates (see Figure 5). The limited supply of office space in the Midtown area has caused asking rents in offices there to increase by nearly $30 per square foot over the past four years, and asking rents reached $82.40 per square foot in March 2007 as vacancy rates declined to 6 percent. Vacancy rates in the Downtown market fell by 8.8 percentage points to reach 6.5 percent, and rental rates rose by almost $14 per square foot to reach nearly $50 per square foot. While there has been some moderation in the market for sales of smaller commercial properties, prices for high-end commercial buildings continue to reach new highs, helping drive real estate transaction tax collections. Although the local housing market has softened, the decline has not been as steep as in other parts of the nation, especially in the south and west.

Figure 5
Manhattan Commercial Property



Note: Data is a four-quarter moving average for premium (Class A) commercial space.
Sources: Colliers ABR; OSDC analysis

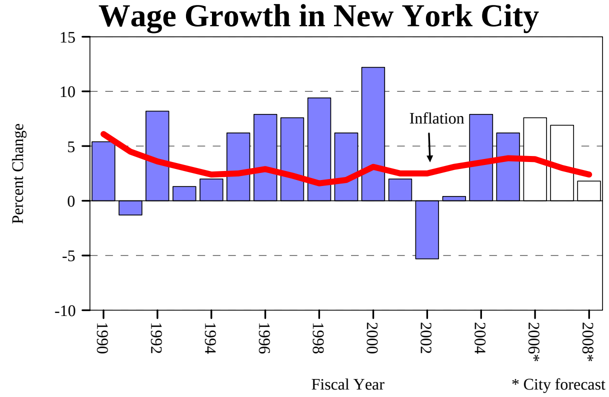
Tourism is booming, and a record 44 million visitors flocked to the City in 2006 (including 7 million from overseas). The rapid growth in tourism—an increase of 9 million visitors in only five years—has pushed both hotel room rates and occupancy rates higher (to reach $271 per night and 85.5 percent, respectively, in 2006). In addition, rising tourism has helped create jobs in the leisure and hospitality sector and in retail trade. The number of overseas visitors is expected to further increase in 2007 as the dollar continues to weaken.

The April Plan is premised on the following economic assumptions.

- Wall Street profits, which reached $20.9 billion in 2006, will decline by about $4 billion annually to $12.6 billion in 2008, before rebounding. Lower profits are expected to reduce year-end bonuses, which reached record levels in 2006.
- Job gains in New York City will slow from 62,200 in 2006 to 47,000 in 2007 and then 30,600 in 2008. Most gains are expected to be concentrated in three sectors: professional and business services, education and health care, and leisure and hospitality.
- Wage growth will slow from 7.6 percent in 2006 to 6.9 percent in 2007 (see Figure 6). Wages are projected to grow by only 1.8 percent in 2008—substantially slower than the projected rate of inflation—because of an expected decline in Wall Street bonuses.

Figure 6

Wage Growth in New York City



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

- The residential housing market will continue to contract until it slowly improves beginning in 2009. The April Plan assumes that the number of residential real estate transactions will decline by 7.3 percent in 2007 and by another 3 percent in 2008, and that residential home prices will decline at an average annual rate of 6 percent in 2007 and 2008.
- The commercial real estate market will further tighten, as vacancy rates in Manhattan's primary office markets continue to drop and rental rates reach new highs. The current strong demand for commercial space is driven by rising office-based employment and the relative lack of new space coming to market—factors that are not projected to change in the near term. Nonetheless, the City expects the number of very large commercial property transactions to moderate in 2008.
- Inflation will slow to 3 percent in 2007 and to 2.4 percent annually beginning in 2008.

Although New York City's economy is currently strong, it faces several risks. First, it remains highly dependent on Wall Street—and although Wall Street continues to report strong profits, an industry slow-down would ripple throughout the local and State economies. While the easing in the residential real estate market has been much milder than elsewhere in the nation, recent problems in the subprime mortgage industry will continue to affect both lenders and borrowers, and an overall tightening of credit standards in response to these problems could have a more serious impact on the entire housing market and consumer spending. In addition, volatility in energy and food prices could put upward pressure on inflation, and the declining value of the dollar will put upward pressure on the prices of imported goods. The Federal Reserve's interest rate policy decisions in the months ahead are also likely to affect the national and local economies.

III. Fiscal Year 2007

Buoyed by an economy that has performed much better than expected, New York City has realized a net total of $8.9 billion in unanticipated resources for fiscal years 2007 and 2008, when compared with the forecasts made by the City in June 2006, and even after addressing $1.6 billion in new funding needs (see Figure 8, next page). As discussed later in this section, the City has used these unanticipated resources to improve its fiscal position.

The funding needs addressed by the City since the beginning of the fiscal year include new labor agreements with the municipal unions; financial assistance to the Health and Hospitals Corporation; higher-than-anticipated pension contributions; and mayoral initiatives to increase education aid and to fund the PlaNYC 2030 proposal.

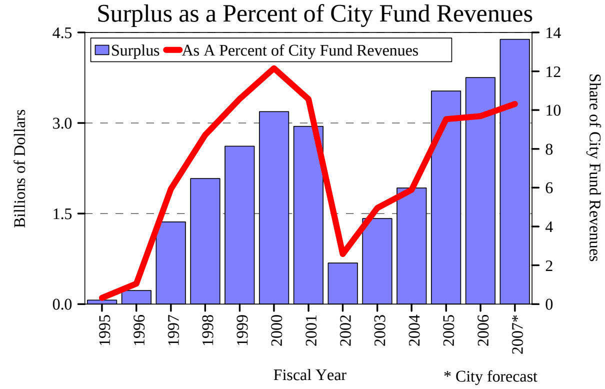
The steps taken by the City to improve its fiscal position include transferring surplus resources to future years, retiring outstanding debt, funding a tax reduction program, and depositing resources into a trust fund to help pay down the liability of post-employment benefits other than pensions, such as health insurance.

As a result of these actions, the City has closed a $3.8 billion budget gap that had been projected for FY 2008, and has reduced the FY 2009 budget gap from $4.6 billion to $1.6 billion and the FY 2010 budget gap by 20 percent to $3.3 billion.

A. The FY 2007 Surplus

The City projects a budget surplus of nearly $4.4 billion in FY 2007. The surplus would surpass last year's record in absolute terms (see Figure 7), but at 10.3 percent of City fund revenues it would be only the fourth-highest in relative terms. These estimates exclude more than $1.2 billion the City has set aside to retire outstanding debt. Thus, in total, even after addressing new funding needs that were identified since the beginning of the fiscal year, the City realized $5.6 billion in unanticipated resources during the course of FY 2007 (see Figure 8). Most of the resources were generated by higher tax collections from Wall Street–related economic activity and real estate transactions ($5 billion).

Figure 7
City Budget Surpluses
Surplus as a Percent of City Fund Revenues



Sources: NYC Office of Management and Budget; OSDC analysis

Figure 8
Financial Plan Reconciliation
July 2006 Plan vs. April 2007 Plan

(in millions)

		Better/(Worse)		
	FY 2007	**FY 2008**	**FY 2009**	**FY 2010**
Surplus/(Gap) Per July 2006 Plan	**- - -**	**$ (3,810)**	**$ (4,584)**	**$ (4,069)**
Revenues				
Business Taxes	$ 2,413	$ 1,546	$ 1,180	$ 1,149
Real Estate Transaction Taxes	1,432	1,079	734	714
Personal Income Tax	739	867	469	412
Real Property Tax	4	382	868	1,312
All Other Taxes	385	352	241	258
Subtotal	4,973	4,226	3,492	3,845
Non-Tax Revenues	293	240	10	14
Total	**5,266**	**4,466**	**3,502**	**3,859**
Net New Needs				
Collective Bargaining	(314)	(626)	(990)	(1,230)
State Budget Impact	(314)	(30)	(30)	(30)
Health and Hospitals Corporation	(203)	(408)	(54)	(148)
Education	(45)	(277)	(267)	(631)
PlaNYC 2030	- - -	(199)	(341)	(377)
Savings from Prior Years' Expenses	400	- - -	- - -	- - -
General Reserve	215	- - -	- - -	- - -
Debt Service	185	339	262	261
Pension Contributions	18	(125)	(542)	(749)
All Other	166	(369)	(377)	(243)
Total	**108**	**(1,695)**	**(2,339)**	**(3,147)**
Agency Gap-Closing Program	**257**	**472**	**346**	**304**
Net Change During FY 2007	**$ 5,631**	**$ 3,243**	**$ 1,509**	**$ 1,016**
Discretionary Actions				
Surplus Transfer	(4,385)	2,025	2,010	350
Retiree Health Benefits Trust Fund	- - -	(500)	- - -	- - -
Debt Retirement	(1,246)	64	639	656
Tax Reduction Program	- - -	(1,022)	(1,127)	(1,214)
Total	**(5,631)**	**567**	**1,522**	**(208)**
Surplus/(Gap) Per April 2007 Plan	**$ - - -**	**$ - - -**	**$ (1,553)**	**$ (3,261)**

Sources: NYC Office of Management and Budget; OSDC analysis

B. Revenue Reestimates

Compared to the forecasts made in July 2006, the City has raised its forecast of FY 2007 City fund revenues by $5.3 billion. Virtually all of this amount comes from higher nonproperty tax revenues, notably taxes on real estate transactions and personal and business income, as described below.

- Business tax collections were $2.4 billion higher than expected in July 2006. Wall Street profits surged in the fourth quarter of calendar year 2006, with full-year profits reaching $20.9 billion—just short of the record $21 billion earned in 2000. In addition, there was a one-time $450 million benefit from the settlement of several outstanding audits of financial firms.
- Real estate transactions generated an additional $1.4 billion. The City's real estate market remains strong—though residential sales have eased somewhat, prices on large commercial transactions are reaching new highs, generating much of the additional revenue.
- Personal income tax collections were $739 million higher than expected, reflecting strong wage growth—propelled by record year-end bonuses for Wall Street—coupled with job growth that was greater than originally reported.
- Higher nontax revenues, primarily from interest income, offset most of the revenue impact of the recent State budget, which reduced unrestricted aid and raised the amount that the City pays the State for the administration of the City's personal income tax.

The increased revenue collections in FY 2007 help raise the base for future collections, but the City expects a portion of this recurring amount would be lost as a result of fewer real estate transactions and a general slowing of the economy. Overall, nonproperty tax revenues are now expected to be higher by $3.8 billion in FY 2008 and by an average of more than $2.5 billion annually in fiscal years 2009 and 2010. Most of these additional resources are from the business, real estate transaction, and personal income taxes. In addition, real property tax collections are now expected to be much higher than anticipated beginning in FY 2008 because the growth in assessed values has been stronger than projected last June. The real property tax is expected to yield an additional $382 million in FY 2008, growing to $1.3 billion in FY 2010.

C. New Needs

As discussed below and shown in Figure 8, the City has addressed net new needs of nearly $1.6 billion for fiscal years 2007 and 2008 that have arisen since the beginning of the current fiscal year.

- Collective bargaining costs are expected to be higher by $314 million in FY 2007, increasing to $1.2 billion by FY 2010, based on recently negotiated or anticipated agreements.
- The enacted State budget reduces general aid to the City by $314 million in FY 2007, largely from a one-year loss of payments under the Aid and Incentives for Municipalities (AIM) program, and by $30 million in subsequent years from an increase in the fee the State charges to administer the City's personal income tax. (The City will benefit next year by a $714 million increase in State education aid.)
- The City has increased its Medicaid spending to enable the Health and Hospitals Corporation (HHC) to obtain supplemental federal Medicaid payments. These costs were partly offset through reductions in City subsidies to HHC for debt service and fringe benefits.
- The City has increased education funding by $45 million in FY 2007 and by as much as $1.1 billion by FY 2011 to address new spending needs and to meet the Mayor's commitment to increase funding to education as part of a resolution of the Campaign for Fiscal Equity litigation.
- The April Plan allocates $199 million in FY 2008 and larger amounts in subsequent years to fund the operating budget impact of the Mayor's PlaNYC 2030 initiative, which is designed to address the City's growing infrastructure needs and environmental concerns.
- The City drew down the general reserve in FY 2007 by $215 million, which still leaves $85 million, and recognized $400 million in savings from overestimating prior years' expenses.
- Debt service will be lower by $185 million in FY 2007 and $339 million in FY 2008 because investment earnings were higher than expected, there were fewer issuances, and there will be no need for short-term borrowing given the City's large cash reserves. These factors, with the exception of savings from short-term borrowing, will also benefit subsequent years.
- Pension contributions are higher by $125 million in FY 2008 and by $749 million by FY 2010 to potentially fund the recommendations of an independent actuarial consultant (with a net value of $200 million annually) and to fund reestimates with a net value of $264 million by FY 2010.

D. Agency Gap-Closing Program

Agency actions are expected to generate $257 million in FY 2007 and $472 million in FY 2008, with the recurring value to decline to slightly more than $300 million by FY 2011, for a cumulative total of $1.7 billion. Most of the resources are expected to come from reestimates ($696 million), funding shifts ($200 million), and reductions in subsidies to libraries and cultural institutions ($92 million). In addition, the Department of Education is expected to reduce overhead costs by $75 million annually beginning in FY 2008 and to reallocate those resources to the classroom.

The Police Department expects to contribute $184 million during the Plan period from the elimination of reserves for salary adjustments, delayed hiring, and higher-than-anticipated retirements. Similarly, the Department of Sanitation will realize savings of $67 million through a reestimate of salary and wage costs. The Administration for Children's Services expects to realize $33 million annually in additional federal funding for foster care through better claims for reimbursement.

The Department of Education expects to generate savings of $75 million annually by reducing the growth in costs associated with private school tuition ($25 million); consolidating regional offices and administration ($25 million); eliminating 97 general education bus routes ($10 million); reforms in minor maintenance and reductions in administrative costs ($10 million); and a reduction in the hours of food service workers to match demand ($5 million). The savings will be retained by the Department of Education and reallocated to educational programs.

E. Discretionary Actions

As shown in Figure 8, the City realized a net benefit of $5.6 billion in unanticipated resources in FY 2007 (even after addressing unforeseen new needs) compared with the forecasts at the beginning of the fiscal year. Just as it did last year, the City plans to use these resources in ways that will improve its financial position. The City plans to use more than $1.2 billion to retire bonds that are callable in FY 2007 but due in fiscal years 2009 and 2010. This will generate interest rate savings of $113 million over the next three years and provide debt relief in fiscal years 2009 and 2010, when the City has projected large budget gaps. The remaining net surplus of nearly $4.4 billion will also be used to help balance the budget in future years by prepaying debt service and subsidies to entities with a financial relationship with the City (e.g., libraries, cultural institutions, HHC, and New York City Transit).

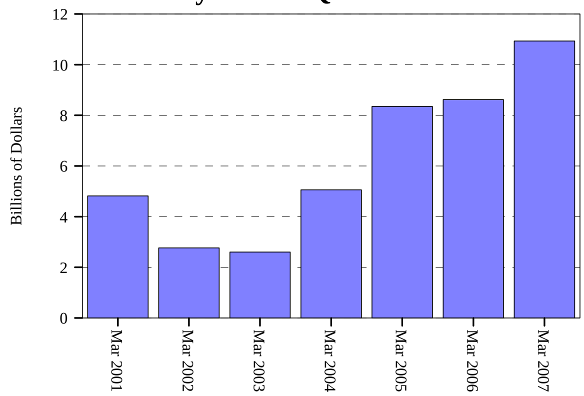
The City also recognized net new resources of $3.2 billion in FY 2008 compared with the estimates made by the City one year ago. The City intends to use these resources in FY 2008 to close the remaining budget gap, increase the amount in the Retiree Health Benefits Trust Fund, and to fund the first-year impact of the Mayor's proposed tax reduction program.

F. Cash Flow

New York City's cash reserves reached a record level of $10.9 billion at the end of March 2007—27 percent higher than the year before—reflecting the strength of the local economy (see Figure 9). As the City's cash reserves have grown, it has been able to reduce its reliance on the bond market to finance its short-term cash needs. In fact, the City met its cash needs during fiscal years 2005 through 2007 without borrowing, which generated annual savings of $75 million, and it does not plan any short-term borrowings in FY 2008. The City plans to use a portion of its current cash reserves to prepay future expenses ($4.4 billion), retire outstanding debt ($1.2 billion), and contribute to the Retiree Health Benefits Trust Fund ($500 million).

Figure 9

New York City End-of-Quarter Cash Balances



Sources: NYC Comptroller's Office; NYC Office of Management and Budget

IV. Impact of the Enacted State Budget

The enacted budget for State Fiscal Year (SFY) 2007-08 increases State education aid to the New York City public school system for next year by $714 million, but reduces aid to other parts of the City's budget by a net of $344 million over the course of this year and next. As shown in Figure 10, nearly all of the negative impact comes from the elimination of revenue sharing payments for one year. In addition, the Health and Hospitals Corporation estimates that the enacted State budget will reduce Medicaid reimbursements by $54 million in FY 2008 by freezing managed care premiums and by making lower-than-expected increases in reimbursement rates for hospitals and nursing homes.

Figure 10
Impact of the State Budget on New York City
(in millions)

	FY 2007	FY 2008	FY 2009	FY 2010
Education Aid	$ - - -	$ 714	$ 1,400	$ 2,264
Other Impacts on the City's Budget:				
AIM Payments (Revenue Sharing)	(307)	- - -	- - -	- - -
Increased Personal Income Tax Administrative Charge	(7)	(30)	(30)	(30)
Total Excluding Education Aid	**$ (314)**	**$ (30)**	**$ (30)**	**$ (30)**

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

The City will continue to benefit from certain State initiatives that were adopted in prior years and that were previously reflected in the City's four-year financial plan. In particular, the State has taken responsibility for funding the local share of costs for the Family Health Plus program and has limited the growth in the local share of Medicaid to about 3 percent annually. These two initiatives are expected to save the City an estimated $706 million in FY 2008; this benefit could rise to $1.3 billion by FY 2010.

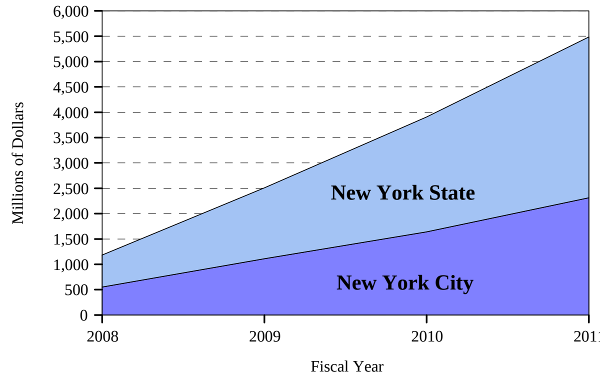
A. Education Aid

The State budget allocates $7.5 billion to the New York City public school system for FY 2008, which is $714 million more than allocated in the current year. The allocation, however, includes $94 million to fund the debt service on $750 million in bonds issued by the Dormitory Authority of the State of New York for capital projects in the City, as part of the State's contribution to the resolution of the Campaign for Fiscal Equity (CFE) litigation. Thus, the net benefit to the Department of Education's operating budget is $620 million, which is still considerably larger than the FY 2007 increase in State education aid ($454 million)—itself considered large at the time.

Moreover, the Governor has proposed increasing education aid Statewide over the next four years by a total of $7 billion ($3.2 billion of which is targeted for New York City). When combined with the Mayor's commitment to increase education aid, funding to the City's public schools would rise by $5.5 billion by FY 2011 (see Figure 11), more than twice the minimum ordered by the State Court of Appeals in resolution of the CFE lawsuit.

Figure 11

Proposed Increases in Education Funding



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

B. Revenue Initiatives

The enacted State budget for SFY 2007-2008 includes a one-year reduction of $307 million in revenue sharing payments to the City under the AIM program, and redistributes some of these funds to localities in distress. Though still uncertain, the State financial plan assumes that AIM payments to New York City will resume next year. In addition, the State will charge the City an additional $30 million to administer the personal income tax, which raises the total charge to $70 million annually.

Although it has no direct impact on the City's budget, the State's expansion of the existing School Tax Relief (STAR) Program will benefit City residents. Statewide, the program will increase by $1.3 billion in SFY 2007-08 to reach $4.7 billion.[2] By SFY 2010-11, the Statewide increase in the STAR program is expected to reach $2.5 billion. The new relief would be based on income, with the largest increases going to home owners with incomes at or below $90,000 ($120,000 in the downstate metropolitan area). The City estimates that through FY 2011, City taxpayers will receive about 17 percent of the Statewide increase in STAR benefits.

In FY 2008, for New York City home owners with incomes of less than $120,000, the revised STAR program would provide married couples an additional benefit of $187 and individuals another $157. (The total STAR benefit would be $629 for married couples and $484 for individuals.) STAR would provide married couples in rental housing an additional benefit of $60 and individual renters an additional $30, bringing the total benefit for renters to $290 for married couples and $145 for individuals.

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[2] A portion of the funding came from eliminating last year's property tax rebate, which was valued at $673 million.

V. Mayor's Tax Reduction Proposal

The Mayor has further expanded the tax reduction program he proposed in January 2007, to a value of nearly $1.4 billion in FY 2008, growing to nearly $1.9 billion by FY 2011 (see Figure 12). The program is designed to ease the growing tax burden on home owners and businesses in New York City and to improve the City's competitiveness with surrounding areas. It now includes components from the PlaNYC 2030 initiative and an increase in cigarette taxes. While the City has the authority to reduce real property tax rates, the other elements of the proposed program, valued at an average of nearly $800 million annually, require State approval and remain uncertain.

Figure 12
Proposed Tax Reduction Program
(in millions)

	FY 2008	FY 2009	FY 2010	FY 2011
Property Tax Rate Reduction	$ 750	$ 810	$ 868	$ 917
Require State Approval				
Home Owner Rebate	256	256	256	256
Small Business Relief	140	177	202	244
Sales Tax on Clothing	110	117	119	122
PlaNYC 2030	53	224	265	281
Child Care Credit	42	43	44	45
Subtotal	1,351	1,627	1,754	1,865
Cigarette Tax Increase	(20)	(20)	(19)	(19)
Total	**$ 1,331**	**$1,607**	**$ 1,735**	**$ 1,846**

Note: The home owner rebate was included in the July Plan.
Source: NYC Office of Management and Budget

The Mayor's proposed tax reduction program includes the following components.

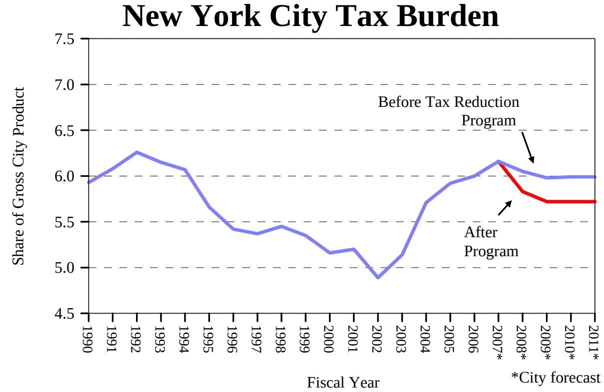
- Reduce the average property tax rate by 5 percent. The average owner of a one-, two-, or three-family home (Class 1) would benefit by $170. The average owner of commercial property (Class 4) would benefit by $3,700.
- Continue the $400 home owner property tax rebate scheduled to end in FY 2007. In recent years, residential property values have grown at a faster rate than commercial property values. Even with the combined benefit of a rate reduction and rebate, the average residential home owner in all boroughs will pay more property taxes next year than in the current year.
- Make several modifications to the general corporation and unincorporated business taxes, including raising credits and deductions, in order to reduce taxes on small businesses.

- Eliminate the City's sales tax on clothing purchases valued at more than $110; taxes have already been eliminated on purchases valued below $110.[3]
- Create a refundable credit targeted at families who have children younger than 3 years old and incomes below $30,000. The credit would be a percentage of the State credit, with a maximum value of about $1,000, and would be phased out as incomes increased.
- Offer tax incentives, including abatements for property owners who install green roofs and solar electric systems, and eliminate the City sales tax on hybrid vehicles as part of the Mayor's PlaNYC 2030 initiative. In addition, a proposed new financing authority (the Sustainable Mobility and Regional Transportation Authority) would securitize personal income tax revenues to finance regional transportation projects.
- Raise the cigarette tax (to reduce cigarette usage) by $0.50 per pack, to $2.00 per pack.

The local tax burden (i.e., City tax revenues as a percentage of the gross city product) has been rising in recent years, primarily because of a hike in property tax rates in January 2003, temporary increases in sales and personal income taxes that were effective from July 2003 through December 2005, and the recent surge in real estate transactions that have pushed up tax collections faster than growth in the overall economy (see Figure 13). While the April Plan expects that the burden will fall in coming years because taxes are expected to decline much faster than the economy, the Mayor's tax reduction proposals would further reduce the tax burden back to the FY 2004 level.

Figure 13

New York City Tax Burden



Note: Tax burden is calculated as the ratio of all taxes to gross city product.
Sources: NYC CAFR, NYC Office of Management and Budget; OSDC analysis

[3] The State sales tax of 4 percent remains in effect, plus another 0.375 percent for the Metropolitan Transportation Authority.

VI. Revenue and Expenditure Trends

The City has realized $9.7 billion in unanticipated City fund revenues for fiscal years 2007 and 2008 compared with the estimates at the beginning of the current fiscal year, based mostly on the unexpected strength in the local economy. Although the City identified some $1.6 billion in new funding needs over the two-year period, the City still reaped a large net benefit of $8.9 billion, including resources from agency actions.

Largely as a consequence of these unanticipated resources, the City closed a $3.8 billion budget gap that had been projected for FY 2008 and reduced the FY 2009 budget gap from $4.6 billion to $1.6 billion, a reduction of 66 percent. While the FY 2010 budget gap has been reduced by 20 percent to $3.3 billion, the FY 2011 gap remains substantial at $4.3 billion.

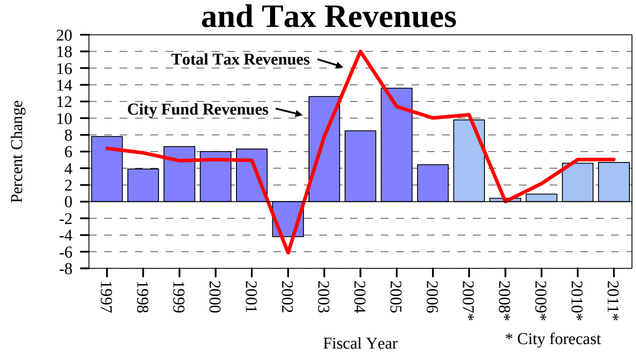
The City's gap estimates reflect the April Plan's assumption that nonproperty tax revenues will decline by 4.9 percent next year and then grow slowly in FY 2009 before resuming a moderate rate of growth in subsequent years. The City's spending estimates assume that wages will increase at 1.25 percent each year beginning in FY 2009 after the expiration of actual or anticipated contracts.

A. Revenue Estimates

The April Plan assumes that nonproperty tax revenues[4] will decline by 4.9 percent in FY 2008 after growing at an average annual rate of 16.3 percent[5] during fiscal years 2004 through 2007. In recent years, tax collections were fueled by surging Wall Street profits and bonuses, a boom in real estate transactions, and higher capital gains realizations. In FY 2008, the City's forecast assumes minimal growth in personal income and sales taxes and sizable declines in business and real estate transaction taxes. Real property tax collections would increase by 7.6 percent even assuming a continuation of the homeowner rebate program as proposed by the Mayor.

Figure 14

Annual Change in City Fund Revenues and Tax Revenues



Notes: Excludes the proposed tax reduction program. Adjusted for debt service on TFA and tobacco bonds and the transfer of TSASC revenues to benefit FY 2008.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

4 Excluding the impact of the Mayor's proposed tax reduction program.
5 Excluding tax increases and other rate and base changes implemented during this period.

The April Plan assumes minimal growth in tax revenues (less than 0.1 percent) and total City fund revenues[6] (0.4 percent) in FY 2008 (see Figure 14). Growth is expected to pick up in FY 2009, but the rate of increase (2.2 percent) would still be much lower than it has been in recent years. In fiscal years 2010 and 2011, tax revenues are projected to grow at an average annual rate of 5 percent as economic activity quickens.

While the local economy is likely to slow during FY 2008, we believe tax revenues will not contract as sharply as anticipated by the City. Even if collections decline by 4 percent rather than 4.9 percent as assumed in the April Plan, the City would realize $500 million in additional revenues.

Figure 15
City Fund Revenues
(Excluding Impact of Proposed Tax Reduction Program)
(in millions)

	FY 2007	FY 2008	Annual Growth	FY 2009	FY 2010	FY 2011	Average Three-Year Growth Rate
Taxes							
Property Tax	$ 12,976	$ 14,220	9.6%	$ 15,363	$ 16,485	$ 17,431	7.0 %
Personal Income Tax	7,589	7,691	1.3%	7,800	8,150	8,582	3.7 %
Sales Tax	4,537	4,664	2.8%	4,783	5,015	5,267	4.1 %
Business Taxes	6,982	6,039	-13.5%	5,819	5,981	6,280	1.3 %
Real Estate Transaction Taxes	3,185	2,636	-17.2%	2,287	2,316	2,372	-3.5 %
Other Taxes	2,891	2,918	0.9%	2,943	3,016	3,096	2.0 %
Subtotal	**38,160**	**38,168**	**0.0%**	**38,995**	**40,963**	**43,028**	**4.1 %**
Miscellaneous Revenues	4,338	4,205	-3.1%	3,781	3,800	3,835	-3.0 %
Unrestricted Intergovernmental Aid	33	340	NA	340	340	340	0.0 %
Grant Disallowances	(15)	(15)	0.0%	(15)	(15)	(15)	0.0 %
Total	**$ 42,516**	**$ 42,698**	**0.4%**	**$ 43,102**	**$ 45,089**	**$ 47,187**	**3.4%**

Note: Personal income tax includes the portion of such revenues used to pay debt service on bonds issued by the TFA. Audits have been allocated to individual taxes. Miscellaneous revenues have been adjusted for the transfer of TSASC revenues. Totals may not add due to rounding.
Sources: NYC Office of Management and Budget; OSDC analysis

The April Plan includes the following assumptions of major revenue trends.

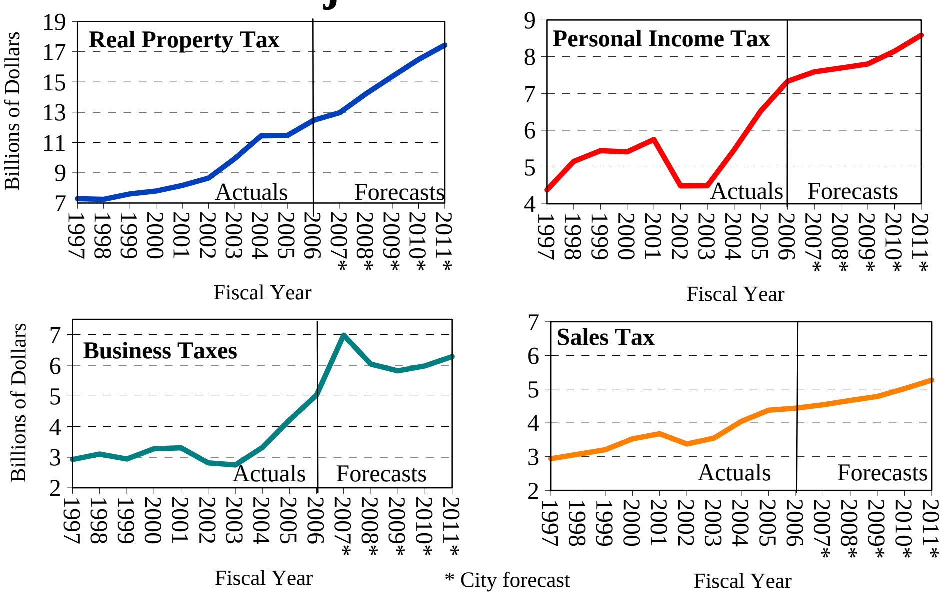
- Real property taxes will increase by 9.6 percent or $1.2 billion in FY 2008 before accounting for the proposed tax cuts (see Figure 15). A portion of this increase ($256 million) reflects the end of the City's home owner rebate program, though the Mayor has proposed its extension. The balance

[6] Our estimates of City fund revenues include the portion of personal income tax revenues dedicated to pay debt service on bonds issued by the Transitional Finance Authority (TFA), and tobacco settlement revenues dedicated to pay debt service on TSASC bonds. The estimate has also been adjusted for the transfer of TSASC revenues to benefit FY 2008.

of the increase reflects a growth in assessed values of 7.5 percent. Although there is evidence that the residential real estate market may be softening in some areas of the City, the phase-in provisions of the property tax law will lessen the impact to the City. (The provisions are designed to protect property owners from extraordinarily large increases in assessments during periods of strong assessed value growth, as well as to lessen the impact to the City during periods when property value growth is weaker.) As a result, real property tax revenues are expected to remain strong throughout the financial plan period, increasing by 8 percent in FY 2009, 7.3 percent in FY 2010, and 5.7 percent in FY 2011.

Figure 16

Major Tax Revenues



* City forecast

Note: Excludes impact of proposed tax reduction program.

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

- Personal income tax collections will grow by only 1.3 percent in FY 2008, due to lower wage growth—caused by a projected slowdown in employment growth and a reduction in Wall Street bonuses—as well as a decline in capital gains realizations. As the economy recovers, collections will also begin to improve (see Figure 16), rising from 1.4 percent in FY 2009 to 4.5 percent in FY 2010 and 5.3 percent in FY 2011.
- Collections from the business taxes (general corporation, banking corporation, and unincorporated business taxes) in FY 2008 will be almost $1 billion less than in FY 2007 (see Figure 16). Part of that decline results from a loss of $450 million in one-time business tax audit collections that

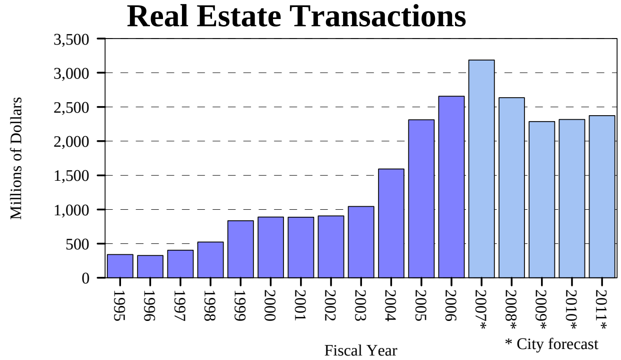
benefited FY 2007. The projected decline in Wall Street profits, coupled with a general decline in business profitability due to slowing in the national economy, are expected to reduce business taxes (after adjustment for the additional audit revenues in FY 2007) by 8.9 percent in FY 2008. The decline is expected to continue in FY 2009, with collections falling by 3.6 percent, before growth resumes with increases of 2.8 percent in FY 2010 and 5 percent in FY 2011.

- Sales tax collections, which were expected to increase by 2.2 percent in FY 2007, will remain subdued (see Figure 16), with gains of 2.8 percent in FY 2008 and 2.6 percent in FY 2009. While strong wage growth and tourism should have boosted collections, the City believes that the weakening real estate market is reducing consumer expenditures. Growth is expected to remain low as the economy slows into 2008.

- Collections from taxes on real property transaction taxes (the mortgage recording and real property transfer taxes) are currently being supported by record sales prices for large commercial properties. Additionally, data from the Mortgage Bankers Association show that rising interest rates have resulted in an unexpected level of refinancing as home owners have switched from adjustable rate mortgages to fixed rate mortgages.

Figure 17

Tax Collections From Real Estate Transactions



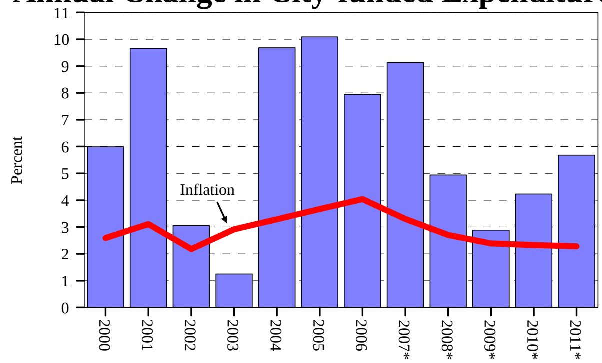
Note: Collections include the mortgage recording and real property transfer taxes.
Sources: NYC Office of Managment and Budget; OSDC analysis

The April Plan assumes that the number of large commercial transactions will diminish and that the City's residential market will show modest declines in sales and prices. Consequently, the financial plan assumes that collections from real estate transaction taxes will peak in FY 2007 (see Figure 17) and then decline by 17.2 percent in FY 2008 and another 13.2 percent in FY 2009. Nonetheless, the City's commercial real estate market is expected to remain strong through the financial plan period, with rents rising and vacancy rates falling. The City expects the residential real estate market to improve beginning in FY 2010, helping to lift collections by 1.3 percent that year and by 2.4 percent in FY 2011.

B. Expenditure Estimates

Figure 18

Annual Change in City-funded Expenditure



*City forecast

Note: Adjusted for surplus transfers, TFA, and TSASC.

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

City-funded expenditures have grown at an average annual rate of nearly 10 percent during fiscal years 2004 and 2005, and an average annual rate of 8.5 percent during fiscal years 2006 and 2007 (see Figure 18).[7] Most of the growth is due to rapidly rising costs for debt service, Medicaid, pensions, and other fringe benefits. The City, however, also made discretionary contributions of $1 billion in each of fiscal years 2006 and 2007 to the Retirees Health Benefits Trust Fund (RHBTF) and has set aside $1.2 billion in FY 2007 to retire outstanding debt. The growth in City-funded expenditures will slow to 4.9 percent in FY 2008 because the City does not plan to repeat the debt retirement initiative and because it plans to make a smaller contribution to the RHBTF.

Figure 19

Estimated City-Funded Expenditures

(Adjusted for Surplus Transfers, TFA, and TSASC)

(in millions)

	FY 2007	FY 2008	Annual Growth	FY 2009	FY 2010	FY 2011	Average Three-Year Growth Rate
Salaries and Wages	$11,178	$12,000	**7.4%**	$12,555	$13,327	$14,158	5.7%
Debt Service	5,445	4,443	**-18.4%**	4,675	5,062	6,149	11.4%
Medicaid	5,040	5,579	**10.7%**	5,467	5,621	5,781	1.2%
Pension Contributions	4,692	5,557	**18.4%**	6,218	6,289	6,289	4.2%
Fringe Benefits	5,275	5,677	**7.6%**	5,969	6,248	6,568	5.0%
Judgments and Claims	591	635	**7.4%**	688	738	795	7.8 %
Public Assistance	450	447	**0.8%**	447	447	447	0.0 %
Pay-As-You-Go Capital	200	200	**0.0%**	200	200	200	0.0 %
Retiree Health Benefits Trust	1,000	500	**-50.0%**	---	---	---	NA
Energy	711	794	**11.7%**	812	811	815	0.9%
General Reserve	85	300	**NA**	300	300	300	NA
Other	7,067	7,666	**8.5%**	7,727	7,921	8,129	2.0%
Total	**$41,735**	**$43,797**	**4.9%**	**$45,058**	**$46,965**	**$49,630**	**4.3 %**

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

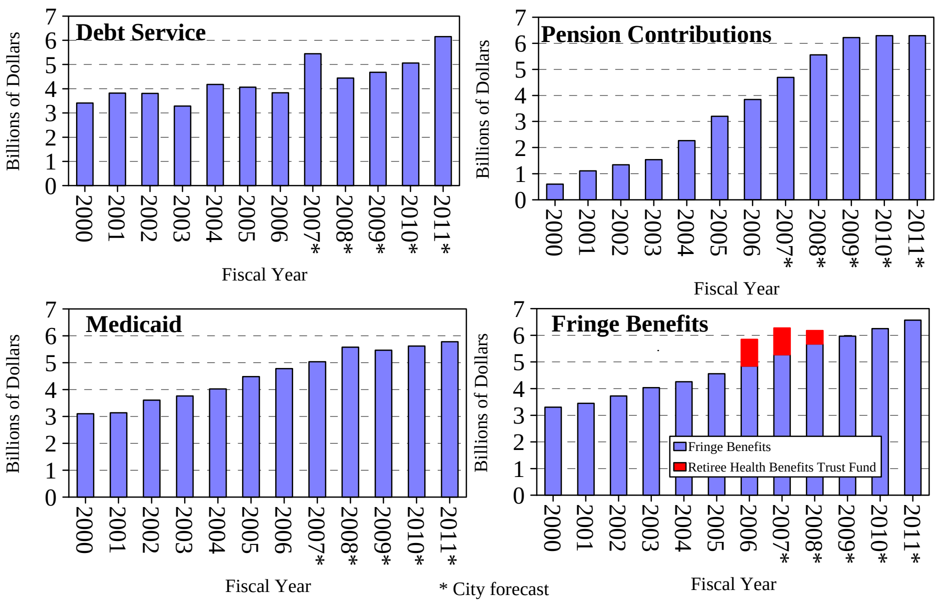
[7] Adjusted for surplus transfers and for debt service on bonds issued by the Transitional Finance Authority (TFA) and by TSASC.

In fiscal years 2009 through 2011, spending will rise by 4.3 percent annually and will continue to be driven by debt service, pensions, and other employee fringe benefits (see Figure 19). The April Plan assumes that spending on pensions, debt service, Medicaid, and employee health insurance will consume an increasing share of City fund revenues, rising from 37 percent in FY 2003 to 49 percent in FY 2011.

The major factors behind the growth in City-funded expenditures are shown in Figure 20 and discussed below.

Figure 20

Trends in Selected Expenditure Categories



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

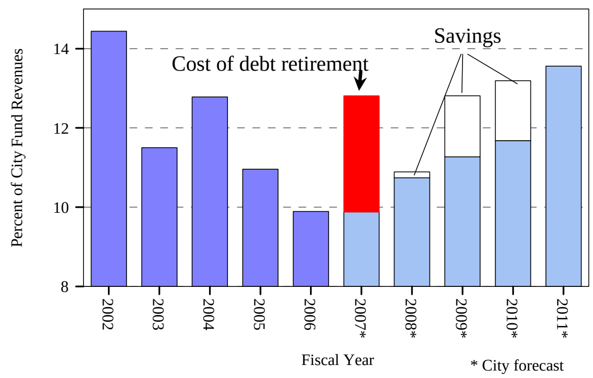
- Salaries and wages will increase by 7.4 percent in FY 2008 to $12 billion, and then grow at about 6 percent annually, reflecting the cost of actual and anticipated labor agreements for the 2000-2008 rounds of collective bargaining. (The Patrolman's Benevolent Association is seeking larger wage increases through arbitration than the City has been prepared to grant through negotiation.) While the April Plan funds annual wage increases of 1.25 percent after the expiration of these agreements, increases at the projected inflation rate would cost an additional $175 million in FY 2009, $450 million in FY 2010, and $795 million in FY 2011.

  The April Plan also allocates $613 million for overtime in the uniformed agencies, which is $92 million less than forecast for FY 2007. Our analysis indicates that the decline is unlikely to occur because the threat from terrorism has not abated and the Police Department has had difficulty meeting its hiring targets.

- Debt service is projected to rise by 42 percent to $5.4 billion in FY 2007, primarily because the City plans to retire $1.2 billion in outstanding debt. The City would realize savings of $64 million in FY 2008, $639 million in FY 2009, and $656 million in FY 2010. Because the benefit is short-term, debt service will reach $6.1 billion by FY 2011, which is 60 percent higher than the level in FY 2006. The debt service burden (i.e., debt service as a percent of City fund revenues), will grow from 9.9 percent in FY 2006 to 13.5 percent by FY 2011 (see Figure 21).

Figure 21

New York City's Debt Burden



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

- Pension contributions will grow from $3.8 billion in FY 2006 to $6.2 billion in FY 2009, and will then level off. Growth is driven by pension fund investment shortfalls during fiscal years 2001 through 2003 and benefit enhancements. In January 2007, the Mayor allocated $200 million for fiscal years 2009 through 2011 to implement the recommendations contained in a City Charter–mandated biennial audit. The pension funds have earned about 15 percent on their investments through April 30, 2007—nearly twice the actuarial assumption—which could result in lower contributions beginning in FY 2009.

- Medicaid will increase by 10.7 percent in FY 2008, to $5.6 billion, and then rise at an average annual rate of 1.2 percent in subsequent years. The State has taken steps in recent years to hold down the growth in the local share of Medicaid. The growth in FY 2008 is significantly higher because the City is providing the Health and Hospitals Corporation with additional resources that year so that the Corporation can obtain supplemental Medicaid payments from the federal government to help balance its budget.

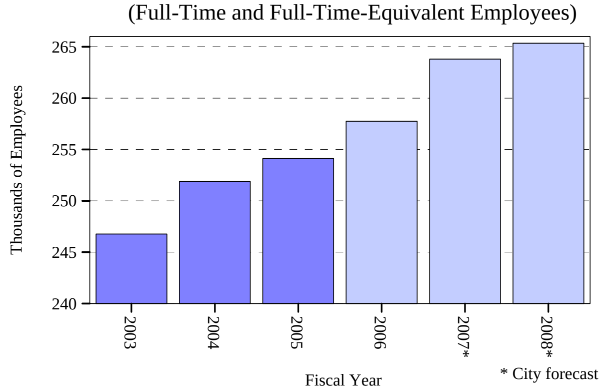
- Fringe benefit costs have been growing at a relatively rapid rate for the past ten years, driven by the rising cost of health insurance premiums. The April Plan assumes that these costs will rise by 7.7 percent in FY 2008 and then grow at an average annual rate of 5 percent in subsequent years. In addition, last year the City deposited $1 billion in unanticipated resources in a trust fund to help pay down the cost of post-employment benefits other than pensions. The City intends to deposit another $1 billion in FY 2007 and $500 million more in FY 2008.

- Energy costs have grown faster than inflation over the past few years, reflecting the impact of Hurricane Katrina, increased international demand for oil, and inadequate refinery capacity in the United States. The April Plan assumes that energy costs will rise by 11.7 percent in FY 2008 to $794 million, reflecting increases in both cost and utilization.
- The cost of judgments and claims (including those of the Health and Hospitals Corporation) will increase by 7.4 percent in FY 2008 to $635 million and then rise at a similar rate in subsequent years. The April Plan assumes that no liability will arise from the cleanup of the World Trade Center site. A federal judge has rejected the City's attempt to cap its liability from the Staten Island Ferry crash at $14.4 million, although the City may appeal the decision. To date, the City has paid $10 million in claims arising from the ferry crash, and it plans to fund future settlements on a pay-as-you-go basis.
- Public assistance expenditures are projected to remain stable during the financial plan period, at about $450 million annually. In April 2007, 363,392 people received public assistance in New York City—a decrease of 69 percent compared to the number that received assistance before the implementation of welfare reform in March 1995.
- The City-funded workforce grew by nearly 11,000 employees between the end of fiscal year 2003 and 2006 (see Figure 22), due largely to the addition of nonpedagogical employees, social services workers, and civilian employees in the uniformed agencies. The April Plan assumes that the City will add another 6,046 employees in FY 2007, including 2,083 employees in health and social services agencies (for which the City has fallen short of its hiring targets in the past). In addition, the April Plan assumes that the City will add another 1,553 employees during FY 2008, mostly in the social services and the uniformed agencies.

Figure 22

City-Funded Workforce

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



Sources: New York City Office of Management and Budget; OSDC analysis

VII. Ten-Year Capital Strategy

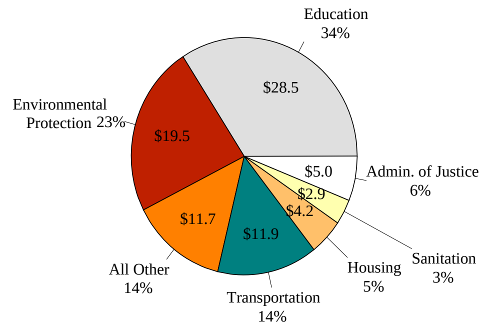
In April 2007, the City released (pursuant to Section 248 of the City Charter) its biennial ten-year capital strategy covering fiscal years 2008 through 2017. This is the largest ten-year strategy ever developed by the City, and calls for investing \$83.7 billion—an increase of \$21.3 billion or nearly 34 percent more than allocated two years ago.

Figure 23

Ten-Year Capital Strategy

2008-2017 Capital Strategy = \$83.7 billion

(in billions)



Sources: NYC Office of Management and Budget; OSDC analysis

As shown in Figure 23, most of these resources would be invested in education (34 percent), environmental protection (23 percent), and transportation (14 percent). In total, the City would invest \$64 billion, or 45 percent more than allocated two years ago, to upgrade and restore capital assets to a state of good repair through rehabilitation and replacement.

Of the \$21 billion in increased capital investments in the current ten-year strategy, half (\$10.5 billion) is targeted for education. In total, the capital strategy would invest \$28.5 billion over the next ten years in educational facilities (an increase of 59 percent over the forecast made two years ago) based on the assumption that the State will continue to match the amount invested by the City. Funding for the Department of Environmental Protection grew by \$3.6 billion—an increase of 23 percent—and is primarily dedicated to upgrading existing water pollution control facilities to ensure continuous and reliable operation and provide increased treatment levels.[8] The capital strategy also includes initial funding of \$1.6 billion for the Mayor's PlaNYC 2030 initiative.

The funding for the capital strategy is expected to come from a combination of City resources (\$65.2 billion, or 78 percent), State resources (\$15.4 billion, or 18 percent), federal resources (\$2.5 billion, or 3 percent), and other sources (\$0.6 billion, or 1 percent). The City's funding will come primarily through the issuance of debt, with the exception of \$800 million in pay-as-you-go funding that will be provided in four annual portions of \$200 million from FY 2008 through FY 2011.

General obligation (GO) bonds, which are funded with property tax revenues and backed by the City's full faith and credit, traditionally have been the primary vehicle used by the City to finance the capital program. The State Constitution limits the

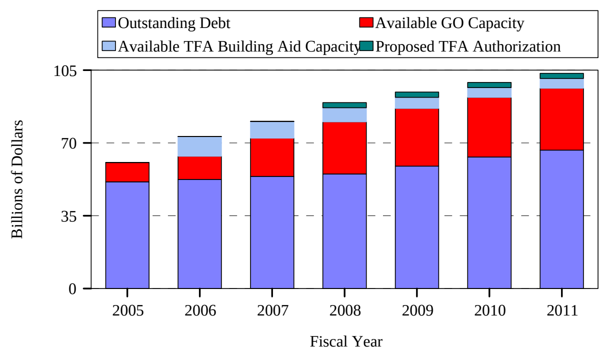
[8] The Croton Filter Project, required by a federal court decree, may need additional City funds because the lowest bidder has withdrawn from the project.

amount of GO debt the City can issue to 10 percent of the five-year moving average of taxable real property values. In March 1997, as the City was approaching its GO debt limit, the State created the New York City Transitional Finance Authority (TFA) to issue bonds backed by the City's personal income tax (PIT). The TFA was initially authorized to issue up to $7.5 billion in debt for general capital purposes, but the authorization was raised in June 2000 to $11.5 billion and in July 2006 to $13.5 billion.[9] In April 2006, the State also authorized the TFA to issue up to $9.4 billion in debt backed with State school building aid to help finance the capital program of the New York City Department of Education. Currently, the City is seeking to increase the TFA's general capital authorization by $2.5 billion, for a total of $16 billion. While TFA-PIT bonds have proven to be a cost-effective financing vehicle, we would prefer that the State and City develop a comprehensive solution to the City's borrowing needs.

Assuming that the proposal to increase the TFA-PIT debt capacity is enacted, the amount of debt that can be issued for the City's benefit—either by the City directly or by related entities—will rise from $61 billion in FY 2005 to $103 billion by FY 2011 (see Figure 24), an increase of 69 percent. About three fourths of the increase reflects the actual and projected growth in taxable real property values.

Figure 24

Borrowing Authorization



Note: Estimates assume that a $2.5 billion increase in the TFA bond cap is enacted into law. Estimat
exclude water and sewer debt, which is expressly exempt from the State constitutional debt limit.

Sources: NYC Office of Management and Budget; OSDC analysis

9 In September 2001, the State authorized the TFA to issue Recovery Bonds in an amount outstanding of up to $2.5 billion to compensate the City for nonreimbursed costs and revenue losses associated with the attack on the World Trade Center. The City issued $2 billion in Recovery Bonds during fiscal years 2002 and 2003, and though it could issue another $545 million under the cap, it has no intention of doing so.

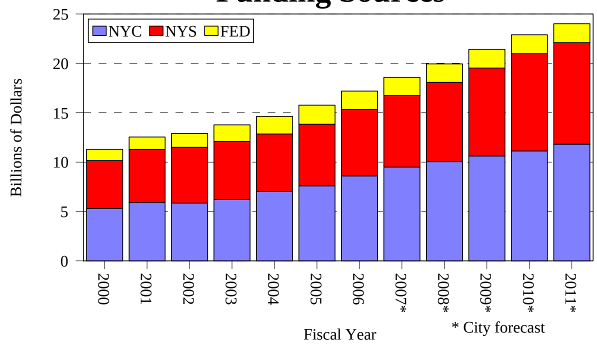
VIII. Semi-Autonomous Agencies

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

A. Department of Education

The April Plan allocates a total of $18.6 billion to the Department of Education in FY 2007, including $2.8 billion for pensions and debt service.[10] Of this amount, New York City is projected to contribute nearly $9.5 billion, or 50.9 percent; New York State is projected to contribute $7.2 billion, or 38.8 percent; and the federal government is expected to provide $1.8 billion, or 9.9 percent (see Figure 25). The remainder will come from fees, grants, settlements, and restricted sources.

Figure 25
Department of Education Funding Sources



Note: Data are adjusted for surplus transfers.
Sources: NYC Office of Management and Budget; OSDC analysis

The Mayor and the Governor have both made a commitment to increase funding to the City's public school system. If the recommendations are included in future budgets, funding to the City's public schools would rise by $5.5 billion by FY 2011, more than twice the minimum ordered by the State Court of Appeals in resolution of the CFE lawsuit. The April Plan assumes that by FY 2011 the City's contribution will rise to $11.8 billion (49.1 percent) and the State's contribution will rise to $10.3 billion (42.8 percent). The enacted State budget increases education aid to New York City public schools by $714 million in FY 2008.[11]

Besides additional funding, the State and the City are focused on improving performance and increasing accountability. The State will now require the City to submit plans, and then report annually, on how it will use the additional State education aid to improve student academic performance and to achieve other measurable educational goals. The City must now also submit a plan to reduce class sizes within five years. In addition, the State Board of Regents will develop statewide

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[10] State law prohibits the City from reducing its funding for education (excluding pensions and debt service) from one year to the next, unless there is a reduction in City revenues. The FY 2008 budget includes City funding of nearly $7.1 billion for operations, which exceeds the State's minimum requirement by $334 million and establishes a higher base level for FY 2009.

[11] This increase includes an EXCEL debt service payment of $94 million made by the State on the City's behalf, which does not benefit the Department of Education's operating budget.

performance targets for measures such as graduation rates and test scores. By 2010, the Board of Regents must establish an accountability system that tracks and monitors individual student progress.

The Mayor's Children First initiative, announced in January 2007, is also designed to improve educational outcomes. Major components of the Mayor's reforms include giving principals more control over school budgets and curriculum; allocating funding to schools based on the needs of individual students; and providing parents with report cards that grade schools on such factors as school safety and student academic progress.

B. New York City Health and Hospitals Corporation

The short-term financial outlook of the Health and Hospitals Corporation (HHC) has greatly improved because of actions taken by the City during fiscal years 2006 and 2007. In FY 2006, the City allocated resources in order to enable HHC to realize a one-time benefit of $1 billion from a supplemental federal Medicaid payment. In January and May 2007, the City provided additional funding so HHC can continue to obtain such payments in FY 2007 and in subsequent years.[12] Although HHC still projects sizable out-year budget gaps, it now expects to end FY 2007 with a surplus of $966 million (excluding resources from management actions). HHC's cash reserves (totaling $1.2 billion in FY 2007) are expected to be sufficient to cover expenses through FY 2009.

While HHC's financial situation has improved, it has become increasingly reliant on supplemental federal Medicaid payments to balance its budget. In January 2007, the federal government proposed a regulation that would limit a portion of the supplemental Medicaid payments beginning in September 2007. In May 2007, Congress enacted legislation delaying implementation of this rule change for one year. Unless the moratorium is extended, HHC could lose $432 million annually in anticipated supplemental payments.

C. New York City Housing Authority

The New York City Housing Authority (NYCHA), which operates on a calendar-year basis, projects a budget gap of $225 million in the current year. Although the NYCHA has not yet made public its plan to balance the budget or its four-year financial plan, it expects to do so shortly. In prior years, the authority used a combination of cash

[12] The financial plan of the Health and Hospitals Corporation includes the receipt of a $1.6 billion supplemental payment in FY 2007. Between fiscal years 2008 and 2011, additional supplemental payments are projected to average more than $800 million annually; receipt is subject to federal approval.

reserves, capital funds, additional City funding, and management actions to balance its budget.

The NYCHA also began last year with a substantial budget gap; it was not until halfway through the year that the NYCHA proposed a gap-closing program. The program counted on additional City subsidies, raising rents for higher-income tenants, and federal actions. The City provided the NYCHA with $100 million in short-term assistance, and although the NYCHA raised rents, the implementation took longer than expected. The federal government, however, did not take the actions anticipated by the NYCHA, which created a shortfall of $101 million in FY 2007 and about $75 million annually thereafter.

The NYCHA is experiencing financial difficulty because rent collections and public subsidies have not been growing fast enough to cover operating expenses, which have been fueled in recent years by rapidly rising pension contributions and health insurance premiums, and the cost of new labor agreements. In addition, the NYCHA receives no subsidies from the State and the City to manage 21 housing developments that were developed by the State and the City. The NYCHA estimates that these units account for $100 million of the current budget gap.

D. New York City Off-Track Betting Corporation

The New York City Off-Track Betting Corporation (OTB) is a public benefit corporation that provides legalized pari-mutuel wagering that was created to generate revenue for the City, the State, and the horse racing and breeding industries. The OTB is required by State law to provide New York City with revenues from a 5 percent surcharge on winning wagers, as well as residual revenues after the payment of all operating expenses and all statutorily mandated distributions to the racing industry, the State, and other localities.

The OTB projects a 4 percent decline in handle in FY 2007 due to increased competition now that Yonkers Raceway, which features video lottery terminals, has reopened. The OTB has managed its cash flow by delaying $9 million payments to Yonkers Raceway and $9 million in distributions to the racing industry. Although the OTB was current in its statutorily mandated payments to the City and State as of April 2007, it has delayed such payments in the past. According to the OTB, it had $21 million in cash on hand at the end of April, which would be insufficient to cover its obligations in the current year if all payments were current. In the OTB's financial statements for fiscal years 2005 and 2006, independent auditors questioned the ability of the OTB to continue as a "going concern."

In response to a draft of this report, the OTB's management stated that "…if additional revenue streams do not become available to enable reinvestments in OTB facilities and deployment of state-of-the-art technology, not only will OTB's ability to continue to operate become questionable, but as well the financial well-being of the entire State racing industry will be adversely impacted…."

In the past, the City has proposed State legislation that would assist the OTB, which the State has rejected. A consultant recently hired by the City recommended that the State restructure the current system of mandatory distributions and also embrace new technologies to facilitate wagering. The OTB could be consolidated or merged with other entities under four proposals submitted by bidders who are competing for the franchise to operate the State's thoroughbred racetracks. The winning bid could be selected as early as June 2007.

E. Hudson Yards Infrastructure Corporation

As part of the City's efforts to redevelop the far West Side of Manhattan, the Metropolitan Transportation Authority (MTA) will construct the extension of the No. 7 subway line, which will be funded through the issuance of $2 billion in bonds by the Hudson Yards Infrastructure Corporation (HYIC). The cost of large construction projects in New York City, however, has been growing faster than expected, and there is currently no agreement on whether the MTA, the HYIC, or the City would fund any cost overruns on the extension.

The HYIC is authorized to issue up to $3.5 billion in bonds to finance the subway extension and other improvements on the far West Side, including new parkland. The HYIC issued bonds in December 2006 and will incur debt service beginning in FY 2008; however, development within the Hudson Yards Special District, which will be assessed with payments in lieu of taxes (PILOTs) to pay the debt service on the HYIC bonds, is not expected to generate sufficient revenues to cover the debt service until some later date.

The City Council has agreed to support, subject to annual appropriation, the interest on up to $3 billion of HYIC bonds to the extent that project revenues are insufficient to cover these costs. (Interest costs are projected to total $322 million through FY 2011.) Repayment of the principal would begin after the project generates sufficient revenues to cover interest costs.

In May 2007, the City released development guidelines for the West Side rail yards—two below-grade rail yards that are owned by the MTA that will be covered with a platform to facilitate development. The guidelines call for an 8-acre park to bisect the properties on an east-west axis, as well as a mix of commercial, retail, and residential towers. Of the 4,500 residential units anticipated for the site, 20 percent must be affordable. The MTA expects to put the rail yards up for bid this spring, and proceeds from the sale would be used to help finance the MTA's capital program.

Also within the Hudson Yards Special District, plans are underway to expand the Jacob K. Javits Convention Center. The Governor's administration has indicated that it is reconsidering the expansion plan approved last year by then-Governor Pataki, which has been criticized as costly and inadequate in size. The current plan would add 300,000 square feet of exhibition space to the current 760,000 square feet, and costs have risen from $1.4 billion in 2005 to between $1.8 billion and $2 billion in 2007. The Empire State Development Corporation and the Convention Center Development Corporation are expected to release a revised expansion plan by the end of the fiscal year.

F. Lower Manhattan Development Corporation

This spring, the Lower Manhattan Development Corporation (LMDC) released a revised General Project Plan for the World Trade Center (WTC) site that reflected the responsibilities of the various stakeholders involved in the rebuilding efforts as amended by an agreement signed in November 2006 between the Port Authority of New York and New Jersey, then-Governor Pataki, Mayor Bloomberg, and Silverstein Properties, the leaseholder of the WTC site.

Under the agreement, the LMDC, in cooperation with the WTC Memorial Foundation, will construct the memorial and memorial museum; Silverstein Properties will build three of the five commercial towers at the site; and the Port Authority will construct the Freedom Tower, Tower 5, a new PATH station, and all subsurface infrastructure at the site. The Port Authority and Silverstein Properties are in litigation with several insurance companies that had policies on the WTC but are contesting the new deal, which would transfer some of Silverstein's insurance proceeds to the Port Authority.

In February 2007, the Port Authority officially authorized the construction of the Freedom Tower, which has increased in cost from $2.5 billion to $2.9 billion, and approved approximately $500 million in construction contracts for foundation work for the building. New York State and the federal government have pledged to lease a total of 1 million square feet of office space in the Freedom Tower. Rising construction costs have also increased the price of the new WTC PATH station, from $2.2 billion to $3.4 billion. The Port Authority is working with the station's architect to identify ways to cut costs without altering the station's distinctive design.

G. PlaNYC 2030

On April 22, 2007, Mayor Bloomberg announced a series of initiatives to combat global climate change and improve the City's environment and infrastructure. The April Plan includes a total of $1.3 billion in funding over four years (see Figure 26) for these initiatives, which are part of the Mayor's "PlaNYC 2030," a comprehensive program to prepare New York for a projected increase in population of approximately 1 million people by 2030. The plan aims to create 300,000 to 500,000 new units of housing and preserve existing affordable housing; reduce commuting times to and from City jobs; create new parkland by opening schoolyards for active recreation and completing undeveloped park sites; plant 250,000 new street trees; improve critical infrastructure, including water, transportation, and energy networks; reduce the production of greenhouse gases; improve the City's air quality; clean up and redevelop polluted brownfield sites; and open the waterfront to recreational uses.

Figure 26
PlaNYC 2030 Operating Budget Impact
(in millions)

	FY 2008	FY 2009	FY 2010	FY 2011
Transportation	$68.6	$239.6	$281.2	$297.5
Energy	82.7	77.3	69.8	62.5
Brownfields	27.5	2.0	2.0	2.0
Parks	11.6	12.8	13.7	30.1
Air Quality	3.6	3.9	4.3	4.8
New Staffing	3.5	4.0	4.9	6.2
Long-Term Planning	1.0	1.0	1.0	1.0
Municipal Land Use Database	0.2	0.2	0.2	0.2
Total	**$198.8**	**$340.9**	**$377.1**	**$404.2**

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

To help fund these initiatives and reduce traffic congestion in Manhattan, the Mayor proposed implementing congestion pricing in Manhattan. Under his proposal, all commercial vehicles operating in Manhattan below 86th Street would be charged $21 per day and all private vehicles driving in the congestion zone would be charged $8 per day. Discounts would be provided for residents living within the zone, and exemptions would be applied to emergency vehicles, taxis and livery cabs, and vehicles with handicapped license plates.

Proceeds from congestion pricing would be used in conjunction with State funding to fund a new public authority, the Sustainable Mobility and Regional Transportation Financing Authority (SMART). SMART would invest in critical infrastructure projects undertaken by other transportation agencies to expand the region's transportation network and bring the system into a state of good repair. In addition to providing funding, SMART would monitor projects to ensure accountability.

The City estimates that meeting the long-term transportation needs identified in the plan could cost as much as $31 billion. Anticipated projects include partial funding of the No. 7 subway line extension and the East Side Access project that will bring Long Island Rail Road service to Grand Central Terminal; an express bus lane to the Lincoln Tunnel; and portions of the Second Avenue Subway project.

While the City needs the State Legislature's approval to create SMART and to implement congestion pricing and other components of PlaNYC 2030, the April Plan includes $50 million in funding for SMART, and expects that funding will reach $220 million in 2009, $260 million in 2010, and $275 million in 2011.

The City's ten-year capital strategy for fiscal years 2008-2017 allocates $1.6 billion to PlaNYC 2030 initiatives (see Figure 27). Most of the additional capital resources would be used to create and improve park space, improve air quality, improve the flow of traffic, and minimize congestion. Individual projects include new parks, planting more than 15,000 street trees on a yearly basis, replacing fuel-burning heating systems in City public schools with more efficient heating and cooling systems, developing a Citywide bike network, and modernizing bridges and roads.

Figure 27
PlaNYC 2030 Capital Expenditures
FY 2008 – FY 2017
(in millions)

	FY 2008 – FY 2017
Parks	$957.1
Air Quality	411.2
Transportation	249.9
Energy	3.0
Housing	2.0
Total	**$1,623.1**

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