May 2018

Tough Times Ahead?

The City's Fiscal Condition Is Stable, At Least for Now

Over the past 17 months, since the inauguration of the Trump Administration, IBO and others have repeatedly warned of the risks posed to the city's financial well-being by actual and proposed federal budget actions. While fiscal uncertainty from potential federal actions continues to loom there has so far been little direct effect on the city's financial plan resulting from federal budget actions. Instead, the need to replace hundreds of millions of dollars in intergovernmental aid has emanated from Albany, not Washington.

The Executive Budget for 2018 and Financial Plan Through 2022 is reactive, with increased spending and increased revenues the product of forces largely outside the city's control. The de Blasio Administration has not used the Executive Budget to launch new large-scale programs or big-ticket initiatives. Compared with his Preliminary Budget, the Mayor's latest plan includes approximately $1 billion in additional city revenue in the current year, much of which results from one-time responses by business owners and investors to changes in federal tax law, and also identifies an additional $750 million of savings and increased agency revenues in 2018 and 2019 through the Citywide Savings Program. But much of this is used to fill the funding shortfalls and new unfunded mandates from the state.

Under the Executive Budget and financial plan proposed by the Mayor, IBO projects that the city will end the current fiscal year with $774 million more in tax revenue than the de Blasio Administration estimates. This additional revenue, coupled with IBO's estimate that current year expenditures will be $98 million greater than the Mayor's Office of Management and Budget (OMB) expects, increases

Total Revenue and Expenditure Projections
Dollars in millions

	2018	2019	2020	2021	2022	Average Change
Total Revenue	**$89,184**	**$90,077**	**$92,557**	**$95,417**	**$98,219**	**2.4%**
Total Taxes	58,853	60,752	63,036	65,564	67,989	3.7%
Total Expenditures	**89,184**	**90,077**	**93,299**	**96,943**	**98,343**	**2.5%**
IBO Surplus/(Gap) Projections	**$0**	**$0**	**($742)**	**($1,526)**	**($124)**	
Adjusted for Prepayments and Debt Defeasances:						
Total Expenditures	$89,035	$92,905	$94,801	$96,943	$98,343	2.5%
City-Funded Expenditures	$63,897	$68,741	$70,535	$72,244	$73,245	3.5%

NOTES: IBO projects a surplus of $4.3 billion, $677 million more than the de Blasio Administration, for 2018 and $825 million for 2019. The surplus is used to prepay some 2020 expenditures, leaving 2018 and 2019 with balanced budgets. Figures may not add due to rounding.

New York City Independent Budget Office

IBO

New York City
Independent Budget Office
Ronnie Lowenstein, Director

110 William St., 14th floor
New York, NY 10038
Tel. (212) 442-0632

Fax (212) 442-0350
iboenews@ibo.nyc.ny.us
www.ibo.nyc.ny.us

the 2018 surplus to $4.3 billion. Rather than the balanced budget OMB projects for 2019, IBO forecasts a surplus of $825 million, the product of our estimate that tax and miscellaneous revenue will be $888 million more than OMB expects and that $64 million in additional spending will be required under the Mayor's Executive Budget proposal.

IBO assumes that the surplus revenue from 2018 and 2019 will be used to prepay 2020 expenses, reducing the 2020 gap by $1.5 billion. In addition, in 2020 IBO forecasts $898 million more revenue and $76 million less spending than projected by OMB. The combination of the prepayment of 2020 expenses with prior year revenues and IBO's forecast of $974 million of additional resources reduces the 2020 gap to $742 million, 1.0 percent of planned city-funded expenditures. If the $1.25 billion in reserve funds sitting in the 2020 budget—dollars not budgeted for any specific expenditure—are not needed to cover unexpected spending needs or revenue shortfalls, they would more than fill the 2020 gap and can help with the projected 2021 shortfall as well. For the last years of the financial plan, IBO projects budget gaps of $1.5 billion (2.0 percent of city-funded expenditures) in 2021 and $121 million (0.2 percent) in 2022. These out-year gaps are of a size the city has routinely managed in the past.

Other key findings from our review of the Mayor's Executive Budget and financial plan:

- IBO's current forecast for total 2018 tax revenues has increased since our March outlook by $882 million, or 1.5 percent. We project that near-term strength in the U.S. and local economies will be followed by weaker growth over the next couple of years. As a result, we expect growth in city tax revenues will also slow, from an estimated 8.4 percent increase this year to a 3.2 percent rise in 2019, when collections will reach $60.8 billion.
- IBO's property tax forecast exceeds the Mayor's projections by $210 million in 2018, rising to $1.0 billion in 2022, mostly due to the Mayor's office carrying larger allowances for refunds, delinquencies, and cancellations. IBO's estimates for the personal income tax and the general corporation tax are also consistently higher each year than the Mayor's from 2018 through 2022.
- After seven years of local employment growth with an average of over 100,000 jobs added annually, IBO expects slower growth this year and next with 70,200 jobs added to the local economy in calendar year 2018 and 60,000 jobs in 2019—contributing to slower tax revenue growth beginning in fiscal year 2019
- Real wages have been declining across many sectors over much of the current expansion but are projected to shift to weak growth over the 2018-2022 period.
- Debt service and fringe benefit costs are the two largest drivers of overall expenditure growth, growing by an average of 8.4 percent and 7.0 percent annually from 2018 through 2022.
- Department of Education spending is expected to grow by $2.7 billion from 2018 through 2022, the largest increase in agency expenditure in dollar terms in the plan.

U.S. and Local Economic Outlook

Economic Overview. IBO's outlook for the U.S. economy has changed little from our forecast in March. A strong labor market with rising incomes will continue to fuel consumer demand. With the addition of considerable fiscal stimulus from federal tax cuts late in 2017 and spending increases early in 2018, we expect economic growth to accelerate this year. Our forecast of 3.0 percent real (inflation-adjusted) gross domestic product (GDP) growth in 2018 is slightly higher than we projected in March, while our forecast of growth in 2019, 2.6 percent, has remained the same. (In our discussion of the economic outlook, years refer to calendar years and monthly and quarterly data are seasonally adjusted.) The federal fiscal stimulus will heighten inflationary pressures, which were already growing in 2017 due to the tight labor market. Inflation will accelerate and interest rates will rise this year and next while the Federal Reserve steps up its efforts to prevent inflation from rising above its target range. IBO's forecast is premised on the success of the Fed's efforts to limit inflation without rattling financial markets. Missteps in monetary policy are a significant risk to the forecast.

IBO's economic forecast for the city anticipates a slowing of the pace of job creation throughout the plan period, accompanied, however, by low unemployment rates and an uptick in wage growth. The outlook for Wall Street profits—though not for financial sector job growth—is strong. While the commercial real estate market is recovering from its recent doldrums, the residential market has been weakening and at best moderate growth is projected for both. In its broad contours the new forecast is similar to IBO's March projections.

U.S. Economy. The current economic expansion will soon be entering its 10th year and IBO expects it will continue at least into an 11th year, which would make it the longest expansion in the post-World War II era. Continued employment growth and wealth effects from

IBO versus Mayor's Office of Management and Budget Economic Forecasts						
	2017	2018	2019	2020	2021	2022
National Economy						
Real GDP Growth						
IBO	2.3	3.0	2.6	1.6	1.9	2.2
OMB	2.3	2.7	2.9	2.3	1.9	1.7
Inflation Rate						
IBO	2.1	2.8	2.5	2.5	2.3	2.2
OMB	2.1	2.2	1.7	2.7	2.5	2.4
Personal Income Growth						
IBO	3.1	4.8	5.1	4.0	3.7	4.0
OMB	3.1	4.1	5.5	5.4	5.1	4.7
Unemployment Rate						
IBO	4.4	3.8	3.5	4.1	4.9	4.9
OMB	4.4	3.9	3.5	3.5	3.5	3.6
10-Year Treasury Note Rate						
IBO	2.3	3.2	4.0	4.0	4.1	4.3
OMB	2.3	3.1	3.8	3.9	4.0	3.9
Federal Funds Rate						
IBO	1.0	1.9	3.5	3.7	3.3	2.8
OMB	1.0	1.8	2.8	3.3	3.4	3.5
New York City Economy						
Nonfarm New Jobs (thousands)						
IBO (Q4 to Q4)	95.1	70.2	60.0	52.4	37.5	45.3
IBO (annual average)	81.0	80.3	63.3	58.1	41.0	43.5
OMB (annual average)	81.1	59.8	53.9	51.7	50.3	35.1
Nonfarm Employment Growth						
IBO (Q4 to Q4)	2.2	1.6	1.3	1.1	1.1	1.1
IBO (annual average)	1.9	1.8	1.4	1.3	0.9	0.9
OMB (annual average)	1.9	1.3	1.2	1.1	1.1	0.8
Inflation Rate (CPI-U-NY)						
IBO	2.0	2.6	2.7	2.6	2.5	2.5
OMB	2.0	1.9	2.0	2.7	2.5	2.4
Personal Income ($ billions)						
IBO	565.7	586.3	608.1	631.1	658.3	683.6
OMB	567.7	590.7	617.1	643.8	670.1	694.9
Personal Income Growth						
IBO	3.3	3.6	3.7	3.8	4.3	3.9
OMB	3.7	4.1	4.5	4.3	4.1	3.7
Manhattan Office Rents ($/sq.ft)						
IBO	78.1	79.0	81.0	82.8	84.4	85.3
OMB	79.0	77.7	81.0	83.2	84.9	86.5

SOURCE: Mayor's Office of Management and Budget
NOTES: Rates reflect year-over-year percentage changes except for unemployment, 10-Year Treasury Note Rate, Federal Funds Rate, and Manhattan Office Rents. The local price index for urban consumers (CPI-U-NY) covers the New York/Northern New Jersey region. Personal income is nominal.

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rising housing and financial asset prices have sustained consumer demand. Adding to overall demand is the federal government's expansionary fiscal policy of tax cuts and spending increases. IBO forecasts an acceleration of real gross domestic product growth from 2.3 percent in 2017 to 3.0 percent in 2018. However, this rate of growth is not likely to be sustained. With an already-tight labor market, rapid economic growth will put upward pressure on prices and lead the Federal Reserve to tighten monetary policy. IBO forecasts still-robust growth of 2.6 percent in 2019, followed by considerably slower growth of 1.6 percent in 2020.

The federal Bureau of Economic Analysis's (BEA) initial estimate of real GDP growth in the first quarter of 2018 is 2.3 percent, somewhat lower than the 3.1 percent growth in the second half of 2017. Slower consumer spending, residential construction, and export sales—all perhaps related to this year's harsh winter in many parts of the country—were major contributors to the slowdown. But on-going measurement problems may also account for some of the apparent slowdown in the first quarter. In recent years BEA has been troubled by a widely noted pattern of underestimating first-quarter growth. If this pattern holds, it is likely that the recent estimate will be revised upward.

IBO's expects faster economic growth in the remainder of the year and into the middle of 2019. With the U.S. economy continuing to add on average about 200,000 jobs each month, consumer demand—the primary driver of economic growth in the current expansion—is expected to remain strong. Households are also in solid financial position to continue spending. Thanks to interest rates that until recently were near historic lows, their debt service burden—the share of disposable income required to stay current on debt obligations—has also remained at historic lows. Moreover, wealth effects are expected to remain strong in the coming year, helped by the recent run-up in the price of stocks. Other conditions favorable to continued economic growth include moderate energy costs and a vigorous global economy that will keep demand for U.S. exports robust. In addition to all these positive factors, recently enacted fiscal policies will further stimulate the economy, at least in the short run.

The bulk of the savings from the new federal tax law that took effect at the beginning of this year will be received by businesses. Still, after-tax disposable income of many (but not all) households will also increase thanks to the new law, helping to extend already strong consumer demand and further boost business profits. To the extent that increased corporate profits are capitalized in stock prices, the wealth effect on consumer spending would also be positive. Moreover, the addition of $320 billion in new federal spending over the next two years will add more fuel to economic growth. (The downside of the substantial increases in the federal deficit caused by these fiscal policies is discussed below.)

IBO forecasts real GDP growth of 3.0 percent in 2018, up from 2.3 percent in 2017. The unemployment rate—4.1 percent in the first quarter of 2018—is already below what most economists consider to be full employment, the threshold under which labor markets are tight enough to spur inflation. Inflationary pressures have been building, and our forecast for 2018 is for an inflation rate of 2.8 percent, well above last year's 2.1 percent rate. We expect that tight labor markets will put upward pressure on inflation-adjusted wages, drawing more participants into the labor force and supporting growth. Despite greater labor force participation, we project that the unemployment rate will continue to drop, reaching 3.8 percent in 2018 and 3.5 percent in 2019; the latter rate would be lower than any monthly rate since 1969. Similarly, a broader measure of unemployment—the Bureau of Labor Statistics U-6 rate, which counts as unemployed part-time workers who would rather have full-time work and workers too discouraged to actively look for employment—has ranged from 8.0 percent to 8.2 percent over the past six months, the lowest levels since 2007.

With little slack in labor markets and other resource constraints, IBO forecasts slower growth beginning in the middle of next year, with real GDP growth averaging 2.6 percent in 2019 and 1.6 percent in 2020. With inflationary pressures in the economy already building toward the end of 2017, even before the extent of the fiscal stimulus was known, the Federal Reserve had signaled its intention to continue increasing the federal funds rate (the rate at which banks lend funds overnight to other banks) several times in 2018, as it did in 2017. Having raised the federal funds rate in March 2018, the Fed has indicated that there will be at least two more increases this year. The increases are expected to be small, and IBO forecasts an average federal funds rate of 1.9 percent for the year as a whole. In order to keep inflation as close as possible to the 2.0 percent rate the Fed considers optimal, we expect the funds rate to rise to 3.5 percent in 2019 and 3.7 percent in 2020.

Increases in the federal funds rate will be accompanied by increases in longer-term interest rates. IBO forecasts a rise in the 10-year Treasury rate from an average of 2.3 percent in 2017 to 3.2 percent in 2018 and 4.0 percent in 2019. Investor concern over the mushrooming of the federal government's budget deficit—from $665 billion this past federal fiscal year to $804 billion and $981 billion in fiscal years 2018 and 2019 according to projections by the Congressional Budget Office—will also have the effect of pushing up interest rates.

Pursuing a policy of fiscal stimulus at this point in the business cycle eschews conventional approaches to economic policymaking. Although the tax cuts will initially spur growth, given that the economy is already at or near full employment the added demand from households, businesses, and government is likely to have more of an impact on prices than on economic output. While lower taxes will encourage businesses to invest, increases in long-term interest rates will have the opposite effect, negating much of the potential impact of the stimulus.

IBO forecasts a gradual acceleration of economic growth in the final years of the forecast period, from the projected low of 1.6 percent in 2020 to 2.2 percent in 2022. This outlook is premised on the Federal Reserve being able to raise interest rates and unwind quantitative easing (the central bank's unconventional policy of purchasing securities following the Great Recession) just enough to slow economic growth and tame inflation, but not so much as to substantially reduce business investment and consumer spending. By putting upward pressure on inflation and interest rates, the fiscal stimulus has complicated monetary policy. Years of historically low interest rates have fueled large increases in the price of equities. With stocks at record highs and—by many measures—overvalued, a misstep by the Federal Reserve risks disruptions that could rapidly deflate asset prices and lead to a bear market or (in the worst case) recession. The difficult challenge facing monetary policymakers is the primary risk to IBO's economic outlook.

Both IBO and the Mayor's Office of Management and Budget (OMB) expect faster economic growth this year and next compared with 2017, although there are differences in the trajectories of the two forecasts. OMB projects real GDP growth of 2.7 percent in 2018 rising to 2.9 percent in 2019, compared with IBO's forecast of peak growth of 3.0 percent this year slowing to 2.6 percent in 2019. Our forecast of more rapid growth in 2018 is accompanied by the expectation of considerably higher rates of inflation (2.8 percent in 2018 and 2.5 percent in 2019) than projected by OMB (2.2 percent and 1.7 percent in 2018 and 2019, respectively). OMB projects slower economic growth over the last three years of the forecast period, falling to just 1.7 percent in 2022. In contrast, IBO expects growth of just 1.6 percent in 2020 followed by somewhat faster growth of 1.9 percent in 2021 and 2.2 percent in 2022.

New York City Economy. IBO's city economic forecast anticipates a slowing of the pace of job creation throughout the plan period, accompanied, however, by low unemployment rates and an uptick in wage growth. In its broad contours the new forecast is similar to IBO's March projections.

Employment. New York City's long employment expansion picked up steam again last year, largely on the back of surging home health care job gains, which topped 20,000 in 2017, accounting for most of the growth in the broader ambulatory health care services sector. Across other sectors that had been bellwethers earlier in the expansion (business services, education, trade, and food services), however, job growth has remained subdued.

IBO expects the pace of New York City job creation to moderate in 2018 and then decelerate over the next three years in step with the forecast trend in the national economy. This projected slackening shows up mostly in health care and to a lesser extent in financial activities, information, leisure and hospitality, and transportation; construction is expected to remain strong this year but decline in 2019 and beyond. But to an unusual extent the health care forecast, and indeed the entire city employment forecast, depends on whether home health care services sustains its recent pace of growth. Home health care employment has doubled in New York City in just six years, from 82,100 in the first quarter of 2012 to 165,500 in the first quarter of 2018, accounting for nearly a third of all the reported job growth in this sector in the entire country.

Labor Force. New York City's unemployment rate stood at 4.2 percent in the first quarter of 2018, a historic low, while the city's labor force participation rate of 60.9 percent was just off of last year's all-time high. Even with slowing payroll employment growth, the city's labor market will remain tight, with the unemployment rate projected to drop to 3.7 percent by the middle of 2019, before eventually edging back to 4.5 percent—still close to full employment—by the end of the financial plan period.

Wages. Adjusted for inflation, New York City's overall average wage fell for the fifth time in six years in 2017—a run that has dropped the real wage below the nadir of the 2009 crisis and recession. IBO expects wage growth to turn slightly positive in 2018 and for the rest of the forecast period. Rising wages are projected across most of the city economy, with health care and manufacturing as notable exceptions, reflecting the fact that even as the pace of job creation slows the city's labor market is expected to remain tight. Moreover, a projected slackening of the recent pace of gains in home health care employment will mean that overall job growth will not be tilted quite as heavily towards low-wage jobs. Even so, we project that the overall average

New York City Payroll Employment Growth
Q4 over Q4 change in thousands

	History					Forecast				
	2013	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**
Total Nonfarm	**117.9**	**136.1**	**117.3**	**67.5**	**95.1**	**70.2**	**60.0**	**52.4**	**37.5**	**45.3**
Total Private	**120.1**	**132.6**	**113.5**	**66.9**	**96.1**	**70.3**	**60.0**	**52.4**	**37.4**	**45.4**
Mining, Logging and Construction	6.1	8.8	11.6	3.5	6.9	7.3	4.9	3.3	2.6	3.4
Manufacturing	1.0	0.3	0.9	(3.2)	(2.6)	0.0	(0.8)	(1.4)	(0.9)	(0.6)
Wholesale Trade	2.1	2.3	1.2	(1.5)	1.0	1.1	0.4	0.1	(0.1)	0.1
Retail Trade	13.3	10.1	(4.9)	(0.5)	2.4	3.5	0.7	(1.9)	(0.0)	1.2
Utilities	(0.1)	0.4	0.3	(0.0)	0.0	0.1	(0.0)	(0.0)	(0.0)	0.1
Transportation and Warehousing	1.1	3.4	5.5	2.6	3.1	1.7	1.9	1.7	1.5	1.8
Information	6.4	3.8	5.1	3.9	4.0	2.0	2.5	2.1	1.6	2.0
Finance and Insurance	0.7	7.9	8.0	(0.9)	4.0	2.0	2.5	2.2	0.7	2.3
Securities, Financial Investments, and Related Activities	(0.7)	3.7	5.1	0.3	1.8	1.6	2.0	1.6	0.6	1.5
Real Estate and Rental and Leasing	2.5	3.2	3.1	2.3	4.9	1.2	1.9	1.3	1.2	1.2
Professional, Scientific, and Technical Services	13.8	16.1	17.7	8.7	9.2	9.1	9.9	11.7	7.8	5.2
Management of Companies and Enterprises	1.9	3.0	(1.3)	1.4	1.9	(0.4)	0.5	1.0	0.5	0.1
Administrative and Support and Waste Management Services	5.0	10.1	13.2	9.6	8.1	9.1	7.9	7.0	4.3	5.9
Educational Services	13.1	12.7	8.8	3.4	3.4	4.8	3.1	2.4	1.5	2.7
Health Care and Social Assistance	23.5	23.2	21.3	24.6	38.0	19.1	17.0	16.3	12.9	14.7
Ambulatory Health Care Services	17.0	17.5	14.6	18.7	23.7	12.6	11.1	11.4	8.8	9.4
Social Assistance	6.2	5.6	5.6	3.6	10.3	4.5	3.8	3.5	3.5	4.4
Arts, Entertainment, and Recreation	6.3	2.4	3.9	0.6	2.9	1.8	0.5	0.1	0.0	0.1
Accommodation and Food Services	19.2	18.3	14.7	8.9	6.9	6.8	4.9	4.5	3.5	4.6
Food Services and Drinking Places	17.8	16.3	14.0	7.8	8.3	5.9	4.6	4.1	3.2	4.1
Other Services	4.2	6.5	4.6	3.5	2.0	1.0	2.0	2.0	0.3	0.7
Government	(2.3)	3.5	3.8	0.6	(1.0)	(0.1)	0.0	0.0	0.1	(0.1)

SOURCES: Bureau of Labor Statistics with IBO seasonal adjustments; Moody's Analytics
NOTE: Home health care is included in ambulatory health care services.

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wage in 2022 will still fall well short of the 2007 peak, and financial investments sector (Wall Street) wages will have recouped only about a third of the ground lost over the past decade.

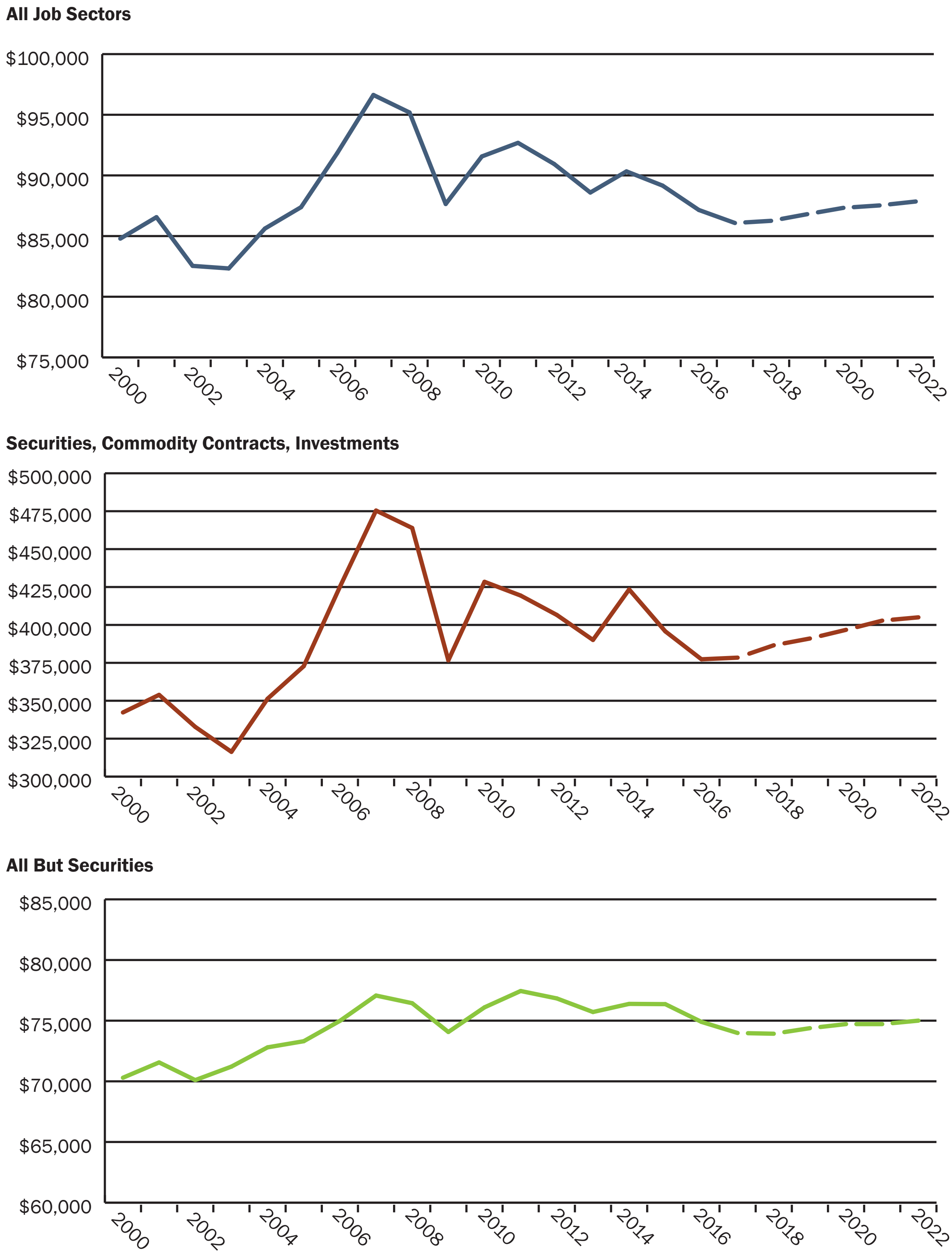
Wall Street. New York Stock Exchange (NYSE) member firm broker dealer profits rose to $24.5 billion in 2017, the highest level in six years. Reflecting increases in the Federal Reserve's benchmark rate, net interest costs jumped $14.1 billion last year and have more than quadrupled over the past two years. But this was more than offset by the $20.7 billion rise in net operating revenues in 2017.

IBO expects profits to slip to $20.1 billion in 2018 and $19.2 billion in 2019, and then average about $20 billion per year over the rest of the financial plan period. Net operating revenues will continue to move on a moderate upward trajectory over the next five years. Net interest costs are projected also to continue to rise in tandem with the benchmark rate through 2020, at which point we expect the Federal Reserve to begin easing monetary policy in response to slower U.S. growth.

Real Estate. Taxable real estate sales in New York City were $93.2 billion in 2017, the lowest level since 2012. Commercial sales were $37.8 billion, less than half their 2015 peak. Residential sales, however, were $55.4 billion, the highest level ever recorded before adjusting for inflation. Last year was the first year since 2010 that the value of residential sales in New York City exceeded that of commercial sales.

Commercial real estate sales were $12.8 billion in the January-March 2018 quarter, well above the level of sales of any quarter in 2017, but well below the 2015 and 2016 levels. Commercial sales for the quarter were bolstered by the $2.4 billion sale of the Chelsea Market property on

New York City Average Real Wages Have Yet To Recover From 2008-2009 Recession



NOTES: In 2017 dollars. Based on IBO re-estimates of Bureau of Economic Analysis definitions of industry employment and wages. 2017 is preliminary.

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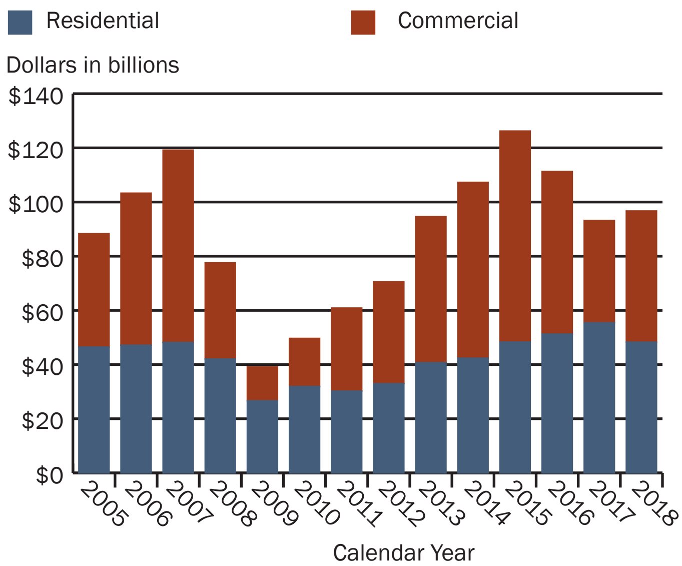
9th Avenue to Google in March. Residential sales for the quarter were $12.0 billion, the lowest quarterly total since April-June 2016.

IBO's real estate forecast is substantially the same as in March. IBO expects residential sales to drop over 10 percent in 2018, with the greatest decline in Manhattan.

IBO Projects a Decline in Residential Sales in 2018, While Commercial Sales Begin to Recover



SOURCE: IBO analysis of Department of Finance data
NOTE: 2018 is forecast.

Commercial sales, on the other hand, will begin a moderate recovery. In 2019 and the following years the value of commercial sales are projected to surpass the value of residential transactions, with modest growth in both sectors continuing through 2022. Several factors will, however, work to make investments in commercial property less attractive: higher mortgage rates, weakness in brick and mortar retailing, slower growth in office-using employment, and a significant amount of new office space coming online. On the residential side, higher mortgage rates and recent policy changes that reduce the tax advantages of home ownership will exert downward pressure on sales growth.

Taxes and Other Revenues

IBO's near-term tax revenue forecast has been revised upward sharply from what we projected in our previous forecast (March 2018), spurred by what we assume to be one-time responses to federal tax law changes. Tax revenue is now expected to total $58.9 billion in 2018, $882 million more than in our forecast from two months ago, and $60.8 billion in 2019, up $553 million since March. The federal effect fades further in 2020 through 2022. By the final year of our forecast (2022), tax revenues are projected to total $69.0 billion, only $63 million higher than in our March forecast. (Unless otherwise noted, years refer to city fiscal years from here on.)

The two largest changes in the 2018 forecast are the $748 million increase for personal income tax and a $155 million downward revision for corporate income tax revenue. For 2019 and subsequent years, the forecasts for all taxes other than personal income, unincorporated business, and sales have either been revised down or had only minor positive changes since March.

With the addition of the large boost in revenues beginning in December, 2018 tax revenues are now expected to be 8.4 percent higher than in 2017, the largest one-year increase since 2013. With less of a kick from federal tax changes expected in 2019, year-to-year growth will slow to 3.2 percent in 2019, and remain in the 3.7 percent to 4.0 percent range in the remaining years of the forecast. This slowdown in annual tax revenue growth reflects not only the expectation of a limited effect from the federal tax law changes but also the anticipation of slower U.S. GDP growth beginning in the second half of calendar year 2019.

IBO projects that revenue growth will average 3.7 annually from 2018 through 2022, which would be the slowest four-year annual average since the end of the Great Recession. Since the recession, the four-year average has ranged from a low of 4.9 percent (2013-2017) to a high of 6.6 percent (2009-2013). The real property tax is expected to show the steadiest and strongest growth, averaging 5.5 percent annually from 2018 through 2022. No other tax is projected to average more than 4.3 percent annually, with several—including the personal income tax—expected to average less than 2.0 percent annual growth between 2018 and 2022.

OMB and IBO have both increased their total tax revenue forecasts from earlier in the year, with OMB's changes larger than IBO's in 2018 and 2022 and IBO's changes larger in 2019 through 2021; as a result, the gaps between the two sets of forecasts have narrowed somewhat since our previous forecasts. Still, IBO's forecast of tax revenues exceeds OMB's in each year of the plan, with the gap growing from $774 million (1.3 percent) in 2018 to $861 million (1.4 percent) in 2019, and $1.7 billion (2.5 percent) in 2022. Throughout the forecast period, much of the difference is attributable to IBO's more robust outlook for PIT, the real property tax, and the corporate income taxes; the property tax difference is particularly wide in 2022 when it exceeds $1.0 billion.

Total revenues, including the city's fees, fines and other miscellaneous sources, state and federal grants and other categorical aid, and interfund revenues are now forecast to total $89.2 billion for the current year, $932 million more than in March, with $882 million of the increase due to

IBO Revenue Projections
Dollars in millions

	2018	2019	2020	2021	2022	Average Change
Tax Revenue						
Property	$26,404	$28,170	$29,703	$31,269	$32,736	5.5%
Personal Income	13,100	12,863	13,166	13,618	13,876	1.4%
General Sales	7,395	7,694	8,150	8,397	8,686	4.1%
Corporation	3,407	3,678	3,776	3,805	3,954	3.8%
Unincorporated Business	2,225	2,287	2,410	2,496	2,629	4.3%
Real Property Transfer	1,393	1,424	1,463	1,524	1,560	2.9%
Mortgage Recording	1,004	935	967	1,013	1,052	1.2%
Utility	374	390	391	394	399	1.7%
Hotel Occupancy	587	595	612	622	632	1.9%
Commercial Rent	851	876	892	921	957	3.0%
Cigarette	36	35	34	33	32	-2.9%
Other Taxes and Audits	2,077	1,806	1,471	1,471	1,477	-8.2%
Total Taxes	**$58,853**	**$60,752**	**$63,036**	**$65,564**	**$67,989**	**3.7%**
Other Revenue						
STaR Reimbursement	$189	$185	$182	$180	$178	-1.5%
Miscellaneous Revenue	7,128	6,816	6,858	6,766	6,745	-1.4%
Unrestricted Intergovernmental Aid	-	-	-	-	-	n/a
Disallowances	85	(15)	(15)	(15)	(15)	n/a
Total Other Revenue	**$7,402**	**$6,986**	**$7,025**	**$6,931**	**$6,908**	**-1.7%**
Less: Intra-City Revenue	**($2,208)**	**($1,826)**	**($1,771)**	**($1,776)**	**($1,776)**	
TOTAL CITY-FUNDED REVENUE	**$64,046**	**$65,912**	**$68,290**	**$70,719**	**$73,121**	**3.4%**
State Categorical Grants	$14,836	$14,986	$15,319	$15,780	$16,265	2.3%
Federal Categorical Grants	8,551	7,561	7,376	7,355	7,275	-4.0%
Other Categorical Aid	1,105	936	930	925	919	-4.5%
Interfund Revenue	646	682	641	638	638	-0.3%
TOTAL REVENUE	**$89,184**	**$90,077**	**$92,557**	**$95,417**	**$98,219**	**2.4%**

NOTES: Corporation tax revenue combines collections of the business corporation tax, the general corporation tax, and the banking corporation tax. Figures may not add due to rounding.

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higher tax receipts. Changes for subsequent years were more modest, with revenue from all sources now expected to total $90.1 billion in 2019, growing to $98.2 billion by 2022.

Real Property Tax. IBO's updated property tax forecast is little changed from our March outlook. Virtually all of the differences between our two forecasts are due to small changes in the projections for property tax reserve items rather than from changes in assessed value or the levy. (The property tax reserve includes provision for the costs of abatements, delinquencies, refunds, and cancellations, as well as revenue from prior-year liabilities and lien sales.)

IBO now projects that property tax revenue for 2018 will total $26.4 billion, an increase of just $57 million (0.2 percent) since March, due primarily to a reduction in the expected cost of the J-51 abatement program and increased proceeds from lien sales. Our forecast for 2019 is $28.2 billion, an increase of 6.7 percent from the current year. After 2019 revenues are projected to grow at an average annual rate of 5.1 percent through 2022, when they are expected to reach $32.7 billion. IBO's forecast for each year from 2019 through 2022 is slightly lower than in March with the difference growing from $13 million in 2019 to $125 million in 2022; virtually all of the change is due to small shifts in our forecasts of reserve components.

Differences between IBO's forecast and OMB's outlook have narrowed and now range between $210 million in 2018 and $558 million in 2021, with relatively small differences (less than $100 million each year) in projections for the levy. The gap is larger for 2022 ($1.0

billion) due to IBO's somewhat higher levy forecast—$402 million greater than OMB's—and IBO's smaller reserve forecast as OMB is carrying much larger allowances for refunds, delinquencies, and cancellations than IBO.

Projections of property tax revenues in the coming years are subject to greater uncertainty than usual due to growing pressure for major changes to the city's property tax system. IBO and other analysts have produced an expanding list of reports documenting inequities and inefficiencies in the current system, primarily the result of provisions of New York State laws that determine nearly all of the parameters of the city's property tax. A federal lawsuit brought by a coalition of homeowners, property owners, and advocates for tenants against the city and state is still pending.

Meanwhile, the City Council, in its response to the Mayor's Preliminary Budget, has called for establishment of a commission to consider comprehensive reform of the property tax, made up of appointees of both the Council and the Mayor. The Mayor has also endorsed a panel and promises to announce its establishment shortly, although his would be made up only of Mayoral appointees.

The extent of changes these commissions could consider will depend on whether they are required to develop proposals that are revenue neutral and whether they focus on differences in tax burdens among homeowner properties or also focus on the even greater disparities between homeowners and renters. With either focus, revenue-neutral proposals would leave some taxpayers better off and others worse off.[1]

Homeowner Rebate. The City Council's response to the Mayor's Preliminary Budget also included a proposal for a property tax rebate of $400 on the primary residence of homeowners—including owners of coops and condos—earning $150,000 or less. In the Council's proposal, homeowners who receive the veteran's exemption would not be eligible for the rebate. The proposed rebate would also provide no benefit for renters. IBO estimates that the rebate would cost roughly $210 million annually, although this estimate is highly dependent on assumptions regarding the number of homes that are primary residences and the incomes of homeowners.

Because of wide differences in tax burdens between types of property and location across the city, the effect of the rebate on average tax bills will differ. Those condominium owners whose income qualifies for the rebate would get a bigger percentage decrease in their property taxes (an average decline of 25.7 percent citywide) than single-family homeowners (an average decline of 9.4 percent). The relatively small number of condominium owners in the Bronx would receive the largest percentage reduction in their taxes, with an average decrease of 88 percent in their tax bills thanks to the rebate. (Data limitations prevent similar comparisons for cooperative apartments.) Among single-family homeowners, owners in the Bronx and Staten Island—who pay higher effective tax rates on average than their counterparts in Brooklyn and Manhattan—would fare slightly better, with reductions averaging 11 percent and 10 percent, respectively, compared with 2 percent in Manhattan and 9 percent in Brooklyn.

Real Estate Transfer Taxes. IBO has made small adjustments since March in its forecasts of the real property transfer tax (RPTT) and the mortgage recording tax (MRT), but the overall trends for the years 2018-2022 remain unchanged. The sum of the two taxes—collectively referred to as the transfer taxes—has been adjusted upward for 2018, based on the strength of RPTT collections. However, at $2.4 billion the projected total for this year is still 5.4 percent below 2017, and the lowest level since 2013. Total transfer tax collections are projected to increase slowly beginning in 2019, reaching $2.6 billion in 2022. This sum is well below the recent nominal peak of $3.0 billion in 2016, and far below the all-time peak of $3.3 billion reached in 2007.

Real Property Transfer Tax. RPTT collections for 2018 are projected to be just under $1.4 billion, an increase of $50 million (3.7 percent) over the March forecast, and a decline of about $22 million (1.6 percent) from 2017. IBO's 2018 forecast has been revised upward to reflect a rebound in the sales of commercial property in recent months.

The RPTT is a tax on the value of real estate sales, and revenue from the tax is directly correlated with the value of property transactions. Commercial sales have been the main driver of trends in RPTT revenue, both because of their greater variability and because commercial transactions are taxed at higher rates than residential transactions. The dramatic decline in RPTT revenue in the wake of the financial crisis, and its subsequent recovery, were the result primarily of variations in commercial sales. In 2015 commercial sales and RPTT revenue reached all-time highs. In 2016 commercial sales fell, but the rise in residential sales pushed RPTT even higher, to almost $1.8 billion. In 2017 residential sales rose sharply, but not enough to offset the steep decline in commercial sales. As a result, RPTT revenue fell to just over $1.4 billion.

IBO projects that RPTT revenue will increase each year beginning in 2019, reaching just under $1.6 billion in 2022. However, the growth rate has been revised slightly downward from our prior forecast, and projected 2022 revenue is now $46 million (2.9 percent) below the forecast in March. The value of commercial sales is projected to exceed the value of residential transactions in each year from 2019 through 2022. Because of this, and because commercial transactions are taxed at higher rates than residential sales, commercial properties will be responsible for well over half of RPTT revenue.

IBO's forecasts are slightly below OMB's in 2018 and 2019, and slightly above in 2020 through 2022. The patterns of the two forecasts are similar, except that where IBO projects a small increase in 2020, OMB projects a modest dip. For the entire 2018 through 2022 period, IBO's forecast of RPTT revenue is a total of $49 million (0.7 percent) above OMB's.

Mortgage Recording Tax. MRT collections for the current year are projected at $1.0 billion, unchanged since our March forecast. The outlook for 2018 represents a drop of 10.2 percent from 2017, and 18.6 percent from 2016. In 2007 MRT revenues hit an all-time peak of almost $1.6 billion in nominal terms, before crashing in the wake of the financial crisis and hitting bottom at $366 million in 2010. Revenue then rebounded, reaching a peak of just over $1.2 billion in 2016.

The MRT is a tax on the value of mortgages used to purchase property, and in some cases, on the value of mortgage refinancings. While RPTT revenue is proportional to the value of property sales, in the case of the MRT the relationship between real estate sales and tax revenue is less direct. The amount of a purchase financed by a mortgage varies from one transaction to another. Moreover, refinancings—which do not involve a property sale—may or may not be subject to the MRT. In general, however, periods of high MRT revenue tend to coincide with periods of declining interest rates and high levels of refinancing activity.

Recent changes in federal tax law reduce the maximum value of residential mortgages whose interest can be deducted for income tax purposes, and also restrict the deductibility of interest from home equity loans. IBO expects these policy changes to reduce mortgage activity, independent of changes in mortgage rates.

The observed decline in MRT revenue since 2016 coincides with increases in mortgage rates. Currently, IBO projects that mortgage rates will continue to rise through mid-2020, and then drop slightly. Also associated with the increase in rates, and with the reduction in the deductibility of interest from home equity loans, a significant drop is forecast in refinancing as a share of total mortgage activity. According to the Mortgage Bankers Association (MBA), for the U.S. as a whole, refinancings represented 43 percent of the value of residential mortgages issued in 2017. The MBA projects that the refinance share will drop to 33 percent in 2018, and 24 percent in 2019. After the projected 10.2 percent drop in MRT revenue in 2018, IBO expects collections to fall by an additional 6.9 percent, to $935 million, in 2019. We project that revenue will slowly rebound beginning in 2020, and reach nearly $1.1 billion in 2022.

IBO's updated forecast follows the same trend as our March forecast, but with sharper declines in 2019 and 2020. The forecast for 2019 has been brought down by $30 million (3.1 percent), and the forecast for 2020 by $20 million (2.0 percent). The forecasts for 2021 and 2022 are unchanged.

IBO's MRT forecast is similar to OMB's, with a decline through 2019 and a subsequent recovery. IBO projects stronger MRT growth than OMB in 2020 through 2022, and for 2022 IBO's forecast is $73 million (7.5 percent) above OMB's.

Commercial Rent Tax. At $851 million, IBO's 2018 forecast for the commercial rent tax (CRT) is 4.2 percent above 2017 collections and unchanged since our last forecast in March. IBO projects average annual growth from 2019 through 2022 of 3.0 percent, with 2022 collections forecast at $957 million, $8 million above the March forecast. IBO's CRT forecasts are all within 1.0 percent of OMB's projections.

The CRT is a tax imposed on tenants renting space for business, professional, and commercial purposes in much of Manhattan below 96th Street. Not-for-profit organizations, subtenants, tenants located in the World Trade Center area, and most retail tenants south of Chambers Street are exempt from the tax. Tenants participating in the Commercial Revitalization Program also receive reductions in their tax bill. Over time both the tax rate and the geographic area subject to the tax have been reduced. In recent years tenants with annual gross rents of less than $250,000, regardless of where they are located, have been exempt, with a sliding scale tax credit applied to tenants with annual or annualized rents between $250,000 and $300,000.

The forecasts of IBO and OMB for 2019 and later reflect the impact of legislation passed by the City Council in November 2017 that seeks to reduce or eliminate the CRT for certain small businesses. The bill, which takes effect July 1, 2018, creates a new credit that eliminates the tax for tenants paying less than $499,999 in annualized rent, providing their total income is $5 million or less. Tenants paying rents in this same range but with incomes of $5 million to $10 million are eligible for a partial tax credit, as are tenants paying from $500,000 to $550,000 whose income does not exceed $10 million.

Personal Income Tax. The city's personal income tax collections have continued to be stronger than anticipated, prompting IBO to raise its forecast for the current year, to $13.1 billion. The huge increase over 2017 revenue —$2.0 billion (18.4 percent)—results from a combination of temporary conditions boosting collections. Changes to federal income taxes enacted in December have altered the timing of PIT collections this year, although subsequent state legislation has severed the links between provisions of the federal tax system and state and city tax law that would have directly changed PIT liabilities for many New Yorkers.[2] PIT collections will decline by 1.8 percent in 2019, to a projected $12.9 billion in our forecast. From 2020 through 2022, revenue growth is expected to resume, although at a more moderate pace, averaging 2.6 percent, annually.

Increases in revenue from the two largest components of PIT collections—withholdings and quarterly estimated payments—account for all of the PIT growth from 2017 to 2018. IBO forecasts $9.4 billion in withholding revenue for the year—14.8 percent more than in 2017. Quarterly estimated payments (excluding those with extensions) are projected to be $2.9 billion, a huge 55.7 percent increase over 2017. Withholdings and estimated payments play a much smaller role in the large upward revision in our 2018 PIT forecast since March, accounting for only $78 million of the $748 million increase. A large part of the revision in our forecast stems from a $175 million upward revision in the projection of offset receipts—periodic payments made to the city from the state's Department of Taxation and Finance (which administers the city's income tax). The other large changes to the 2018 forecast are a lower estimate for refunds and an increase in our projections for final returns and estimated payments made by taxpayers who file for extenstions.

Withholdings. Throughout 2018, withholding receipts—by far the largest component of PIT revenue—have swelled in comparison to the previous year. The strength of withholding revenue this year is partly due to a change in state law enacted last spring that eliminated the remaining component of STAR-related benefits delivered through the city's tax on personal income—the roughly 6 percent reduction in marginal PIT rates for filers with income under $500,000. Beginning in July 2017, withholding tables were adjusted to reflect the elimination of the reduced rates and the resulting increase in city residents' PIT liabilities, (Total city revenue is not affected by the elimination of STAR because the increase in PIT revenue is offset by the loss of the state's reimbursement to the city for the foregone PIT under STAR.[3])

Withholding receipts in December 2017 through March of this year—the period when securities firms and many other companies in the financial and professional services industries typically award employee bonuses—are generally larger than in other months. This year the bonus season boost to withholdings was particularly large for two reasons. One, the bull market on Wall Street in calendar year 2017 and a five-year high of New York Stock Exchange-member profits fueled a substantial increase in bonus compensation, in turn augmenting income tax withholding receipts. Two, federal tax reform enacted in 2008 required many managers of offshore hedge funds to repatriate and pay taxes on deferred compensation that had been held in hedge funds' offshore accounts since 2008. The 2008 legislation gave managers up to 10 years to repatriate already earned deferred compensation. With the 10-year deferral period coming to an end on December 31, 2017, a substantial amount of prior earnings that had been deferred became taxable, greatly adding to PIT withholdings.

Quarterly Estimated Payments. In contrast to withholdings, revenue from estimated payments initially lagged in 2018. Starting in December, however, estimated payments surged. These payments—the second largest component of PIT revenue—are made quarterly by taxpayers who are self-employed or who anticipate realizing capital gains from the sale of real property and financial assets. (Estimated payments are also made by taxpayers filing for extensions beyond the April 15th deadline, but these are excluded from this discussion.) A large amount of revenue from estimated payments made in January—the month in which most taxpayers make the last quarterly payment—was expected. Equities markets reached new highs in the past year and many investors, including some who had deferred capital gains in 2016 in anticipation of federal tax cuts, chose instead to realize capital gains in 2017. Moreover, the fourth quarterly payment was expected to be high as many taxpayers were believed to have underpaid their first three quarterly payments against calendar year 2017 liability and would therefore need to make a larger final quarterly payment.

But the Tax Cuts and Jobs Act (TCJA) enacted by Congress in December generated a further surge of estimated payments that were received by the city in late December and the very beginning of January. TCJA's $10,000 limit on the amount of state and local tax payments that can be claimed as an itemized deduction from federal adjusted gross income motivated large numbers of taxpayers across the country—including many New Yorkers—to prepay state and local taxes by the end of December, giving themselves the full benefit of the deduction one last time before the limits came into effect on January 1. Even though the fourth quarterly payment was not due until later on in January, almost $1.4 billion in PIT estimated payments were received from city taxpayers in the last week of December and first week of January; the latter were payments that had likely been made before January 1. Combined estimated payment revenue for the two months was $1.9 billion, which dwarfed collections in previous years.

Final Returns, Refunds, & Extension Estimated Payments. Compared to projections made at the time of the Preliminary Budget, IBO has lowered its 2018 forecast of refund payments and increased its forecasts of payments made with final returns and, especially, of extension estimated payments. With the surge of withholdings and quarterly estimated payments that became evident in December, it was thought that many taxpayers were likely to have overpaid their liability for calendar year 2017. As a result, we cautiously predicted a large decline in final returns, a large increase in refunds, and a decline in estimated payments made by taxpayers filing for extensions. But final returns to date in 2018 (through April) are already greater than projections made in March, and we now forecast $411 million for the entire year, a slight increase over 2017 revenue. Refunds to date in 2018 are greater than in the same period last year, but not by as much as previously expected. IBO now forecasts $1.3 billion in refunds for 2018. Finally, extension payments to date dwarf the amount projected in March. We have raised the forecast of extension payments by $286 million, to $745 million, only slightly less than 2017 extensions.

After 2018. IBO's forecast for PIT revenue in 2019 is $12.9 billion—a decline of $237 million (1.8 percent) from the amount projected for 2018. The city's economy is expected to continue adding a large number of jobs in calendar year 2018 (70,200, from Q4 to Q4), accompanied by an acceleration of personal income. But the set of conditions that swelled PIT revenue this year are not expected to recur. Barring additional effects from state and federal reforms, IBO projects slower withholding growth, a decline in quarterly estimated payments, and an increase in refunds in 2019.

Annual increases in PIT revenue are expected to resume in 2020, though a gradual slowing of employment growth through calendar year 2021 will keep PIT growth modest. IBO forecasts PIT revenue increasing at an average annual rate of 2.6 percent in 2020 through 2022, with a projected $13.9 billion in PIT revenue in the final year.

Differences with OMB's Forecast. IBO's forecast of PIT revenue exceeds OMB's Executive Budget forecast in each year, with the largest differences in the current year forecast ($442 million, or 3.5 percent) and in 2019 ($485 million, or 3.9 percent). IBO's higher forecasts of extension payments and final returns accounts for about two-thirds of the difference with OMB in 2018. The difference in the 2019 forecasts comes entirely from IBO's projection of greater withholdings growth and a smaller decrease in estimated payments. After 2019, IBO forecasts slower withholding and estimated payments growth, on average, than does OMB. As a result, differences between the two forecasts are much smaller, averaging $193 million a year for 2020 through 2022.

Business Income Taxes. The city's business income tax collections peaked at $6.0 billion in 2015 and subsequently declined for two consecutive years, falling to $5.5 billion in 2017. IBO projects a return to growth starting in the current fiscal year, with business tax collections increasing by 3.3 percent to $5.6 billion in 2018, and growing faster, by 5.9 percent, to reach nearly $6.0 billion in 2019. More moderate growth is expected after that, at an average annual rate of 3.4 percent from 2020 through 2022. By the end of the forecast period, IBO projects that total business tax revenues will reach $6.6 billion, an increase of $1.1 billion over collections in 2017.

Corporate Taxes. Since state and city business tax reform in 2015, most corporations are taxed under the business corporation tax, with a limited amount of revenue still being collected from general corporation tax and banking corporation tax taxpayers, including S-corporations and firms with audits and extensions still open from tax years prior to the reform. Declines in combined corporate collections have driven the decline in overall business tax revenue that has been underway for the past two years. For 2018, IBO projects a third year of modest decline at 1.1 percent ($38 million), bringing corporate collections down to $3.4 billion.

IBO had previously projected growth to return this year, driven by indicators such as rising corporate profits and earnings in key industries such as finance, trade, and information. But through the first two quarters of fiscal year 2018, receipts have been lower than expected, suggesting that the recovery in corporate tax revenue has again been delayed. However, collections have been improving as the end of the fiscal year approaches, with preliminary data from April looking particularly strong. This recent surge may be due in part to changes in tax law at the federal level, as businesses begin to take advantage of a friendlier corporate tax environment.

IBO projects robust growth in corporate tax revenue for 2019, increasing by 7.9 percent ($270 million) to reach $3.7 billion. Growth in collections is expected to slow down again after that, rising by 2.7 percent in 2020, 0.8 percent in 2021, and 3.9 percent in 2022. Weaker growth in 2020 and 2021 is consistent with IBO's forecast of a slowdown in U.S. GDP growth beginning in the middle of calendar year 2019, as upward pressure on wages and prices leads the Fed to accelerate its planned increases in interest rates, and businesses and financial markets adjust to this new environment. Finance, the sector that contributes more than any other to the city's corporate tax collections, is particularly sensitive to changes in interest rates and growth in the U.S. economy.

Unincorporated Business Tax. Whereas corporate tax receipts have continued a trend of weakness into 2018, collections from the unincorporated business tax (UBT) have been particularly strong. IBO projects that after a minor decline in 2017, UBT revenue will increase by 11.0 percent ($220 million) in 2018, bringing collections to $2.2 billion. Growth is expected to continue throughout the rest of the forecast period, but at a more moderate rate, with revenue increasing 2.8 percent ($62 million) in 2019, and an average annual rate of 4.8 percent from 2020 through 2022, reaching $2.6 billion by the end of this period. A major driver of the UBT forecast is earnings from the professional services sector, which accounts for the largest share of the city's noncorporate businesses (partnerships, sole proprietorships, and limited liability companies) subject to the tax. Despite IBO's forecast of weaker general economic performance after 2018, we expect growth in the professional services sector to soften but continue throughout this period, yielding more stable growth for UBT revenue.

IBO's forecast for total business tax revenue is 2.3 percent ($129 million) higher than OMB's for 2018, and 1.7 percent ($100 million) higher in 2019. Almost all of this is attributable to differences in expected corporate revenue. OMB projects a more substantial decline in corporate collections for 2018 at 4.3 percent ($147 million), whereas the strengthening of recent collections leads IBO to forecast a smaller decline of 1.1 percent ($38 million). Some of this difference is made up in 2019, as OMB projects even more robust recovery in corporate tax collections, growing by 8.9 percent ($295 million), compared with IBO's predicted growth of 7.9 percent ($270 million). IBO's projections of slightly higher growth in the out-years, for both corporate taxes and the UBT, result in a widening gap between the two forecasts, reaching 8.0 percent ($489 million) by 2022.

One factor that could affect business income tax collections moving forward is the shifting landscape of federal tax law, and changes to local tax law in response. New York City, like many state and city governments, uses federal definitions of taxable income and other items from federal tax returns as a starting point for calculating tax liability. In its most recent budget legislation, the State of New York made many changes to state and city income tax laws, decoupling the state and city from several provisions in the federal Tax Cuts and Jobs Act of 2017. Other federal provisions remain unaddressed, however, such as a cap on the deductibility of business interest expenses. Such issues may necessitate additional action by the state in the future. IBO's current revenue forecast is based on the assumption that the city and state have or will have effectively decoupled their business taxes from all recent changes in federal law, as intended, and therefore includes no adjustments for direct impacts of federal tax policy.

Sales Tax. The general sales tax is the city's third largest source of tax revenue, accounting for about 13 percent of total revenue from taxes. Sales tax collections were up 5.6 percent through the first three quarters of the current fiscal year. IBO projects sales tax revenue of $7.4 billion for 2018 overall, a 5.4 percent increase over 2017.

Revenue growth of 4.0 percent is projected in 2019 (to $7.7 billion) and 5.9 percent in 2020. But these growth rates are lifted by the expiration of the Sales Tax Asset Receivable Corporation (STARC) intercept three-quarters of the way through 2019. Instituted to recoup $600 million in savings owed to the state from the city's refinancing of STARC bonds, the intercept siphoned off $50 million from city sales tax collections in 2016, $200 million in 2017 and again in 2018, and is scheduled to absorb a final tranche of $150 million in 2019.

Excluding the impact of the STARC intercept, the sales tax forecast reflects the confluence of expected weakening

Impact of Sales Tax Receivable Corporation Intercept on New York City Sales Tax Revenue Growth								
	2015	2016	2017	2018	2019	2020	2021	2022
Growth With STARC	3.8%	2.5%	1.5%	5.4%	4.0%	5.9%	3.0%	3.4%
Growth Without STARC	3.8%	3.2%	3.7%	5.2%	3.3%	3.9%	3.0%	3.4%
STARC Impact on Growth	0.0%	-0.7%	-2.1%	0.1%	0.8%	2.0%	0.0%	0.0%

NOTE: 2018-2022 are forecast.

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growth in the city economy and underlying factors mediating the relationship between the economy and taxable sales.

Historically sales tax revenue growth has been constrained by a long-term trend decline in the portion of disposable personal income devoted to consumption of taxable goods and services; as is the case in many jurisdictions, the city's sales tax base has only partially adapted to the changing composition of final output and demand. But against this downward pull there is the boost to taxable sales provided by the enormous expansion of tourism and of visitor spending in New York City since the turn of the new century, with spending by international visitors playing an especially key role. Fears that current global political tensions might lead to declines in tourism have so far not been borne out.

More recently, the "retail apocalypse" overtaking brick-and-mortar sales establishments—and evidenced in the lack of growth in New York City retail employment since 2014—may accelerate the decline in the ratio of taxable sales to disposable income. But here again there is an at least partially offsetting factor, namely the expanding net that city and state sales taxation has been casting over Internet sales.

IBO's sales tax forecast essentially equals OMB's for the current year and is $68 million lower in 2019. However, OMB has yet to recognize the final tranche of STARC; otherwise IBO's forecast would run $82 million higher than OMB's in 2019. OMB's forecast exceeds IBO's each year in 2020 through 2022, although the difference is less than $100 million a year.

Spending

Much as IBO projects higher revenues than the de Blasio Administration based on the Mayor's latest budget plan, we also estimate that total city spending including city, state, and federal funds will be somewhat higher this year and next, though our estimates for total spending in 2020 through 2022 are lower than the Mayor's. IBO projects total city spending will be $90.1 billion in 2019 under the contours of the Mayor's latest budget plan—$900 million more than the $89.2 billion we estimate spending will total this year. We project total spending will rise to $93.3 billion in 2020 and reach $98.3 billion in 2022. Adjusting for the use of prior budget surpluses to prepay some expenses for upcoming years, IBO anticipates total city spending will increase from $89.0 billion in 2018 to $92.9 billion next year and grow to $94.8 billion in 2020.

Factors Driving Spending Growth. After adjusting for prepayments, very few agencies are forecast to have average annual growth that exceeds the citywide average of 2.5 percent, in fact most agencies average negative expenditure growth across the plan period. Much of the growth in spending the next four years is driven by increased spending in two areas: fringe benefits for city employees and debt service (note that most fringe benefits and all debt service are not carried within the budgets of city agencies). IBO estimates that in 2018 the city's expenditure on debt service and fringe benefits will comprise 18.2 percent of the total budget. By 2022 these two expenses will make up 21.2 percent of the entire city budget.

IBO projects that in 2018 citywide fringe benefit costs will total $10.4 billion (about 11 percent of total city spending after adjusting for prepayments). Fringe costs increase in each year of the plan period and by 2022 these costs will exceed $12.2 billion (12.4 percent of adjusted total city expenditures), an annual average growth rate of 4.1 percent. The single largest factor driving growth in fringe costs is health insurance. Even accounting for the health care savings attributed to labor settlements with the municipal unions, IBO estimates that health insurance costs will increase by an average of 5.4 percent per year from 2018 through 2022.

After adjusting for the prepayment of debt service costs, IBO estimates that the city's debt service expenditures will increase from $6.2 billion in 2018 (7.0 percent of total city spending) to $6.9 billion in 2019, an 11.2 percent increase. By the end of the financial plan period we project that debt service costs will total $8.6 billion (8.7 percent of total city expenditures), an increase averaging 8.4 percent a year

IBO Expenditure Projections *Dollars in millions*						
	2018	2019	2020	2021	2022	Average Change
Agency Expenditures	**$64,566**	**$64,025**	**$64,062**	**$64,481**	**$64,921**	**0.1%**
Fringe Benefits	10,389	10,534	11,228	11,718	12,207	4.1%
Labor Reserve	63	1,445	1,785	2,259	1,699	n/a
Total Agency Expenditures	**$75,018**	**$76,003**	**$77,075**	**$78,458**	**$78,827**	**1.2%**
Other Expenditures						
Debt Service	$6,231	$6,929	$7,511	$7,903	$8,608	8.4%
Pensions	9,632	9,852	9,903	10,162	10,367	1.9%
Judgments and Claims	712	697	712	727	742	1.0%
General Reserve	50	1,000	1,000	1,000	1,000	n/a
Capital Stabilization Reserve	-	250	250	250	250	n/a
Expenditure Adjustments	(400)	-	121	220	325	n/a
FY 2017 Budget Stabilization Account and Discretionary Transfers	(4,180)	-	-	-	-	n/a
FY 2018 Budget Stabilization Account	4,329	(3,652)	(677)	-	-	n/a
FY 2019 Budget Stabilization Account	-	825	(825)	-	-	n/a
Subtotal	**$91,392**	**$91,904**	**$95,070**	**$98,719**	**$100,119**	**2.3%**
Less: Intra-City Expenditures	($2,208)	($1,826)	($1,771)	($1,776)	($,776)	
TOTAL EXPENDITURES	**$89,184**	**$90,077**	**$93,299**	**$96,943**	**$98,343**	**2.5%**

NOTES: Expenditure adjustments include energy, lease, and nonabor inflation adjustments. Figures may not add due to rounding.

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from 2018 through 2022. The Department of Education (DOE) is the only agency projected to experience sizable real (inflation-adjusted) budget increases across the plan period. From 2018 through 2022 IBO expects DOE expenditures will grow by 2.7 percent per year, to reach $28.1 billion. Growth in DOE's city-funded expenditures is driven by increases in funds needed to cover costs from the last union settlement, a rise in Fair Student Funding, the Universal Literacy initiative, and the replacement of state aid that was anticipated but not received with local dollars.

Expenditure Re-estimates. IBO estimates that total city-funded spending will be $98 million greater in 2018 and $64 million greater in 2019 than presented in the Mayor's Executive Budget. Conversely, our forecast of city-funded spending is lower than the de Blasio Administration projects for the subsequent years of the financial plan: $76 million less in 2020, $321 million less in 2021, and $430 million less in 2022.

Lower Spending. IBO's forecast of lower overall expenditures than the Mayor presents in the Executive Budget is primarily the result of our re-estimate of the city's health insurance costs coupled with re-estimates in debt service, sanitation, and for cash assistance.

· Debt Service Savings. Although IBO projects that debt service costs will grow at a faster rate than other major city expenses, we expect these costs will be lower than the de Blasio Administration has assumed for 2019 in the Executive Budget. OMB has reduced its variable interest rate assumptions for 2018 but has left its rates for 2019 unchanged. Even with interest rates expected to continue rising, the rates assumed by OMB for 2019 are likely much higher than experience suggests. IBO's assumption of lower variable rate interest reduces our forecast of debt service costs by $33 million in 2019.

· Health Care Costs Re-estimates. The city's provision of health insurance for current and retired city employees is budgeted to total $6.3 billion in 2018. By 2022 these health care costs are budgeted to increase to $8.7 billion. Based on recent trends in spending and our own forecast of growth in health care costs, IBO estimates that the city will spend $200 million less on health care than OMB projects for 2019, with $73 million of the savings in the Department of Education. By 2022 IBO's forecast of health care spending is $890 million below OMB's, with $341 million of the savings attributable to DOE. The remainder of estimated savings in health care costs is divided among all other city agencies.

· Department of Sanitation Expenditures. IBO projects that Department of Sanitation (DSNY) expenditures will be lower than presented in the Executive Budget. Based on the department's historical spending we expect that in 2018 DSNY will spend $26 million less in city funds than currently budgeted. Similarly, IBO estimates that DSNY will require less funding than budgeted for 2019 through 2021: $27 million less in 2019, $23 million less in 2020, and $14 million less in 2021. The reduction in spending is primarily the result of over-budgeting for the costs related to the closure of Fresh Kills Landfill, offset slightly by our increased estimates for waste prevention and recycling other than personal service costs.

· City Overestimates Cash Assistance Expense. IBO projects additional expenditure savings based on the de Blasio Administration's overestimate of cash assistance costs. Based upon recent cash assistance caseloads, IBO estimates city-funded cash assistance will be lower than OMB estimates by $18 million in 2018 and $10 million in each year from 2019 through 2022. In addition, we estimate that federal funds for cash assistance will be $48 million lower than OMB estimates in 2018 and $57 million lower each year in 2019 through 2022, while state funding will be $7 million lower in 2018, and $4 million lower annually in 2019 through 2022.

Higher Spending. Savings derived from IBO's re-estimates of debt service, health care insurance, and other areas mentioned above are offset by our estimates of increased expenditures for overtime in uniformed agencies, education, homeless services, parks, the Board of Elections and the Campaign Finance Board, and the Departments of Small Business Services and Buildings.

· Uniformed Agencies Overtime Expenses. The city's uniformed agencies often underestimate their annual cost for overtime expenses. IBO estimates that over the financial plan period the budgets for the police department (NYPD), fire department (FDNY) and Department of Correction (DOC) will require a total of $500 million in additional city funds for overtime expenses.

Through March 2018 the NYPD has spent $525 million of $635 million budgeted for the department's overtime expenses. IBO estimates that the NYPD will spend an additional $25 million in both 2018 and 2019 on overtime expenses (4 percent of annual budgeted overtime expenditures). In 2020 through 2022 we estimate that the department will spend an additional $50 million annually on NYPD overtime expenses (8 percent of annual budgeted overtime expenses).

Similarly, IBO estimates that the fire department's current plan for overtime expenditures is underfunded. Through March 2018 the FDNY has spent $248 million. For 2019 the department has budgeted $253 million for overtime expenses. We assume that the FDNY will need an additional $50 million annually from 2019 through 2022 (a 20 percent increase over the annual budgeted overtime expenses).

The Department of Correction's planned expenditures for overtime are also typically less than the actual year-end totals. In 2018 so far the DOC has spent $166 million on overtime expenses. But the department's 2019 overtime budget of $157 million is less than the amount already spent this year. We estimate that DOC will need an additional $25 million of city funds each year from 2019 through 2022 (a 16 percent increase over annual budgeted overtime expenses).

The uniformed agencies, particularly the NYPD and FDNY, rely on millions of dollars from the federal and state governments to fund operations. The Executive Budget assumes $230 million of federally funded spending by the NYPD in 2018, decreasing to $15 million in 2022. Over the previous three years the NYPD averaged $290 million of federally funded expenditures. Based on the department's recent funding history, IBO estimates that the NYPD will receive an additional $25 million in 2018, $150 million in 2019 and $200 million a year in 2020 through 2022 from the federal government. In addition, IBO assumes the NYPD will receive $50 million of additional state funding each year from 2019 through 2022.

Federal funding for the FDNY has averaged $139 million over the last three years. The Executive Budget includes annual federal funding for the department that is much lower than recent experience would suggest. As a result we estimate an additional $25 million of federally funded expenditures in 2018 and $75 million annually from 2019 through 2022.

· Department of Education Re-estimates. In prior years, issues with implementation of the Special Education Student Information System hampered the Department of Education's efforts to secure reimbursement for eligible Medicaid expenses. When the budget was adopted last spring it appeared that the DOE had finally overcome the implementation issues and as a result the de Blasio Administration assumed that the DOE would be able to obtain $97 million a year in reimbursements annually. But the department has only received reimbursement for $2 million of Medicaid claims so far this year. Until

Pricing Differences Between IBO and the de Blasio Administration
Items that Affect the Gap
Dollars in millions

	2018	2019	2020	2021	2022
Gaps as Estimated by the Mayor	**$-**	**$-**	**($3,216)**	**($2,857)**	**($2,254)**
Revenue					
Taxes					
Property	$210	$381	$408	$558	$1,034
Personal Income	442	485	197	228	154
General Sales	(4)	(68)	(17)	(94)	(93)
General Corporation	109	85	170	165	350
Unincorporated Business	20	16	38	28	139
Real Property Transfer	(11)	(35)	28	39	28
Mortgage Recording	16	(3)	43	61	73
Utility	(8)	3	(5)	(16)	(22)
Hotel Occupancy	(2)	(11)	7	7	2
Commercial Rent	3	9	(1)	5	8
Cigarette	-	-	-	-	-
Other Taxes and Audits	-	-	-	-	-
Total Taxes	**$774**	**$861**	**$869**	**$982**	**$1,673**
STaR Reimbursement	-	-	-	-	-
Misc. Revenue	-	27	29	30	30
TOTAL REVENUE	**$774**	**$888**	**$898**	**$1,012**	**$1,702**
Expenditures					
Debt Service	-	$33	-	-	-
Fringe Benefits:					
Health Insurance - Education	-	73	154	264	341
Health Insurance - City University	-	3	7	11	16
Health Insurance - All Other Agencies	-	125	258	425	533
Sanitation	26	27	23	14	-
Public Assistance	18	10	10	10	10
Education	(57)	(105)	(56)	(82)	(108)
Homeless Services	(56)	(108)	(108)	(108)	(110)
Fire	-	(50)	(50)	(50)	(50)
Police	(25)	(25)	(50)	(50)	(50)
Correction	-	(25)	(25)	(25)	(25)
Parks	(4)	(10)	(12)	(12)	(12)
Board of Elections	-	(12)	(30)	(30)	(30)
Campaign Finance Board	-	-	-	-	(40)
Small Business Services	-	-	(43)	(45)	(45)
Buildings	-	-	(1)	(1)	(1)
TOTAL EXPENDITURES	**($98)**	**($64)**	**$76**	**$321**	**$430**
TOTAL IBO PRICING DIFFERENCES	**$677**	**$825**	**$974**	**$1,332**	**$2,132**
IBO Prepayment Adjustment 2018/2019	(677)	(825)	1,502	-	-
IBO SURPLUS/(GAP) PROJECTIONS	**-**	**-**	**($742)**	**($1,526)**	**($124)**

NOTES: Negative pricing differences (in parentheses) widen the gaps, while positive pricing differences narrow the gaps. Remaining banking corporation tax revenues reported with general corporation tax.Figures may not add due to rounding.

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DOE establishes a better track record for Medicaid reimbursements, it is highly unlikely that the city will be reimbursed at planned levels.

Accordingly, IBO estimates that in 2018 and 2019, DOE's Medicaid reimbursements will total $41 million each year, the amount that the department was able to recoup in 2017. We assume that by 2020 the DOE will have the special education information system fully functional and therefore we have not modified the de Blasio Administration's estimates for Medicaid reimbursement in 2020 through 2022. To offset the loss of federal reimbursements, we assume that city funds will cover the shortfall: $57 million in 2018 and $57 million in 2019.

IBO's projections of DOE spending on charter schools diverge somewhat from those of the de Blasio Administration. For 2019, we anticipate 3,115 more charter school students than projected by the Mayor. We also expect charter school enrollment to increase by 3,599 more than estimated by the de Blasio Administration in 2020, with the difference increasing to 6,930 in 2022. As a result, IBO projects that the DOE's charter school costs will be greater than planned by $48 million in 2019, $56 million in 2020, $82 million in 2021, and $108 million in 2022.

· Homeless Services Funding Shift. IBO estimates that the funding levels in the Executive Budget for the provision of homeless shelter services are consistent with current shelter census projections. However, we believe that the distribution of funding by source requires adjustment. The city assumes the cost of homeless shelter provision and is reimbursed through federal and state sources for a portion of those costs. Historically the city has received less in Federal Temporary Assistance for Needy Families reimbursements for the provision of family shelter services than is assumed in the Executive Budget. As a result, IBO projects that the Executive Budget overestimates federal reimbursement by $68 million in 2018, $111 million a year in 2019 through 2021, and $112 million in 2022. We expect that a portion of this lost funding will be made up by the state, but the preponderance will need to be funded by the city. IBO estimates that the city-funded portion of the budget for the Department of Homeless Services (DHS) will increase by $56 million in 2018, $108 million in 2019 through 2021, and $112 million in 2022.

· Parks Department Underfunding. Based upon historical agency spending over the last five years IBO projects that the parks department's budget is underfunded in areas such as auto maintenance, technical expenses, general supplies, city zoo expenses, executive management, human resources operations, and for the Parks Equity Initiative. IBO estimates that the parks department will require an additional $4 million of city funds in 2018, $10 million in 2019 and $12 million in each year from 2020 through 2022 to appropriately fund these agency operations.

· Election Related Funding Re-estimates. The city's Board of Elections (BOE) and Campaign Finance Board (CFB) budgets are often underfunded in the out-years of the financial plan. Based upon the agency's recent annual expenditure history, IBO estimates that BOE will require an additional $12 million in city funds for 2019 and $30 million a year in 2020 through 2022. Based on the CFB's expenditures in the most recent citywide election year ($54 million in 2014) IBO estimates the board will require an additional $40 million in 2022, the year of the next citywide election cycle.

· Small Business Services Additional Program Funding. In 2014 the City Council approved the one-year allocation of funds to supplement the wages of certain school bus drivers, attendants, dispatchers, and mechanics who had experienced sizable reductions to their wages following the rebidding of bus contracts. Initially the supplemental wages were to be made available for only one year and capped at $42 million. But funding has been added by the de Blasio Administration each year since 2014. In the Executive Budget OMB added $42 million in 2019 and $2.1 million in 2020 for these costs but did not include them in the remainder of the plan period. IBO assumes that the de Blasio Administration will continue the pattern of providing these wage supplements; as a result we estimate an additional $40 million in city funds will be needed in 2020, rising to $42 million a year in 2021 and 2022.

In addition, based upon historical spending patterns, we estimate that the city will continue to fund the Graffiti Removal Program. The Executive Budget includes funding for this Department of Small Business Services program in 2018 and 2019 but not in the out-years of the plan. IBO assumes an additional $3.1 million annually in city funds for 2020 through 2022 for this program.

New Spending. Unlike in prior plans, many of the largest increases in agency spending in the 2019 Executive Budget are related to unforeseen increases in the cost of city services or to account for shortfalls in state-funding estimates or unfunded state mandates. The Executive Budget does not include much additional funding related to the introduction of new policy initiatives or the expansion of existing programs.

Nearly the entirety of new agency spending in the current fiscal year occurs in just four agencies: the Department of Education, the Department of Homeless Services, the fire department, and the Department of Sanitation.

Action, or inaction, by Albany led to the need for an additional $531 million of city-funds in 2019, and approximately $295 million a year in 2020 through 2022. Unfunded state mandates account for $362 million of the 2019 increase, with $108 million attributable to the costs related to implementation of the state's Raise the Age legislation and $254 million for the city's share of the state-initiated subway action plan (the latter will also require a $164 million increase in the city's capital plan). In 2020 through 2022 unfunded state mandates account for approximately $160 million of additional need annually, including $130 million for Raise the Age implementation and $30 million annually for funding the Close to Home program. In addition to these mandates the city has included an additional $140 million in 2019 and $136 million annually in 2019 through 2022 to cover a portion of the shortfall in anticipated state aid for the city's schools.

Several increases in the Executive Budget were made to account for unanticipated shortfalls in funding for certain agency costs. The DHS budget increased by $186 million in the current year and $159 million in each subsequent year of the financial plan to account for the re-estimated cost of providing shelter for the homeless. These funds are in addition to the $150 million added to the agency for shelter costs in February's Preliminary Budget. The 2018 executive budget also includes $80 million in tuition reimbursement for special needs students who cannot be adequately served by the city's public schools and require placement in a private special needs school.

Some spending increases are triggered by nature and formulas, and are outside the city's direct control. The budget for snow removal is set by a formula in the City Charter. But snow removal this year cost $23 million, or 27 percent, more than budgeted under the formula and has resulted in formula-driven increases of nearly $14 million next year and $27 million in the succeeding years for snow removal.

Savings Plan. Since the release of the first quarter financial plan last fall OMB has initiated savings programs that provided over $4.1 billion in additional resources (both expenditure reductions and revenue increases) over the course of the financial plan period, with $1.9 billion of those additional resources identified for 2018 and 2019. The Executive Budget includes additional savings that add just under $1.4 billion in resources over the financial plan period, with $753 million of that total projected for 2018 and 2019.

OMB assigns each initiative within the savings program into one of two categories: those that generate savings by improving agency efficiency and those that generate savings through other means such as re-estimating spending or eliminating vacant positions. According to OMB, 28.7 percent of the cumulative savings program through 2022 is the result of initiatives that increase agency efficiency; for 2018 and 2019, agency efficiencies are responsible for 20.0 percent of the additional resources.

IBO's analysis of the savings program finds that the share of resources derived from efficiency initiatives is less than OMB projects: roughly 17.5 percent, or $717 million, of the total $4.1 billion savings program. In 2018 and 2019, the share of savings classified by IBO as resulting from efficiency initiatives is 10.3 percent.

Resources derived from the vast majority of the savings plan initiatives would likely have become available without any proactive effort by the agencies or OMB. Over 31 percent of the additional resources in the savings plan, $1.3 billion, in 2018 through 2022 are derived from re-estimates of debt service expenditures. Debt service cost re-estimates occur in nearly every financial plan and would have happened in the absence of the savings program. IBO estimates that an additional 21.9 percent, or $898 million, of the savings program is the result of agency under-spending. Approximately 13 percent, $519 million, of additional resources realized in the savings program are the product of agencies tapping into new revenue sources or identifying funds from other than city sources to finance portions of their expenses. Over $413 million, 10.1 percent, of the total savings program is the result of the elimination of vacancies or the accrual of budget authority that is no longer needed.

Capital Expenditures. The city-funded portion of the Executive Capital Plan for 2018 through 2022 totals $74.5 billion, $2.5 billion (3.5 percent) more than the Preliminary Capital Plan. All of the growth between the plans occurs in 2020 through 2022 as the de Blasio Administration, in an effort to "right size" the capital plan, pushed many project commitments out of 2018 and 2019 and into the plan's final three years.

The Executive Capital Plan for 2018 is $4.5 billion (23.0 percent) less than the Preliminary Capital Plan for 2018 and $1.3 billion (7.2 percent) less for 2019. In contrast, the

Executive Capital Plan for 2020 through 2022 increased by a total of $8.4 billion, a 24.7 percent increase over the Preliminary Capital Plan for those years.

As a result of shifting commitments to the latter years of the Executive Capital Plan, only 20.5 percent of the entire 2018-2022 plan is now scheduled for the current year. Meanwhile, planned commitments in 2019, the largest year of the five-year plan in dollar terms, make up only 22.7 percent of the entire plan's commitments. By way of comparison, in the Preliminary Capital Plan over 50 percent of city-funded commitments were planned for 2018 and 2019 with 26.6 percent planned for 2018 alone.

For the current year, the only areas of growth in planned commitments result from the state mandate that the city provide $164 million in capital funding for the emergency subway action plan. The parks department's capital plan increased by $515 million over the five-year capital plan period. The Executive Capital Plan includes an additional $47 million for the Coney Island Beach Operations Headquarters, $47 million for the Staten Island Indoor Pool, an additional $50 million for the Hudson River Park Trust, and $50 million for the reconstruction of the Lasker Ice Rink. Highway projects under the Department of Transportation increased by nearly $306 million in the latest capital plan, including $49 million more for pedestrian security projects and an additional $299 million for the expansion of ferry service.

Pressure Points. IBO's revenue and expenditure re-estimates reduce the budget gaps forecast for the out-years of the financial plan period, leaving shortfalls of $742 million in 2020, $1.5 billion in 2021, and $124 million in 2022. These gaps are of a size the city has readily managed in the past and are largely—if not entirely—subsumed by the reserves already carried within the budget for each year. Such optimism must be tempered by the uncertainty that exists in every budget process. State actions have already added more than $500 million in city funded spending to the budget for 2019, with the imposition of unfunded mandates and the reduction of planned support creating unforeseen city expenditure needs. With no cessation in sight to the feuding between the executives at the city and state level, the threat of additional funding responsibilities being passed along to the city cannot be dismissed.

Another potential source of fiscal pressure is the need to renegotiate many of the labor contracts settled in the Mayor's first term. Many of these contracts are expiring. The de Blasio Administration has set aside funds to cover 1 percent annual raises and stated that any additional benefits such as paid parental leave would require givebacks to offset the costs. If the Mayor moves away from this position as the contracts are settled it would be necessary to find millions of dollars not currently budgeted.

Governor Cuomo's recent issuance of an executive order declaring a public housing disaster at the New York City Housing Authority (NYCHA) and creating an Independent Emergency Manager to oversee the resolution of the problem has the potential to force the city to increase capital expenditures by millions if not billions of dollars. The Governor's order empowers the manager to create a financial plan, request funding and select contractors to complete any work determined necessary. While the manager may work within the city's existing capital budget constraints, there is the potential that city expenses on NYCHA could skyrocket.

While the doomsday prophecies related to federal funding cuts have yet to transpire, the potential for actions that would endanger the city's receipt of federal funds remains a possibility. The Trump Administration continues to pressure cities to accept its immigration policies at the risk of the loss of considerable federal funding. New York City has maintained its pro-immigration position but has yet to feel any economic pain as a result. If the federal government makes good on its threats the city could stand to lose many millions of dollars of federal funding. The President has also proposed budgets that would reduce, if not eviscerate, health and social service, transportation, and other funding that if approved by Congress would force the city to make difficult choices about which, if any, shortfalls it could cover. The continued unpredictable behavior of the Trump Administration makes certain that a high level of uncertainty will endure for the foreseeable future.

The adoption of the 2019 budget will be the first budget under the newly minted Speaker and leadership of the City Council. The Speaker has already made it clear that despite his affinity for many of the policies of the de Blasio Administration, he would not tread lightly in budget negotiations. The City Council has supported a few of the policies that the Mayor included in the Executive Budget, such as increases in Fair Student Funding and student literacy programs, but the two sides remain far apart on some of the Council's biggest expense budget priorities. The Council's support of the Fair Fare to provide reduced price MetroCards for the poor and the property tax rebate for all property owners earning less than $150,000 are estimated to cost the city $400 million annually. The Council is also urging that the Mayor add $500 million annually to the reserves already in the budget.

In addition to the major expense items, the Council has also sought to add billions of dollars to the city's capital plan. The Council's response to the Mayor's Preliminary Budget included requests for over $4 billion in additional capital funding: $2.5 billion for infrastructure at NYCHA, $789 million for the expansion of the city's solar energy capture program, $400 million to improve the combined sewer overflow system, $225 million to increase expenditures for school accessibility and school security, $79 million for a new animal shelter in Queens, $60 million for library upgrades citywide, and $30 million for the reconstruction of Orchard Beach. While capital projects are funded almost exclusively with revenue from bond sales, the issuance of additional debt would increase the city's already burgeoning debt service payments.

All Things Considered

While some fiscal observers have criticized the Mayor's Executive Budget for its growth in spending and lack of new reserves, IBO finds that a considerable portion of the new spending is driven by state actions and that the budgeted reserves are substantial. There is little in the way of new program spending and the amount of reserves built into the budget exceeds our shortfall projections in two out of the three years for which we estimate there are budget gaps.

IBO's most recent economic forecast and our re-estimates of city revenues and expenditures, suggest that the city's fiscal condition is stable, with near-term budget surpluses and future year gaps of a size that the city has routinely managed in past years. We estimate that the city will end 2018 with a surplus of $4.3 billion, $149 million more than the surplus for 2017. The surplus of $825 million we project for 2019 would reduce the 2020 gap to $742 million. Additionally, our forecasts of revenue and expenditures in the last two years of the financial plan reduce the city's budget gap in 2021 to $1.5 billion and an almost insignificant $124 million in 2022.

If the city is unable to close these gaps with additional revenues or agency cost savings, the $1.25 billion in reserves budgeted for each year of the financial plan are available to help bring the budget into balance. In addition, the city could draw on billions set-aside for the cost of future retiree health benefits, which have been used in the past to help eliminate budget gaps.

While external factors could undermine the city's financial plan, the available reserves could at least mitigate, and perhaps cover, new demands on the city's finances, depending on the magnitude of any change. The potential for continued upheaval resulting from the clash between the Governor and the Mayor and the uncertainty in funding from Washington pose one set of risks to the de Blasio Administration's financial plan and could force elected officials to make hard choices about the use of the city's reserve funds. The potential for a recession poses another and perhaps more debilitating fiscal risk. In all likelihood the city's reserves would only be sufficient in the face of a recession to buy some time while policymakers find ways to bring the budget into balance.

Although the city is carrying a record level of reserves, these funds are best thought of as way to cushion the city against fiscal or economic blows rather than a safeguard to weather all budget storms. But sizable reserves can themselves be a risk as recent events have shown. With New York City "sitting on" billions in reserve, Albany felt empowered to make decisions that will cost the city more than $500 million next year and millions more in future years.

Endnotes

[1]http://ibo.nyc.ny.us/iboreports/addressing-the-disparities-winners-losers-in-two-property-tax-reform-scenarios-april-2018.pdf

[2]Adjusted gross income, filing status, allowable itemized deductions, credits, and other items in New York State and City income tax law are defined with direct reference to analogous items in the federal law. Several changes to the federal tax code enacted by Congress in December in the Tax Cuts and Jobs Act could have directly affected state and local tax liability, such as the limits to the amounts of state and local taxes and mortgage interest payment that can be itemized as deductions. State legislation enacted as part of the recent state budget altered the state tax code and the city's administrative code to prevent many TCJA provisions from flowing through to the state and city personal income taxes.

[3]Beginning in 1999 the STAR program reduced city marginal PIT tax rates by roughly 6 percent. While this lowered city residents' PIT liability, the city's budget was made whole through a state aid payment equal to the loss in tax revenue. In previous years the state eliminated the lower marginal rates for tax filers with incomes above $500,000. In its budget for fiscal year 2017-2018, the state eliminated lower rates for all other filers, effectively raising their PIT liabilities. The state is replacing the benefit tax filers had previously received through the lower STAR rates with a credit of equal value against state income tax liability. Though the elimination of lower rates was retroactive to January 1, 2017, there was no impact on city PIT revenue until July 1, the start of the 2018 city fiscal year, when withholding tables were adjusted. The new withholding tables are boosting 2018 withholding receipts by an estimated $319 million.