A Cautiously Better Outlook: Fewer Job Losses, Higher Tax Revenues

WITH THE NATIONAL ECONOMY STARTING TO EMERGE from a severe recession and evidence suggesting that the local recession, while still painful, may not be as bad as originally projected, the outlook for city tax revenues has much improved since the current budget was adopted last spring. This suggests that the city's fiscal outlook for 2011 and beyond may be less fraught than previously thought. In this fiscal outlook report, IBO has concentrated on updating its economic and tax revenue forecasts.

Tax revenues for fiscal year 2010 are expected to total $35.5 billion, 1.9 percent higher than in 2009. Without substantial increases in the sales and real property taxes, and changes in the business income taxes that together yield an estimated $809 million in new revenues this year, 2010 would have marked a second consecutive year-over-year decline in tax collections. The expanding U.S. economy will help tax revenue grow by 7.4 percent in 2011 to $38.1 billion, when revenues finally exceed the total collected in 2008. In 2012 and 2013 tax revenue growth is expected to average 6.0 percent annually. IBO's key findings are:

• IBO’s outlook for the New York City economy is now less dark than in the previous spring’s forecast. Local job losses are now forecast to total 157,200 jobs from the third quarter of 2008 when city employment peaked at 3.8 million to mid-2010 when the losses are expected to end.

• With the exception of the financial sector, job losses to date in almost every other major sector have been less steep than anticipated, while employment in health and education actually rose.

• The turnaround in the financial sector, which has benefitted from low interest costs and government guarantees, has been particularly dramatic. IBO now projects record Wall Street profits of $59 billion this calendar year—a dizzying U-turn from the unprecedented losses of 2007 and 2008.

• With a shallower local downturn and higher Wall Street profits and compensation, tax revenues are now expected to be higher than IBO and the Bloomberg Administration anticipated last spring. IBO’s current outlook for fiscal year 2010 tax revenues is $389 million higher than the Mayor’s latest projection released November 16. Our revenue forecast for 2011 is $958 million more than the Mayor’s projection, which is largely unchanged for future years, since the spring.

Beyond the usual risks inherent in any forecasting effort, key uncertainties such as the still unclear outcome of financial regulatory reform and how New York State’s fiscal difficulties will
affect the city’s economy and budget, could significantly alter the
city’s fiscal outlook.

Careful readers will also note this year’s outlook report includes
no specific estimates of the budget gap. This is because when
the Mayor’s Office of Management and Budget (OMB) released
a first quarter budget report last month, it made almost no
changes to projections of operating expenses in the financial plan
beyond the current year. With the revenues and a few expense
items updated for the current year but the subsequent years in
the financial plan only marginally updated from last spring’s
adopted budget there are no comprehensive Mayoral estimates of
the magnitude of the budget gaps facing the city after this year.

ECONOMIC OUTLOOK

U. S. Economy. The recent U.S. downturn,
called the “Great Recession” by some, may
be over—at least based on national output.
But the recovery underway is fragile. With
continued employment losses and stubbornly
high unemployment expected to persist well
into next year and credit markets remaining
tight, near-term growth is projected to be slow.
Strong, self-sustaining economic growth is not
forecast until 2011 and beyond. Moreover, there
are significant risks to this outlook that could
delay the recovery or even plunge the economy
back into recession. (Unless otherwise noted,
all references to years in the Economic Outlook
section refer to calendar years.)

With 20 months from peak to the likely
trough, this U.S. downturn is longer and deeper
than any since World War II. But economic
growth returned in the third quarter of 2009,
when real (inflation-adjusted) gross domestic
product (GDP) increased at an annual rate
of 2.8 percent, after declining for five of the
six preceding quarters. Spending on durable
goods grew at an annual rate of 20.1 percent,
while residential investment grew at a 19.5
percent annual rate. The federal government’s
“Cash for Clunkers” program and the first-time
home buyer tax credit contributed to these
gains. Federal fiscal relief for state and local
governments helped to moderate government
job losses and tax increases. Exports benefited
by the decline of the dollar and rose at a 17.0
percent annual rate.

Although unprecedented efforts by the
Federal Reserve and fiscal policy makers have
stabilized the financial system, credit remains
constrained. The Federal Reserve has signaled
that it will not raise interest rates any time
soon, and banks appear to have regained
confidence in each other. But bank confidence

<table>
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<td>May 2009 versus November 2009</td>
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<th>IBO Economic Forecasts: May 2009 versus November 2009</th>
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<tr>
<td>National Economy</td>
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<td>Real GDP Growth</td>
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<tr>
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<td>November 0.4 -2.5 1.7 3.9 5.3 3.6</td>
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<td>Inflation Rate (CPI-U)</td>
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<td>May 3.8 -1.0 1.7 2.0 2.0 2.0</td>
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<td>November 3.8 -0.5 1.7 1.8 2.1 2.0</td>
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<td>Personal Income Growth</td>
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<td>November 2.9 -2.2 1.7 4.9 6.2 5.6</td>
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<td>Unemployment Rate</td>
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<td>November 5.8 9.2 10.2 9.0 7.1 5.9</td>
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<td>November 3.7 3.4 4.6 5.4 5.8 5.1</td>
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<td>Federal Funds Rate</td>
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<tr>
<td>November 1.9 0.2 0.4 2.1 4.0 4.5</td>
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<tr>
<td>NYC Economy</td>
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<tr>
<td>Non-farm New Jobs (thousands)</td>
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<td>May 47.7 -141.6 -84.2 33.0 69.3 54.9</td>
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<tr>
<td>November 47.7 -84.1 -45.1 42.2 71.2 73.5</td>
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<td>Employment Growth</td>
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<tr>
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<tr>
<td>November 1.3 -2.2 -1.2 1.2 1.9 1.9</td>
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<tr>
<td>Inflation Rate (CPI-U-NY)</td>
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<tr>
<td>May 3.9 -0.5 1.9 2.6 2.7 2.6</td>
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<td>November 3.9 0.2 1.7 2.5 2.8 2.8</td>
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<tr>
<td>Personal Income ($ billions)</td>
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<tr>
<td>May 432.5 420.1 424.1 440.8 465.9 500.6</td>
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<tr>
<td>November 432.8 431.4 430.2 445.3 471.1 501.0</td>
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<td>Personal Income Growth</td>
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<tr>
<td>May 4.7 -2.9 0.9 3.9 5.7 7.4</td>
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<tr>
<td>November 4.1 -0.3 0.3 3.5 5.8 6.3</td>
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<tr>
<td>Manhattan Office Rents ($/sq.ft)</td>
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<td>May 84.16 69.59 59.01 56.11 56.53 59.39</td>
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<tr>
<td>November 84.16 69.79 60.90 54.53 52.33 53.69</td>
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</table>

SOURCE: IBO.
NOTES: Rates reflect year-over-year percentage changes except for unemployment, 10-Year Treasury Bond 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.
in “Main Street” remains low. Particularly hard hit have been small businesses—which historically account for much of the new job creation in the economy. These firms have faced great difficulty in getting financing to order the inventory that will be needed when demand returns.

U.S. employment data for October show a one-month loss of 190,000 jobs. This loss was sharply smaller than the monthly losses earlier in this recession. Since employment peaked in December 2007, 7.3 million jobs have been lost, with over half lost in the six months between November 2008 and April 2009, when monthly losses each exceeded 500,000 and averaged 645,000.

The smaller job losses in October resulted from a decline in the number of workers being laid off. However, while businesses have curtailed layoffs, there is little evidence that hiring has begun to expand. In past recessions, there has generally been a lag between the time output picks up and businesses begin to hire. In this interim period, businesses typically increase hours for remaining employees and hire temporary workers. But so far in the current recovery, hours worked remain at record lows and temporary jobs are actually declining.

The U.S. unemployment rate climbed to 10.2 percent in October, its highest level in decades. Measures of underemployment, which include workers employed part-time involuntarily, also climbed.

Looking forward, IBO expects the nation’s output to grow weakly through late next year, with GDP rising just 1.9 percent in 2010. The foreclosure crisis, which is far from over, will remain a significant impediment to growth. According to Moody’s Economy.com, a full 8 percent of 52 million outstanding first mortgage loans are at risk of foreclosure. The Obama Administration’s loan modification plan may help some of these homeowners, but most are not expected to qualify. Meanwhile, housing prices—and thus household wealth—are expected to decline further, putting an additional drag on consumer spending. Declining fiscal stimulus spending is also expected to become a constraint on GDP growth by this time next year. Household spending is another factor underlying IBO’s forecast of weak GDP growth in 2010, with personal savings rates expected to remain higher than in recent years. IBO forecasts continued U.S. job losses through mid-2010, with the total job loss for the recession reaching 7.8 million.

With continuing job losses and slow hiring, IBO projects the unemployment rate to increase from an average of 9.2 percent in 2009 to 10.2 percent on average in 2010. The unemployment rate typically increases early in an economic recovery as the number of job-seekers encouraged to return to the labor force in search of employment exceeds the number of new jobs being created.

Stronger, self-sustaining growth is forecast for subsequent years, with GDP growth projected to rebound to 3.9 percent in 2011 and 5.3 percent in 2012, before moderating to 3.6 percent in 2013. Similarly, annual employment growth accelerates from 2.1 percent in 2011 to 3.5 percent in 2012. With the resumption of employment growth, the rate of unemployment falls below 10 percent early in 2011 and continues to decline steadily but gradually, reaching 5.9 percent in 2013.

After deflation of 0.5 percent this year due to the economic downturn, the Consumer Price Index is expected to rise 1.7 percent in 2010. Despite stimulative fiscal and monetary policies that are likely to continue in the next couple of years, the inflation rate is expected to stay under 2 percent through the middle of 2011 because high unemployment and unused productive capacity will dampen growth and inflationary pressures.

**New York City Economy.** New York City’s economy turned down after the national economy, but IBO expects local employment to turn up at the same time national employment resumes growing in the third quarter of 2010—a much smaller cumulative employment loss than was predicted last spring. IBO has slashed its projected employment loss to 157,200 jobs, or 4.1 percent of the city’s recent peak employment in the third quarter of 2008, with a small gain in public-sector employment partially offsetting the loss of 164,000 private-sector jobs. Last May, IBO’s forecasted loss was 254,500 jobs, including 233,600 jobs in the private sector.

IBO’s less pessimistic forecast of local job losses is not attributable to fewer expected losses in the financial sector. In our current forecast, the financial activities sector (excluding real estate) accounts for an even larger share of the city’s expected employment loss—59,000 jobs (16.9 percent of the sector’s recent peak employment level), with about two-thirds of these jobs already gone and losses expected to continue through the second quarter of 2012. (In May, the projected loss was 56,800 jobs, or 16.2 percent of peak employment.) Over two-thirds of the projected employment decline for finance consists of 40,700 jobs in the high-paying securities industry, more than one-fifth of securities employment at its most recent peak in the first quarter of 2008.

For Wall Street firms that have survived the financial crisis, however, the current picture is surprisingly bright. With greatly reduced interest expenses resulting from interest costs near historic lows, various forms of Federal Reserve backing for
Job Losses Are Projected for All but One Industry

Thousands of Jobs

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<thead>
<tr>
<th></th>
<th>-80.0</th>
<th>-60.0</th>
<th>-40.0</th>
<th>-20.0</th>
<th>0.0</th>
<th>20.0</th>
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<td>Securities subsector (2008:Q1-2012:Q2)</td>
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<td>Professional and business services (2008:Q3-2010:Q3)</td>
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<td>Construction (2008:Q1-2010:Q2)</td>
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<td>Retail (2008:Q3-2010:Q4)</td>
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<td>Manufacturing (2008:Q3-2010:Q2)</td>
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<td>Information (2008:Q3-2011:Q3)</td>
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<td>Transportation (2008:Q2-2010:Q2)</td>
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<td>Leisure and hospitality (2008:Q3-2010:Q2)</td>
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<td>Health, education, and social services (2008:Q3-2010:Q2)</td>
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</table>

SOURCE: IBO.

NOTE: Employment peaks and projected troughs vary by sector. The recent peak of total private-sector employment was 2008, third quarter and the projected trough is 2010, second quarter, and this time period is used to determine peak-to-trough employment changes for manufacturing, which steadily sheds jobs, and health, et al., which steadily gains employment.

financial firms’ securities and loans, the field of competitors reduced, and workforce and other operating costs down, securities firms have enjoyed staggering profits so far this year. IBO projects total Wall Street profits of $58.9 billion for 2009 overall. While profits of this magnitude are not expected to continue, healthy profits of $16.2 billion are expected for next year, followed by annual profits of $12 billion to $14 billion during the rest of the forecast period.

The professional and business services sector, which includes temporary help, legal services, advertising, and many other support services, is expected to lose 46,600 jobs (7.6 percent of the industry’s peak employment) by the third quarter of 2010. With tight credit markets, a glut of new apartments, and high office vacancy rates, the construction industry is also suffering badly. IBO projects a loss of 20,500 jobs, or nearly one out of six construction jobs held in the first quarter of 2008, when the industry hits bottom in mid-2010.

Retail trade employment is expected to bottom out in the fourth quarter of 2010, after shedding 19,300 jobs (6.4 percent), while the leisure and hospitality industry is projected to lose 9,900 jobs, or 3.2 percent of its peak employment, by the second quarter of 2010. These industries could benefit from the weakened dollar, which helps attract high-spending foreign visitors.

The health and education sector (including social assistance) is the only major industry without projected losses during the downturn, and it is expected to maintain healthy growth throughout the forecast period. From the most recent peak during the city’s downturn. Included in the city’s expected job loss between the third quarter of 2008 and the second quarter of 2010 is a loss of 16,300 jobs from manufacturing (a 17.2 percent decline).

By the third quarter of 2010, total employment in the city is expected to resume growing, albeit slowly for several quarters. IBO forecasts that small employment gains for construction, transportation, and leisure and hospitality will initially combine with ongoing employment growth in health and education to more than offset continuing losses in the financial sector and other industries. Growth in professional and business service employment is expected to resume by the fourth quarter, to be followed by upturns in retail and information in 2011. In the second half of 2012, employment in finance is expected to turn around and grow again, though at an anemic rate. By the end 2013, the industry is projected to have 15.4 percent fewer jobs than its recent peak.

Overall employment growth is expected to accelerate from the second half of 2010 through late 2012. After that, employment growth moderates. IBO forecasts annual employment growth of 1.9 percent for 2013. As compared to the U.S. economic recovery, the New York City recovery—measured by employment—is expected to be somewhat slower. IBO forecasts a return to our most recent peak employment level of 3.8 million in the first quarter of 2013, while the U.S. is expected to regain its recent peak employment by the third quarter of 2012.

IBO now projects local personal income declines of 0.3
percent for both 2009 and 2010. The outlook for this year is significantly brighter than IBO’s May forecast of a 2.9 percent decline, in part because there have been fewer job losses this year than previously forecast. Although the employment forecast for the financial sector has not improved and wage data from the federal Quarterly Census of Employment and Wages (QCEW) for the first quarter of 2009 show a sharp drop in financial sector wages from a year earlier, the Wall Street profit forecast for 2009 has improved greatly. Wall Street bonuses at the end of this year are expected to nearly equal the income lost with the citywide projected loss of 84,100 jobs in 2009. Additional job losses are predicted for the first half 2010, but Wall Street bonuses in the first quarter combined with some job growth in the second half of the year are expected to keep the decline in overall 2010 personal income similar to the decline this year.

Historical data from the QCEW show that total New York City wages earned outside the financial industry are highly correlated with wages earned inside the industry. IBO forecasts a step up in annual personal income in 2011 as employment starts to expand, but significant annual growth rates of 5.8 percent to 6.3 percent are not expected until subsequent years when financial sector employment again begins to expand.

**Risks to the Economic Forecast.** IBO’s national and local economic forecasts are subject to various risks. One can argue that the federal fiscal stimulus spurred the consumer and business spending that fueled last quarter’s growth in U.S. output (GDP). But that stimulus has only a limited lifespan. If stimulus spending phases out as scheduled over the next year, it remains to be seen whether the U.S. economic recovery will be strong enough to become self-sustaining.

In March 2010, the New York State Department of Labor will release newly "benchmarked" data on New York City employment. The benchmarked data, which are based on administrative records for all workers covered under the state's unemployment insurance system, are more accurate than the estimates generated by the department’s monthly survey of payroll employment. The difference between the benchmark and the survey data is often particularly large during recessions and transitional periods, because it is very difficult to measure the number of establishments being created or going out of business through survey responses. In March 2009, the U.S. Bureau of Labor Statistics released preliminary figures suggesting that U.S. payroll employment was 0.6 percent (824,000 jobs) lower than indicated in the monthly survey; final estimates of the U.S. benchmarking will be released in February 2010. It is not known at this time if the benchmarking revision of the city's employment due out the subsequent month will also be negative.

There are also risks to both the national forecast and, especially, the local economic outlook from uncertainty about the long-term effects of potential regulatory reforms affecting financial firms and markets. Reforms are likely to include requirements that firms hold more capital for certain investments or trades in order to decrease firms’ leverage and reduce risk. There are also proposals for greater transparency in markets for derivatives and in the operations of other financial firms such as hedge funds. Depending on the outcome of these decisions, New York could wind up with a less profitable but potentially less volatile industry at the core of its economy. In the near term, banks’ choices of how much of this year’s bonuses to pay in stock will affect how soon and how big the impact on tax revenues will be.

**REVENUE OUTLOOK**

With an improved outlook for both the national and local economy, plus enacted increases in a couple of major taxes, IBO has increased its forecast of New York City tax revenue significantly in the current year and the out-years of the financial plan period. (In this section, years refer to fiscal years, unless otherwise noted.) Total tax revenues, including those dedicated to the Transitional Finance Authority, are now projected to equal $35.5 billion in 2010, $649 million (1.9 percent) more than total collections in 2009. With economic growth expected to gain momentum by the end of calendar year 2010, the city’s tax receipts are expected to increase more rapidly in future fiscal years. The forecast for 2011 total tax revenue is $38.1 billion, 7.4 percent growth over 2010. The forecast for 2012 and 2013 are $40.0 billion and $42.8 billion, respectively—annual growth of 6.0 percent on average for the two years.

The modest 1.9 percent tax revenue growth that IBO now forecasts for 2010 stands in contrast to IBO’s May forecast, which projected that revenue this year would be 6.3 percent less than anticipated 2009 collections. IBO has increased its 2010 forecast by $2.6 billion, of which $809 million (31 percent) reflects several tax policy changes—sales tax increases and a package of business tax reforms—that had been proposed at the time the budget was adopted last June, but were not enacted until later in the summer. With job losses not as severe as previously projected and the expectation of substantial bonus compensation, the personal income tax forecast has been revised sharply upward, by $724 million. The projection of record-breaking 2009 profits in the securities industry have generated large increases in the forecasts of the three business income taxes—increases which total $524 million (including $159 million resulting from the enacted tax reforms). An improved outlook for sluggish property markets has led to increases in the mortgage recording and real property transfer tax projections,
Despite the upward revisions since May in IBO’s annual forecasts for most of the major tax sources, our current forecast for 2010 still incorporates declines from 2009 in revenues from the business income, personal income, real property transfer, and hotel occupancy taxes. Of the major taxes, revenues are projected to increase in 2010 for only the property, sales, and mortgage recording taxes, with rate changes accounting for most of the sales tax increase and for about 40 percent of the property tax increase. After 2010 growth resumes for virtually all taxes, with the business income taxes, personal income tax, and transfer taxes growing at the fastest rates.

OMB’s November tax revenue update was almost entirely limited to 2010. OMB raised its 2010 tax revenue forecast by $1.6 billion to $36.0 billion, with $809 million of the increase due to adoption of the changes in tax policy. Beyond the effect of the tax changes, there are large increases since June in the 2010 forecasts of the personal income tax, the banking corporation tax, the unincorporated business tax, and revenue from business tax audits. IBO’s outlook for tax revenues for 2010, which had been lower than OMB’s last spring, now exceeds OMB’s latest forecast by $389 million.

The projected cumulative 28.9 percent fall in business tax revenues from 2007 to 2010 would be the worst in city history. In contrast to 2008 and 2009, when receipts of at least one of the three taxes grew (the UBT in 2008 and the BCT in 2009), IBO forecasts declines in 2010 of all three business taxes. The current plunge reflects the staggering $62.8 billion in losses by New York Stock Exchange member firms from the middle of calendar year 2007 through the end of calendar year 2008, as well as the broader contraction in the city economy where real gross output declined by an estimated 3.1 percent from the third quarter of calendar year 2008 to the second quarter of 2009.

Though declines are projected for 2010, IBO has raised its forecast of revenues from each of the three taxes, the result of better-than-expected performance and improved outlook for the city economy since May—especially in the (relatively volatile) components that pertain most closely on the business tax base. Private payroll employment in New York City is now expected to decline by far less than previously predicted, the current estimate of gross city product (GCP) for calendar year 2009 is 4.4 percent

### IBO Tax Revenue and STAR Aid Forecasts

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<thead>
<tr>
<th>Tax Revenue</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>Average Change</th>
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<td>Property</td>
<td>$14,338</td>
<td>$16,038</td>
<td>$17,198</td>
<td>$17,753</td>
<td>$18,313</td>
<td>6.3%</td>
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<td>Personal Income</td>
<td>$6,588</td>
<td>$6,507</td>
<td>$7,170</td>
<td>$7,588</td>
<td>$8,364</td>
<td>6.1%</td>
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<td>General Sales</td>
<td>$4,594</td>
<td>$4,881</td>
<td>$5,266</td>
<td>$5,539</td>
<td>$6,112</td>
<td>7.4%</td>
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<tr>
<td>General Corporation</td>
<td>$2,320</td>
<td>$2,226</td>
<td>$2,595</td>
<td>$2,849</td>
<td>$3,193</td>
<td>8.3%</td>
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<tr>
<td>Unincorporated Business</td>
<td>$1,785</td>
<td>$1,517</td>
<td>$1,579</td>
<td>$1,672</td>
<td>$1,839</td>
<td>0.7%</td>
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<td>Banking Corporation</td>
<td>$1,099</td>
<td>$531</td>
<td>$595</td>
<td>$741</td>
<td>$873</td>
<td>-5.6%</td>
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<tr>
<td>Real Property Transfer</td>
<td>$742</td>
<td>$663</td>
<td>$691</td>
<td>$778</td>
<td>$905</td>
<td>5.1%</td>
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<td>Mortgage Recording</td>
<td>$515</td>
<td>$537</td>
<td>$594</td>
<td>$647</td>
<td>$725</td>
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<td>Utility</td>
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<td>$405</td>
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<td>$431</td>
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<td>Hotel Occupancy</td>
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<td>$333</td>
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<td>Cigarette</td>
<td>$96</td>
<td>$97</td>
<td>$95</td>
<td>$94</td>
<td>$92</td>
<td>-1.1%</td>
</tr>
<tr>
<td>Other Taxes, PILOTs, and Audits</td>
<td>$1,422</td>
<td>$1,188</td>
<td>$998</td>
<td>$1,001</td>
<td>$1,000</td>
<td>-8.4%</td>
</tr>
<tr>
<td><strong>TOTAL TAXES</strong></td>
<td>$34,823</td>
<td>$35,472</td>
<td>$38,089</td>
<td>$39,991</td>
<td>$42,784</td>
<td>4.7%</td>
</tr>
<tr>
<td><strong>STAR Aid</strong></td>
<td>$1,188</td>
<td>$913</td>
<td>$962</td>
<td>$1,014</td>
<td>$1,097</td>
<td>-2.0%</td>
</tr>
<tr>
<td><strong>Total Taxes with STAR</strong></td>
<td>$36,011</td>
<td>$36,385</td>
<td>$39,051</td>
<td>$41,005</td>
<td>$43,881</td>
<td>4.5%</td>
</tr>
</tbody>
</table>

**SOURCE:** IBO.

**NOTES:** Personal income tax includes revenue dedicated to Transitional Finance Authority debt service. Figures may not add due to rounding.

Business Income Taxes. For the current year and the out-years, IBO has substantially increased its forecasts of revenues from New York City’s three business income taxes: the general corporation tax (GCT), banking corporation tax (BCT), and the unincorporated business tax (UBT). Still, projected 2010 revenue from the three taxes together—$4.3 billion—is 17.9 percent less than collections last year and 28.9 percent less than the $6.0 billion revenue peak in 2007. A $1.7 billion fall in business tax revenue would be record-breaking, the result of the financial crisis and ensuing recession. However, the quick reversal of fortune on Wall Street and the expectation of an ongoing recovery by the end of calendar year 2010 underlie the forecast of 11.3 percent average annual revenue growth from 2011 through 2013. IBO’s forecast incorporates the effects of the Business Tax Conformity Package enacted in Albany, which is discussed below.
higher than IBO’s May projection, and the capital value-added portion of GCP (the remainder after subtracting employee compensation) is 8.7 percent higher. Most dramatic of all is the turnaround in the prognosis for Wall Street profits. In May we expected a loss of $4.7 billion in calendar year 2009. Now, however, IBO projects record profits of $58.9 billion in 2009—a dizzying U-turn from the unprecedented losses in calendar years 2007 and 2008. While the surge of Wall Street profits is certainly welcome news for the city’s fiscal condition, a turnaround in financial firms’ tax liabilities will not be as dramatic. Firms will be able to carry forward losses from prior years to offset income and dampen liability in the current and future fiscal years.

The improved outlook for city employment, output, and Wall Street profits has also increased our estimates of business tax revenues after 2010. Collections are expected to resume growing in 2011 through 2013 yet combined revenue in 2013 is $5.9 billion, still below the peak reached six years earlier. The projected revenue trajectories of each business income tax are reported below. Note that without the impact of federal stimulus provisions and the business tax conformity package, IBO estimates that the 2009 decline would have been $155 million (4.9 percent) and the projected 2010 decline $1 billion (16.3 percent).

**Business Tax Conformity Package.** The federal stimulus package enacted earlier this year accounts for the loss of considerable amounts of BCT and GCT revenue due to write-offs for accelerated depreciation, at least through 2011. But these losses are more than offset by the effects of the Business Tax Conformity Package enacted in Albany this summer. The conformity package comprises numerous provisions with a variety of revenue-raising and revenue-reducing effects on city revenue. Combined financial reporting requirements affecting corporate affiliates, real estate investment trusts, and regulated investment companies will have one of the largest effects, increasing business tax revenues in 2010 by an estimated $132 million, rising to $205 million in 2013. Phasing in a single-sales factor formula for apportioning business income to New York City, to replace the current three-factor (property, payroll, and sales) formula, will reduce business tax revenue, by an estimated $38 million in 2010, rising to $174 million in 2013 and by even greater amounts in later years. Raising the UBT credit will completely offset UBT liability for businesses with incomes under $100,000 and reduce the tax’s revenues significantly.

Because the various components of the reforms have a variety of sometimes contradictory effects, their combined impacts on each of the business income taxes differ significantly in direction over time as well as magnitude. Together the reforms are expected to progressively decrease UBT receipts over time, by an estimated $21 million in 2010 and $62 million in 2013. In contrast, the package is expected to progressively increase BCT revenue, by $46 million in 2010 rising to $112 million by 2013. The effect on the GCT is also to increase revenue, but by smaller amounts each year—$132 million in 2010 falling to $88 million in 2013. (The reforms also altogether raise minor amounts of utility and hotel tax revenues.)

**General Corporation Tax.** GCT revenue fell by $193 million (6.2 percent) in 2008 and $612 million (20.9 percent) in 2009. For the current fiscal year, IBO projects a further $94 million (4.1 percent) decline in GCT revenue, a relatively small amount in comparison to the losses of the two previous years. Indeed, absent the federal stimulus and the tax conformity package, the GCT would be projected to eke out a $1 million gain in 2010. For 2011 through 2013, IBO forecasts a return to relatively robust (though by no means record-setting) growth—an average rate of 12.8 percent per year. The 2013 GCT forecast is $3.2 billion, $68 million (2.2 percent) above the 2007 revenue peak. Since the 2010 budget was adopted, OMB has not changed its GCT forecast, which for 2010 is $70 million less than the IBO projection.

**Banking Corporation Tax.** The BCT is an extremely volatile tax, plunging $590 million (48.4 percent) in 2008, jumping $471 million (74.9 percent) in 2009, and now projected by IBO to drop again by $568 million (51.7 percent) in 2010, to $531 million. This decline is roughly in line with the percentage fall of BCT revenue in the first quarter of the fiscal year. With the faster economic growth after 2010 and the increasing boost from the tax conformity package, BCT is expected to increase by an annual average of 18.1 percent from 2010 through 2013—brisk but far from the fastest, three-year growth rates on record. By
2013, BCT revenue is projected to be $873 million, far less than the $1.2 billion received in 2007. The Mayor’s budget office has increased its 2010 BCT forecast by $150 million—a larger upward revision than IBO made—and the OMB projection is $144 million greater than IBO’s.

Unincorporated Business Tax. UBT revenue peaked at $1.9 billion in 2008, a year later than GCT and BCT revenues. The UBT slipped 3.7 percent ($68 million) in 2009, the largest percentage decline in the history of this unusually shock-resistant tax. IBO projects a much larger $267 million (15.0 percent) revenue fall-off in 2010, to $1.5 billion; only a small amount of the decrease will be due to the $21 million in small business tax relief included in the Business Tax Conformity Package. Through the first quarter of fiscal year 2010, UBT receipts are 8.0 percent less than in the same quarter of 2009. From 2010 through 2013 IBO forecasts an average of 6.6 percent UBT growth per year, moderate in comparison to the pace of the other two business taxes. OMB has increased its UBT forecast for 2010 by $100 million above the level in the 2010 Adopted Budget, about half the increase IBO made, and its forecast is now slightly larger than IBO’s, by $16 million.

Personal Income Tax. With the near-term economic outlook looking brighter (if not bright), IBO has substantially increased its forecasts of personal income tax (PIT) collections for the current fiscal year and the following two years. IBO is now forecasting only a small decline in PIT revenue for 2010, from $6.6 billion to $6.5 billion. (All amounts include PIT revenue dedicated to the Transitional Finance Authority.) The 2010 projection is $724 million (12.5 percent) more than IBO had projected in May. After 2010, when local employment begins to increase again and the nation’s economic recovery strengthens, PIT growth is expected to become robust. As with the current year forecast, the new forecasts of 2011 and 2012 revenue are also higher than the May forecasts, but by smaller amounts. Projected 2013 revenue remains almost the same.

For 2010 IBO forecasts a 1.2 percent decline in PIT revenue, a far smaller decline than it had projected in May. Part of the increase in projected 2010 revenue comes from withholding. The forecast of withholding collections is 5.1 percent less than 2009 withholding, but this decrease is less than what we had projected in May because the number of jobs the city has lost during the recent recession is less than previously forecast. Also the record amount of profits Wall Street firms earned during the first half of this calendar year will lead to a sharp increase in bonus compensation in the coming months—by an estimated 40 percent at investment and commercial banks according to a recent state Comptroller report on New York City’s securities industry. However, to the extent that firms’ shift towards stock options and away from cash, the impact on city tax revenues will be muted.

The 2010 forecast incorporates a 16.3 percent decline in estimated payments revenue, but still relatively less than both the year-to-date decrease in collection and the projected decline in May. The upturn in financial markets and higher projections of capital gains realizations are expected to generate substantial increase in final estimated payments of tax year 2009 liability, which will be made mostly in January 2010. Also boosting the 2010 forecast are an expected decline in refunds (relative to both 2009 refunds and IBO’s May forecast) and a jump in revenue from offsets, an accounting adjustment between the city and the state, which collects PIT revenue for the city. OMB also increased its 2010 PIT forecast but by a much smaller amount ($292 million) than did IBO; and our 2010 forecast is $228 million more than OMB’s.

After 2010, when both the national and city economies are expected to resume solid economic growth, IBO forecasts robust PIT growth, averaging 8.7 percent from 2010 to 2013. The projections of employment and personal income in the city for calendar years 2010 and beyond are higher than they had been in the spring, and the PIT revenue forecast for 2011 is $7.2 billion, 10.2 percent greater than 2010 collections. Because the expiration of preferential tax rates on capital gains income at the end of calendar year 2010 is expected to generate a run-up in capital gains realizations late next year, estimated payments are expected to surge in 2011. The 2011 forecast for the PIT overall is $439 million (6.5 percent) greater than what had been projected in May. Projected revenue growth in 2012 is 5.8 percent, when over a year of expanding employment in the city is expected to generate strong 9.5 percent withholding growth that will offset the decline of capital gains revenue from the spike expected in 2011. Continued employment and withholding growth and a rebound in estimated payments are expected to contribute to a further increase in PIT revenue, from a projected $7.6 billion in 2012 to $8.4 billion in 2013.

Transfer Taxes. Tentative signs of a modest recovery in the real estate market, a general improvement in the economic outlook, and the strength of collections to date in the current fiscal year have all led to increases in IBO’s forecasts of the city’s two property transfer taxes: the real property transfer tax (RPTT) and the mortgage recording tax (MRT). Combined revenues of the two are projected to total $1.2 billion in 2010, a decline of almost two-thirds from the 2007 peak of $3.3 billion. But the outlook for each tax in the current year differs: compared to 2009, IBO forecasts a $79 million (10.6 percent) decrease
in RPTT receipts to $663 million, but a modest $22 million increase in MRT collections to $537 million. After 2010 RPTT revenue growth resumes and MRT growth accelerates, each at double-digit rates from 2010 to 2013 as real estate markets—first residential and then commercial—increasingly gain strength. But even with the forecasts of accelerating revenue growth, in 2013 transfer tax revenues will total an estimated $1.6 billion, less than half the 2007 peak and similar to the level of 2004.

When residential and commercial markets were booming earlier in the decade, transfer tax receipts provided a disproportionate share of the run-up of city tax revenue, which expanded at an average annual rate of 11.7 percent from 2002 to 2007. Since 2007 collection of these taxes has slumped along with the real estate markets. It is still too early for definitive conclusions about the extent to which real estate markets will recover from their downturn in the current recession, but there are some indications of improved conditions.

The aggregate value of residential sales increased slightly over the six months ending September 30, but is still at pre-2003 levels. After bottoming out in the second quarter of calendar year 2010, the median price of one-, two-, and three-family homes outside Manhattan rose in the third quarter by 11.5 percent to $435,000. However, the number of sales declined slightly, and is only about half the level that prevailed earlier in the decade. Also from the second quarter to third quarter, the number and aggregate value of sales of Manhattan apartments (both coops and condominiums) increased, though the median sales price dipped slightly, to just under $800,000.2

The commercial real estate market continues in a deep slump. Transactions valued at over $500 million during fiscal years 2006 through 2008 were responsible for a significant share of transfer tax revenue, but they have practically disappeared, dropping from 15 taxable transactions in 2007 to none in 2009. So far this fiscal year there has been one transaction over $500 million (815 Eighth Avenue). Nevertheless, there are two factors that may stimulate an increase in commercial real estate activity, if not higher prices. First, the continued weakness of the dollar, combined with low interest rates and prices that have dropped significantly from their peak, make commercial real estate in New York City increasingly attractive to foreign investors.

Second, commercial owners who bought at or near the peak of the market may increasingly find it difficult to hold on to their properties. There have been several high-profile examples of these commercial “distress sales,” and it is widely reported that the massive Stuyvesant Town/Peter Cooper Village apartment complex may soon join the list.

Mortgage Recording Tax. The modest 4.3 percent rise in MRT revenue projected for the current year reflects an anticipated increase in refinancing, as projected by the Mortgage Bankers Association, and relatively strong collections in the year’s first quarter. MRT collections are projected to increase by 10.6 percent in 2011. Refinance activity generates MRT but not RPTT revenue, and though the share of total mortgage activity due to refinancing is projected to decline after 2011, MRT growth is expected to remain strong—averaging 10.5 percent in the next two years and reaching $515 million by 2013. For all but 2013, these forecasts are roughly 5 percent to 7 percent higher than the amounts IBO projected in May.

Real Property transfer Tax. The projected 10.7 percent decline in 2010 RPTT revenue is less than half, in percent terms, of what IBO had forecast in May. An upturn of RPTT collections is forecast for 2011, when projected revenue grows by 4.2 percent, and then accelerates in the next two years, when commercial property sales rebound and increase at a faster pace than residential sales. From 2011 to 2013, RPTT revenue is projected to grow at an average annual rate of 14.4 percent and reach $905 million. In each fiscal year, the current IBO forecasts are roughly 5 percent to 10 percent higher than the May forecasts.

In contrast to the increases in transfer taxes that IBO has made for 2010, OMB lowered its forecasts. IBO’s forecasts of the MRT and RPTT are, respectively, $89 million and $97 million above OMB’s.

Real Property Tax. The city’s real property tax (RPT) collections have held up during the economic crisis and real estate market contraction. The recent resiliency of the property tax has less to do with real estate market conditions than with the tax’s structural stability—as well as an increase in the tax rate. IBO forecasts an increase in RPT revenue from $14.3 billion in 2009 to $16.0 billion in 2010—an 11.8 percent increase that partially offsets projected revenue declines of almost all other major taxes. Continued revenue growth throughout the financial plan period is also expected, though at slower rates. Due primarily to higher final assessments in 2010 and a lower estimate of delinquencies (nonpayment of the tax), IBO’s RPT forecasts are higher than those made in May.

IBO’s forecast reflects a higher tax rate that began to take effect last year and suspension of the rebate program in 2010 and going forward. Unlike other taxes, the city has authority to change the property tax rate without state legislative action. As a result, Mayors and City Council Members often consider increases in the property tax during fiscal difficulty, as was the case last winter. In December 2008, the city rescinded a 7
percent tax cut that had been enacted in June 2007. This rate increase was phased in—half in 2009 and half now in 2010. This action boosted RPT collections by $591 million in 2009 and, with the tax cut fully reversed, by $1.3 billion to $1.5 billion in subsequent years. Additionally, as of fiscal year 2010, the city has ended the $400 homeowner rebate enacted in 2005, which will increase RPT revenue by $255 million annually.

The 2010 forecast is roughly $275 million more than what IBO had forecast in May, an upward revision that stems from two factors. First, the final assessment roll for 2010 came in higher than IBO forecast, especially for utility property that is assessed by the state, and for commercial property. Second, IBO has reduced the forecast for the property tax reserve by about $100 million. A portion of the total levy (what property owners are billed) is set aside in a reserve that accounts for abatement programs, delinquencies, prior-year collectables, refunds, and cancellations (reductions in tax bills by the Tax Commission), with RPT revenue equaling total levy minus the reserve. Given the weak economy, IBO had forecast higher delinquencies and more appeals of assessments. Preliminary data for 2010 suggest, however, that delinquency and cancellations—two of the largest components of the reserve—will not be as high as forecast, leading to a downward revision of the reserve.

Property tax revenue is expected to grow 11.8 percent in 2010—an increase of $1.7 billion. As in 2009, collections this year would have increased even if the rebate program continued and the tax rate were not enacted. This is due to the structural stability of the tax, whereby changes in market conditions, both positive and negative, are only gradually reflected in assessments and tax bills. Despite the general weakness of real estate markets, billable assessed value—the base for computing the tax—grew by 6.7 percent this year, reflecting the pipeline of assessment increases from prior years (when property values climbed) still being phased in.

Due to the gradual rate at which the real estate contraction is reflected in assessments, IBO forecasts billable assessed value to grow another 6.8 percent in 2011, before slowing to 3.7 percent in 2012 and 3.1 percent in 2013. This slowdown in assessment growth becomes apparent in the latter years of the forecast.

The IBO forecast for 2011 is $571 million higher than our forecast in May. A significant share of the increase in 2011 is simply a reflection of the higher assessments seen in the final 2010 assessment roll. There was, however, some limited change in the forecast of growth rates for specific property types. IBO is now forecasting slightly slower growth among small homes and commercial property, but faster growth among larger residential buildings and utility property. Also, since May IBO has reduced the 2011 forecast for delinquencies and cancellations by around $200 million. The 2012 and 2013 RPT forecasts have also been revised upward, by smaller amounts.

**Class 1.** The market value of small homes in Class 1 (mainly one- to three-family homes) on the assessment roll has declined the last two years, by a cumulative 5.9 percent. This decline largely reflects property markets in calendar years 2007 and 2008 when the local housing market was holding up better than markets elsewhere. The decline will accelerate, however, as more recent prices begin to be reflected in the assessment roll. IBO forecasts continued market value declines, of 8.9 percent in 2011 and 3.2 percent and 1.6 percent in 2012 and 2013, respectively. Due to the cap in assessed value growth, while market value grew an average of 14.6 percent from 2005 to 2008, billable assessed value had been growing by only 4.8 percent a year. The recent sustained declines in market value are evidenced in billable assessed value growth of 1.1 percent a year from 2010 to 2013. (Assessed value continues to grow in the face of market value decline because many properties in Class 1 are assessed at well below their target assessment ratio of 6 percent—for 2010 the average assessment ratio is 4.5 percent.)

**Class 2.** Residential property in Class 2 (rental buildings and most cooperative and condominium buildings) saw a 2.0 percent decline in market value in 2010. As a whole, Class 2 is expected to see very gradual acceleration in market value growth from 1.8 percent in 2011 to 2.0 percent in 2012, before picking up to 4.3 percent in 2013. In 2011 and 2012, IBO expects higher market value growth among Manhattan coops and condominiums, offset by

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**Assessed Values Still Grow As Market Values Decline**

![Assessed Values Still Grow As Market Values Decline](chart)

**Percent Change in Market Value**

- 20% (2003)
- 15% (2004)
- 10% (2005)
- 5% (2006)
- 0% (2007)
- -5% (2008)
- -10% (2009)
- -15% (2010)
- -20% (2011)
- -25% (2012)
- -30% (2013)

**Percent Change in Billable Assessed Value**

- 20% (2003)
- 15% (2004)
- 10% (2005)
- 5% (2006)
- 0% (2007)
- -5% (2008)
- -10% (2009)
- -15% (2010)
- -20% (2011)
- -25% (2012)
- -30% (2013)

**Sources:** IBO; Department of Finance assessment rolls.

**Note:** Numbers for 2011, 2012, and 2013 are projected.
slower growth among all rental buildings and coops and condominiums in the other boroughs.

State law requires that when assessing cooperative and condominium buildings, the Department of Finance (DOF) use income from comparable rent-regulated buildings, rather than sales prices. Thus, the fall in apartment prices is not directly captured in the market values used for tax purposes. The higher growth for Manhattan coops and condominiums is also partly the result of administrative policies regarding assessment of large buildings. In the case of coops, particularly in Manhattan, DOF has been using more high-rent apartment buildings as comparables. DOF also recently switched to using gross income multipliers (GIMs), which increase as a building’s rental income—on a per square foot basis—increases. From 2009 to 2010, market value per square foot, a function of income and the GIM, increased among the roughly 30 percent of apartment buildings with the highest incomes, while it decreased for the rest. The increases and decreases were more pronounced for buildings with the highest and lowest per square foot incomes, compared to those in the middle of the distribution. Given that most Manhattan apartment buildings generally have higher per square foot incomes, many saw market value growth in 2010, and this pattern is carried forward in IBO’s forecast of DOF’s market values.

For all Class 2 buildings with more than 10 units, market value changes are phased in over five years, which moderates year-to-year changes. The pipeline of assessment changes waiting to be phased in is currently $3.6 billion. As increases from earlier years are replaced by slow (or negative) growth in recent years, the pipeline shrinks and billable assessment growth slows. Billable assessments are expected to grow 7.7 percent in 2011, reflecting strong growth from 2007 to 2009. From 2011 to 2013, the growth rate of billable assessed value is expected to slow, to an average of 1.9 percent a year.

Class 4. Commercial property in Class 4 has seen a slowdown in market value growth, from 15.2 percent in 2008 to 7.0 percent in 2009 and 4.6 percent in 2010. IBO forecasts that this overall trend will continue, with market value growth of 3.0 percent in 2011, down to 1.8 percent in 2013. There is significant variation in market value within Class 4, however. IBO projects that, with high vacancy rates and declining asking rents, Manhattan office buildings will see a decline in market value through the forecast period. Because there is a lag in reporting income (2010 market values were based on 2007 and 2008 incomes and expenses with no adjustment for changes in price levels), the decline in value for Manhattan office buildings is expected to be just 0.7 percent in 2011, increasing to 2.4 percent in 2012 and 2.3 percent in 2013. Other commercial property in the city is forecast to see market value growth in 2011 to 2013. While some of this reflects continued strength in some retail corridors, DOF’s administrative policies also contribute to the observed growth. First, DOF has recently been proactively increasing the market value of vacant commercial land to more closely reflect actual sales prices. Second, the department has been more aggressive in imputing the income and expenses of commercial properties that do not file their required income and expense statements—by imputing the highest income and lowest expenses of comparable properties that file to those that do not. Under this policy, nonfilers have generally seen large market value increases.

As with Class 2, changes in value stemming from market conditions phase in over a five-year period, creating a pipeline. As of 2010, IBO estimates the pipeline in Class 4 to be $8.5 billion, declining to $4.4 billion by 2013. As a result, the billable assessed value growth, which averaged 8.7 percent a year from 2007 to 2010, is slowing, to a projected average of 5.7 percent a year from 2010 to 2013.

**General Sales Tax.** The improved economic outlook in general, upward revisions in forecasts of personal income growth, and recently enacted rate and base increases have all led IBO to raise its revenue forecast for the city's general sales tax. The enacted tax increases are expected to cause sales tax revenue to rise in 2010, rather than decline as previously forecast. After 2010, the strengthening of the national, local, and foreign economies is expected to fuel steady and strong collections growth.

IBO projects that collections of New York City's sales tax will reach $4.9 billion in 2010—6.3 percent ($287 million) greater than 2009 revenue. This forecast is far greater than IBO had projected in May, before the enactment of three distinct increases in the tax. Effective August 1, 2009 the city's sales tax rate was increased from 4.0 percent to 4.5 percent, boosting 2010 revenue by an estimated $468 million and by progressively larger amounts thereafter. At the same time, New York City's local exemption for clothing and footwear costing $110 or more was repealed, increasing revenue by an estimated $108 million in 2010 and more in subsequent years. (Clothing purchases costing less than $110 remain fully tax-exempt.) Additionally, a sales-tax exemption on electrical and natural gas distribution was repealed.

Despite the increased revenue estimates, rising unemployment, low levels of consumer confidence, an increase in personal savings, and a decline in the number of overseas visitors are all depressing sales tax revenue. Without the $650 million that all the enacted tax increases together are expected to add to collections this year, IBO would still be forecasting a decline in...
Forecasting near a turning point in the business cycle is a particularly fraught endeavor, which increases the risks inherent in all projections. If federal stimulus spending ends before the nascent economic recovery has developed into self-sustaining growth, the U.S. economy is likely to slide back into recession, deepening the local downturn and erasing the rise in city tax revenue IBO currently anticipates. Conversely, IBO’s economic forecast assumes a somewhat slower recovery in the U.S. economy than many forecasters are projecting and to the extent that our outlook is too pessimistic, faster economic growth could accelerate the pick-up in tax revenues for the city. Longer term, potential structural changes to the city’s critical financial sector could also significantly affect New York City’s economic outlook.

The uncertainty stemming from New York State’s fiscal problems also poses risks to the city’s recovery. Sizable cutbacks in state spending, particularly in the state’s two biggest spending areas, education and Medicaid, could result in layoffs in the city’s public schools and hospitals or pressure to maintain current levels of service by using city resources. Tax increases at the state or city level, depending in part on what taxes are increased and by how much, could also be a drag on local recovery.

Finally, although the revenue forecast suggests that there will be additional resources available for the 2010 budget, and throughout the financial plan, there are several big ticket items that OMB is counting on to help balance the 2011 budget which have yet to materialize. The budget includes savings from initiatives from prior financial plans that total over $500 million for 2011. These consist of a new pension tier, which would have to be negotiated with the unions and enacted by the state Legislature, and a health insurance 10 percent co-pay that also would require collective bargaining. There have been no reports of progress on either item to date. It is likely that the city will be forced to push at least some of these anticipated savings into future years, thereby opening new holes in this year’s budget. To the extent that the additional tax revenue anticipated by IBO is used to plug the holes in the financial plan.

**ENDNOTES**

1. Unless noted otherwise, employment data are seasonally adjusted.
2. The median price is highly dependent on the types of apartments sold, and a decline could signal a move to smaller units.
3. The increase in the 2010 assessment roll also revises upward the forecasts of future assessments and, in turn, RPT revenue.
4. As a result of this change, the combined state and local sales tax rate imposed in the city increased to 8.875 percent. In addition to the city sales tax, this rate includes the 4.0 percent rate of New York State’s general sales tax and a 0.375 percent rate of the Metropolitan Commuter Transportation District tax.

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