March 2012

Analysis of the Mayor's Preliminary Budget for 2013

IBO's Reestimate Of the Mayor's Preliminary Budget for 2013 And Financial Plan Through 2016

IBO

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Overview

On March 5, IBO presented the highlights of our then just-completed economic and revenue forecast at a hearing of the City Council's Finance Committee. Three days later, the state's Department of Labor issued its annual "benchmarking" of the employment numbers, replacing survey-based data with figures based on actual payrolls. These annual revisions are generally modest in scope. Not this time. The revisions presented by the labor department were dramatic and led IBO to undertake a new economic and revenue forecast incorporating the updated jobs numbers.

This report presents our new economic forecast and tax revenue projections along with our review and adjustments of the Mayor's spending plans under the Preliminary Budget for Fiscal Year 2013 and Financial Plan through 2016. Among the findings of our report:

- New York City will add 60,500 jobs in calendar year 2012 and an average of 72,400 per year over the 2012-2016 period.
- Tax revenues are expected to rise by 4.3 percent this fiscal year and total $41.4 billion. In 2013, tax revenues are forecast to increase by an additional 5.5 percent and reach $43.6 billion.
- Spending on the city's traditional general education public school classrooms will decline by $203 million (3.3 percent) in 2013 under the Mayor's plan.
- Charter school allocations will be $51 million higher than the $779 million reflected in the budget plan for 2013, and $82 million more than budgeted for 2014 based on already approved plans for new charter schools.
- The cost of homeless shelters for families will be an estimated $37 million more than budgeted for this year and $76 million more than planned for 2013 because the number of families in shelters is generally rising and their length of stay has increased.
- The pension changes passed in Albany will save the city $27 million less in 2015 and $56 million less in 2016 than projected by the Mayor based on the Governor's original proposal. Additionally, health insurance costs are projected to be an average of $45 million higher annually than the Mayor estimated in 2013-2016.

Much like last year's Preliminary Budget, many of the measures to save city funds or raise revenue in order to close the projected shortfall for the upcoming fiscal year were first introduced in the prior November's

Total Revenue and Expenditure Projections
Dollars in millions

	2012	2013	2014	2015	2016	Average Change
Total Revenues	$67,345	$69,788	$70,460	$73,310	$76,476	3.2%
Total Taxes	*41,355*	*43,641*	*45,330*	*48,060*	*51,023*	*5.4%*
Total Expenditures	67,345	69,244	72,645	75,241	77,017	3.4%
IBO Surplus/(Gap) Projections	**$-**	**$544**	**$(2,184)**	**$(1,932)**	**$(542)**	
Adjusted for Prepayments:						
Total Expenditures	$69,737	$70,594	$72,645	$75,241	$77,017	2.5%
City-Funded Expenditures	$49,045	$50,822	$52,868	$55,407	$57,081	3.9%

SOURCE: IBO

NOTES: IBO projects a surplus of $1.350 billion for 2012, $53 million above the Bloomberg Administration's forecast. The surplus is used to prepay some 2013 expenditures, leaving 2012 with a balanced budget. Estimates exclude intra-city revenues and expenditures. Figures may not add due to rounding. City-funded expenditures exclude state, federal and other categorical grants, and interfund agreement amounts.

Financial Plan. Still, the Mayor's February 2012 budget plan includes several important changes. A significant portion of these changes—in dollar terms and public attention—involve prospective revisions to the city's pension contributions for its employees. But there are other changes as well such as increases in projected tax revenues and savings from lower-than-expected interest costs on borrowing for the city's capital plan.

Based on IBO's latest revenue and spending estimates, the city will end the current fiscal year with a $1.4 billion surplus. The surplus in this year's budget results from a number of factors: projected tax collections have increased since the budget was adopted last June, the implementation in 2012 of $464.7 million in new measures to cut spending and raise revenues, and the use of $425 million less than expected of the $1 billion reserved in anticipation of adjustments by the city Actuary in how the city's annual pension contribution is calculated.

In addition, the plan includes $500 million in savings due to adjustments of previous years' expenditures and revenues (known as prior-year payables) and by reducing the city's general reserve for the current year by $200 million. While the amounts may change from year to year, both these adjustments that are typically recognized in the second half of the fiscal year are routine steps which produce annual savings.

With the expectation that the 2012 surplus will be used to prepay some of next year's expenditures and that the Mayor's plan for just over $1.0 billion in cost-cutting and revenue-raising initiatives for 2013 will be approved, we estimate the city will generate a surplus of $544 million next year. But that surplus is also dependent upon a number of other assumptions. One critical assumption is that U.S. economic growth continues to strengthen as it did towards the end of calendar year 2011. It also counts on the Bloomberg Administration's plan to generate $1.0 billion through the sale of new taxi medallions being approved by the courts and that the sale meets its revenue goal. Additionally, it expects that $1.0 billion from the Retiree Health Benefits Trust will be used to help balance the 2013 budget—along with the use of another $1.0 billion to help reduce the 2014 budget gap, effectively wiping out the fund that had ostensibly been set aside to help meet future retiree health costs.

Even with the use of the retiree health trust funds, IBO estimates a budget shortfall of $2.2 billion in 2014, or 4.3 percent of tax and other city-generated revenues.

We urge readers not to compare IBO's surplus and gap estimates with those contained in the Preliminary Budget and Financial Plan because our projections are built off job numbers that were substantially revised by the state labor department after the Mayor released his budget plan.

In addition, readers should note that this report was completed as state legislative leaders came to an agreement on the state budget. This report does not reflect changes in the Governor's proposals, which have not been formally approved.

Jobs and Taxes Revenues Poised for Growth

Following the state labor department's revision of its jobs estimates for New York City, IBO now projects the city will sustain strong employment growth over the next few years. With an increase of 72,700 jobs in calendar year 2011 and our forecast of average annual growth of 72,400 in 2012-2016, IBO expects the city will gain 435,000 jobs over the six-year period—in comparison, during 1994-2000 the city gained 438,000 jobs over eight years.

Coupled with this increase in local employment is a forecast of rising tax revenues. IBO projects tax collections will total $41.4 billion in fiscal year 2012, 4.3 percent over 2011. We expect tax revenues will rise an additional 5.5 percent in 2013 and total $43.6 billion. Over the 2014-2016 period tax collections are expected to rise at an average annual rate of 5.4 percent and total $51.0 billion in 2016.

While this is considerable growth, it falls well short of the double digit tax revenue increases experienced in 2004 through 2007 as the city recovered from the previous recession and the aftermath of September 11. The reason for the more modest tax growth now—in contrast to the projected strong pace of job gains—is the expectation of relatively weak Wall Street revenues and profits over the near term. As a result of this weakness, the securities industry will not generate the growth in wages and jobs—and tax revenues— that has been associated with the past two economic recoveries.

IBO's employment forecast for calendar year 2012 shows an increase of 60,500 jobs, but few of these will be on Wall Street. Most of the growth is expected in leisure and hospitality, (16.900), education and health care services (16.900), business services (12,400), and wholesale and retail trade (10,100). In contrast, IBO projects the securities industry will add just 700 jobs, and the entire financial activities sector will increase by only 1,100 jobs. Job growth is expected to remain modest on Wall Street through 2016 while the same sectors leading the growth in 2012 are projected to continue to lead employment increases throughout the period.

Because of the comparatively modest wage levels in many of the sectors that we project will have the largest increases in employment, IBO's latest tax revenue forecast for 2012-2016 is not substantially higher than our December forecast, when we expected far less employment growth. Still, a large share of the 5.5 percent increase in tax collections projected for the upcoming fiscal year come from the personal income tax, a reflection of growing employment. The business income taxes and property transfer taxes also are leading contributors to the rise in tax revenues.

Gap Closers Include Spending Cuts and Revenue Increases. The budget plan for 2013 includes about $6.0 billion in cumulative gap-closing measures—the so-called Program to Eliminate the Gap, or PEGs—that began with the January 2008 Financial Plan. The total PEG amount assumes that $1.0 billion in proposals that are part of the 2013 Preliminary Budget are approved by the City Council. Reductions in city-funded spending account for $881.6 million of the PEGs, including outright spending cuts; the supplanting of city dollars with state, federal, or private funds; and reestimates of the amount of city funds needed to provide particular services. An additional $137.5 million is expected to come from the collection of more fees, fines, and other revenues—but no new taxes or tax rate increases.

While the new proposals to reduce spending do not include any layoffs of teachers—one of last year's most contentious issues—or uniformed personnel, some of the planned spending reductions will lead to layoffs or attrition as vacancies go unfilled. For example, the Department of Housing Preservation and Development intends to lay off 11 administrative staff to save $792,000 and the Department of Transportation's ongoing conversion of single-space parking meters to Muni Meters will enable the agency to lay off 47 workers and allow 50 other positions to go unfilled or have current staff redeployed to save a combined $6.8 million.

Some of the other proposed spending reductions will not have a direct effect on city staffing but would likely affect staffing at organizations providing city-funded services. One example is the Department of Youth and Community Development, which plans to eliminate funding for seven Beacon programs, saving $2.1 million, and reducing the number of Out-of-School Time slots by 2,300 to about 53,700, saving $5.9 million (see page 38 for more details). Another example is the plan to reduce the city subsidy to arts and cultural programs by $6.1 million. Although the reduction is not expected to affect staffing at the Department of Cultural Affairs, the Bloomberg Administration estimates that it will lead to the layoff of 109 workers at the subsidized organizations (see page 39 for more details).

On the other side of the PEG ledger, the Mayor has proposed a variety of initiatives aimed at increasing revenue. Nearly a third of the increased revenue anticipated for 2013, $50.5 million, is expected to be generated by the Department of Finance through steps such as a sophisticated new tax auditing process, better assessments of hard-to-value properties such as cell towers and billboards, and improved reviews of tax exemption renewals. Among the other efforts to produce more revenue are the Department of Health and Mental Hygiene's expectation of increased restaurant inspections and resulting fines (an additional $3.8 million in revenue), increased commercial parking rates in Manhattan ($4.0 million in revenue), and the implementation of a new fee by the fire department for "safety protocol inspections" ($8.4 million in revenue).

There are number of other revenue measures, most very explicit and at least one surprisingly vague. The Human Resources Administration expects to collect $2.1 million in overpayments to public assistance recipients by recouping funds from people who agreed to be financially responsible for immigrants to the U.S. The Department of Parks and Recreation anticipates generating $13.0 million in new revenue, but has not stated how this will be accomplished (see page 38 for more background).

The Mayor's Preliminary Budget also includes some measures to raise revenues or reduce costs that are carried over from prior plans. A proposal put into the May 2011 Financial Plan to take effect in fiscal year 2013 would charge some nonprofits for trash collection. The sanitation department projected revenue of $17.2 million but the exact number and type of nonprofits that would be charged is unknown. The sanitation department recently commissioned a survey of the nonprofits that currently have their garbage collected for free. Legislation has been introduced in the City Council that would prevent the city from charging nonprofits for trash collection.

Some of the spending reductions introduced in prior financial plans have been repeatedly restored by the City Council. Because the Council can only restore funding one year at a time, no funds are in the budget for these services in 2013 through 2016. One example of this is the proposal to close 20 fire companies. First proposed for fiscal year 2011, the City Council provided $37.4 million that year and $40.9 million this year to keep the fire companies open. But there is no funding in the budget plan for 2013 through 2016. Another example is case management services in certain supportive housing programs for people with AIDS/HIV. Since 2010, the Council has restored funds for these services, including $2.7 million for the current year. But no funds are now budgeted for 2013-2016. Similarly, the Council provided $3.6 million this year to prevent the elimination of 105 positions for child protective workers at the Administration for Children's Services. The Mayor's budget plan does not include these funds.

City Spending Continues to Rise. Despite the proposed spending reductions, including those that recur in future years, city expenditures continue to grow. IBO projects that total city spending, adjusted for the use of surpluses for prepayments, will rise from $69.7 billion this year to $70.6 billion in 2013 and $72.6 billion in 2014. Looking only at city funds, again adjusting for the use of surpluses, IBO estimates spending will increase from $49.0 billion this year to $50.8 billion in 2013 and $52.9 billion in 2014.

The projected growth in city spending comes despite the fact that for most city agencies expenditures are expected to remain flat or decline. For example, IBO projects police department spending will fall by $175 million in 2013 from $4.7 billion this year and decline at average rate of 1.0 percent through 2016. Likewise, spending by the Administration for Children's Services is expected to fall by $154 million in 2013 from $2.9 billion this year and decline at an average rate of 1.4 percent through 2016.

The largest growth among major categories of spending, both in absolute dollars and percentage terms, are in just two portions of the city budget: health and other fringe benefits for city employees and debt service on the money the city borrows to build schools, fix roads, buy fire trucks, and fund other needs in the capital plan.

Despite lower-than-expected borrowing costs, spending on debt service is projected to climb $666 million next year and reach $6.3 billion (after adjusting for the use of prior-year surpluses to prepay a portion of 2012 and 2013 debt service). Debt service is projected to increase by an additional $519 million in 2014 and total $6.8 billion. Over the 2012-2016 financial plan period, debt service is expected to rise at an average annual rate of 7.3 percent. Although interest rates are very low and the city has taken advantage of low rates to refinance existing debt, spending on debt service continues to grow, driven by the size of the capital budget. (See pages 49-52 for more details on debt service and the city's capital budget,)

The cost of health insurance and other fringe benefits for city employees is growing at a similar rate. IBO estimates that the cost of fringe benefits is projected to rise by $319 million in 2013 and total $4.8 billion (after adjusting for the use of the Retiree Health Benefits Trust to pay a portion of this cost and excluding fringe benefit costs of the education department). Fringe benefit costs are expected to grow by an additional $350 million in 2014 and total $5.2 billion. Over the 2012-2016 financial plan period, health insurance and other fringe benefit costs are projected to increase at an average rate of 7.3 percent.

Another portion of the budget that continues to grow, although at a considerably slower pace, is education. Spending by the Department of Education is projected to grow by $335 million next year and total $19.7 billion (excluding funds for the labor reserve). Much of this growth is attributable to an anticipated 4 percent rise in state aid, a rise the Governor has

IBO Expenditure Projections
Dollars in millions

	2012	2013	2014	2015	2016	Average Change
Health & Social Services						
Social Services						
Medicaid	$6,466	$6,510	$6,647	$6,826	$6,924	1.7%
All Other Social Services	2,968	2,843	2,820	2,836	2,836	-1.1%
HHC	76	68	67	67	67	-3.0%
Health	1,618	1,533	1,529	1,517	1,517	-1.6%
Children Services	2,859	2,705	2,702	2,702	2,702	-1.4%
Homeless	860	872	871	871	871	0.3%
Other Related Services	562	452	440	436	436	-6.2%
Subtotal	**$15,408**	**$14,984**	**$15,076**	**$15,255**	**$15,352**	**-0.1%**
Education						
DOE (excluding labor reserve)	$19,326	$19,661	$20,216	$20,537	$20,842	1.9%
CUNY	745	732	721	723	717	-0.9%
Subtotal	**$20,070**	**$20,393**	**$20,937**	**$21,260**	**$21,559**	**1.8%**
Uniformed Services						
Police	$4,720	$4,545	$4,537	$4,536	$4,535	-1.0%
Fire	1,806	1,749	1,699	1,654	1,654	-2.2%
Correction	1,086	1,066	1,075	1,055	1,055	-0.7%
Sanitation	1,332	1,343	1,463	1,462	1,462	2.4%
Subtotal	**$8,945**	**$8,703**	**$8,774**	**$8,707**	**$8,706**	**-0.7%**
All Other Agencies	**$7,476**	**$7,152**	**$7,336**	**$7,461**	**$7,637**	**0.0%***
Other Expenditures						
Fringe Benefits (excluding DOE)	$3,852	$3,843	$4,193	$5,573	$6,001	*7.3%***
Debt Service	3,383	4,928	6,797	7,163	7,436	*7.3%**
Pensions	7,875	8,020	7,948	7,867	7,971	0.3%
Judgments and Claims	655	685	718	754	790	4.8%
General Reserve	100	300	300	300	300	n/a
Labor Reserve:						
Education	-	-	-	-	-	n/a
All Other Agencies	82	164	323	540	796	n/a
Expenditure Adjustments	(502)	72	243	362	470	n/a
TOTAL Expenditures	**$67,345**	**$69,244**	**$72,645**	**$75,241**	**$77,017**	**3.4%**

SOURCE: IBO
NOTES: *Represents the annual average change after adjusting for prepayments.
**The annual average change excludes the Retiree Health Benefits Trust fringe adjustment.
Expenditure adjustments include prior-year payable, energy and lease, and non-labor inflation adjustments.
Estimates exclude intra-city expenses. Figures may not add due to rounding.

made contingent upon other factors. IBO projects education department spending will increase by an additional $555 million in 2014 and total $20.2 billion. Over the 2012-2016 financial plan period, education department spending is projected to rise at an annual rate of 1.9 percent, although little of this increase is expected to reach general education classrooms. Most of the increase will be used outside the traditional school system, with charter schools, privately run special education schools, and pre-kindergarten special education services being some of the education department's fastest-growing expenses. (See pages 19-23 for more details on education spending.)

Pension costs are also expected to increase slowly under the Mayor's February 2012 budget plan. But this forecast assumes approval of the city Actuary's recommendations for changing how the city's pension contributions are calculated as well as the Governor's proposal for a new and less costly pension plan for future employees. With the state Legislature's approval of a modified version of the Governor's budget proposal for a new pension tier, IBO estimates the savings for the city will be somewhat less than projected in the Mayor's plan: $27 million less in 2015 and $56 million less in 2016.

Assuming the changes proposed by the Actuary occur, the city's pension contribution is projected to grow by $145 million in 2013 and total $8.0 billion. Pension costs are then expected to fall by $72 million in 2014. Over the 2012-2016 financial plan period, pension contributions are projected to grow at an average rate of just 0.3 percent and total just under $8.0 billion in 2016— a modest $96 million more than in 2012 (See pages 45-47 for more details on the proposed enacted and pension changes.)

Potential Pitfalls. There are a number of factors that could upend IBO's tax revenue and spending projections under the Mayor's budget plan. One such factor is the risks to our economic forecast. The growth in the U.S. economy seen towards the end of calendar year 2011 could be undermined by continuing problems in the euro zone. Rising oil prices due to growing tensions with Iran and slower economic growth in China could also weaken the recovery. Closer to home, gridlock in Washington over U.S. tax, spending, and debt policy could also hamper the recovery nationally and locally. And while IBO's forecast has sought to recognize the effects that increasing regulations may have on Wall Street profits and what that means for local tax collections, the consequences could be very different than estimated.

Another factor that could have a considerable effect on the budget is the fate of the Mayor's plan to generate $1 billion in revenue through the sale of new taxi medallions. That plan is now tied up in court. In December, a judge ruled that the Taxi and Limousine Commission must develop a long-term plan to increase the number of wheelchair accessible taxis in the city—of the more than 13,000 yellow cabs in the city just 231 are accessible—before the Bloomberg Administration could go ahead with the medallion sale. The city has appealed the ruling.

The proposals that would ease the rise in city pension contributions over the financial plan period must surmount hurdles. The changes in how the city's pension contributions are calculated must be approved by each of the boards of the city's five pension funds. Within this set of changes in assumptions and methodologies, the plan to lower the assumed rate of return on pension fund investments from 8.0 percent to 7.0 percent must be approved by the state Legislature.

A different set of labor issues could also affect IBO's budget projections. Contracts with some of the city's largest labor unions expired some two or more years ago—District Council 37 in March 2010 and the United Federation of Teachers in October 2009 are two examples. There is no money in the budget for raises for teachers (or principals) over the period that other city employees received 4.0 percent increases, and no funding for increases for any unions in 2011 and 2012. But the Mayor has stated that any wage hikes for the period in which no funds have been set aside must be offset by productivity gains or givebacks. For the 2013-2016 period, funds sufficient to cover 1.25 percent raises have been put into the labor reserve. Each 1.0 percent increase in salary not paid for with labor savings would cost the city about $290 million, including additional pension costs.

Making Ends Meet. While IBO projects a substantial increase in employment, tax revenues are forecast to rise at a relatively moderate pace as Wall Street revenues and profits are expected to remain comparatively weak. IBO's projection of a $544 million surplus in 2013 is dependent upon the Mayor's plan for tapping $2.0 billion in nonrecurring sources of funds—along with proposals for $1.0 billion in measures to reduce spending and raise revenue and a $1.4 billion surplus in 2012. Even with the use of the last $1.0 billion remaining in the Retiree Health Benefits Trust Fund, 2014 still has a budget shortfall of $2.2 billion. The city's fiscal challenges may be easing, but they have not vanished.

Economic Outlook

U.S. Economy

A year ago the United States appeared to be poised for what IBO's March 2011 Outlook called the "long-awaited acceleration of the economy's expansion." But the wait turned out to be longer than anticipated, as a series of shocks and drags—the earthquake and tsunami in Japan, the brinksmanship over raising the federal debt limit and subsequent downgrading of U.S. government debt, state and local government austerities, sovereign debt turmoil in the euro zone, the continuing weight of tight credit and foreclosures on housing markets, and a variety of pressures on and within the banking sector—blunted growth through much of 2011. (All years in this section refer to calendar years, unless otherwise noted.)

In the last quarter of the year, signs of strength emerged again, particularly in private-sector employment, and we are in some ways in a similar position now as we were a year ago: anticipating an accelerating recovery, but mindful of the risks that might (again) disrupt the economy's momentum.

IBO expects real gross domestic product (GDP) growth to climb over the next three years, from last year's weak 1.7 percent to 2.4 percent in 2012, 3.0 percent in 2013, and 3.6 percent in 2014. This will carry with it enough employment growth to finally make significant inroads into the stubbornly high unemployment rates of recent years. We project unemployment to average 8.1 percent this year, gradually declining to 7.8 percent in 2013 and 5.9 percent by 2016. This forecast assumes another two years of very accommodative monetary policy (the federal funds rate kept close to zero) as well as extension of the Bush tax cuts now set to expire in 2013, at least for those with incomes under $250,000. Congress will have to enact an extension of these cuts by the end of the year. Further extension of the 2 percentage point payroll tax cut would also require Congressional action, but in this case we assume that the cut will expire as scheduled at the end of this year.

This forecast also prices in the recent surge in oil prices, driven by rising tensions with Iran. Crude oil prices are projected to remain above $100 per barrel throughout the forecast period, though not far above, topping $110 only by the end of 2016. But the headwinds from these developments may prove stronger than predicted. Higher energy and commodity costs, along with slow growth in Europe, are already being blamed for a spate of reductions in 2012 corporate earnings forecasts.

Probably the most immediate of the risks to this outlook remains the euro zone. The forecast assumes a mild downturn in Europe through the first half of 2012—but no worse. Yet it is by no means certain that the threat of contagion from the sovereign debt crisis has been contained, and the exposure of the world's banking system to sovereign debt uncertainties was underscored by Moody's move in February 2012 to place 17 global and 114 European financial institutions on review for possible credit downgrades.

Yet another source of uncertainty is China. Behind the stellar economic performance of recent years, there are signs of slower growth, fiscal strains, and a deflating real estate bubble.

Domestically, the federal government continues to grapple with both short and long-term fiscal imbalances, with large question marks over tax, spending, and debt policy as well as over the regulatory reach of Washington. The extent to which these uncertainties have dampened and may continue to dampen the recovery is itself the subject of debate.

But it is not only government debt that casts a long shadow over an otherwise brightening economic picture. Total domestic household indebtedness peaked at $13.9 trillion, in nominal terms, in the second quarter of 2008, and since then has fallen by $678 billion (this is through the fourth quarter of

IBO Economic Forecast

	2011	2012	2013	2014	2015	2016
National Economy						
Real GDP Growth	1.7	2.4	3.0	3.6	3.3	2.9
Unemployment Rate	8.9	8.1	7.8	7.2	6.5	5.9
Inflation Rate	3.2	2.1	2.4	2.9	2.4	2.0
NYC Economy						
Real GCP Growth	3.2	3.4	4.0	3.0	2.9	2.8
Nonfarm New Jobs, *thousands*	72.7	60.5	68.7	78.3	81.0	73.3
New Jobs in Trade, *thousands*	11.2	10.1	13.4	9.9	9.9	9.3
New Jobs in Information, *thousands*	4.8	5.0	5.0	4.0	3.0	2.9
New Jobs in Financial Activities, *thousands*	11.5	1.1	4.0	7.5	8.9	6.6
New Jobs in Professional and Business Services, *thousands*	20.4	12.4	14.9	17.0	16.5	16.1
New Jobs in Education, *thousands*	4.8	3.6	2.1	3.5	4.7	4.2
New Jobs in Health Care Services, *thousands*	8.0	8.2	7.8	8.4	8.8	6.8
New Jobs in Leisure and Hospitality, *thousands*	20.3	16.9	12.4	12.3	11.1	11.8
New Jobs in Government, *thousands*	-12.5	-2.9	-2.5	3.9	3.6	2.2
Nonfarm Employment Growth	2.0	1.6	1.8	2.0	2.0	1.8
Unemployment Rate	9.0	8.6	8.6	7.8	6.4	5.7
Inflation Rate (CPI-U-NY)	2.8	2.6	3.1	3.4	2.9	2.5
Personal Income, *dollars in billions*	451.9	470.4	495.6	524.6	553.0	581.6
Personal Income Growth Rate	4.7	4.1	5.3	5.9	5.4	5.2
NYSE Member Firm Profits, *dollars in billions*	7.7	12.5	15.2	14.9	14.3	14.3

SOURCE: IBO

NOTES: Rates reflect year-over-year percentage changes except for unemployment. The local price index for urban consumers (CPI-U-NY) covers the New York/Northern New Jersey region. Personal income is nominal. For 2011, New York City personal income and growth rates are estimated, pending Bureau of Economic Analysis release.

2011). Most of this was due to the severe impact of the housing slump—and then the broader crisis and recession—on both existing mortgage holdings and new mortgage activity. But all this deleveraging has only lowered the household debt to GDP ratio from 96.4 percent to 86.3 percent, which is still far above pre-mortgage bubble norms—it had been under 70 percent of GDP prior to 2000. Household debt *service* burdens have, for now, come down much further, due largely to current extremely low interest rates. As rates return towards normal, households will be confronted again with the weight of their borrowing.

The Local Forecast

A dramatic revision to the Department of Labor's estimates of the pace of job creation in New York City in 2011 has led IBO to significantly strengthen its local economic forecast. IBO now expects city job growth to average 72,400 (1.8 percent) per year over the 2012-2016 plan period. This is a substantial improvement over our December forecast, which projected annual growth of 52,500 (1.4 percent) over this period. However, for key sectors and measures of the economy there is still no return to the heights scaled prior to the crisis and recession.

New York City fared considerably better than the rest of the nation in terms of job losses during the recession (a loss of 3.6 percent peak-to-trough in the city versus a 6.5 percent loss in the rest of the nation), but considerably worse in terms of aggregate real wage losses (a loss of 12.4 percent over 2008 and 2009 in the city, compared with a 5.3 percent loss in the rest of the nation). Nearly two-thirds of the city's total wage losses were in the securities sector, reflecting the impact of record declines in Wall Street compensation. But much smaller real average wage declines were also spread across many other sectors in the city.

In 2010 and 2011 the city continued to display its economic resilience, matching or exceeding the nation on most measures of economic growth. Indeed, the recent extraordinary benchmark revisions to the city's payroll employment numbers have emphatically pointed up the city's recent strength. Revised seasonally adjusted city employment grew by 72,700 in 2011, or 2.0 percent—nearly double the 1.1 percent employment growth rate for the U.S. as a whole. (Prior to the benchmark revision, it appeared that city employment grew by only 0.9 percent in 2011.) The seasonally adjusted private-sector gain was even larger—85,100, a mark surpassed just once since at least 1950.

Indeed, very strong employment growth in January pushed seasonally adjusted city employment back above the previous peak reached in September 2008—meaning that New York City has now recovered all of the jobs (though of course not the same jobs) lost in the recession. Moreover, January brought city employment very near its modern high—August 1969.[1]

However, not all of the revised signs painted a brighter economic picture. Though the year's employment gains were large, they weakened progressively throughout 2011, falling from increases of 25,300 in the first quarter to 19,700 in the second, 12,300 in the third, and just 7,000 in the fourth quarter. (January's jump, just noted, broke this trend.)

Moreover, while the count of jobs added by city *businesses* in 2011 was revised strongly upward, the count of the number of New York City *residents* working was actually revised down. The new data show only 5,000 more city residents employed in 2011 than in 2010, and both the average number of unemployed (353,700) in 2011 and the unemployment rate (9.0 percent) for the year were worse than previously estimated.

This divergence cannot be put down to the notion that nonresidents took nearly all of the net jobs added in the city in 2011. Particularly given the areas where the city saw the job gains—almost two-thirds in trade, leisure and hospitality, and education and health services—that explanation does not appear plausible. Nor does it appear likely that factors such as residents shifting from self-employment to payroll employment can explain much of so large a gap between the payroll reports of city businesses and the household survey of city residents. Ultimately, we are simply left with a discrepancy between the two series. This is not the first time these data series have diverged widely. For example, during both the 1989-1992 and 2001-2003 downturns, the decline in the number of jobs located in New York City was far greater than the decline in the number of city residents with jobs.[2]

More conflicting signals have been coming from the financial sector. While the securities industry added jobs through most of 2011 (instead of only in the first quarter, as previously estimated), the broker-dealer profits of New York Stock Exchange (NYSE) member firms were negative in both the third and fourth quarters, resulting in just $7.7 billion in profits for the year as a whole—the worst performance in a decade except for the meltdown of 2007-2008. Moreover, member firm revenues slipped in 2011 (to $146.1 billion) and were well under half of their pre-crisis peak ($352.0 billion in 2007).

NYSE member firm revenues are expected to slide even further (down to $139 billion) in 2012, albeit with a rebound in profits to a still modest $12.5 billion—though it is only by dint of exceptionally low interest expenses (largely stemming from Federal Reserve policy) that any NYSE firm profits will be eked out at all. Concurrent with all this, IBO is projecting a 20 percent drop in the 2011 Wall Street bonus pool that is mostly paid out in early 2012, and no growth in overall average wages (including bonuses) in the securities sector in 2012.[3]

Because of these factors—the slippage in growth in the latter part of 2011 and the ripple effects of stagnant securities industry wages—IBO projects payroll job growth to dip to 60,500 (1.6 percent) in 2012. The forecast annual private sector increase is 63,400—again down from 2011 but still quite robust relative to our previous prediction for 2012. Most of the growth is expected in leisure and hospitality (+16,900) and education and health care services (again +16,900) followed by business services (+12,400) and trade (+10,100).

Personal income growth will also slip a bit to 4.1 percent (in real dollars, 2.5 percent) in 2012. This is lower than IBO forecast in December, before the scale of the new cutbacks in Wall Street pay began to come into focus. The unemployment rate will edge down to a still-high 8.6 percent.

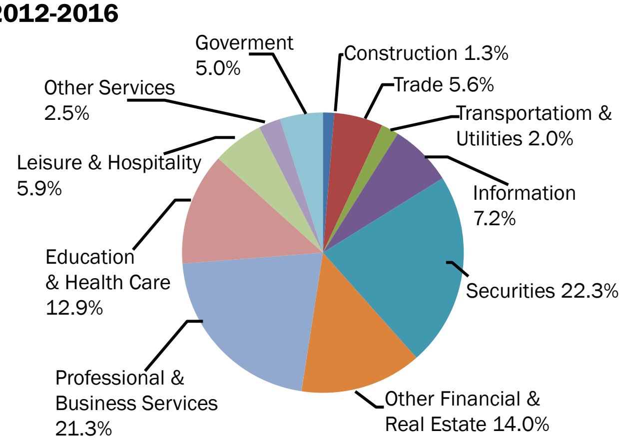
In 2013 and beyond, IBO expects the tempo of the expansion to quicken, with projected payroll job growth rising to 68,700 (1.8 percent) in 2013 and averaging 77,500 (1.9 percent) per year over 2014-2016. By the end of this period the unemployment rate will have declined to 5.7 percent –still above the 4.9 percent low hit in 2007. After 2012, personal income will grow by an average of 5.4 percent per year (3.4 percent adjusted for inflation).

If this forecast is borne out, the city will have gone six years with payroll job growth not falling below 60,000 (1.6 percent) in any year, and will have added nearly 435,000 jobs over this stretch—a pace that would best any previous expansion on record.[4] And yet underpinning all this is an expectation of muted—by pre-crisis standards—financial sector employment and compensation growth accompanied by relatively modest NYSE member revenues (expected to have recovered only to $189 billion by 2016) and profits (averaging about $14.6 billion per year from 2013 through 2016).

Instead, the main drivers of the expansion through 2016 will be the sectors we have already mentioned. For the entire 2012-2016 period, the education, health care, and social assistance sector is the largest contributor to employment growth, averaging gains of 15,600 jobs (2.0 percent) per year and accounting for 21.6 percent of the jobs added in the city. (This breaks down to 8,000 jobs added per year in health care services, 4,000 per year in social assistance, and 3,600 per year in education.) Next is the professional and business services sector, averaging growth of 15,400 jobs (2.5 percent) per year and generating 21.3 percent of total city jobs added. This is followed by the tourism-fueled leisure and hospitality sector with an average increase of 12,900 jobs (3.5 percent growth) per year, good for 17.8 percent of total jobs added, and then wholesale and retail trade, averaging 10,500 (2.2 percent) annual jobs growth and contributing 14.5 percent of the overall city jobs gain. These four big sectors combined account for three-quarters of the forecast employment growth in New York City.

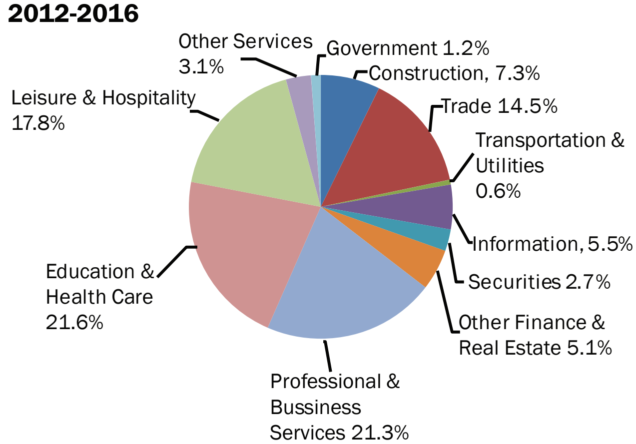
Construction is also expected to rebound over the forecast period, growing at an average rate of 4.3 percent, or 5,300 jobs per year from 2012 through 2016. This is driven mainly by a revival in commercial real estate activity, where the recovery in sales since mid-2010 points to growing demand for new space. The expectation of considerable additional space from projects at the World Trade Center and other buildings nearing completion, rather than weak demand, is the principle factor in IBO's projection of almost flat Manhattan office rents through the forecast period. IBO projects steady growth in the information sector,

Shares of New York City Aggregate Real Wage Growth, 2012-2016



SOURCE: IBO
NOTE: Manufacturing contributes -0.8% to 2012-2016 New York Cityaggregate wage growth.

Shares of New York City Employment Growth, 2012-2016



SOURCE: IBO
NOTE: Manufacturing contributes -0.6% to 2012-2016 New York City employment growth.

averaging 2.2 percent, or 4,000 jobs per year over the forecast period. But as mentioned above, we anticipate weaker growth in financial activities: outside of securities, 1.3 percent (3,700 jobs) per year, and in the securities industry itself even slower average growth of 1.1 percent, yielding just 1,900 jobs per year. Viewed from a different perspective, the securities industry will account for less than 1 of every 37 jobs we expect to be created in the city from 2012 through 2016. Only transportation and utilities, government, and manufacturing do worse in our forecast, the former two nearly flat and the latter declining slightly over the forecast period.

The scaling back of financial sector compensation and employment growth reflects both cyclical and secular factors—all of which, in one way or another, arise from the aftershocks of the financial crisis and recession. These factors include exposure to the European debt crisis and the new regulatory environment and its unfolding diverse impacts on industry costs and profitability.[5]

The sense of a structural shift in securities—or at least in the role this industry plays in the New York City economy—is also reflected in figures showing industry shares of forecast wage growth in the city. What stands out is that in 2012 through 2016 the securities industry is projected to account for only 22.3 percent of the aggregate real wage growth forecast by IBO. While this share is still large relative to industry's share of job growth, it pales in comparison with the better than 60 percent of aggregate wage change (both growth and decline) churned out by Wall Street over the prior decade, much less the close to 40 percent averaged over the 1980s and 1990s.

One significant risk to the city economic forecast presented here is that other parts of the local economy—in particular, business services, trade, and leisure and hospitality—will not 'decouple' from the subdued growth in Wall Street profits, wages, and employment as much as we are anticipating. This forecast is also vulnerable to all the threats to the national economic recovery discussed above.

Endnotes

[1]Official seasonally adjusted employment data start in 1990, but unofficial estimates put the city's seasonally adjusted payroll employment peak at about 3,836,000 in August 1969. The January 2012 surge brought the city up to 3,829,300 (a number still subject to revision).

[2]Over 1989-1992, the city economy lost 328,100 jobs—while the number of employed residents fell by just 144,500. Over 2001-2003, the job decline was 184,200, but resident employment dropped only 41,000. Conversely, the five quarter decline in city jobs (135,400) in 2008-2009 was tracked pretty closely by the decline in residents employed (122,400). This urges caution in comparing changes in city unemployment rates across past recessions.

[3]This is a preliminary estimate extrapolated from personal income tax withholding data and industry reports. It will be revised as Quarterly Census of Employment and Wages (QCEW) data for the securities industry are updated. These are currently available through the second quarter of 2011, but we will need the third quarter just to finalize the previous year's (2010) bonus pool estimate. The 2011 bonus pool estimate will not be final until we have the QCEW through the third quarter of 2012—probably in June 2013.

[4]Continuous employment statistics for New York City go back to 1950. Heretofore the strongest expansion since that time was in 1993-2000 when the city gained 438,000 jobs over eight years.

[5]These impacts include proprietary trading limits, lower returns on equity for banks required to hold additional capital, and higher costs related to the swaps push-out rule, which prevents banks from holding certain types of derivatives in order for their deposits to be insured by the Federal Deposit Insurance Corporation.

Taxes and Other Revenues

IBO's forecast of tax and other revenues for fiscal year 2013 totals $69.8 billion, an increase of 3.6 percent over the amount expected in the current year. Tax revenues (up by 5.5 percent) and other city revenues (up by 20.3 percent thanks to the anticipation of a one-time infusion of $1.0 billion) account for all of the revenue increase for next year as noncity revenues—including state and federal aid—are expected to shrink by $920 million to $19.8 billion. After 2013, total revenues are expected to grow at an annual average rate of 3.1 percent, with virtually all of the increase due to expected gains in tax revenues which are forecast to grow at an annual average rate of 5.3 percent in 2014 through 2016.

The first part of this section presents IBO's tax revenue forecast, with detailed discussion of each of the city's major tax sources. It concludes with a brief overview of the outlook for non-tax revenues.

Tax Revenues

IBO's tax revenue forecast for fiscal year 2012 is $41.4 billion, an increase of 4.3 percent over the prior year. Growth is expected to accelerate to 5.5 percent in 2013, with tax revenues reaching $43.6 billion. Revenue growth will slow in 2014 to 3.9 percent before rebounding to over 6.0 percent in each of the last two years of the forecast. Much of the increase forecast for this year stems from strength of the personal income tax (PIT) and the real property tax, with the business income taxes and taxes on property transactions contributing significantly to next year's growth. In 2014 through 2016, we expect revenue growth to be spread across all of the city's major tax sources and tax revenues are forecast to reach $51.0 billion by the end of the period.

The expectation of steady tax revenue growth is broadly consistent with IBO's economic forecast: after some weakness in calendar year 2012, we expect sustained gains in local employment and personal income, partly offset by continued weakness in the securities industry. Although IBO projects that annual tax revenue will grow throughout the forecast period, this growth is expected to be slower than in any of the years of the 2003-2007 expansion, which included double-digit growth in 2004 through 2007.

IBO's forecast remains somewhat higher than the city's tax revenue forecast when the 2012 budget was adopted last June—particularly for 2013 and beyond. With the upward revision to the local employment and earnings picture counterbalanced by the worsening outlook for the securities industry, IBO's tax revenue outlook is little changed from our December forecast and is somewhat lower for 2015 and 2016, as most of the anticipated acceleration in local output, employment, and personal income is expected to have occurred by 2014.

Real Property Tax. With the publication of the tentative assessment roll in January, the outlook for the city's real property tax revenue for 2013 has already been largely determined. After a period for consideration of taxpayer requests for review, the Department of Finance will publish a final assessment roll in May that will then be used to determine tax bills for the start of the fiscal year. IBO projects that property tax revenues will grow from $17.8 billion in 2012 to $18.3 billion in 2013, a 2.6 percent increase. This forecast of 2013 revenues is $70 million lower than IBO's December 2011 forecast due to slower than projected growth on the tentative assessment roll as well as changes in the reserve for abatements, delinquencies, and other adjustments. Property tax revenue growth is expected to accelerate slowly after 2013, averaging 5.1 percent annually in 2014 through 2016, when revenue will reach $20.9 billion.

When the 2013 roll is finalized in May, IBO forecasts that market value in the city will total $838.1 billion, an increase of 2.9 percent over 2012. This growth is

IBO Revenue Projections
Dollars in millions

	2012	2013	2014	2015	2016	Average Change
Tax Revenue						
Property	$17,803	$18,263	$18,959	$19,888	$20,944	4.1%
Personal Income	8,035	8,788	8,988	9,778	10,662	7.3%
General Sales	5,814	6,152	6,458	6,761	7,098	5.1%
General Corporation	2,635	2,788	2,908	3,106	3,331	6.0%
Unincorporated Business	1,684	1,855	1,970	2,151	2,356	8.8%
Banking Corporation	1,162	1,354	1,414	1,566	1,692	9.9%
Real Property Transfer	924	993	1,105	1,194	1,239	7.6%
Mortgage Recording	527	628	714	780	820	11.7%
Utility	407	417	426	433	438	1.8%
Hotel Occupancy	468	474	461	456	478	0.5%
Commercial Rent	617	636	655	674	694	3.0%
Cigarette	69	68	66	64	63	-2.5%
Other Taxes, Audits, and PEGs	1,211	1,224	1,207	1,208	1,208	-0.1%
Total Taxes	**$41,355**	**$43,641**	**$45,330**	**$48,060**	**$51,023**	**5.4%**
Other Revenue						
STaR Reimbursement	$790	$864	$866	$870	$875	2.6%
Miscellaneous Revenues	4,498	5,527	4,503	4,560	4,656	0.9%
Unrestricted Intergovernmental Aid	25	-	-	-	-	n/a
Disallowances	(15)	(15)	(15)	(15)	(15)	n/a
Total Other Revenue	**$5,298**	**$6,375**	**$5,353**	**$5,416**	**$5,516**	**1.0%**
Total City Funded Revenue	**$46,653**	**$50,016**	**$50,683**	**$53,476**	**$56,539**	**4.9%**
State Categorical Grants	$11,323	$11,389	$11,506	$11,644	$11,762	1.0%
Federal Categorical Grants	7,759	6,919	6,816	6,739	6,737	-3.5%
Other Categorical Aid	1,058	954	950	948	934	-3.1%
Interfund Revenues	551	509	504	504	504	-2.2%
TOTAL Revenues	**$ 67,345**	**$ 69,788**	**$ 70,460**	**$ 73,310**	**$ 76,476**	**3.2%**

SOURCE: IBO

NOTES: Estimates exclude intra-city revenues. Figures may not add due to rounding.

slightly higher than last year's 2.6 percent increase, which came on the heels of two years of aggregate market value decline. Assessed value for tax purposes on the 2013 roll is projected to grow 3.9 percent over 2012. The final assessment roll for 2013 is expected to total $161.5 billion in assessed value for tax purposes—a reduction of 1.6 percent ($2.7 billion) from the tentative roll.[1]

This projected decrease is a greater than usual change in the roll. IBO expects routine tentative-to-final roll adjustments—such as Tax Commission appeals, corrections, adjustments for properties under construction, and general exemption processing—to reduce assessed value by $1.5 billion. In addition, there will be a large decrease in assessments for tax purposes from late renewals of tax exemptions for nonprofit organizations, offset by a small increase for correction of too generous exemption amounts granted under the state's school tax relief (STAR) program. Taxpayers will be billed for the difference (about $30 for a homeowner) between the STAR benefit granted and what it should have been.

For 2014, IBO forecasts an increase in aggregate market value of 3.1 percent, with further increases of 3.4 percent and 3.6 percent in 2015 and 2016, respectively. IBO projects growth of 3.9 percent in aggregate assessed value for tax purposes in 2014. With the pipeline of prior assessed value increases in commercial properties (assessment changes are phased in over five years for most income-producing properties plus coop and condo buildings) replenished by the strong growth beginning in 2012, the rise in assessed value for tax purposes accelerates over the forecast period to an annual average of 4.6 percent.

After the Department of Finance completes the assessment roll, the actual property tax levy is determined by the City Council when it sets the tax rates for each class. IBO's property tax revenue forecast, as does the Bloomberg Administration's, assumes that the average tax rate during the forecast period will be 12.28 percent, the rate set by the City Council in December 2008 when it enacted the Mayor's proposal to rescind a short-lived 7.0 percent rate reduction. While the overall average rate is expected to remain frozen, individual class rates will vary under a formula that is largely determined by state law.

The amount of property tax revenue in a fiscal year is determined not only by the levy, but also by the delinquency rate, abatements granted, refunds for disputed assessments, and collections from prior years. Taking these other factors into account, IBO projects that property tax revenue for 2012 will total $17.8 billion, 5.5 percent higher than revenue for 2011. For 2013, IBO forecasts property tax revenue of $18.3 billion—2.6 percent more than projected for this year. From 2014 through 2016, revenue growth is expected to average 4.7 percent a year, with revenue reaching $20.9 billion by the last year of the forecast period. The projected revenue growth in 2013 through 2016 (4.1 percent) is barely half the 8.1 percent average annual growth seen in the preceding four years (2009 through 2012), when the lags in the city's property tax system sustained assessment growth even as market values were stabilizing or falling.

Mortgage Recording and Real Property Transfer Taxes. Revenues from the real property transfer tax (RPTT) and the mortgage recording tax (MRT)—collectively referred to as the transfer taxes—are now in their second year of recovery following the recession and collapse in the market for real estate. For the foreseeable future, however, revenues will continue to fall well short of the levels reached during the real estate boom. IBO expects the combined revenue from the two taxes in 2016 to total almost $2.1 billion—above the levels at the start of the boom in 2004 ($1.6 billion) but far below the 2007 peak of $3.3 billion.

The recovery in real estate markets that began in 2010 has continued, albeit at an uneven pace. The aggregate value of taxable real estate sales recorded during the first quarter of fiscal year 2012 (July-September 2011) was almost $19.0 billion, the highest quarterly total since July-September 2008. During the second quarter (October-December 2011) taxable sales fell sharply—by 31.1 percent for residential sales and 30.2 percent for commercial sales—to $13.2 billion. IBO projects slower commercial sales growth in 2013-2016. The projected completion of Towers One and Four at the World Trade Center site by the end of calendar year 2013 will add 4.8 million square feet to the stock of Manhattan office and retail space. The resulting downward pressure on commercial rents and building prices will act as a brake on office sales in the short term. By 2016, commercial sales are projected to reach $42.4 billion, more than three times the level of 2010, but still far below the 2007 peak of $71.4 billion.

RPPT collections dropped significantly in October-December 2011 compared with the July-September quarter, but rebounded somewhat in January-February 2012, primarily on the commercial side. IBO's RPTT forecast for 2012 is $924 million—an increase of 16.2 percent over 2011. RPTT growth is being driven primarily by commercial real estate sales. IBO expects this trend to continue in 2013 when revenues will reach $993 million. Starting in 2014, IBO projects residential sales to grow at a faster pace than commercial sales. By 2016, RPTT revenue is projected to be just under $1.24 billion, around 72 percent of the 2007 peak of $1.73 billion.

MRT revenues fell 77.1 percent between their peak in 2007 ($1.6 billion) and their trough in 2010 ($366 million), and have been slower to recover than the RPTT. However, IBO forecasts strong growth of MRT revenues in 2012—to $527 million, 21.4 percent above 2011 revenue. In addition to mortgage activity related to property purchases, the combination of historically low interest rates and some easing in credit markets is stimulating refinancing activity. According to the Mortgage Brokers Association, refinancing activity is currently strong, but is expected to diminish later this year as the pent-up demand for refinancing is satisfied and interest rates rise.

The MRT does not follow the value of real estate sales as closely as does the RPTT, because not all sales involve a mortgage and not all new taxable mortgages involve a sale. Also, the foreign buyers who account for a significant share of the luxury housing market in the city can often secure financing in their home countries or pay cash and therefore incur no MRT liability.

IBO expects MRT revenues to increase at a faster rate than RPTT revenues during 2013 through 2016, as credit eases and the residential market begins to grow faster than the commercial sector. IBO expects MRT revenues to be $628 million in 2013 (an increase of 19.2 percent). Even with continued growth, MRT collections are expected to be just $820 million by 2016, slightly over half their 2007 peak.

Personal Income Tax. IBO projects PIT revenues of $8.0 billion in 2012, an increase of 5.1 percent over 2011, although withholding—which accounts for about 70 percent of total PIT collections—is expected to remain unchanged. The estimated 20.0 percent decline in securities industry bonuses is offseting the strong employment gains during calendar year 2011. Over half of the revenue increase this year is due to a technical adjustment in state/city offsets which does not directly reflect employment and income growth in the city. The balance of PIT growth this year is attributable to estimated payments, which are currently up 14.0 percent over last year, but are expected to slow considerably in the remaining months to show an annual gain of only 5.0 percent, and final return payments net of refunds.

For 2013, we expect PIT revenue to grow by 9.4 percent to $8.8 billion, with projected increases in withholding, estimated payments, and final returns. The 4.2 percent withholding growth is largely driven by IBO's forecast of strong growth in personal income and a larger bonus pool attributable to our expectation of somewhat higher Wall Street profits. Estimated payment growth of 19.3 percent next year is partly a function of our assumption that the preferential rates for capital gains in the federal income tax system as well as the lower marginal rates on high-income taxpayers will expire at the end of December 2012. Taxpayers will have an incentive to speed up capital gains realizations before the changes take effect, producing higher capital gains tax liability and a temporary spike in estimated payments.

After 2013, PIT revenue grows rapidly, averaging 6.7 percent annual growth in 2014 through 2016. IBO expects withholding collections to increase an average of 8.1 percent, driven by local employment gains ranging from 68,700 to 81,000 jobs a year and increases in personal income averaging 5.4 percent annually. Estimated payments are expected to shrink 6.9 percent in 2014 because of the capital gains realizations that will be shifted to 2013, but then resume growing at an average rate of 9.9 percent in 2015 and 2016.

The projected average annual PIT growth rate from 2012 through 2016 is 7.3 percent—solid growth though slower on average than PIT revenue growth during previous local expansions. After removing the impact of tax policy changes, PIT revenue grew at an average annual rate of 11.8 percent from 2003 through 2008. Average annual growth was even higher—11.4 percent—in 1994 through 2000 after similar adjustments.

Business Income Taxes. After a relatively strong rebound in 2011, total revenue from the three business income taxes was basically flat through January 2012, with net fiscal year to date revenue up 1.1 percent over the prior year. For the year as a whole, IBO forecasts a modest increase of $181 million (3.4 percent) in business tax collections—the result of a large decline in banking corporation tax (BCT) receipts offsetting most of the expected increases in general corporation tax (GCT) and unincorporated business tax (UBT) collections. IBO expects stronger business income tax revenue growth of 9.4 percent in 2013 and growth averaging 7.2 percent a year for the remainder of the forecast period. Combined revenues will total $5.5 billion in 2012 and reach $7.4 billion by 2016.

For 2012, IBO projects robust growth of 15.7 percent in GCT revenue, slow growth of 0.5 percent for the UBT, and a 13.7 percent decline in BCT revenue. Through January, GCT revenue is up $161.9 million (16.4 percent) for this fiscal year. Slightly slower growth is projected for the remainder of the year yielding a projected full-year increase of $356.5 million (15.7 percent). Wall Street firms returned to profitability in 2009 (although profits were an anemic $7.7 billion for 2011) but the huge losses of 2007 and 2008 resulted in large net operating loss reserves which can be carried forward for tax purposes. As a result, current and future corporate profits will not immediately translate into GCT revenues.

BCT revenue has grown more than fourfold in the last decade but the growth has hardly been steady as double-digit percentage increases and decreases from year to year have been the norm for this tax. From 2010 to 2011, BCT revenue grew 38.9 percent to reach $1.3 billion, its highest level ever. For 2012, IBO projects a 13.7 percent drop in collections, to $1.2 billion. The

BCT's inherent volatility is exacerbated by very large fluctuations in refunds, the result of adjustments to tax liabilities based on losses and gains not recognized until a year or more after they are incurred.

The UBT grew 7.4 percent to $1.7 billion in 2011, reversing much of its revenue decline from 2008 through 2010. So far in 2012, UBT receipts are 4.4 percent below the same period last year. IBO projects a very modest increase of 0.5 percent in UBT for the year as a whole.

For 2013, IBO projects strong revenue growth from the business income taxes of 9.4 percent to reach $6.0 billion. Unlike 2012, revenue from all three taxes is expected to increase with a $153 million (5.8 percent) rise in the GCT, a $171 million increase (10.2 percent) in the UBT, and a BCT increase of $192 million (16.6 percent).

IBO projects that business income tax revenue growth will slow to 4.9 percent in 2014 before bouncing back to average annual growth of 8.3 percent for 2015 and 2016. For the GCT, we project net revenue growth averaging 6.1 percent over 2014-2016. The BCT is expected to increase, but below historical levels, with growth of 4.5 percent in 2014 and average growth of 9.4 percent over 2015-2016. The UBT is projected to climb steadily to reach $2.4 billion by 2016—with growth averaging 8.3 percent in 2014 through 2016.

General Sales Tax. Based on IBO's revised economic forecasts of personal income, employment growth, and Wall Street bonuses, as well as analysis of collections to date this fiscal year (through January they are 4.7 percent higher than last year), IBO projects 2012 sales tax revenue of $5.8 billion—4.1 percent higher than 2011 collections. This relatively modest projected revenue increase is due to our expectation of slower growth in spending by local consumers and foreign visitors through the remainder of this fiscal year. With expected city job growth of 1.6 percent and 1.3 percent growth in the average wage and salary (nominal), local consumer spending in calendar year 2012 is not expected to grow as fast as it did in 2010 and 2011. Given the importance of financial services and related industries to the local economy, the projected weakness in financial sector employment and compensation is expected to reduce financial industry employees' spending in the city's leisure and hospitality, accommodation, and food services sectors, leading to lower sales tax collections. Finally, economic difficulties in the euro zone are likely to curtail tourist spending.

After 2012, growing economic momentum at home is expected to boost sales tax revenue growth. For 2013, IBO forecasts $6.2 billion in sales tax revenue—5.8 percent greater than our projected revenue for this year. The acceleration of revenue growth is primarily due to the expectation that consumer spending will increase significantly above 2012 levels, driven by a pick-up in national and local employment, accelerating New York City wage and salary growth (from 1.3 percent in calendar year 2012 to greater than 6.5 percent in each of the following two years), and resumption of economic growth in Europe. After fiscal year 2013, IBO projects sales tax revenue growth to average 4.9 percent through 2016, when revenue is expected to reach $7.1 billion.

Hotel Occupancy Tax. Hotel occupancy tax collections are projected to grow strongly in 2012 and 2013, but then decline in subsequent years due to the expiration of a temporary 0.875 percentage point increase in the hotel room tax rate. For 2012, IBO forecasts tax revenue of $468 million—10.9 percent higher than 2011 revenue. This strong growth is due to another record year for tourism in the city: according to NYC & Co., the city's tourism bureau, an estimated 50.5 million tourists visited New York City in calendar year 2011—an increase of 3.5 percent over the previous year. IBO expects the euro zone economy to slow this year, reducing the spending of tourists from the continent and causing hotel tax revenue to grow just 1.3 percent in 2013, reaching $474 million.

Hotel tax revenue is expected to then decline by 2.9 percent in 2014 to $461 million due to the scheduled reduction of the current hotel room occupancy tax rate of 5.875 percent to 5.0 percent on November 30, 2013. If the higher rate were once again extended, IBO projects that the expected recovery in the city's tourism sector would result in hotel tax revenue growth of 5.2 percent for 2014. By 2016, revenue is expected to rebound to $478 million as the global economy gains momentum and tourism picks up.

The pause in revenue growth in 2013 is due to the euro zone financial crisis, which is widely expected to dampen consumer and business spending of euro zone visitors. If the euro zone's economy slows further than anticipated, our forecast of hotel tax revenues is likely to prove too optimistic. According to NYC & Co., in calendar year 2011 visitors from the euro zone and the United Kingdom accounted for 44.0 percent of the city's estimated 10.3 million international tourists. Even though only 20.4 percent of visitors to the city in that year were from foreign countries, these international visitors accounted for 46.3 percent of total spending by tourists because on average they stay more than twice as long in the city and spend almost four times as much money as domestic tourists. Although the expected decline in European visitors may be somewhat offset by an increase in visitors from fast-growing emerging market countries such as Brazil and the gradual recovery of the U.S economy, it is not anticipated—at least for next year—that such a change in the mix of visitors will be enough to maintain the hotel tax revenue growth in 2010 through 2012.

Other Revenues

The city's nontax revenues combine a variety of fees, fines, charges, interest income, and other miscellaneous revenue, which sum to $5.3 billion this year. In addition, the revenue forecast includes other revenues from noncity sources such as categorical state and federal aid. The tally for the latter group in 2012 is $20.7 billion.

The city nontax revenues are expected to be fairly flat with the exception of 2013 when the city expects to realize $1.0 billion from the sale of 1,800 new taxi medallions for cabs with enhanced accessibility. This one-time transaction accounts for virtually all the jump in city nontax revenues to $6.4 billion in 2013. Nontax revenues are forecast to fall back to $5.4 billion in 2014.

Federal categorical revenue—forecast to total $7.8 billion in the current year—is expected to shrink to $6.9 billion in 2013 as some of the remnants of the federal stimulus programs expire. Noncity revenues are expected to remain fairly flat after 2013.

Endnotes

[1]When IBO refers to market values and assessments, the reference includes only taxable property. The assessed value for tax purposes (also referred to as billable taxable value) reflects the required phase-in of assessment changes for apartment, commercial, and industrial buildings. In this report billable taxable values are shown before applying the STAR exemptions.

Education

Classroom Spending to Decline in Traditional Public Schools, Payments to Nonpublic Schools to Rise

Classroom spending in the city's traditional public schools would decline under the Mayor's Preliminary Budget by $119 million (1.5 percent), with a larger reduction for general education classrooms. While the Department of Education's (DOE) overall budget would increase by $183 million—slightly less than 1 percent—increases in the amounts allocated to special education prekindergarten programs ($109 million); charter schools, contract schools, and foster care payments ($86 million); and special education instruction and support ($134 million) absorb all of this increase and more, resulting in a $203 million (3.3 percent) decrease in planned spending on general education classroom instruction. Other areas of growth in the department's budget include pupil transportation ($57 million) and employee fringe benefits other than pension contributions ($54 million). Additional areas where spending will decrease include school facilities, school food services, and central administration.

The Preliminary Budget does not fully account for the additional cost of charter schools that have already been approved for opening in September 2012, nor does it include enough funding to maintain the current level of classroom services beginning in 2014. IBO's estimate of the combined shortfall is $27 million in 2013, which grows to $258 million by 2016. Covering these additional costs as the budget process moves forward will require either additional funding from the city or reduced spending elsewhere in the DOE budget.

Sources of Funding for Education Department Budget
Dollars in millions

	2009	2010	2011	2012	2013
City Support	$7,273	$7,167	$7,768	$9,167	$9,231
State Support	8,652	8,072	8,123	8,113	8,349
Foundation Aid	6,152	5,573	5,430	5,327	5,462
Other	2,500	2,499	2,693	2,786	2,888
Federal	1,735	2,961	2,795	2,042	1,957
Other	243	298	253	128	97
Total	**$17,903**	**$18,499**	**$18,939**	**$19,450**	**$19,633**

SOURCES: IBO; February 2012 Preliminary Budget

The DOE's 2013 budget will reach $19.6 billion under the Preliminary Budget. Local support for DOE will increase by $95 million to $9.2 billion, state support will increase by $236 million, to $8.3 billion; while federal support will decrease by $86 million, to $1.96 billion, and other categorical funding will decrease by $32 million.

School Budgets. A comparison of budgets for classroom instruction suggests that school budgets will be tighter in 2013 than they are in 2012. Using the categories most readily available to budget analysts—units of appropriation tracked in the city's Financial Management System—the overall amount budgeted for general education and special education classrooms combined increased by $162 million in 2012. IBO's analysis of individual school budgets for those years shows a decline of $104 million in 2012 in the amount allocated to individual school budgets, including a $97 million drop in spending on school staff. As in past years, some of the money in the classroom instruction units of appropriation was allocated to central accounts and did not make it to school budgets. This reduction in the individual school-level budgets likely reflects the savings resulting from staff attrition combined with assorted budget cuts imposed centrally. While these "classroom" units of appropriation *increased* in 2012, they are budgeted to *decrease* by $119 million in 2013.

Details of 2013 Preliminary Budget. The three main segments of the DOE's expense budget—services to schools, nonpublic school payments, and systemwide costs—show little change in their shares of the budget at 71 percent, 14 percent, and 16 percent, respectively. Services to schools, budgeted at $13.7 billion for 2013, include classroom instruction, instructional support, instructional administration, and non-instructional support services. The nonpublic school

Department of Education Budget, by Program Area

Dollars in millions

	2009	2010	2011	2012	2013 (Preliminary)
TOTAL DOE BUDGET	**$17,904**	**$18,501**	**$18,943**	**$19,451**	**$19,633**
Services to Schools	**$13,612**	**$13,704**	**$13,829**	**$13,764**	**$13,703**
Classroom Instruction	**$8,273**	**$7,820**	**$7,831**	**$7,993**	**$7,874**
General Education	6,399	6,052	6,006	6,140	5,937
Special Education	1,147	1,020	1,052	1,058	1,106
Citywide Special Education	727	748	773	795	831
Instructional Support	**$2,407**	**$2,804**	**$2,926**	**$2,713**	**$2,741**
Special Education Instructional Support	447	489	510	580	631
Categorical Programs	1,960	2,315	2,416	2,133	2,110
Instructional Admin	**$220**	**$213**	**$134**	**$145**	**$145**
Operational Admin	220	213	134	145	145
Noninstructional Support	**$2,712**	**$2,867**	**$2,938**	**$2,913**	**$2,943**
School Facilities	749	744	759	618	595
School Food Services	384	409	380	415	410
School Safety	217	295	298	302	304
Pupil Transportation	968	996	1,017	1,076	1,132
Energy & Leases	394	423	484	502	502
Nonpublic and Charter Schools	**$1,565**	**$1,902**	**$2,175**	**$2,632**	**$2,827**
SE Prekindergarten Contracts	**$740**	**$853**	**$943**	**$1,084**	**$1,194**
Prekindergarten Transportation	97	135	128	133	148
Prekindergarten Tuition	643	718	815	951	1,046
Charter School, Contract School, Foster Care Payments	**$764**	**$977**	**$1,162**	**$1,477**	**$1,562**
Blind and Deaf Schools	-	-	-	59	59
Charter Schools	311	418	572	737	779
Contract Schools (in-state)	236	268	321	330	368
Contract Schools (out-of-state)	32	35	32	44	49
Carter Cases	144	215	183	246	236
Nonresident Tuition/Foster Care	27	27	37	47	57
Tax Levy Match for Chapter 683	14	14	17	14	14
Nonpublic School & FIT Payments	**$61**	**$72**	**$70**	**$71**	**$71**
Nonpublic School Payments	23	26	24	26	26
Technology Payments	38	46	46	45	45
Systemwide Costs	**$2,727**	**$2,895**	**$2,939**	**$3,055**	**$3,103**
Fringe Benefits	**$2,355**	**$2,536**	**$2,601**	**$2,746**	**$2,800**
Fringe Benefits	2,314	2,502	2,589	2,746	2,800
Collective Bargaining	41	34	12	0	0
Central Administration	**$372**	**$359**	**$338**	**$309**	**$303**

SOURCES: IBO; February 2012 Departmental Estimates

NOTES: Fiscal Years 2008-2011 are actual spending. Fiscal years 2012 and 2013 are projections. Does not include debt service and pensions. Includes intra-city sales. Figures for 2009, 2010, and 2011 do not match totals in table on page 19 due to rounding. These numbers are taken from the Preliminary Budget and do not reflect IBO reestimates.

portion of the budget, totaling $2.8 billion, includes special education prekindergarten contracts, charter school, contract school, and foster care payments along with pass-through payments for nonpublic (private) schools and the Fashion Institute of Technology. Systemwide costs of about $3.1 billion make up the balance of the operating budget, consisting of fringe benefit expenditures and central administrative spending.

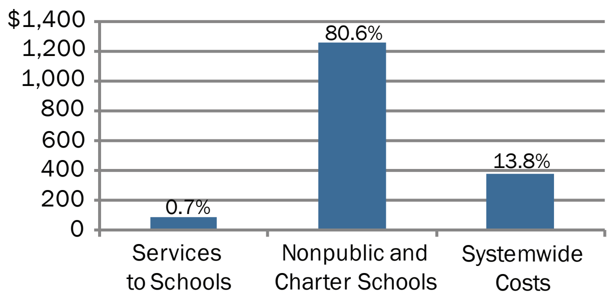
Although services to schools continue to be the biggest share of the education budget, growth in this area of spending has been nearly flat since 2009 while the nonpublic school payments portion continues to grow. The latter increased by almost $480 million this year (22 percent), largely driven by special education prekindergarten, charter, and contract school payments. The growth anticipated for 2013, $195 million (7.4 percent), is lower than in the previous year.

Within the traditional public schools, special education spending is budgeted to increase by $135 million for 2013, while general education classroom instruction funding decreases by $203 million. Other services to schools expected to decline next year include some non-instructional support services such as school facilities ($23 million) and school food services ($5 million.)

Fringe benefit costs for 2013 will reach $2.8 billion, a 2.0 percent year-over-year increase. The increase is mostly due to health insurance benefits. Unlike other city departments, the DOE budget includes a labor reserve to absorb the cost of labor settlements. However, there is currently no money allocated in the reserve for the bargaining round that covers the years since the teachers' and the principals' contracts expired in October 2009 and March 2010, respectively.

Spending Growth in Other Categories Far Above Services to Schools

Change in Total Spending 2009-2013, dollars in millions



SOURCES: IBO; Mayor's Office of Management and Budget

IBO Reestimates

IBO reestimated some of the projections in the Mayor's Preliminary Budget for DOE. As a result our forecasts of total DOE spending differ by relatively modest amounts from those in the Mayor's Preliminary Budget, although the differences grow over time. The differences are in our estimates for spending on classroom instruction, state categorical programs (for this year only), and the required payments to charter schools.

For 2012, our estimate for classroom instruction and categorical spending is based on analysis of actual spending so far this year. We project that spending in those areas will be $86 million less than the estimate in the Preliminary Budget. For 2013, IBO again expects classroom instruction spending to be lower, by $24 million, but that will be offset by the need for an additional $51 million in charter school payments that have not been included in the Preliminary Budget. The extent of the underestimate for charter school payments increases to $82 million in 2014, $112 million in 2015, and $143 million in 2016. In those three years, IBO estimates that the current budget for classroom instruction understates what would be needed to maintain current levels of service by $26 million, $98 million, and $115 million, respectively.

Assuming that the differences in classroom instruction and charter school payments are covered by adding city funds to the DOE budget—rather than shifting resources within the department's budget—city funded spending would be $27 million higher in 2013, $108 million higher in 2014, and $258 million higher in 2016.

The city has maintained that any salary increase will be funded through higher productivity, although it is difficult to see how that could be achieved retroactively.

Nonpublic School Payments. The total nonpublic school payments portion of the budget will increase by 6.5 percent in 2013 to a total of over $2.8 billion. The Financial Plan projects this to reach $3.5 billion by 2016. These payments include contracts for special education services for prekindergarten students, tuition at private schools for certain special education students, state-mandated payments to charter schools, and "pass-throughs" of support for private schools and the Fashion Institute of Technology.

Prekindergarten contracts for special education are expected to be over $1.1 billion in 2012 and reach $1.2 billion in 2013 driven by a $141 million increase in payments to the contracted school vendors. The DOE estimates that roughly 32,000 students received services from these vendors this year. These payments are expected to increase by an additional $108 million in 2014.

Spending on "Carter cases" and other contract special education schools covers tuition for students when it has been determined that they require services that are not available in the regular public schools. After many years of dramatic increases up through 2012, cost of Carter cases appears to be leveling off in 2013. The DOE's spending in this area is largely determined by court decisions, limiting the department's ability to control these costs.

The DOE payments to charter schools consist largely of a per capita payment for each student enrolled in a charter school plus some special education support. This expense increased by $165 million this year to $737 million. For charter schools, increased enrollment has been the primary cause of the growth in spending.

The amounts budgeted for charter school growth in the Preliminary Budget do not account for new charter schools that will open in September 2012. According to officials at the Mayor's Office of Management and Budget, those estimates are not received from the DOE until later in the budget cycle. However, the State Education Department has already identified 26 new charter schools scheduled to open in New York City in September. IBO projects that as a result an additional 3,763 students will be attending charter schools next fall than are accounted for in the Preliminary Budget. Thus, we estimate that spending on charter schools for 2013 will be at least $51 million higher than the $779 million that is reflected in the Preliminary Budget. (See sidebar on page 21 for further discussion of IBO's reestimate.)

We also anticipate that the city will see a similar number of new charter schools opening in September 2013. Combining the effects of new schools to be opened in 2012 and 2013, we estimate that the cost of charter schools will be $82 million more in 2014 than the current Financial Plan estimates. These additional costs will grow to $143 million by 2016, even if no new charter schools were to open after September 2013.

Changes in State Aid

The Governor's Executive Budget projects increases in school aid of 4.0 percent in each of the next two years, $805 million in 2013 and $879 million in 2014. Foundation aid is the largest single source of state aid, accounting for about 78 percent of general support aid. Under the terms of the Governor's Executive Budget, $290 million of the 2013 increase would be for general support including foundation aid, $265 million would go to support increased reimbursement in expense-based aid programs, and $250 million would be allocated for performance-based or competitive grants. Historically, New York City typically receives roughly 41 percent of all foundation aid distributed across the state. However, the city is concerned that building aid—much of which is spoken for to finance the DOE's capital program—has been included in the calculation for aid increases this year, thereby reducing the amount of unrestricted aid available. The Preliminary Budget assumes that total state aid will increase by about $236 million in 2013.

The state is implementing several budget reforms that could affect New York City, if not this year, then in the future. Last year's state budget capped annual school aid increases at 4.0 percent or the growth in personal income across the state. Going forward there will also be two-year appropriations for school aid which should facilitate the planning process. In recognition of increased spending for special education due to both enrollment increases and growing program costs, this year's state budget includes proposals that are intended to constrain early intervention and special education prekindergarten costs, although the changes would take several years to generate significant savings. (City spending on early intervention flows through the Department of Health and Mental Hygiene rather than the Department of Education.) The proposed changes are aimed at reducing potential abuse and include requiring greater scrutiny of provider selections and separation of evaluation from service provision.

The Governor's budget proposal would also change the teacher disciplinary hearing process. The primary change alters the payment arrangement, shifting the costs to the school districts—including the city—and the employee unions. The Governor has indicated that any savings to the state will be directed back to school districts to reduce reimbursement lags. The Governor's budget also included incentives to reach agreements on the teacher evaluation process. At stake was $700 million in Race to the Top federal stimulus funding. A deal was reached in time to secure the federal funding but the new evaluation system still needs to be in place by January 2013 or the city might lose its share of the basic 4.0 percent increase in state spending. A tentative agreement has been reached although many details remain unresolved.

Campaign for Fiscal Equity. Foundation aid, which was to provide much of the new state aid expected under the resolution to the Campaign for Fiscal Equity (CFE) lawsuit has been declining since 2009. All school districts in the state were originally promised a minimum 3.0 percent annual increase in aid under the 2007 legislation, effectively ending CFE. But since 2009, the state has frozen foundation aid and extended the date by which it promises to fully implement the foundation aid increases that were set under the initial parameters back in 2007. Meanwhile, the state will continue to mandate that school districts with underperforming schools maintain their spending obligations under the Contracts for Excellence plans required to receive the state money.

The city expects foundation aid to remain stagnant for the foreseeable future. CFE, which had increasing state aid for high needs districts as one of its fundamental goals, has ironically evolved into an unfunded mandate forcing many districts to increase spending to meet state "contracts" while the state has essentially capped its aid well below the original legislated targets.

State & Federal Changes Affect Some Major City Programs

Federal Funding to Decline for Key Housing Programs

Cuts to federal appropriations for housing programs mean the city will receive less funding through the Community Development Block Grant (CDBG) and HOME Investment Partnership this year— two crucial sources of expense and capital funding for the Department of Housing Preservation and Development (HPD). The impact of these cuts will differ because the Department of Housing and Urban Development (HUD) has also begun using updated census data to determine the city's annual funding allocations through the formula grants.

The use of the new data increases the cut for the HOME funds—which provides capital funding for the city's affordable housing programs—and combined with the cut in appropriations results in an overall reduction of 45 percent compared with last year. On the other hand because it uses a different allocation formula, applying the new data slightly offsets the appropriations cut for the Community Development Block Grant, resulting in an overall reduction of 8 percent in CDBG funding compared with last year. While the city projects that the impact of these cuts will not be felt immediately, they will undoubtedly affect the city's ability to develop and maintain affordable housing.

Changes in the funding allocations based on the new Census data were announced by HUD shortly before the city released its Preliminary Budget in January, thus the changes are not recognized in the current expense budget or Capital Commitment Plan. The city expects to reflect the impact of the HOME and CDBG cuts in the Financial Plan when the Executive Budget is released.

Effects of New Census 2010 Data. Federal fiscal year 2012 marks the first time that HUD used data from the 2010 Census and the Census Bureau's annual American Community Survey to determine funding levels for its community development grants. While CDBG and HOME have overlapping goals to provide decent, affordable housing to low-income communities, the funding formulas for each grant are calculated differently, which—prior to application of the across-the-board appropriation cuts—resulted in the lower HOME allocation and the higher CDBG allocation for the city compared with past years.

For the HOME program, the city lost funding on all of the factors on which the allocation is based, including family poverty rate, substandard rental units, and rental housing built before 1950 occupied by low-income families. Because this suggests living standards for poorer city residents are improving, the new data reduced the city's award by about 12 percent compared with last year. This reduction is applied before the 38 percent overall appropriations cut is added, which brings the cut to about 45 percent.

Using the same data sources—but different indicators with different weights—increased the city's CDBG allocation by about 3 percent this year compared with last year, which helped offset the federal government's overall 11 percent appropriations cut to the program, for a total 8 percent reduction in CDBG funds for the city. Three main indicators determine CDBG funding for New York City: the city's poverty rate, which decreased slightly in the new data; the rate of decline in the city's population growth compared with other U.S. cities, which increased slightly; and the amount of pre-1940s housing, which also increased and is mainly responsible for the city's higher allocation.

While an increase in housing built before 1940 may seem impossible, there are several ways for this to occur. First, if housing built before 1940 is renovated and existing units are subdivided into new units, they count as new pre-1940s housing. Similarly, if a structure built before 1940 is converted to housing from some other use it is also considered new housing. Lastly, HUD has reported that survey differences between the new and old data sources also contribute to the increase in older housing counts. Although HUD's pre-1940 housing estimate is now closer to counts derived from the city's property tax data than the older numbers, HUD's count is still about 300,000 units lower.

City's HOME Grant Cut by Nearly Half. Last year (in federal fiscal year 2011), HPD received a HOME allocation of about $110.5 million. Due to the new data used in the allocation formula and federal appropriation cut, the city's federal fiscal year 2012 award is about $60.3 million. In recent years, HOME funds have made up about 29 percent of HPD's capital commitments. The funding has mainly gone to developing supportive housing programs for populations with special needs and new construction programs for low-income rental housing. In addition to the capital funding, HPD can use 10 percent of its annual HOME grant for administrative purposes, which flows through the city's expense budget. This year, about $7 million of HOME funds have been budgeted to pay the salaries of about 120 staff.

Because HOME funds can be spent over several years and given the timing of the federal budget, the Bloomberg Administration reports that it does not expect the HOME cut to impact its capital plan until after city fiscal year 2014. (It also expects it can delay the cut on the expense side, although this may be more difficult.) According to HPD's current Capital Commitment Plan, which does not yet reflect the cut, about 79 percent of HOME capital funds planned from fiscal years 2015 through 2018 are for special needs housing—making up about 89 percent of the overall funds planned for this category ($224 million of the $251 million). New housing construction projects receive 19 percent of HOME funds planned for the same period. However, these projects also receive significantly more in city capital funding, with HOME funds making up just 14 percent of HPD's total planned commitments for new housing construction. The remaining 2 percent of HOME funds are planned for programs that preserve existing affordable housing.

While the city does not expect the cut to impact the budget until after fiscal year 2014, this is not the first cut to HOME funds in recent years. Last year's federal budget reduced HOME funds by 11 percent. In addition, the President's proposed federal fiscal year 2013 budget holds HOME funding at its current appropriation level. As HOME funds become an increasingly scarce, the city will need to look for new financing models for recipient programs, especially its special needs housing programs, as it seeks to continue to increase the amount of affordable housing in the city.

Cut to Community Development Block Grant Mitigated. The city's CDBG award for federal fiscal year 2012 is $149.7 million—about $13.6 million, or 8 percent, less than it received last year, significantly smaller than cuts to the HOME program. Unlike HOME funds, the city divides its CDBG award across several agencies, including HPD and the departments of Sanitation, City Planning, Education, and Youth and Community Development. However, HPD receives the largest share, usually around 60 percent of the grant. Like HOME funds, CDBG funds can also be spent over several years. In addition, the city counts as CDBG funding the revenue directly generated from the use of CDBG funds, including, for example fines relating to code enforcement programs funded by the grant. Overall, CDBG (annual awards and program income) fund about 23 percent of HPD's expense budget, with most of that money going towards housing code enforcement programs.

Because the city has discretion as to how much grant funding it allocates to each agency—along with the roll of past CDBG awards and HPD's ability to generate additional program income—it is unlikely that HPD will see its CDBG funding levels reduced by the full 8 percent when the city allocates the federal fiscal year 2012 grant among recipient agencies in the Executive Budget. However, like HOME, the federal fiscal year 2011 CDBG allocation was also cut by 16 percent, which led to 5 percent cuts in 2012 and 2013 for HPD, increasing to 10 percent in the out-years. In addition, the President's proposed budget for federal fiscal year 2013 holds CDBG funding levels steady. While the loss of federal support for affordable housing this year may not have a significant immediate effect, it will affect the city's ability to meet its housing goals in the future.

State Actions Drive Cuts to Public Assistance Spending

The Preliminary Budget projects that total spending on cash assistance including the basic grant and rent subsidies will be $1.4 billion in 2012, a decrease of 6.7 percent from 2011. Spending in 2013 is projected to decrease by an additional 4.5 percent before leveling off in the later years of the Financial Plan. The projections represent a significant break from recent trends; from 2007 through 2011 total public assistance spending rose by nearly 30 percent. Both the recent increases and the projected decreases in spending reflect in large part decisions made by state officials, including increasing the size of the basic grant and eliminating state and federal funding for the Advantage Rental Assistance program.

In contrast, changes in the cash assistance caseload have had only a limited impact on grant spending. The recent economic downturn resulted in a modest increase in the number of public assistance recipients in the city. As the local economy slowed, the welfare rolls rose from 334,000 in September 2008 to 358,000 in December 2009, an increase of 7.1 percent. Since then the caseload has stabilized, with 353,000 individuals receiving cash assistance in December 2011.

Basic Grant Increase. The bulk of welfare expenditures are for the traditional cash assistance program, which provides eligible recipients with a basic grant to cover general expenses such as food and clothing, and specific grants to cover shelter and utility costs. A major factor contributing to increased public assistance spending over the last few years has been the state's decision to increase the size of the basic grant. After the basic grant was frozen for nearly two decades, the state increased the value of the grant by 10 percent in July 2009 and an additional 10.0 percent in July 2010. Each of these increases added about $40 million to total grant spending in the city. A final 10 percent increase was scheduled for July 2011, but in an effort to limit state spending the 2011-2012 state budget delayed this increase until July 2012.

In order to limit the impact of this mandated increase on local budgets (in New York State localities share with the state the cost of public assistance not covered by federal dollars), the state agreed to cover the local share of the incremental costs through March 31, 2012, using state and federal funds. After that point, however, the city—and other counties across the state—will be responsible for its share of the costs, adding significantly to the city's welfare expenditures.

The Governor's 2012-2013 Executive Budget proposes to further delay the final round of increases to the basic grant by splitting it into two rounds of 5 percent increases to take place in July 2012 and July 2013; the city's Preliminary Budget assumes implementation of this delay. No further increases in the basic grant are scheduled after July 2013. City-funded expenditures for the basic grant are projected to increase by nearly $40 million in 2013, however, as local governments become responsible for their share of the basic grant increases.

Rent Subsidies. Another major factor driving public assistance cost increases over the last few years is the Advantage Rental Assistance program, which has provided rent subsidies for up to two years to families and individuals moving out of the city's shelter system. The program has been administered by the Department of Homeless Services, although the rent subsidies have been paid from the cash assistance budget at the Human Resources Administration. While the Advantage program was initiated by the city in 2007, its approval by the state made the program eligible for state and federal support. At its peak, the city was responsible for about a third of the program's costs, with federal and state funding accounting for the rest.

As the shelter population increased, the Advantage program emerged as a key component of the city's strategy for reducing homelessness. At the same time the cost of the program grew rapidly, from $54 million in 2008 to about $210 million in 2010 and 2011. Beginning in April 2011, however, state officials eliminated all state and federal funding for Advantage, a loss of over $130 million a year. In response the city ended the program, although a lawsuit kept the city paying some subsidies through January 2012. The city's termination of the Advantage program has removed another significant factor driving recent increases in public assistance spending, although it is likely to result in additional costs in the city's shelter system. (See page 35 for more details.)

Public Assistance Funding Shift. While total cash assistance spending—including city, state, and federal funds—is expected to decrease over the next few years, another recent state action will limit the city's savings. The state legislation that implemented the 1996 federal welfare law for New York established different funding formulas for New York's cash assistance programs: the Family Assistance program for families with minor children was funded with 50 percent federal, 25 percent state, and 25 percent local funds, while the Safety Net programs for single adults and families who have used up their five-year federal limit on assistance were both funded with 50 percent state and 50 percent local funds. The 2011-2012 state budget included, however, what was identified as a one year funding switch: Family Assistance would be funded with 100 percent federal funds, and Safety Net would be funded as 29 percent state and 71 percent local. The state's 2012-2013 Executive Budget proposes to maintain these new funding formulas. Based on the present makeup of the caseload, the Preliminary Budget assumes that this switch will cost the city nearly $40 million a year.

Limited Availability of TANF Funds. Under the 1996 federal welfare law, New York State receives $2.4 billion in Temporary Assistance for Needy Families (TANF) block grant funds each year. These funds are used to pay for the federal share of Family Assistance grants, with the remainder available to pay for other programs aimed at helping low-income New Yorkers. With the size of the block grant frozen at its 1996 level, however, its inflation-adjusted value has decreased over the years by nearly 40 percent. In addition, the state's new cash assistance funding formulas mean that a greater portion of the TANF block grant is needed to fund grant costs. As a result, these other TANF-funded programs are competing for a shrinking pool of resources.

This year's state Executive Budget includes only two line item allocations of TANF funds in addition to the Family Assistance grants and other base commitments such as state administrative staff: the Flexible Fund for Family Services block grant to local governments, and the TANF contribution to the Child Care Block Grant (CCBG). While the flexible fund block grant would be increased modestly from $951 million to $964 million, the annual TANF allocation to the Child Care Block Grant would be significantly reduced from $393 million to $300 million. The Executive Budget proposes to replace the TANF funds with $93 million in state funds to prevent a decrease in CCBG allocations to localities, although the action raises questions about the availability of child care funds in future years.

Summer Youth Employment. Among the programs left without TANF funds is the city's Summer Youth Employment Program (SYEP). Over the years, the city's summer jobs program has relied on TANF for a significant portion of its funding. In the summer of 2009, the peak year, SYEP received $19.5 million in TANF funds as part of a $67.0 million budget that enabled 51,000 youth to participate in the program. Since then, however, reductions in TANF and other funding streams have forced the program to downsize. By last summer, for the first time in several years, no TANF funds were allocated for SYEP. Instead, the program received $8.5 million in state funds as part of a $43.5 million budget that enabled the program to enroll about 31,000 youth. At present, the expected budget for this coming summer is $39.0 million, including $13.7 million in state funds proposed in the Executive Budget to replace the lost TANF funds, and $20.6 million in city funds proposed in the city's Preliminary Budget. If no other funds become available, the program would be able to serve about 26,000 youth, or about half the number served in 2009.

The Governor's Medicaid Proposals: Short-Term Costs and Long-Term Savings for New York City

The Governor's January 2012 Executive Budget included two proposals that if implemented would eventually result in significant Medicaid savings for New York City and other localities across the state. The first would slow the rate of growth of the local share of Medicaid and then cap local Medicaid payments in dollar terms at their calendar year 2014 level. The second would gradually shift liability for the local share of administering the program to the state government, although in the near-term local spending on administration may go up.

Reduction in the County Cap. Under current state law, most of New York City's Medicaid costs are capped at calendar year 2005 levels, plus a yearly inflation adjustment. The amount of the inflation adjustment was slightly higher in calendar years 2006 and 2007, but has been held steady since calendar year 2008 and is now effectively limited to an increase of $128.6 million each year. A proposal in Governor Cuomo's Executive Budget would further reduce the local contribution to Medicaid by phasing out the inflation adjustment completely. In calendar year 2013, counties' Medicaid payments would be capped at 102 percent of the previous year's payment. In calendar year 2014, payments would be capped at 101 percent of the previous year's payment. Finally, counties'

New York City Medicaid Payments Under the County Cap
Dollars in millions, state fiscal years

Actuals	Cap	Increase in the Cap: Dollars	Increase in the Cap: Percents	Projected	Cap Under: Current Law	Cap Under: Proposed Law	Savings to New York City
2006-2007	$4,472.7	$-	-	**2011-2012**	$5,123.9	$5,123.9	$-
2007-2008	4,609.4	136.7	3.1%	**2012-2013**	5,252.5	5,252.5	-
2008-2009	4,738.0	128.6	2.8%	**2013-2014**	5,381.2	5,357.6	(23.6)
2009-2010	4,866.6	128.6	2.7%	**2014-2015**	5,509.8	5,411.2	(98.6)
2010-2011	4,995.3	128.6	2.6%	**2015-2016**	5,638.4	5,411.2	(227.3)

SOURCES: IBO; Mayor's Office of Management and Budget; state Department of Health
NOTE: The cap amounts exclude city payments for elective abortions, supplemental payments to HHC, and enhanced federal reimbursements awarded to the city through stimulus legislation.

payments would be capped at the 2014 level in calendar year 2015 and all subsequent years.

There would be no savings for localities from this proposal in the upcoming state fiscal year but the state projects that counties would save $61.1 million in state fiscal year 2013-2014, with the savings growing to $369.6 million in state fiscal year 2015-2016. State budget officials estimate that about 70 percent of the statewide savings would accrue to the city. IBO's own projections show more modest city savings of $23.6 million in state fiscal year 2013-2014, increasing to $227.3 million by state fiscal year 2015-2016.

State Takeover of Medicaid Administration. Another state Executive Budget proposal would transfer responsibility for Medicaid administration from the state's counties (the five counties of New York City are treated as one county for Medicaid administration purposes) to the state Department of Health (DOH) in phases, with the shift to be completed by April 1, 2018. Beyond specifying this completion date, the proposal contains no specific timeline for the transition and many of the practical details of how it will occur remain uncertain. The budget legislation states that the takeover could be accomplished either by using existing state DOH staff or contracted entities (including units of local government), or a combination of the two. Employees who currently work on Medicaid administration at the local level would be eligible to transfer to comparable positions with the state, although there would likely not be enough slots for all current employees.

The state has also not released specific details regarding how the Medicaid administration takeover will be funded. In part, they are relying on the move to a centralized, automated system to streamline the enrollment process and reduce associated costs. But getting this system up and running will require start-up funding. Initially, some of the cost of the takeover would be financed by the counties, by capping state reimbursement of local government Medicaid administration spending. As described above, each county's Medicaid payment to the state is currently capped and is based on aggregate spending for Medicaid services and administration in calendar year 2005. However, since its capped contribution has fallen far below actual Medicaid expenditures, New York City now receives substantial reimbursement for costs it incurs in administering Medicaid. In fact, under current accounting practices, the state applies New York City's entire Medicaid payment towards service costs and fully reimburses all of its administrative expenses using state and federal funds. Under the Governor's proposal, these reimbursements would be limited to a preset amount and would not increase over time.

Starting April 1, 2012, counties would only be reimbursed by the state for Medicaid administration costs up to an "administrative cap amount." They would be allowed to submit claims for costs above this amount for federal reimbursement, at a 50 percent match rate, for one additional year. According to the legislative language attached to the Governor's proposal, the aggregate administrative cap amount for the counties as a whole would be equal to the amount included in the state fiscal year 2011-2012 enacted budget for Medicaid administration. Each county's individual administrative cap amount has not yet been announced and is subject to the discretion of the state

DOH Commissioner, but is expected to be proportionate to each county's share of total Medicaid administration costs in calendar year 2011; in that year, New York City was responsible for approximately two-thirds of total costs. A signal that the state thinks the administrative cap will be lower than counties' actual expenses is that they are projecting state savings of $23 million in state fiscal year 2012-2013.

Net Impacts of Medicaid Proposals. Estimates of the savings that will accrue to the city from the Governor's proposal to lower the growth rate in the county cap are fairly straightforward. The fiscal impacts of the administrative cap proposal are considerably more ambiguous. The state has released estimates of state savings from this proposal through state fiscal year 2015-2016; however, they have not provided any estimates of county-level impacts. Given the lack of details or a timeline for the state takeover of Medicaid administration, it is reasonable to assume that counties' administrative responsibilities will likely remain substantial in the short term. Therefore, any savings the state accrues from limiting administrative reimbursements will translate into added costs for the counties. As the state gradually takes over the administration of Medicaid this is expected to change.

IBO's projections of the city's future Medicaid payments assume that localities will not see their workloads decrease in the short term and will therefore have to absorb any administrative costs above the administrative cap amount. For example, the state is projecting that they will save $23 million by limiting administrative reimbursements in state fiscal year 2012-2013 so IBO assumes that the counties will have $23 million in added costs that year. The city's share of the $23 million is uncertain, but will likely be in the magnitude of $15.6 million to $16.6 million. Even if these costs are combined with savings from the reduction in the county cap, IBO estimates that the city will bear greater overall Medicaid costs for the next two years to three years.

The point at which these costs turn into savings largely depends on how the city's administrative cap is set. Under any reasonable scenario, the savings to the city would become significant—in the magnitude of $85 million to $95 million—by state fiscal year 2015-2016, which spans city fiscal years 2015 and 2016, and would get progressively larger over time. The Mayor's budget office has come to a similar conclusion and is anticipating small net losses to New York City through 2016. Due to the uncertainties surrounding the administrative cap proposal, however, the Mayor's Office of Management and Budget did not adjust projections of the city's Medicaid payments in the Preliminary Budget.

New Cuts Threaten Funding Streams For City Public Hospitals

The Mayor's Preliminary Budget projects that the Health and Hospitals Corporation's (HHC) expenses will continue to outstrip revenues in 2012 through 2016, leading to growing operating deficits and dwindling cash reserves. There are a number of factors contributing to HHC's lagging revenues, including a patient mix that contains a persistently high share of the uninsured—8.8 percent of in-patient discharges in the first half of 2012 lacked public or private coverage. (In comparison, the average share of uncompensated care for all New York City hospitals was 3.0 percent of discharges in 2008.)

Medicaid Proposal Fiscal Impacts on New York City

Dollars in millions, state fiscal years

	2012-2013	2013-2014	2014-2015	2015-2016
Scenario 1: NYC Bears 68% of County Costs from Administrative Cap				
Reduction in County Cap	$-	$(23.6)	$(98.6)	$(227.3)
Cap on Administrative Reimbursements	15.6	63.8	97.5	132.6
Net Cost/(Savings)	$15.6	$40.2	$(1.1)	$(94.7)
Scenario 2: NYC Bears 72% of County Costs from Administrative Cap				
Reduction in County Cap	$-	$(23.6)	$(98.6)	$(227.3)
Cap on Administrative Reimbursements	16.6	67.5	103.2	140.4
Net Cost/(Savings)	$16.6	$44.0	$4.6	$(86.9)

SOURCES: IBO; state Department of Health

In addition, financial support from all levels of government has been dropping in recent years. HHC is heavily reliant on Medicaid funding, and several rounds of state level cost-cutting initiatives have taken a toll on the corporation's revenues. With the state having adopted a two-year Medicaid budget last year, the Governor's Executive Budget this year contains no significant new cuts in this area. However, cuts to federal funding for Medicare and Medicaid are scheduled to go into effect in 2013 and 2014, respectively, and the Mayor has proposed additional cuts to HHC's city funding in 2013.

Looming Federal Health Care Cuts. The failure of the Congressional "super committee" to come to an agreement on the federal budget deficit triggered an automatic 2.0 percent reduction in Medicare provider rates that is scheduled to go into effect on October 1, 2012. Due to these reductions, as well as other changes to Medicare payment methodologies enacted through the Affordable Care Act (ACA), HHC is projecting their Medicare fee-for-service revenues will drop from $625 million in 2012 to $616 million in 2013 and down to $585 million in 2016. Another ongoing issue concerns the Medicare Sustainable Growth Rate formula, under which Medicare physician payment rates are scheduled to decrease by 27.4 percent as of January 1, 2013. Congress has not allowed large scheduled decreases under this formula to occur in the past; however, they have also not altered the underlying provisions. Given the absence of a long-term solution for this problem—one proposal on the table is to cut hospital payments to pay for higher physician rates—and the current impasse on federal deficit reduction, it is possible that even larger cuts in the corporation's Medicare revenue will occur in the coming years.

Reductions in federal funding for Medicaid will also affect HHC revenues. The Affordable Care Act is funded in part through reductions to the Disproportionate Share Hospital (DSH) program that are scheduled to go into effect on October 1, 2013. This program provides supplementary Medicaid payments to hospitals that serve a high proportion of Medicaid patients and the uninsured. In New York State, federal DSH funds are disbursed to hospitals through direct intergovernmental transfers (with a 50 percent local funds match) and indirectly through the Indigent Care Pool. The city has used the DSH program extensively to leverage federal dollars to bolster its support of HHC. Although the ACA legislation specifies the total dollar amount by which federal DSH funding will be reduced nationwide, much uncertainty remains. The Department of Health and Human Services has not yet determined how the nationwide reduction will be allocated among the states, and there are also proposals to cut DSH funding more deeply to help with the federal deficit or to fund other health care initiatives. For example, a recent Congressional agreement to delay scheduled cuts in Medicare provider payments was funded by extending reductions in DSH payments through federal fiscal year 2021. Under the original legislation, the DSH cuts would have expired in 2020.

The potential impacts of reductions in federal DSH payments on New York State and on HHC are substantial since both receive a comparatively large share of federal DSH money. In the current federal fiscal year, New York State has been allocated $1.6 billion in DSH funds, which is approximately 14.2 percent of the national total and is a larger allotment than any other state. HHC projects that they will receive $356 million of these funds through intergovernmental transfers—22.1 percent of the state total—in addition to DSH funds received through the Indigent Care Pool.[1] Assuming that HHC's DSH reductions are proportionate to the aggregate reductions, IBO estimates that HHC would lose $16 million in federal funds in federal fiscal year 2014, increasing to a high of $177 million in federal fiscal year 2019. If the city's matching payments are also scaled back, these losses would double. Although HHC's most recent financial plan assumes that the city will maintain its share of DSH payments despite the federal reductions, the city has not committed to doing so.

New Cuts to the Unrestricted City Subsidy. Two years ago, the Mayor's Preliminary Budget for 2011 included a plan to increase HHC's unrestricted city subsidy from approximately $5 million to $32 million annually starting in 2012. Since then, several rounds of budget cuts have reduced the amount of the proposed increase and as a result, HHC projects their 2012 unrestricted subsidy at $22.5 million. A budget cut included in the November 2011 Financial Plan would have reduced HHC's unrestricted city subsidy by an additional $1.5 million in 2012 and by $4.3 million annually beginning in 2013. The $1.5 million reduction

Medicaid Disproportionate Share Hospital Program Reductions
Dollars in millions

	Federal Fiscal Years							
	2014	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**
Aggregate Federal Funds Reductions	$500	$600	$600	$1,800	$5,000	$5,600	$4,000	$4,000
Estimated % Decrease in Aggregate Federal Funds	4%	5%	5%	16%	44%	50%	35%	35%
New York State's Estimated Federal Funds Losses	71	85	85	256	710	795	568	568
HHC's Estimated Federal Funds Losses	16	19	19	57	158	177	126	126
HHC's Estimated Total Funds Losses	32	38	38	114	315	353	252	252

SOURCES: IBO; Mayor's Office of Management and Budget; state Department of Health; Kaiser Family Foundation
NOTES: HHC's estimated Disproportionate Share Hospital (DSH) losses exclude losses through the Indigent Care and related pools. Estimates of HHC's total DSH losses assume that city matching funds will be reduced to the same extent as federal funds.

was rescinded for 2012, but the cut beginning in 2013 still stands. Combined with previously scheduled cuts, the unrestricted subsidy would be reduced to $15.3 million in 2013.

Impacts on Cash Balances and Staffing at HHC. With pressure on HHC funding from these various factors, HHC only expects operating revenues to increase 6.1 percent by 2016, while operating expenses are on pace to increase by 15.0 percent. HHC projects a net loss of $874 million in 2012, and cash balances dropping from $687 million to $105 million by the close of 2016. Even these estimates may be somewhat optimistic, as they are based on a series of corrective measures such as unspecified state and federal actions, enhanced city funding for DSH, and ongoing restructuring and cost containment initiatives at HHC including reduced staffing levels. HHC has already reduced its staff from 35,582 full-time equivalents in February 2009 to 33,114 in December 2011, a 6.9 percent reduction, and is now implementing a hard hiring freeze through at least April 2012.[2] HHC leadership has stated that they may need to increase their staff reduction target for 2013 by 50 full-time equivalents in order to absorb the latest cut to their unrestricted city subsidy. HHC has also recently outsourced, or moved forward with plans to outsource, various nonmedical functions at their facilities, including laundry operations, environmental services management, and plant maintenance management.

While the corporation has prioritized cost-containment in areas that do not directly affect patient care, some restructuring initiatives have had service impacts. HHC closed 6 of its 81 community clinics—five child health clinics and one dental clinic—in 2011 and now plans to consolidate and reduce the number of patient beds at the Coler-Goldwater facility, a portion of which will be relocated to the North General campus in

The Health and Hospital Corporation's Financial Plan
Dollars in millions

Preliminary Budget - Projected	**2012**	**2013**	**2014**	**2015**	**2016**
Total Operating Revenues	$7,052.8	$7,144.3	$7,240.0	$7,369.9	$7,483.5
Total Operating Expenses	7,940.9	8,313.2	8,611.5	8,875.3	9,128.2
Total Interest Income and Expense	(86.0)	(94.0)	(96.0)	(96.0)	(96.0)
Profit/(Loss) Before Other Changes in Net Assets	**$(974.0)**	**$(1,262.9)**	**$(1,467.5)**	**$(1,601.4)**	**$(1,740.7)**
Total Corrective Actions	$100.4	$471.3	$747.6	$956.7	$1,156.7
Profit/(Loss) After Corrective Actions	**$(873.6)**	**$(791.6)**	**$(719.9)**	**$(644.7)**	**$(584.0)**
Prior Year Cash Balance	553.1	687.1	470.7	287.7	165.6
Accrual to Cash Adjustment	1,007.6	575.2	537.0	522.6	522.8
Closing Cash Balance	**$687.1**	**$470.7**	**$287.7**	**$165.6**	**$104.5**

SOURCES: IBO; Health and Hospitals Corporation
NOTE: Projections of operating revenues and expenses assume cuts to city funding for child health and developmental evaluation clinics, which was restored in 2012, will be implemented in future years.

Harlem. Due to a series of cuts included in previous budget cycles but not yet implemented, additional community clinics may close in 2013 if the funding is not restored again this year.

Proposed Juvenile Justice Reform Presents City with Potential Challenges and Benefits

Over a year ago, Mayor Bloomberg called upon the Governor to return control of New York City's juvenile offenders to the city. In his 2012-2013 Executive Budget, the Governor has partially answered the Mayor's call by proposing a Juvenile Justice Services Close to Home Initiative, which would authorize New York City to provide juvenile justice services to all adjudicated juvenile delinquents residing in the city who require placement in a nonsecure or limited secure facility as determined by the family court.

If the initiative is approved by the Legislature, the city would regain custody of all city juveniles currently placed in nonsecure facilities run by the state's Office of Children and Family Services (OCFS) beginning in September of this year. City youth in limited secure facilities would be transferred starting in April 2013. The city (and state) would likely see future budget savings if the plan is fully implemented, although at this point there are none reflected in the city's Financial Plan.

Presently, when a family court judge determines that a juvenile delinquent—a youth of at least 7 but not yet 16 years of age who has been found to have committed a delinquent act—needs to be confined, the juvenile is placed in one of three types of facilities operated either directly by or under contract with OCFS. Secure facilities provide the most controlled and restrictive setting of all three residential programs. They operate much like maximum security prisons. Limited secure facilities provide a less restrictive setting than secure centers and nonsecure facilities afford the least restrictive environment. Secure facilities are only found in rural areas of the state and all services are provided on-site. Limited secure facilities are primarily located in nonurban areas upstate, while nonsecure facilities are found in both rural areas and urban communities typically outside the city. Placement in an OCFS facility almost always guarantees that a city youth will be separated from his or her family and community. Advocates contend that this separation is detrimental to the reform process and results in increased rates of recidivism.

In response to the negative outcomes associated with juveniles in placement, the city has launched three alternative to placement programs. These programs are typically home-based and involve intensive counseling along with monitoring by the Department of Probation. It has been shown that youth who participate in alternative to placement programs like the Administration for Children's Services' Juvenile Justice Initiative or the Department of Probation's Enhanced Supervision Program have a substantially lower rate of recidivism. In addition, the annual costs to administer these programs are much less than that of placement in an OCFS-operated residential facility, which costs approximately $270,000 per youth per year according to testimony given by the Mayor in January to the state Legislature.

Placement costs have become an issue for the city in recent years. While the number of juveniles being sent to OCFS facilities has steadily decreased since 2007, the total costs associated with these placements have remained comparatively flat. For example, the number of city youth in OCFS placement in 2010 was half that of 2007, but city costs decreased by only 5.8 percent over those three years. The decline in city spending has not been commensurate with the decline in placements due to the way the state calculates the rate it charges the city for each juvenile in placement. Currently, OCFS determines the rate by dividing total system costs—what it costs OCFS to operate all juvenile placement facilities—by the total number of care days used by each locality. The state then reimburses each locality for 50 percent of these costs. Because the state's rate is set based on recouping total OCFS costs, the amount the city pays the state will never adjust proportionately to changes in the number of city placements; instead it will continue to increase as long as OCFS costs remain flat. To actually see a reduction in city costs, overall OCFS costs would have to decrease.

In theory, the Governor's Close to Home proposal should yield budget savings for both the city and the state. The proposal would allow the city to maintain custody of approximately two-thirds of all youth requiring placement in a facility (one-third will continue to be placed in state-run secure centers), while the state provides the city with a block grant appropriation to fund its share of the costs of administering youth placement. Youth avoid being placed in facilities far from their families and communities, and the city regains control of program administration and costs. In return, the state would be permitted to close down underutilized upstate facilities, resulting in projected annual savings of $4.4 million beginning in state fiscal year 2014-2015. As for the facilities the state currently operates in New York City, they could be leased back to the city for $1 a year under the legislation. The Mayor's office anticipates that the city will lease at least three of these facilities, and contract with providers to accommodate the rest of the population. Construction of new facilities is not expected at this time.

While the proposal appears to be advantageous for both parties, there are potential pitfalls along the way. The legislation calls for the city to develop a plan detailing how it will provide juvenile justice services for those youth being transferred from OCFS limited secure and nonsecure facilities. At least one public hearing on this plan must be conducted before it may be submitted to OCFS and the state Division of the Budget for review and approval. Both the plan and the public hearing would have to be completed closely following enactment of the legislation so that the city will be ready for the physical transfer of youth from nonsecure facilities starting in September. That means that a plan must be prepared, a public hearing held, contracts with providers put in place and facilities for confinement identified and retrofitted by the end of summer.

In addition to these logistical challenges, it is not clear what the net fiscal impact on the city would be. Although the proposed state block grant would grow from $8.6 million in 2012-2013 to $41.4 million in 2014-2015, the overall costs of the new program cannot be quantified yet, especially in the early years when there will be start-up costs related to opening new facilities and training new staff.

Endnotes

[1]IBO's analysis excludes the impact of federal DSH reductions on HHC's Indigent Care Pool revenues, as this pool is funded through a complex formula utilizing multiple funding sources. HHC projects their total revenue from the Indigent Care and other related pools at $437 million in 2012.
[2]These numbers exclude central office, home health, and enterprise information technology staff.

City Budget Initiatives

Homeless Shelter Costs Likely to Exceed Budget Estimates

The Department of Homeless Services (DHS) is likely to face budget challenges in 2012 and even tougher choices in 2013. With a growing census and longer lengths of stay in the city's homeless shelters, costs are going up, and—in the case of family shelter—these costs appear likely to exceed what the city has budgeted for this year and next. Additionally, the lack of a new program or policy to replace the Advantage rental subsidy program that ended last year may further increase costs, especially for family shelters. Lastly, the city has proposed initiatives that were expected to produce savings, but legal challenges and lack of City Council approval have kept them from being implemented. While the city has begun to scale back the savings expected in 2012, the full savings are still in the budget for 2013 through 2016.

Shelter Census and Length of Stay. The Department of Homeless Services divides its shelters into two groups—family shelter and single adult shelter—and for both groups the average daily census and average amount of time homeless populations remain in shelter has been rising over the past year. The average number of single adults in shelter has increased in 2012, 8,382 adults in the first five months of fiscal year 2012 compared with 8,054 adults for the same period in 2011. The average daily census for family shelter is also slightly higher than it was in 2011. In the first five months of 2012 the daily census averaged 9,583 families, compared with 9,427 families during the same period last year.

The shelter population has increased, in part because both families and individuals are staying longer in shelter. During the first five months of 2012, the average amount of time families remained in shelter was nearly 11 months (327 days), more than two months longer than during the same period in 2011 (257 days). The average shelter stay for single adults also increased, albeit by just 21 days from 242 days in the first five months of 2011 to 263 days in the same period this year.

One reason for the increase in shelter stay, especially among families, is that last April the city ended Advantage, a rental subsidy program that helped families leave shelters by paying a portion of participants' rents for up to two years; although some Advantage subsidies did go to single adults, the vast majority of the subsidy program went to families. (See IBO's Advantage blog post for details.)

The city ended Advantage when the state withdrew both its funding as well as the federal match for the program. However, a court order stemming from a lawsuit brought by homeless advocates forced the city to keep paying subsidies through January for those who had already signed leases under the program—costing the city $71 million in 2012. The court order was lifted in February and thus far the courts have twice upheld the city's decision to end the program, but advocates have indicated they intend to appeal the latest ruling. It is likely that some of the families that had been receiving subsides before the court order was lifted will face eviction and eventually return to shelter.

Current Shelter Budget. Budgeted family shelter costs for 2012 and 2013 are currently lower than 2011 actual expenditures, despite the increase in length of stay and census. The city spent $417.5 million in city, state, and federal funds for family shelter in 2011, including shelter operations, intake and placement, and administration and support; funding for Advantage is not included in these numbers. City funding for family shelter in 2011 was $155.2 million. For 2012, the city has budgeted $22.0 million less ($395.4 million in total for family shelter, about $122.6 million of which are city funds), and a total of $374.6 million for 2013 ($121.2 million are city funds). Based on IBO's

Department of Homeless Services Adult Shelter
Dollars in millions

	Actual	Projected	
	2011	2012	2013
Administration & Support	$8.1	$9.3	$8.2
Intake and Placement	8.0	9.2	9.2
Operations	252.0	273.7	261.4
Total Adult Shelter	**$268.1**	**$292.1**	**$278.8**

SOURCES: IBO, Mayor's Office of Management and Budget
NOTE: Adult shelter costs include city, state, and federal funds.

Department of Homeless Services Family Shelter
Dollars in millions

	Actual	Projected	
	2011	2012	2013
Administration & Support	$5.8	$8.0	$9.7
Intake and Placement	23.5	23.8	23.8
Operations	388.2	363.6	341.0
Total Family Shelter	**$417.5**	**$395.4**	**$374.6**

SOURCES: IBO, Mayor's Office of Management and Budget
NOTE: Family shelter costs include city, state, and federal funds.

estimates of shelter costs, this suggests that family shelter could cost about $37.0 million more this year than budgeted (about $12.0 million of which would be city funds) and as much as $76.0 million more in fiscal year 2013 (about $24.0 million in city funds) given the increasing length of stay, higher census, and lack of a replacement for the Advantage program.

Unlike the family shelter budget, the current budget for adult shelter is higher than actual expenditures from last year. In 2011, adult shelter cost $268.1 million, with city funds making up $202.6 million of that total. For 2012, however, the city budgeted $292.1 million for adult shelter ($204.9 million of which are city funds). Given the average cost of shelter for adults, the current budget amount for adult shelter may actually be on the high side. While the amount planned for adult shelter for 2013 is less than budgeted in 2012 ($278.8 million, with $200.8 million in city funds), it is still higher than actual expenses in 2011.

Implementation of Initiatives Stalled. DHS has also been unable to implement two cost-saving measures that were first introduced in the November 2010 Financial Plan and meant to begin this fiscal year. The first measure would have families with three or fewer children share apartment-style housing—each family would have their own bedrooms but share kitchens and bathrooms. The policy change, however, requires City Council approval, which has yet to happen. Some City Council members have voiced concerns over the measure and approval is uncertain. The change was to be phased in throughout the year, but given the delay in implementation, the Bloomberg Administration has already reduced the expected city savings in 2012 from $4.5 million to $2.3 million. (The policy change would also reduce state and federal costs given that shelter costs are shared). And DHS still anticipates getting the full cost savings from the policy—$9.1 million in city funds—for 2013 and beyond.

In addition, a cost-saving measure planned for adult shelter has also been delayed as a result of lawsuit brought against DHS by the City Council and the Legal Aid Society. The proposed policy, which was originally projected to begin in 2012 and save the city $2.0 million a year, would require people entering adult shelter to meet eligibility requirements similar to those currently enforced for applicants to family shelter. The City Council and homeless advocates sued the city and in mid-February the trial court found that the city could not implement the policy. However, the finding was based on the public review process required for the change, not the legality of the policy itself. The Bloomberg Administration has said it will appeal the ruling. The Mayor's budget office has already restored the projected savings in 2012; but the Financial Plan assumes the savings for 2013 and subsequent years.

Attrition Incentive Program Falls Short of Target

When this year's budget was negotiated last spring, it included initiatives to achieve $29.1 million in savings in the Department of Parks and Recreation (DPR) for 2012. An initial proposal in the Executive Budget for 2012 was replaced in the Adopted Budget with an alternative plan, and it was revised again in the November 2011 Financial Plan. This most recent iteration of the program has again fallen short of the savings targets and a reduction in the anticipated savings or alterative initiative is expected in the upcoming Executive Budget.

The original proposal was a voluntary Attrition Incentive Program for 665 workers, roughly 23 percent of full-time city-funded staff at the department at the end of 2011. It was expected to save the city $29 million beginning in 2012. Under the program, an employee leaving full-time employment at the parks department was guaranteed a six month seasonal position for up to three years, and it was expected that employees near retirement would sign up. Negotiations with the union representing the workers were unsuccessful and the Adopted Budget for 2012 replaced the attrition program with layoffs for 465 employees (16.2 percent of city-funded staff) in 2012. This alternative was expected to achieve the same savings.

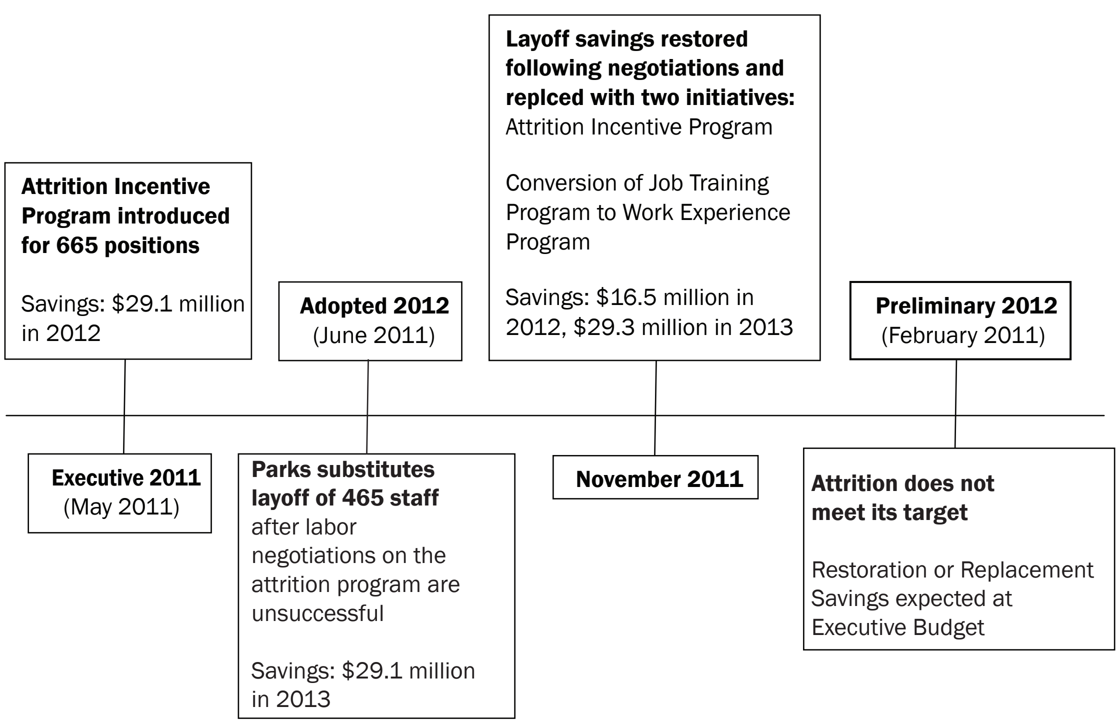
Although the layoffs were included in the Adopted Budget, negotiations resumed over the summer and the layoffs were averted. DPR substituted two initiatives to replace layoffs in the November 2011 Financial Plan. Together, the two initiatives were expected to save $16.5 million in 2012 (about 57 percent of the savings originally expected), and $29.3 million beginning in 2013, essentially the same amount that had originally been projected.

One initiative is replacing Job Training Program (JTP) participants at the parks department with federally funded Work Experience Program (WEP) workers, for a city savings of $6.8 million this year and $13.9 million next year. According to the Mayor's budget office, 330 full-time equivalents were cut in 2012 and additional cuts will be made to bring the total reduction in full-time equivalents to 700 for 2013 (about half the program). Individuals who would have been assigned to the parks department via JTP are now assigned as WEP workers; while WEP workers perform similar duties with no city-funded costs, they can only work roughly half as many hours as JTPs. Although the Bllomberg administration has begun to implement this change, it is facing opposition from some council members and union leaders.

The second initiative was a reintroduction of the Attrition Incentive Program for 330 parks department employees. Even at roughly half the original target, if fully implemented the program would reduce parks department city-funded staff by 11.5 percent (about 10 percent of all DPR full-time staff). With a mid-year start, the attrition program was expected to achieve $9.7 million in savings this year and a full-year savings of $15.4 million in 2013.

Enrollment in the program has not met the targets and the parks department has indicated that once again, a partial restoration or replacement program will be announced in the Executive Budget. According to the Mayor's Office of Management and Budget, 121 parks department employees, 4.2 percent of city-funded staff

Timeline of Selected Department of Parks and Recreation Saving Efforts



SOURCES: IBO; Mayor's Office of Management and Budget; Department of Parks and Recreation at the start of the year, have signed up for the program, which is expected to yield $3.9 million savings. The Preliminary Budget was not adjusted to reflect the lower take-up rate in 2012; the plan still assumes $9.7 million in savings this year and a reduction in full-time city-funded parks employees from 2,740 at the end of December 2011 to 2,417 by the end of the year—a decline that includes some other attrition besides what is anticipated from the Attrition Incentive Program.

Parks Department Plans to Somehow Raise $13 Million in Revenue

In November 2011, the Bloomberg Adminstration introduced another initiative for the parks department to generate $13 million in revenue annually, beginning in 2013. The department has not yet provided details on how it will achieve this target. Given that some similar efforts to generate additional revenue a few years ago were rolled back, there is uncertainty about whether this initiative can be attained.

Although lacking in specifics, the proposal to generate $13 million in annual revenue is relatively ambitious. Currently, the parks department is responsible for collecting $72.6 million from concessions, fees, permits, and fines (called miscellaneous city revenue). The new proposal would be a 17.9 percent increase over the department's revenue for 2012. According to both the parks department and the Mayor's budget office, the department is developing a proposal to achieve this target, though no details have been provided. More information is expected in the Executive Budget. Generating revenue through the sale of naming rights at city sites is one option reportedly under consideration.

Past efforts to generate revenue through the sale of naming rights in parks have proved difficult, and given the short time frame to implement the initiative, there is a strong chance that the department will not be able to meet this $13 million goal, at least for next fiscal year. An initiative to sell naming rights, expected to generate just $3 million a year, was introduced in January 2008 to begin in 2009. After nearly two and half years during which no revenue was collected, the city officially ended the effort in November 2010. Similarly, a proposal to generate $2 million a year from an indoor tennis center at Central Park, introduced at the same time, was also abandoned in November 2010.

Youth Services: Budget Cuts Would Mean Loss of Thousands of After-School and Other Program Slots

The Mayor's Preliminary Budget for 2013 includes significant funding reductions to some core programs at the Department of Youth and Community Development (DYCD) including the Out-of-School Time (OST), Beacon, and Runaway and Homeless Youth (RHY) programs. The 2012 Adopted Budget included over $60 million in one-year funding for DYCD programs; this funding remains uncertain for 2013. In addition, the November 2011 Financial Plan included new cuts that would further reduce after-school services if they are implemented as planned. On top of these Financial Plan reductions, DYCD recently released a new Request for Proposal (RFP) for OST that would essentially cut the number of program slots in half.

Out-of-School Time. The department's OST program provides activities for school-age youth during after-school hours, on weekends, and during school vacations. OST programs are offered at no cost to participants and provide a mix of academics, recreational activities, and cultural experiences for elementary, middle school, and high school students. OST service providers operate mostly in public school buildings and in facilities of the parks department and the New York City Housing Authority.

Under the Preliminary Budget total spending on OST in 2013 would be $75 million, down $19 million from 2012. The November 2011 Financial Plan included a proposed $6 million (7.0 percent) reduction to OST programs beginning in 2013. This cut would reduce the number of OST slots by 2,300. Also in November 2011, DYCD released a new RFP for elementary and middle school OST programs; the agency restructured OST high school programs in 2009. The new RFP allows for a total budget of nearly $70 million for the elementary and middle school programs. This amount reflects the November plan cut and assumes that the $12 million that was added for OST by the City Council as part of the 2012 Adopted Budget will not be available in 2013 or later years.

While the OST program currently serves about 46,000 youth in about 420 elementary and middle school programs, the new RFP provides only enough funding for about 27,000 slots which would be targeted in high poverty zip codes. Advocates and elected officials, however, have expressed concern with the reduced capacity and have pointed out that some higher income zip codes contain significant pockets of poverty. In response to the RFP, DYCD received over 1,200 applications but will only be able to fund about 220 programs.

Beacons. DYCD supports 80 Beacon community centers located in public schools. These centers operate six days a week (42 hours) in the afternoon and evenings, including weekends, school holidays, and during the summer. Beacons provide a range of activities for young people and adults, such as tutoring, college prep, basketball, martial arts, general equivalency diploma training, and English for Speakers of Other Languages programs.

Under the Preliminary Budget, various changes would leave spending on Beacons in 2013 at $43.2 million, down $6.1 million from 2012. The Preliminary Budget included a partial restoration of a November 2011 Financial Plan reduction of $535,000 for Beacons for 2012 that would have eliminated about 990 slots in the current year. Nevertheless, the Preliminary Budget still reflects a November plan reduction of $2.1 million for 2013 that would eliminate seven Beacons in regions with the lowest need—as defined by DYCD. In addition, the 2012 Adopted Budget included a City Council restoration of $2.3 million to prevent reductions in services at 66 city-funded Beacons; this was a one-year restoration and these funds are not in the 2013 budget. The 14 federally funded Beacon programs are not affected by this cut.

Runaway and Homeless Youth. The department's Runaway and Homeless Youth (RHY) program offers services to homeless youth, and whenever possible works to reunite them with their families. Services provided include: street outreach, crisis shelters, drop-in centers, and transitional independent living facilities. Under the Preliminary Budget, spending for RHY for 2013 is projected at $5.4 million, about $7.3 million less than 2012. As part of an earlier round of budget cutting, the November 2010 Financial Plan included proposals to eliminate the city's street outreach contracts and reduce the level of funding for the drop-in centers for a savings of about $330,000; the 2012 Adopted Budget restored these funds for 2012 only. The 2012 Adopted Budget also included a one-year City Council restoration of $6.8 million for youth shelters, this restoration made up a little over half of the agency's total RHY budget. Unless these funds are added to the 2013 budget, services for homeless youth would be significantly reduced from current levels.

Cultural Organizations Becoming Increasingly Dependent on Adopted Budget Restorations

The Department of Cultural Affairs (DCA) offers two categories of operating support to cultural organizations in New York City. The department provides subsidies to the Cultural Institutions Group (CIG), 34 organizations housed within city-owned property, ranging from large, world renowned institutions such as the Metropolitan Museum of Art, to small organizations that primarily serve local communities like the Queens Theater in the Park. For organizations not operating out of city-owned property, the Cultural Programs Unit distributes Cultural Development Fund (CDF) grants to more than 850 nonprofit arts and cultural organizations offering citywide and community-based programs.

Although the Mayor's Preliminary Budget contains no new cuts in cultural subsidies, city funding for cultural organizations is slated to fall by 36.9 percent between 2012 and 2013, from $148.9 million to $94.0 million, largely because of prior decisions already incorporated in the city's Financial Plan.

The drop in funding is due to three factors: 1) when the budget was adopted last June the Mayor and the City Council restored scheduled cuts to the cultural budget for one year only, leaving in place cuts slated to take effect beginning in 2013; 2) Council initiatives and member items for fiscal year 2012, which totaled nearly $9.0 million, have been eliminated from the 2013 funding level (initiatives and member items are traditionally added on an annual basis); and 3) the November 2011 Financial Plan introduced an additional cut of 6.0 percent ($6.1 million) beginning in 2013. This 6.0 percent reduction would primarily affect the operating budgets of the CIGs, with a smaller impact on the Cultural Development Fund. If all of the reductions incorporated in the Preliminary Budget

Restorations and Additions to the Cultural Affairs Budget
City Funds Only, Dollars in thousands

Fiscal Year	2009	2010	2011	2012
Executive Budget	**$142,558**	**$130,513**	**$109,547**	**$100,065**
Mayoral Restorations	-	-	6,400	13,451
Council				
Restorations	5,000	19,499	25,933	29,548
Initiatives	800	5,900	4,780	5,800
Member Items	2,657	2,436	2,856	3,097
Other Adjustments	1,558	-	-	(6)
Adopted Budget	**$152,573**	**$158,348**	**$149,516**	**$151,955**
Total Restorations	8,457	27,835	39,969	51,896
Restorations & Additions Year-to-Year Increase %	-	229%	44%	30%

SOURCES: IBO; Mayor's Office of Management and Budget

remain in effect when the 2013 budget is adopted and the Council fails to provide new money for their own initiatives and member items, the CIGs face a decrease in funding of $34.0 million (31.6 percent), while CDF grant funding would be reduced by $20.8 million (57.5 percent).

Subsidy Reductions. Since November 2008, DCA subsidy reductions have been included in eight different financial plans. But each year, when the budget is adopted, the City Council and the Mayor act to mitigate the impact on cultural institutions by at least partially restoring subsidies for the new fiscal year. This past June, the Mayor and the City Council restored $43.0 million in subsidies and the Council provided an additional $8.9 million for initiatives and member items.

While it has been common practice for Mayors to propose cuts to cultural programming only to agree to restorations when approving the budget, the magnitude of these reductions and restorations has increased over time. The total amount of restorations and additions to the DCA budget has increased steadily from $8.5 million in the 2009 Adopted Budget to $51.9 million in 2012. This process could make it increasingly difficult to find enough funds to maintain current levels of cultural subsidies, while adding to the uncertainties faced by the organizations that depend on these funds.

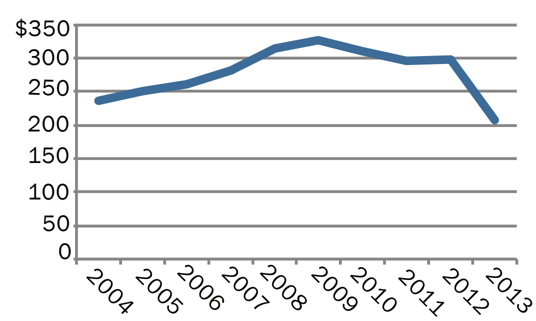
Library Subsidies Could Hit Lowest Levels in a Decade

New York City provides support for general operating and energy costs in the form of a subsidy payment to each of the city's three public library systems: the New York Public Library (NYPL), which operates branch libraries in Manhattan, the Bronx, and Staten Island; the Brooklyn Public Library; and the Queens Borough Public Library. The city also provides a separate funding stream for the New York Research Libraries which are housed within the NYPL system. Each system has extensive autonomy in deciding how to budget these funds.

Since January 2010, library subsidies have been reduced in five different financial plans. Each year when the budget was adopted the libraries received a partial restoration of the subsidy for the new fiscal year, offsetting some of the cuts made in earlier financial plans. This past June, the Mayor and the City Council restored $83 million in subsidies, keeping library funding levels relatively flat from 2011 to 2012. The 2013 Preliminary Budget proposes total funding of $207 million for the public library system, a decrease of 30.4 percent from 2012. This decrease reflects the fact that last spring's restorations were limited to 2012 only, and the impact of an additional reduction included in the November 2011 Financial Plan that is scheduled to grow even deeper this July.

City subsidies for the libraries have fluctuated over the past decade. In 2004, the subsidies totaled $236.6 million and then rose steadily to $326.7 million in

A Decade of Rising and Falling Library Subsidies
Dollars in millions



SOURCES: IBO; Mayor's Office of Management and Budget; New York City Comptroller's Comprehensive Annual Reports, 2004-2011
NOTE: Annual allocations have been adjusted to reflect prepayments.

2009. The $207.0 million proposed for next year would be the lowest amount over the 10 years.

As a result of cuts in recent years, libraries have been forced to reduce service hours and staff. For example, as part of the November 2011 Financial Plan the Bloomberg Administration proposed a 6 percent reduction in operating subsidies for 2013 and beyond. This reduction is expected to result in lower service levels systemwide. The New York Public Library is forecasting a reduction in average service from 5.9 days per week to 5.6 days per week, with the Brooklyn Public Library projecting a reduction from 5.5 days per week to 5.3 days per week and the Queens Borough Public Library predicting a reduction from 5.4 days per week to 5.2 days per week. These estimates assume that the $83 million that was restored for 2012 will also be restored for 2013; if not, the service reductions would likely be far greater than those listed here.

In the 2008 Adopted Budget, amid frustration with the routine of budget cutting followed by restorations, the Mayor and the City Council agreed to permanently add funding to the libraries' baseline subsidies to ensure that all branches could provide full six-day service. A few years later, the city's deteriorating budget situation led to new proposed cuts to a broad array of public services including the library subsidies; reductions that have been partially restored each year when the budget is approved. However, the reductions that have already been implemented and others now scheduled suggest that fulfilling the agreement to provide six-day service is not likely to be achieved in the foreseeable future.

Twenty Fire Companies Once Again Scheduled to Be Deactivated

Under the Mayor's Preliminary Budget for 2013, a total of 20 fire department (FDNY) companies would be taken out of service next year, with the firefighters redeployed to other assignments. (A fire company refers to a group of firefighters assigned to staff a fire truck on a daily, around-the-clock basis.) This would constitute a roughly 6 percent reduction in the total number of engine and ladder companies. Although the Mayor had proposed that the companies be deactivated for the current fiscal year, $40.9 million in funding was restored to the agency's budget by the City Council when the budget for this year was approved last June, forestalling this reduction for at least one year. This marked the third consecutive year in which the Council restored funding when adopting the budget to prevent fire companies from being deactivated.

Fewer Firefighters, More Firefighter Overtime

	Actual			Projected	
	2009	2010	2011	2012	2013
Firefighter Staffing	11,459	11,080	10,646	10,787	10,282
Overtime Spending *(millions)*	$127.6	$157.7	$197.9	$238.6	$226.0

SOURCES: IBO; Mayor's Office of Management and Budget
NOTES: 2009-2011 is actual staffing levels as of June 30 of that year; for 2012, authorized staffing as of June 30, 2012. For 2013, staffing and overtime figures assume the closing of 20 fire companies.

If the 20 companies are deactivated as proposed in the coming year, authorized firefighter staffing within the agency would decline by 505 positions; about 25 firefighters are required to staff each fire company on an around-the-clock basis. This would bring authorized staffing down from the current level of 10,787 to 10,282 by June 2013.

At present over 300 authorized firefighter positions are vacant due to ongoing legal challenges to FDNY hiring practices, which have caused the department to delay hiring a new class of firefighters since July 2008. With the department unable to replace firefighters leaving for retirement and other reasons with new hires, the need to continue staffing all companies has led to an increased reliance on firefighter overtime spending.

The proposed level of firefighter overtime spending next year is $226.0 million, down slightly from $238.6 million in the current year. The decline in overtime spending next year rests, however, on an assumption that funding will not be restored to keep open the 20 fire companies currently scheduled to be closed in July.

According to the Mayor's office, the testing process for new firefighter applicants was to begin in March 2012. The most optimistic scenario now calls for a new class of recruits to enter the fire academy in March 2013 and then be ready for deployment in the field by July 2013, the first month of fiscal year 2014.

Proposed Police Staffing for 2013 Remains Constant

Actual Police Staffing							Proposed Staffing	
1990	1995	2000	2005	2007	2009	2011	2012	2013
31,985	36,429	40,285	35,489	35,548	35,641	33,777	34,413	34,413

SOURCES: IBO; Mayor's Office of Management and Budget

NOTES: Figures above are either actual or proposed end-of year (June 30) staffing levels. Includes uniformed police personnel of all ranks.

Proposed Police Officer Staffing To Remain Level Next Year, Civilian Positions to Decline

Under the Mayor's Preliminary Budget for 2013, authorized uniformed staffing in the police department (NYPD) would remain at the current level of 34,413. Police officer staffing has been relatively stable in recent years after declining sharply from a peak of 40,285 in June 2000.

Meanwhile, under the Mayor's Preliminary Budget, budgeted civilian staffing within the NYPD would decline by over 300 positions next year, from 14,411 this year to 14,107 by June 2013. The decline would be achieved through attrition rather than layoffs. This comes after a drop in civilian staffing each year since fiscal year 2009, when the NYPD employed over 15,000 full-time civilian personnel.

Efforts to achieve budgetary savings by reducing civilian positions within the department increase the likelihood of police officers being called upon to perform administrative or other support functions, thereby reducing their availability for direct law enforcement activities. In its most recent quarterly civilianization report to the City Council, the police department acknowledged that as of December 2011 there were over 500 "full duty" police officers performing tasks that could instead be performed by less costly civilian personnel.

Labor Costs

The expense budget of each city agency includes funds to pay the wages and salaries of its current employees, but other labor-related expenses are funded in the city's miscellaneous and pension budgets. The miscellaneous budget includes funding for fringe benefits for most agencies' employees and the labor reserve contains funding for future wage and/or expected retroactive increases that have not yet been settled by collective bargaining agreements or administrative orders for non-union personnel. Funding for the labor reserve in the Preliminary Budget reflects the Bloomberg Administration's assumption that any wage increases in the current round of bargaining will be paid for by increases in productivity or other contractual offsets.

The projections of the city's pension funding obligations in the Preliminary Budget were made using revisions of actuarial methods and economic and demographic assumptions recommended by consultants and endorsed by the Actuary. The budget also incorporated projected savings from altering pension benefits for future public-sector employees, but the Bloomberg Administration's estimates were based on the full implementation of the package of pension changes proposed in January by Governor Cuomo. However, the reforms recently enacted in Albany, creating a new pension system—Tier V—for city workers, are not as extensive, and IBO's estimate of pension reform is based on the enacted Tier V changes.

Health Insurance Costs Growing, Retiree Health Trust Funds Depleted

For civilian employees of most city agencies, the city funds fringe benefits—such as health insurance, welfare fund benefits, Social Security contributions, unemployment insurance, and worker's compensation—out of the miscellaneous budget, not the budgets of the specific agencies in which employees work. Only the budgets of the Department of Education (DOE) and the City University of New York (CUNY) include all of the fringe benefits of their employees. Similarly, some fringe benefits for uniform services personnel—who comprise most employees in police, fire, sanitation, and corrections—are funded within their departments' budgets.

Health Insurance. Whether funded through the miscellaneous budget or the DOE and CUNY budgets, health insurance is the most expensive of the city's fringe benefits obligations, accounting for just under 62 percent of fringe benefit costs in 2012. The Financial Plan provides a total of $4.8 billion in 2012 for active and retired employee's health insurance, a 10.4 percent increase over 2011 funding. This total includes $672 million withdrawn from the Retiree Health Benefit Trust (RHBT) to cover a large part of the $1.6 billion cost of retirees' insurance in that year (see below).

IBO projects that health insurance costs for current and retired employees will be $5.2 billion in 2013—a 7.9 percent increase over this year—with annual increases of 9.0 percent on average in the next three years, bringing projected health insurance costs to $6.7 billion in 2016. IBO's estimates of health insurance costs are slightly higher than the Bloomberg Administration's—by an average of $45 million annually after 2012—due to our projections of steeper increases in premium rates after 2014 and an estimated $25 million annual cost of a November 2011 state law expanding coverage for autism disorders that was not taken into account in the Preliminary Budget.

The city projects its contributions for active personnel's health insurance on the basis of changes in HIP premium rates, which were recently set at 8.5 percent increases for 2013, down from the 9.5 percent assumed by the city prior to the Preliminary Budget.[1]

To help fund health insurance payments for retired employees, the city plans to draw down the balance of the money in the Retiree Health Benefit Trust—$672 million in 2012, and $1.0 billion a year in 2013 and

2014. The RHBT was established in 2006, using part of that year's budget surplus to take an initial step toward providing for the city's unfunded retiree health insurance liability. After making contributions to the fund totaling $2.5 billion through 2007, the city made no additional contributions and has now begun drawing down the fund for budget relief. By using the RHBT to fund benefits paid to current retirees, the city frees up an equivalent amount of money for other uses. Assuming no additions to the RHBT fund in the coming years, these withdrawals will effectively deplete the fund by the end of 2014.

Little in Reserve for Expired Labor Contracts

The city sets aside money in the labor reserve for future and/or expected retroactive wage increases for city employees. Money in the miscellaneous budget's labor reserve covers employees in all agencies except the Department of Education, which contains a separate labor reserve within its budget. When wage increases are agreed to through collective bargaining or established by administrative orders for workers not included in bargaining units, money is taken out of the reserve and added to the expense budgets of specific agencies.

As of January 2012, the general labor reserve (not including DOE) contained $82.1 million for use in this fiscal year, $164.3 million for use in 2013, and larger amounts for use in subsequent years—$323.4 million, $539.7 million, and $795.8 million in 2014, 2015, and 2016, respectively. These amounts reflect the city's forecast of the size and timing of wages increases in future collective bargaining agreements, including retroactive agreements for employees whose labor contracts have already expired.

Labor contracts for a large number of union members have expired—many in calendar year 2010—and funding for the labor reserve in the Preliminary Budget is based on the Bloomberg Administration's proposals of three years of no wage increases for the current round of bargaining covering 2010 through 2012, followed by two 1.25 percent increases. According to the Bloomberg Administration, any additional wage increases would need to be funded through increased productivity or other contractual offsets. This assumed pattern of wage growth is far less than the two compounded 4 percent annual wage increases established for civilian personnel for the 2008-2010 bargaining period.

Most Collective Bargaining Agreement with Major Unions Have Expired

Collective Bargaining Unit	Contract Expiration Date	Active Membership
Uniformed Personnel		
Police Benevolent Association	7/31/2010	22,843
Uniformed Firefighters Association, Local 94	7/31/2010	7,926
Correction Officers Benevolent Association	10/31/2011	7,470
Sanitation Workers, IBT, Local 831	9/20/2011	6,007
Detectives Endowment Association	3/31/2012	5,058
Sergeants Benevolent Association	8/29/2011	4,574
Uniformed Fire Officers Association, Local 854	3/26/2011	2,407
Lieutenants Benevolent Association	10/31/2011	1,720
Pedagogical Employees		
United Federation of Teachers	10/31/2009	117,385
Professional Staff Congress	10/19/2010	7,443
Council of Supervisors and Administrators	3/5/2010	5,983
Civilian Employees		
AFSCME, District Council 37	3/2/2010	75,958
IBT, Local 237	9/25/2010	7,957
Principal Administrative Association., CWA, Local 1180	10/5/2010	6,044
Organization of Staff Analysts	8/24/2010	3,257
Traffic Enforcement Agents, CWA, Local 1182	3/9/2010	2,355

SOURCES: IBO; Office of Labor Relations; Mayor's Office of Management and Budget
NOTES: Collective bargaining units with less than 1,000 members are excluded. Active members as of mid-March 2012, city personnel only.

Moreover, the state's Public Employment Relations Board (PERB) has declared impasses in negotiations between the city and the United Federation of Teachers (UFT) and the Council of Supervisors and Administrators (CSA), whose contracts expired in October 2009 and March 2010, respectively. If the PERB determines that teachers and DOE supervisors are entitled to retroactive raises with no productivity offsets, the city would need to find other sources of funds because DOE's labor reserve contains no money for wage increases for that contract round. The City Comptroller has estimated that the retroactive cost to DOE of settlements comparable to the two 4 percent raises other municipal unions received during the 2008-2010 contract period would be $1.7 billion.

Pensions Changes: New Tier Saves Less than Budgeted, Shifts in Actuarial Methods Has Upfront Savings

New York City's pension budget funds the city's contributions to a variety of pension systems. The overwhelming majority of contributions are made to one of five funds the city maintains to cover its workers and retirees. The city also contributes to pension funds for personnel of the cultural institutions and libraries that the city supports, although they are not formally city workers, and to a defined-contribution plan for the full-time pedagogical staff at CUNY's community colleges who opt for that plan over a defined-benefit pension fund.[2]

Funding. In the February plan, the cost for total contributions to all pension systems is expected to total $8.0 billion dollars in 2012. Pension costs increase to $8.1 billion in 2013 and then stabilize at $8.0 billion annually in subsequent years. Almost all the contributions—98.0 percent—are made with city funds, with most of the remaining funded by transfers of state and federal aid.

The Preliminary Budget incorporates two important changes: (1) new actuarial methods and changes in demographic and economic assumptions, which together increase the projected cost of the city's pension obligations; and (2) projected savings resulting from state legislation changing pension terms for new hires. Subsequent to the release of the Preliminary Budget the state enacted a pension overhaul bill that includes some but not all of the changes sought by the Bloomberg Administration. The result is a new pension tier—Tier V—for city employees hired after April 1, 2012. In addition to these major changes, a recent New York State Supreme Court decision poses another risk to the pension budget—one not

City-Maintaned Funds Responsible for Almost All Pension Outlays

	City-Funded Members	Funding, *dollars in millions* 2011	2012	2013	2014	2015	2016
City-Mantained Pension Systems							
New York City Employees' Retirement System	346,000	$1,278.3	$1,569.1	$1,618.5	$1,621.0	$1,621.0	$1,670.1
Teachers' Retirement System	203,000	2,427.6	2,656.4	2,755.0	2,843.8	2,882.8	3,030.7
Police Pension Fund	82,000	2,083.6	2,432.7	2,441.0	2,332.4	2,289.3	2,230.7
Board of Education Retirement System	41,000	170.5	1,004.7	1,005.4	980.1	970.4	989.7
Fire Department Pension Fund	28,000	890.7	213.7	204.5	214.4	213.6	235.1
Other Pension Systems							
Cultural Institutions Retirement System	19,000	21.3	22.7	23.7	24.6	25.6	26.4
Teachers Insurance and Annuity Association-College Retirement Equities Fund	1,000	26.3	27.0	27.0	27.0	27.0	27.8
New York State and Local Employee's Retirement System, Library Employees	1,000	19.3	22.1	26.4	31.8	38.4	39.5

SOURCES: IBO; Mayor's Office of Management and Budget; Pension Payroll Management System; Comprehensive Annual Financial Report
NOTES: 2011 is actual, all otherst are projected. Not listed are four pension funds long closed to new members but still paying benefits to about 35 retirees. Rough estimates of members assembled by IBO from multiple sources. Cultural Institutions Retirement System includes all members, not just city-funded. For Teachers Insurance and Annuity Association-College Retirement Equities Fund and New York State and Local Employee's Retirement System, active members only.

accounted for in the February plan.

Changes in Pension Assumptions. Based on the recommendations from a recent audit made by the Hay Group, a management and compensation consulting firm, the New York City Office of the Actuary has proposed several changes in actuarial methods and revised the economic and demographic assumptions used to project the city's financial obligations for all five of its pension funds. Together these changes would increase the city's pension costs.

The recommendation that would have the greatest impact on projections is lowering the actuarial interest rate (AIR) by a full percentage point from 8 percent to 7 percent. The AIR is the anticipated rate of return on the current and future assets of the pension funds. The AIR is also used as the discount rate determining the present value of the plans' expected future benefit payments. Absent any increase in contributions from current employees, a lower AIR means that the city's contributions must grow to make up for the assumption that investment returns will be lower. Another recommendation in the report is for the city to adopt an "entry age normal" actuarial cost method (ACM), the method most commonly used by public-sector pensions. This ACM more explicitly recognizes actuarial gains and losses, allowing easier monitoring of how actuarial gains and losses, as well as other unfunded liabilities, are contributing to the overall costs of the pension systems. The proposed AIR and ACM changes require approval from each of the Boards of Trustees of the five city-maintained retirement systems, as well as approval by the state Legislature.

The Actuary also recommended increasing the inflation rate assumption from 2.5 percent to 3.0 percent, and increasing the assumed rate of general wage growth from 3.0 percent to 3.5 percent. Several changes in demographic assumptions were also proposed, such as revising mortality tables to reflect the fact that city employees are living longer.

In anticipation of the changes in the ACM, the AIR, and in the economic and demographic assumptions, the city had added $1 billion dollars in annually recurring costs to the pension budget to pay for these expected changes. While the audit resulted in recommendations that significantly raise the city's required contributions, the city has determined that it will only need to use $575 million of that reserve annually, in part because it plans to amortize the increased liabilities over 22 years—longer than the standard 15-year amortization period. This generates annual savings to the city's budget of $425 million in 2012 and 2013.

Tier V Pension. The package of pension changes recently approved in Albany creates a Tier V pension program for New York City public sector workers, effective April 1, 2012. (For state workers, the new program would be Tier VI.) Though less extensive than those proposed by Governor Cuomo in January, Tier V makes significant changes to current pension benefits for new employees. (Those currently in a pension system and former members eligible to be reinstated into their former tier are not affected.) A summary of significant changes affecting different pension plans covering city employees is available here. For some or all of the plans, Tier V does the following:

- Lengthens the vesting period from 5 years to 10 years and raises the minimum age at which retired members can receive full pension benefits from 62 to 63.
- Lowers benefits under early retirement options.
- Replaces a flat basic employee contribution rate of 3 percent with a progressive schedule of rates, from 3 percent for those with salaries under $45,000 to 6 percent for those with incomes above $100,000.
- Requires employee contributions for all years of service, not just the first 10 years
- Increases from three years to five years the period over which final annual salary is averaged to determine benefit levels.
- For civilian workers, limits the amount of overtime pay that is pensionable (that is, included in the calculation of final annual pay).
- Limits the use of other types of pay from pensionable amounts.
- Reduces the pension multiplier factor, increasing the number of years of service needed to receive full pension benefits (50 percent of final average salary) from 25 to 27.5.
- Increases the cost of buying back prior years of service from 3 percent to 6 percent of wages.

Tier V Budget Savings. IBO estimates the creation of Tier V will reduce New York City's pension costs by $6 million in 2014, $53 million in 2015 and $99 million in 2016. These projections take into account the actuarial changes recommended by the Hay Group. Introducing the new tier produces no substantial savings until 2015 because there is a one-year lag between the valuation date at the end of the fiscal year—when the Actuary determines how much the city needs to contribute to the pension funds—and when the contribution is actually made. (The small amount of savings in 2014 comes from new hires in the last quarter of 2012 who enroll in Tier V.) Excluded from the calculations are potential savings due to the effects of changes to the state retirement system to which the city contributes for the pensions of library employees.

The Bloomberg Administration's budget, released in February, included projected savings from a new pension tier, but its estimates were based on the more extensive package of changes proposed by Governor Cuomo in January. Based on the Governor's proposal, the Preliminary Budget projected savings of $80 million in 2015 and $155 million in 2016—$27 million greater in 2015 and $56 million greater in 2016 than IBO's estimates.

Additional Potential Pension Costs. A recent court ruling may add to the city's pension costs. In January, the State Supreme Court ruled in a case brought by the Patrolmen's Benevolent Association that Tier III uniformed city police and fire employees hired after July 1, 2009 are entitled to a benefit previously received only by their coworkers in Tier II: a city-funded offset or reduction to their pension contributions not to exceed a 5 percent contribution rate. If the ruling is sustained on appeal, affected personnel would no longer contribute any money toward their pensions because the current Tier III contribution rate is only 3 percent—less than the maximum offset. In addition, the Police and Fire Department Pension funds would also have to refund all Tier III employee contributions with interest.

Based on employee contributions that have been deducted to date for the almost 4,100 Tier III employees affected by this decision, IBO anticipates that by the end of 2012, $7.8 million would have to be refunded, including interest. Going forward, the ongoing costs to the city of assuming pension contributions for Tier III police and fire employees would grow significantly—from an estimated $17.2 million in 2013 to $83.0 million in 2016—as the fire and police departments hire more personnel and Tier III members move up the wage ladder.

Endnotes

[1] The HIP rate also determines the city's contributions for the health insurance of retirees not yet eligible for Medicare.

[2]In addition, the city contributes to four pension funds long closed to new members but still paying benefits to about 35 retirees, including three who worked for the once-private BMT and IRT subway systems.

Capital Spending, Financing, & Debt Service

Four-Year Capital Commitment Plan

The February 2012 Capital Commitment Plan that was released with the Mayor's Preliminary Budget provides $35.1 billion for the city's capital program, covering the period 2012 through 2015. The total represents an increase of $688 million, or 2.0 percent, from the level of capital funding in the September 2011 commitment plan.

Although the capital program is primarily city-financed, approximately 20 percent of its total funding comes from state, federal, and private grants; the February 2012 plan includes $7.1 billion in such noncity funding. There is little change since September (a reduction of $7 million) in these noncity funding sources in the current plan.

Capital commitments for the plan period 2012 through 2015 are largely concentrated in three areas—education, environmental protection, and transportation—that comprise $20.8 billion in total funds, or nearly 60 percent of the entire capital plan.

Education projects constitute the largest share, $8.7 billion (24.7 percent) of total capital commitments. There was no change in the total amount of planned capital commitments for education projects from the September plan, although there were changes in timing within the plan period. Commitments for the current year were reduced by $375 million, with increases in 2013 and 2014 of $275 million and $100 million, respectively.

While overall capital commitments for education were unchanged, the annual amendment to the School Construction Authority's (SCA) separate five-year capital plan leverages lower project costs to add to planned new classroom seats even as a greater share of the planned spending is directed towards improving existing facilities. The SCA recently reported cost savings from large construction projects and negotiated lease agreements due to greater competition from bidders. These lower costs allowed the SCA to increase the plan for new capacity by almost 4,800 seats, an increase of 16.4 percent, bringing the total new seats in the five-year plan to 33,888, while simultaneously shifting a larger share of the dollars in the plan to rehabilitation of existing structures.

Environmental protection projects account for the second largest share, $7.8 billion or 22.2 percent of total capital commitments. While there was just a small increase in funding of $88 million (1.1 percent) for the plan period, there were major shifts in funding between project types.

The total for water pollution control projects over the plan period increased by $481 million. A significant portion of the increase, $347 million, is for centrifuge upgrades as well as other improvements at various wastewater treatment plants. Water mains, reservoir,

City Revises Four-Year Capital Commitment Plan
Authorized commitments, dollars in millions

	2012	2013	2014	2015	TOTAL
February 2012 Plan Funds					
City	$12,434	$7,082	$4,854	$3,564	**$27,934**
Noncity	2,817	1,604	1,660	1,057	**7,138**
TOTAL	**$15,251**	**$8,686**	**$6,514**	**$4,621**	**$35,072**
September 2011 Plan Funds					
City	$12,980	$6,028	$4,719	$3,512	**$27,239**
Noncity	3,115	1,324	1,612	1,094	**7,145**
TOTAL	**$16,095**	**$7,352**	**$6,331**	**$4,606**	**$34,384**
$ Change					
City	$(546)	$1,054	$135	$52	**$695**
Noncity	(298)	280	48	(37)	**(7)**
TOTAL	$(844)	$1,334	$183	$15	**$688**
% Change					
City	-4.2%	17.5%	2.9%	1.5%	**2.6%**
Noncity	-9.6%	21.1%	3.0%	-3.4%	**-0.1%**
TOTAL	**-5.2%**	**18.1%**	**2.9%**	**0.3%**	**2.0%**

SOURCES: IBO; February 2012 and September 2011 Capital Commitment Plans

NOTE: Plan figures exclude inter-fund agreements, contingency amounts and the reserve for unattained commitments.

and treatment projects increased by $156 million; notable increases include $41 million for Hurricane Irene related emergency contracts, $28 million for the Dam Safety program, and $17 million for the Croton Filtration Plant.

Conversely, there was a net decrease of $496 million in water supply projects. Funding for the repair of the Delaware Aqueduct fell by $513 million, while about $16 million was added to various other water supply projects. The cut in funding for the project to repair the leaking aqueduct in the four-year plan is expected to be offset by an increase in funding starting in 2016. The Department of Environmental Protection expects to revise the capital plan next year to reflect a more realistic construction schedule.

Transportation projects account for the third largest share, $4.3 billion or 12.3 percent, of total capital commitments. Compared with September 2011 there was an increase of $175 million (4.2 percent) for the plan period as a whole, with larger year-to-year swings in project funding. Planned commitments for transportation projects decreased by $366 million in the current year and increased by $464 million in 2013. In the remaining years of the plan period, total planned commitments for transportation increased by $77 million from the September 2011 plan.

The largest change represents year-to-year funding shifts and increases in highway and highway bridge projects, which saw a reduction of $325 million in the current year, and an increase of $432 million in 2013 as well as a combined increase of $62 million for 2014 and 2015. Among the major projects shifted from 2012 to 2013 were the Mill Basin Bridge over the Belt Parkway ($216 million), $46 million for Safe Routes to Schools for 94 schools, and $27 million for street reconstruction projects including 94th Street west of the Aqueduct racetrack.

Applied Sciences Initiative. Capital funding for the Applied Sciences NYC initiative, a competitive bidding process through which Cornell University, with partner institution Technion-Israel Institute of Technology, was selected to build a technology and engineering campus on Roosevelt Island, was added to the capital plans of the Department of Small Business Services and the Health and Hospitals Corporation.

The Department of Small Business Services capital plan now includes $100 million in city funding for infrastructure and construction costs for the new campus. Most of the funds, $72 million, are in the current four-year plan for 2013, while the remaining $28 million is expected to be spent in 2016 through 2021.

The Health and Hospitals Corporation's capital plan already included $178 million in funding added a year ago to relocate the Goldwater campus of the Coler-Goldwater Hospital from Roosevelt Island to the former North General Hospital site in Harlem. With the decision to locate Cornell's new technology campus on Roosevelt Island, an additional $86 million was included in the February 2012 commitment plan to accelerate the Goldwater move to accommodate Cornell's plans.

Administrative Services. The Department of Citywide Administrative Services also saw an increase of $294 million in capital funding. There was a net increase of $194 million for general services; notable changes include increases of $72 million for citywide administrative systems, $58 million for citywide electronic data processing, and $31 million for electronic data processing at the Financial Information Services Agency, offset by a $45 million reduction for energy efficiency initiatives. Another $70 million in funding was added at properties owned by the city—much of it for projects that had originally been scheduled for 2012—and $30 million was added for courts in the Bronx and Brooklyn.

Paying for the Capital Program

Borrowing. To finance the city's 2012-2015 Capital Commitment Plan, the city will borrow money by issuing three types of debt: general obligation (GO), Transitional Finance Authority (TFA), and Municipal Water Finance Authority (NWY). GO debt is backed primarily by the city's property tax, and TFA debt is backed by the personal income tax. NYW debt is backed by fees and charges levied on users of the New York City water and sewer systems. The proceeds of new money water authority debt are pledged exclusively to capital improvements for the city's water and sewer system. GO and TFA debt proceeds fund the remainder of the city-funded capital program.

City Debt Issuance Trends. The Mayor's Office of Management and Budget projects that annual levels of new bond issuance will total about $5.0 billion a year from 2012 through 2015, down from 2010 and 2011, before dipping in 2016. Annual new money bond issues reached $5.4 billion in 2009, peaked at $7.0 billion in 2010, and then declined to $5.8 billion in 2011. The city currently anticipates GO and TFA bond issuance from 2012 through 2016 will total $24.5 billion.

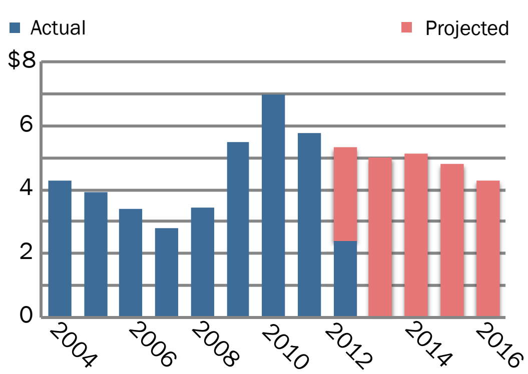
Annual borrowing is based on the city's cash needs for capital projects. Cash needs are roughly correlated with city capital expenditures in each year. Because a capital commitment (when the city registers a contract for the project) in one year can result in capital expenditures in that year, in a later year, or spread out over a few years, there is only a weak relationship between capital expenditures and capital commitments.

Debt Service. Debt service—the cost of repaying principal and/or interest on outstanding bonds—is a function of the amount of outstanding debt and the terms that were obtained when the debt was issued. Debt service reflects GO and TFA borrowing, as well as several smaller obligations. Debt service for NYW borrowing is not reflected in the city budget as it is paid directly by the water authority—a self-financing public benefit corporation.

Historically Low Interest Rates. In the Preliminary Budget, the Mayor's budget office has again recognized significant debt service savings due to extraordinarily low interest rates, particularly for the city's substantial outstanding variable rate debt. In this plan, the city is

Selected City Bond Issues

Dollars in billions



SOURCES: IBO; Mayor's Office of Management and Budget
NOTE: Includes GO and TFA new money bond issues. Excludes refunding bonds,TFA Recovery Bonds, TFA Building Aid Revenue Bonds and Muncipal Water FInance Authority Bonds.

recognizing savings on general obligation variable-rate demand bonds (VRDBs) of $55.4 million in 2012 and $14.5 million in 2013.

As of the Preliminary Budget, the city had $6.4 billion of GO VRDBs outstanding, and as of October had an additional $3.3 billion of TFA VRDBs. These variable rate bonds may be tax exempt or taxable, but the bulk of GO VRDBs are tax exempt ($6.2 billion). The Bloomberg Administration's baseline interest rate assumptions on these bonds are 4.25 percent for tax exempt and 6.0 percent for taxable. The city's projections of interest expenses are conservative and revisions to reflect lower interest rates have been done incrementally and slowly; adjustments are made only when they can be done with certainty. With the Federal Reserve signaling continuing low interest rates likely through late calendar year 2014, the Mayor's budget office has begun making downward adjustments for fiscal years 2012 and 2013 earlier than it has in the past.

For 2010 and 2011 downward revisions to VRDB interest rate assumptions were begun at each respective fiscal year's Adopted Budget. Interest rate assumptions were revised downward four times in each of the two fiscal years, reaching rates of 0.32 percent on tax-exempt bonds and 0.8 percent on taxable bonds for 2010, and 0.3 percent on tax exempt and 1.0 percent on taxable for 2011. City expectations of the amount of variable rate debt outstanding can also affect debt service, but the fiscal impact of changes in projected debt outstanding has been relatively modest. These revisions to rates and bonds outstanding allowed the city to recognize savings of around $270 million each year, with over 95 percent of the savings attributable to the rate adjustments.

For 2012, the city began revising VRDB interest rate assumptions downward in its January 2011 Preliminary Budget, six months before adoption. Since then, the city has recognized about $230 million of savings for 2012 due to reducing interest rate assumptions to 0.8 percent on tax-exempt bonds and 1.5 percent on taxable bonds, with an additional $8 million in savings from reductions in the amount of outstanding variable rate GO debt.

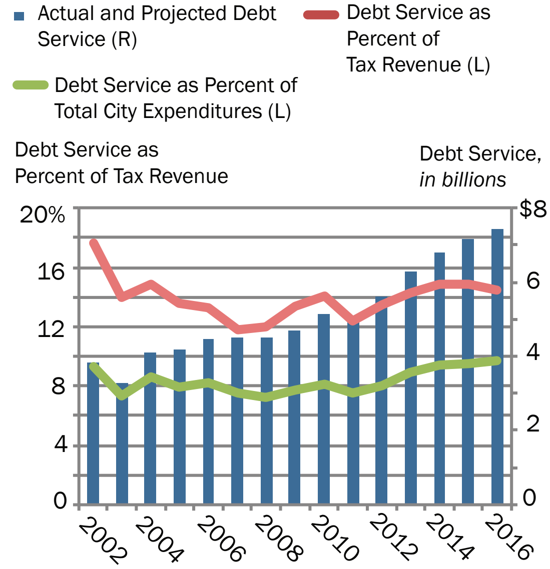
For 2013, interest rate assumptions for variable rate debt were revised still earlier—in November 2011. As of the February 2012 Preliminary Budget, the city has recognized $97 million in savings by reducing rate assumptions to 2.72 percent on tax exempt bonds and 4.5 percent on taxable bonds. Those savings are offset slightly by a $4 million increase in variable rate debt service resulting from higher projections for the amount of variable rate debt outstanding. However, rate assumptions for 2014 and beyond remain at 4.25 percent and 6.0 percent for tax exempt and taxable bonds, respectively.

The low interest rates of the past several years have allowed the city to recognize more than $875 million in savings for fiscal years 2010 through 2013 on GO variable rate debt alone. Additional savings have been realized on TFA variable rate debt and through favorable rates on GO and TFA fixed-interest borrowing—both new money and refunding issuances.

With the Federal Reserve signaling that it will maintain its current low federal funds rate through calendar year 2014, there is reason to believe that the city will be able to recognize substantial additional savings going forward. Should Federal Reserve rates remain near recent years' levels, 2012 and 2013 VRDB rates would likely end up close to 0.3 percent on tax-exempt bonds and 1.0 percent on taxable bonds, generating additional savings. If, when the Federal Reserve begins raising rates, it does so at a slow pace, the city could realize interest savings for fiscal years 2014 and beyond, as well.

Growth in Debt Service. Debt service, adjusted for prepayments and defeasances, is expected to total $5.6 billion in 2012, a 13.4 percent increase from $4.9 billion in 2011. This would be the largest one-year percentage increase in debt service since an increase of 25.8 percent from 2003 to 2004. There was an unusual year-over-year drop in debt service expense in 2011, which came in at $102 million less than forecast in the Preliminary Budget, due largely to the interest rate trends discussed above. Given the stable low interest rates, the city is likely to realize some additional debt service savings for this year. Because

Debt Service and Debt Service as Shares Of Tax Revenuesand Expenditures



SOURCES: IBO; Mayor's Office of Management and Budget
NOTES: Fiscal years 2012–2016 are projected. Adjusted for prepayment of debt service. Projections based on IBO tax revenue and expenditure forecasts.

the terms of much of the city's debt outstanding (other than variable rate debt and new issuances) predate the current interest rate environment, the budgetary impact is likely to be moderate at best. The $5.6 billion would represent 13.5 percent of IBO's forecast of city tax revenues, roughly in line with the average ratio of the past decade.

Debt service is projected to grow at a slightly lower rate of 12.0 percent in 2013, but faster than IBO's projected growth in tax revenues, rising to 14.3 percent of those revenues. In 2014, debt service growth falls to 8.3 percent, but continues rising to 14.9 percent of projected tax revenues. In 2015 and 2016, projected debt service growth slows and begins declining as a percentage of forecast tax revenues.

Debt service as a share of city expenditures is also rising, from 8.0 percent in 2012 to 8.9 percent in 2013. In the remainder of the forecast period, IBO expects debt service as a percent of expenditures to grow from 9.4 percent in 2014 to 9.7 percent in 2016.

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