Review of the Financial Plan of the City of New York

March 2014

Report 12-2014

New York State
Office of the State Comptroller
Thomas P. DiNapoli

Office of the State Deputy Comptroller
for the City of New York
Kenneth B. Bleiwas

Additional copies of this report
may be obtained from:

Office of the State Comptroller
New York City Public Information Office
633 Third Avenue
New York, NY 10017

Telephone: (212) 681-4840

Or through the Comptroller's website at: www.osc.state.ny.us

Please notify the Office of the State Deputy Comptroller at (212) 383-3916 if you wish to have your name removed from our mailing list or if your address has changed.

Contents

I. Executive Summary

On February 12, 2014, the City of New York revised its four-year financial plan (the "February Plan") to update its revenue and expenditure forecasts, and to begin reflecting the priorities of the new mayoral administration (see Figure 1). Since the beginning of the fiscal year, the City has raised its tax revenue forecast by more than $5 billion through FY 2018 because the economy is outperforming the City's expectations. These resources contributed to a $1.8 billion surplus in FY 2014 (which the City will use to balance the FY 2015 budget), and also permitted the City to greatly reduce the out-year budget gaps, increase reserves, rescind planned budget cuts, and address other budgetary needs such as additional funds for snow removal.

All of the labor agreements with the City's unions have expired, some as long ago as 2008. The new administration has indicated that settling these contracts with 152 separate bargaining units will be a priority. While the City is seeking cost savings and other efficiencies from its unions to help fund these agreements, the net cost could be substantial. As discussions are just beginning, the final cost and structure of the agreements may not be known for some time.

The February Plan includes a number of new initiatives, including the Mayor's proposal to provide high-quality full-day prekindergarten services to all eligible children by January 2016, and to expand after-school programs for middle-school students. The Mayor has asked the State to approve an increase in the personal income tax rate for the City's highest earners to fund these initiatives. The Governor instead has proposed allocating State resources to phase in, over five years, similar programs across the State. More will be known about the cost of these initiatives and the sources of funding by the time the Mayor presents his executive budget in May 2014.

Although not included in the February Plan, the City is also asking the State to increase education aid beyond the amounts recommended by the Governor in his executive budget. In making the case for additional aid, the City points to the State's failure to fulfill an earlier promise to increase State education aid to the City as part of the resolution of the Campaign for Fiscal Equity lawsuit. The City estimates that State education aid to the City is about $2.7 billion less than promised years ago. A new lawsuit was recently filed alleging that the State has failed to meet its funding commitments.

New York City has experienced solid economic growth in recent years, which has helped fuel tax collections, but not all economic indicators have returned to their prerecession levels, and there remain areas of concern. The broadest measure of the local economy, the Gross City Product, is only now returning to its prerecession level.

Employment growth has been very strong with the addition of 275,000 jobs since 2009 (two and a half times as many jobs as were lost in the City during the Great Recession), and total employment has reached a new record (4 million). Most of the job growth, however, has been concentrated in lower-paying industries (e.g., retail trade). While the unemployment rate has declined to 7.8 percent, the lowest level in five years, it is higher than before the recession and higher than the national rate. About half of unemployed people in the City have been without a job for more than six months, and this figure has barely budged for three years.

The New York Stock Exchange reports that the broker/dealer operations of its member firms (the traditional measure of industry profitability) earned $16.7 billion in 2013. Profits were much lower than last year, but it was still a good year by historical standards. Although the securities industry in New York City is 12.6 percent smaller than it was before the recession, it remains profitable and well compensated.

Debt service and health insurance costs are projected to grow by $4.6 billion (47 percent) between fiscal years 2013 and 2018, and to consume 24 percent of City fund revenue by FY 2018. While pension contributions are now growing slowly after years of rapid growth, the City's pension forecasts do not include the potential impact of new labor agreements. The municipal workforce declined by 15,666 employees between fiscal years 2008 and 2012 as budget cuts were imposed to weather the Great Recession. Although staffing levels grew by 2,000 employees last year and are slated to increase by another 3,900 workers by June 2014, staffing would remain well below the prerecession peak.

At the end of FY 2013, the City's unfunded obligation for post-employment benefits other than pensions totaled $92.5 billion, nearly $39 billion more than in FY 2006. The City deposited surplus resources into the Retiree Health Benefits Trust during the last economic expansion to help fund this future liability, but instead has used the trust as a rainy-day fund to help balance the budget. The City had planned to draw down $1 billion from the trust in FY 2014, but the Mayor has rescinded the planned transfer.

Although revenue collections could be higher than anticipated in the February Plan, the City still faces a number of large budget risks (see Figure 2). Besides the potential cost of collective bargaining, the City is counting on the receipt of $1.2 billion during fiscal years 2015 through 2017 from the planned sale of 1,600 taxi medallions, which still requires State approval. In addition, the Health and Hospitals Corporation could require further financial assistance from the City, and federal aid for recovery from Superstorm Sandy could fall short of expectations.

The City's financial outlook has improved greatly since the depth of the Great Recession. The City's economy is growing steadily and the February Plan forecasts a balanced budget for FY 2015. The out-year budget gaps have been reduced to $1.1 billion in FY 2016, $530 million in FY 2017 and $370 million in FY 2018, far smaller than projected two years ago. The City's gap estimates, however, do not yet reflect the impact of unfinished labor negotiations, which casts a shadow of uncertainty over the City's financial plan.

Figure 1
New York City Financial Plan
(in millions)

	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
REVENUES					
Taxes					
General Property Tax	$ 19,781	$ 20,782	$ 21,815	$ 22,703	$ 23,579
Other Taxes	26,240	27,480	28,744	29,848	30,872
Tax Audit Revenue	710	709	709	709	709
Subtotal: Taxes	$ 46,731	$ 48,971	$ 51,268	$ 53,260	$ 55,160
Miscellaneous Revenues	7,281	6,782	6,808	6,831	6,489
Unrestricted Intergovernmental Aid	- - -	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(1,743)	(1,696)	(1,669)	(1,679)	(1,684)
Disallowances Against Categorical Grants	(15)	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 52,254	$ 54,042	$ 56,392	$ 58,397	$ 59,950
Other Categorical Grants	871	843	830	826	822
Inter-Fund Revenues	546	520	513	513	513
Federal Categorical Grants	8,409	6,402	6,384	6,370	6,369
State Categorical Grants	11,737	11,905	12,275	12,747	13,143
Total Revenues	**$ 73,817**	**$ 73,712**	**$ 76,394**	**$ 78,853**	**$ 80,797**
EXPENDITURES					
Personal Service					
Salaries and Wages	$ 22,424	$ 22,466	$ 22,748	$ 23,017	$ 23,340
Pensions	8,321	8,330	8,448	8,553	8,729
Fringe Benefits	8,795	9,173	9,836	10,557	11,352
Subtotal: Personal Service	$ 39,540	$ 39,969	$ 41,032	$ 42,127	$ 43,421
Other Than Personal Service					
Medical Assistance	$ 6,365	$ 6,447	$ 6,415	$ 6,415	$ 6,415
Public Assistance	1,376	1,396	1,396	1,402	1,402
All Other[1]	23,460	22,033	22,385	22,894	23,188
Subtotal: Other Than Personal Service	$ 31,201	$ 29,876	$ 30,196	$ 30,711	$ 31,005
Debt Service [1,2]	$ 5,737	$ 6,733	$ 7,294	$ 7,624	$ 7,825
FY 2013 Budget Stabilization & Discretionary Transfers [1]	(2,838)	- - -	- - -	- - -	- - -
FY 2014 Budget Stabilization[2]	1,770	(1,770)	- - -	- - -	- - -
General Reserve	150	600	600	600	600
Subtotal	$ 75,560	$ 75,408	$ 79,122	$ 81,062	$ 82,851
Less: Intra-City Expenses	(1,743)	(1,696)	(1,669)	(1,679)	(1,684)
Total Expenditures	**$ 73,817**	**$ 73,712**	**$ 77,453**	**$ 79,383**	**$ 81,167**
Gap To Be Closed	**- - -**	**- - -**	**$ (1,059)**	**$ (530)**	**$ (370)**

Source: NYC Office of Management and Budget

1 Fiscal Year 2013 Budget Stabilization and Discretionary Transfers total $2.807 billion, including GO of $2.727 billion, net equity contribution in bond refunding of $16 million and subsidies of $64 million. In addition, the Fiscal Year 2012 Budget Stabilization included $31 million for the prepayment of Fiscal Year 2014's debt service.

2 Fiscal Year 2014 Budget Stabilization totals $1.770 billion.

Figure 2
OSC Risk Assessment of the City Financial Plan
(in millions)

	Better/(Worse)				
	FY 2014	**FY 2015**	**FY 2016**	**FY 2017**	**FY 2018**
Surplus/(Gaps) per February Plan	**$ - - -**	**$ - - -**	**$ (1,059)**	**$ (530)**	**$ (370)**
Tax Revenue	300	375	250	275	275
Medicaid Reimbursement	(35)	(120)	(150)	(150)	(150)
Overtime	(50)	(100)	(100)	(100)	(100)
OSC Risk Assessment	**215**	**155**	**- - -**	**25**	**25**
Surplus/(Gaps) per OSC [3,4]	**$ 215**	**$ 155**	**$ (1,059)**	**$ (505)**	**$ (345)**
Additional Risks and Offsets [5,6,7]					
Taxi Medallion Sale	- - -	(481)	(360)	(400)	- - -

---

3 All of the contracts with the unions that represent the municipal workforce have expired, some as long ago as 2008. The February Plan does not include resources for retroactive wage increases, and includes funding for annual wage increases of 1.25 percent during the financial plan period, which is lower than the projected inflation rate. The City had estimated that the cost of providing retroactive wage increases to all employees (without offsetting savings) and wage increases at the local inflation rate would total $7.8 billion in FY 2014 and more than $3 billion annually thereafter (see Section VI, "Expenditure Trends," for further discussion of collective bargaining).

4 The February Plan includes a general reserve of $150 million in FY 2014 and $600 million in each of fiscal years 2015 through 2018. The City also has a reserve of $1 billion for disallowances of federal and State aid, which, if not needed for that purpose, could be used to help balance the budget. The Retirees Health Benefits Trust, which the City has used in the past as a rainy-day fund, has a balance of $1.4 billion.

5 The February Plan assumes that the 14 percent personal income tax surcharge (valued at more than $1 billion annually), which is scheduled to expire on December 31, 2014, will be extended as it has been every two to three years since it was enacted in 1991.

6 Over the past ten years, the City has realized average annual savings of $514 million from an overestimation of prior years' expenses. The February Plan does not anticipate such savings during the financial plan period.

7 The February Plan includes the Mayor's proposal to fund high-quality full-day universal prekindergarten and after-school programs for middle-school students by increasing the personal income tax rate by 0.0534 percent for households earning more than $500,000 per year (which requires State approval), making the proposal budget-neutral. While the Governor opposes the proposed tax increase, he has proposed investing more than $2.2 billion over five years to support a phase-in of universal full-day prekindergarten programs and an expansion of after-school programs throughout the State. The cost of these initiatives and the sources of funding will likely be known by the time the Mayor presents his executive budget in May 2014.

II. Economic Trends

The national economy has expanded without interruption for more than three years, although growth has been slow and there continue to be soft patches. Growth now appears to be strengthening and most economists predict the nation's economy will grow by about 3 percent in 2014, which is in line with long-term historical trends. Although there continue to be some mixed economic indicators, the national economic recovery remains on track.

The improvement in the national economy has led the Federal Reserve to begin scaling back, in measured steps, its bond-buying program, which has held down long-term interest rates in an effort to stimulate the economy. The Federal Reserve has indicated that it will keep short-term interest rates near zero until "well past" the unemployment rate target of 6.5 percent (the national unemployment rate declined to 6.6 percent in January 2014), as long as inflation remains low, because of concerns over broader conditions in the labor markets. For example, the share of unemployed people who have been out of work for more than six months makes up an unusually large portion (50 percent) of all unemployed people, and the number of people who are working part time but would prefer to work full time remains very high.

New York City's economy has resumed growing, but not all economic indicators have returned to their prerecession levels, and areas of concern still exist. Employment growth has been very strong, but much of the City's job growth has been concentrated in lower-paying industries, and the unemployment rate is relatively high. The median household income of City residents has declined in recent years (after adjusting for inflation), and rental housing has become less affordable. The broadest measure of the local economy, the Gross City Product, is only now returning to its prerecession level. The City expects economic growth to accelerate over the next three years, rising from 1.1 percent in 2013 to 2.8 percent in 2016.

Figure 3

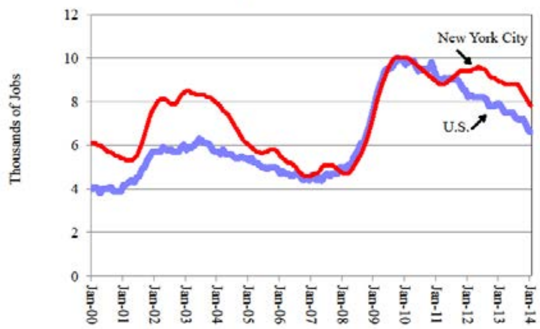
Annual New York City Employment

Sources: NYS Department of Labor; NYC Office of Management and Budget

Job growth has been very strong over the past three years (averaging 2.3 percent annually), outpacing job growth in the nation (1.5 percent) and in New York State (1.4 percent). Since 2009, the City has added 275,000 jobs (see Figure 3), two and a half times as many jobs as were lost during the recession, and employment has reached a new record of 4 million jobs. (Employment growth in the private sector averaged 2.8 percent over the past three years, rivaling the fastest three-year rate of growth in the past 50 years.) While the City expects job growth to remain strong, it assumes that growth will slow from an average of 86,000 jobs annually over the past three years to an average of nearly 55,000 jobs (1.3 percent).

However, a disproportionate share of the new jobs are concentrated in lower-paying employment sectors. For example, almost half of the jobs created since the recession have been in home health care, restaurants and bars, and retail trade. Each of these areas have average salaries ($26,010, $25,030, and $36,550, respectively) that are significantly lower than the average salary for all nonfinancial private sector employees in the City ($64,390). In addition, job growth in the securities industry in New York City has been much weaker during the current economic recovery (accounting for only 1 percent of the jobs created in the City's private sector) than it was during each of the prior two recoveries (when it exceeded 10 percent).

Figure 4
Unemployment Rates



Note: Data have been seasonally adjusted.
Sources: U.S. Bureau of Labor Statistics; NYS Department of Labor; OSC analysis

The citywide unemployment rate has fallen over the past three years from a recessionary peak of 10.1 percent in January 2010 to 7.8 percent in January 2014, the lowest level in five years. Nevertheless, the unemployment rate is higher than before the recession and higher than the national rate (see Figure 4). Some of the City's boroughs, neighborhoods and segments of the population are experiencing even higher rates of unemployment. For example, 19 percent of the working-age population lacks a high-school diploma, and the unemployment rate for residents without a high-school diploma was 17.2 percent.

Long-term unemployment is also a problem in New York City. About half of the unemployed people in the City have been without a job for more than six months, and the share has barely budged for three years, far longer than any time since 2000 (see Figure 5). After the prior recession, the percentage of the population that was unemployed for more than six months quickly returned to historical levels. The share of residents without a job for at least two years has also risen sharply.

Figure 5
Percent of Long-Term Unemployed in New York City

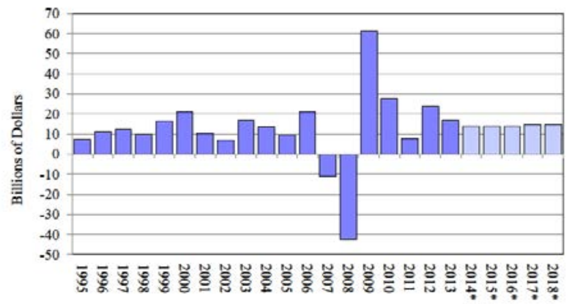
Source: U.S. Census Bureau

Low-wage jobs and high unemployment are taking a toll on household income. Median household income in the City has been stagnant in recent years (it declined by 7.1 percent between 2008 and 2012, after adjusting for inflation). In addition, a larger share of households in the City had incomes below the poverty level in 2012 (18 percent) than before the recession (13 percent).

Wall Street is an important component of the local economy and a major source of tax revenues. After posting two years of record losses in 2007 and 2008 (see Figure 6), Wall Street has been profitable for five consecutive years (including the three best years on record), aided by the Federal Reserve's low-interest-rate policies.

Figure 6

Wall Street Profits



Sources: NYSE Euronext; Securities Industry and Financial Markets Association; NYC Office of Management and Budget

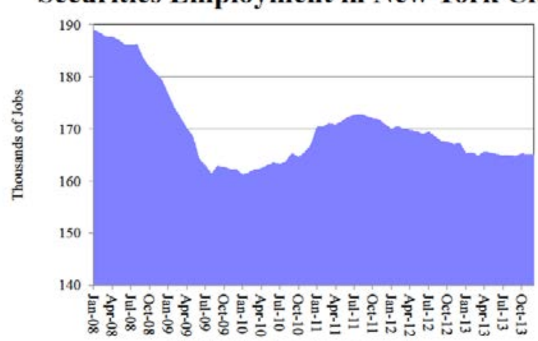
Although Wall Street had a good year in 2013, it was less profitable than in 2012. The broker/dealer profits of the member firms of the New York Stock Exchange (the traditional measure of industry profitability) declined from $23.9 billion in 2012 to $16.7 billion in 2013. The Office of the State Comptroller (OSC) believes that profitability could be constrained over the next few years by rising interest rates, continued litigation expenses and the implementation of new regulations. The City expects industry profits to total $14 billion in 2014.

In response to regulatory reforms intended to reduce excessive risk, Wall Street has changed its compensation practices to reward long-term performance (e.g., a larger share of bonuses is deferred to future years). The February Plan assumes that bonuses (cash bonuses supplemented by bonuses deferred from prior years) will decline by 5 percent in 2013.

OSC also estimates that employment in the securities industry totaled 165,200 jobs in New York City in December 2013 (see Figure 7), 12.6 percent lower than before the financial crisis. After strong job growth during the first part of the recovery, the securities industry resumed downsizing. Employment levels appear to be stabilizing, but ongoing pressures on profitability will likely hold down employment growth in the near term.

Figure 7

Securities Employment in New York City



Note: Data have been seasonally adjusted.
Sources: NYS Department of Labor; OSC analysis

The City's tourism industry remains strong. NYC & Company (the City's tourism agency) estimates that the total number of visitors to New York City increased, to 54.3 million in 2013, for a fourth-consecutive record year. Hotel occupancy rose to the highest level on record (nearly 89 percent), and the average daily room rate ($294) is slightly below its peak.

The City's real estate markets also continue to improve. Data from the City's Department of Finance indicate that the median home value for one-, two- and three-family homes, which declined by almost 20 percent during the recession, has since recovered about half its value. Values for condominium and cooperative apartments in Manhattan did not decline during the recession as much as other home values, and have returned to their prerecession levels.

While much of the activity in the residential markets is centered on high-end properties, the City has a shortage of affordable housing. OSC has reported that, even after the benefit of government subsidies, 44 percent of the City's rental households in 2011 were paying at least 30 percent of their incomes toward housing (which is considered to be the limit of affordability). Moreover, one-fifth of City households faced a severe rent burden, devoting at least half of their incomes to housing.

The City's commercial real estate market, perhaps the strongest in the nation, is also improving. In 2013, the average asking rent in Manhattan's primary office market rose and the vacancy rate declined. Since 2009, rents have risen by 11.3 percent. Neither measure has recovered from the recession. The upcoming completion of several towers at the World Trade Center will significantly increase the inventory of Manhattan office space, which is expected to lead to a temporary increase in the vacancy rate (to 13.3 percent by the end of 2014) and a slight drop in the average asking rent. As this new space is absorbed, vacancy rates are expected to fall and rents are expected to rise in 2015 and throughout the remainder of the financial plan period.

Improvements in the real estate market have helped the construction industry, but the industry has recovered only one-fourth of the 20,000 jobs it lost during the recession. Although building permits increased sharply in 2013 (partly due to Superstorm Sandy rebuilding in Queens and Staten Island), they remain far below prerecession levels.

Job growth in the City has been strong, and the local economy is expected to grow steadily during the financial plan period. While the securities industry is smaller than before the financial crisis, the rise of the technology sector is creating additional higher-paying jobs. Nonetheless, some segments of the local economy continue to suffer the effects of the recession, and there remain risks (e.g., the pace of interest rate increases) that could change the outlook. In addition, recent developments on the Crimean Peninsula have added a new element of uncertainty to the international economic outlook.

III. Changes Since the June 2013 Plan

Since the budget for FY 2014 was adopted in June 2013, the City has recognized more than $7 billion in unplanned resources through FY 2017, mostly from higher revenues ($4.7 billion), as well as from lower health insurance and debt service costs (see Figure 8). These resources increased the FY 2014 surplus by $1.6 billion to nearly $1.8 billion (which the City used to balance the FY 2015 budget), and also permitted the City to reduce the out-year budget gaps, rescind planned budget cuts, fund new initiatives and replenish reserves.

Tax collections are projected to be higher by $3.9 billion through FY 2017, largely because of higher real property values ($1.9 billion), personal income tax collections ($1.2 billion) and real estate transaction activity ($750 million). The City expects to receive an additional $546 million in one-time miscellaneous revenues, mostly from the sale of City-owned buildings ($232 million) and a refund of health insurance premiums ($103 million).

Health insurance and debt service costs will be lower by $2.3 billion through FY 2017. EmblemHealth, the City's principal insurer, did not seek a premium rate increase for FY 2015 after the former Mayor announced his intention to seek new carriers for the City's health insurance plans for municipal employees. The City projects significant debt service savings because interest rates have been lower than expected, resulting in savings from lower costs for new issuances, from variable rate debt and from refinancing outstanding debt.

The City used these unplanned resources to close a $2 billion budget gap projected for FY 2015, and to narrow gaps in later years (from $1.8 billion to $1.1 billion in FY 2016, and from $1.4 billion to $530 million in FY 2017). The City also doubled the general reserve to $600 million annually beginning in FY 2015, and rescinded the planned withdrawal of $1 billion from the Retiree Health Benefits Trust. The City created the trust to help fund the future cost of post-employment benefits other than pensions, but has instead used the trust as a rainy-day fund.

The City also rescinded most of the budget cuts planned for fiscal years 2015 through 2018; permanently funded many of the initiatives included in the FY 2014 budget at the request of the City Council; and funded a number of new initiatives. For example, the City rescinded $166 million in cuts to libraries and cultural institutions, and added more than $160 million annually to social services agencies to continue programs such as day care, after-school programs and services for seniors. The City also added $44 million annually to keep open 20 fire companies.

The February Plan reflects the Mayor's request that the State raise personal income taxes on the City's highest earners to fund full-day universal prekindergarten for all students and to expand after-school programs for middle-school children. The City estimates that these initiatives would cost about $530 million in FY 2015 and more in subsequent years. The proposal is budget-neutral because both the anticipated revenue and cost of the programs are included in the February Plan.

The February Plan also includes funding for a number of smaller mayoral initiatives, such as rent relief for people with HIV/AIDS; an inspector general to monitor Police Department policies and procedures (such as stop-and-frisk); additional shelter beds for runaway and homeless youths; public outreach to increase participation in income and food assistance programs; and a municipal identification card program.

Figure 8
Financial Plan Reconciliation–City Funds
February 2014 Plan vs. June 2013 Plan
(in millions)

	Better/(Worse)			
	FY 2014	**FY 2015**	**FY 2016**	**FY 2017**
Surplus/Gaps Per June 2013 Plan	**$ - - -**	**$ (1,965)**	**$ (1,769)**	**$ (1,382)**
Revenue Reestimates				
Real Estate Transaction Taxes	550	81	99	20
Personal Income Tax	494	106	246	332
Real Property Tax	213	454	556	667
Other Taxes	160	(47)	32	(76)
Tax Program (UPK & After-School Programs)[8]	- - -	530	533	569
All Other	547	30	80	(7)
Total	**1,964**	**1,154**	**1,546**	**1,505**
Drawdown of Reserves				
Rescind Withdrawal from Retiree Health	(1,000)	- - -	- - -	- - -
General Reserve	300	(300)	(300)	(300)
Total	**(700)**	**(300)**	**(300)**	**(300)**
Expenditure Reestimates				
Debt Service	502	234	104	95
Health Insurance	66	404	439	477
Judgments and Claims	55	55	55	55
Pension Contributions	(5)	(1)	80	230
Social Services	(35)	(162)	(180)	(180)
Uniformed Agencies	(111)	(171)	(156)	(115)
Libraries and Cultural Institutions	- - -	(166)	(166)	(166)
UPK & After-School Programs[8]	- - -	(530)	(533)	(569)
Other Expenditures	(108)	(180)	(179)	(180)
Total	**364**	**(517)**	**(536)**	**(353)**
Net Change During FY 2014	**1,628**	**337**	**710**	**852**
Surplus/(Gap)	**$ - - -**	**$ (1,628)**	**$ (1,059)**	**$ (530)**
Surplus Transfers[9]	(1,628)	1,628	- - -	- - -
Gaps Per February 2014 Plan	**$ - - -**	**$ - - -**	**$ (1,059)**	**$ (530)**

Sources: NYC Office of Management and Budget; OSC analysis

8 The February Plan includes a proposal to fund full-day universal prekindergarten (UPK) and after-school programs for middle-school students by increasing the personal income tax rate by 0.0534 percent for households earning more than $500,000 per year.

9 The June 2013 financial plan projected a surplus of $142 million for FY 2014, which brings the surplus projected for FY 2014 to nearly $1.8 billion.

IV. Projected Budget Gaps

The City projected large cumulative three-year budget gaps (averaging more than $13 billion) during the financial crisis and resulting recession. Since June 2011, the cumulative gap has declined quickly as the economic recovery has taken hold. The February Plan projects budget gaps of $1.1 billion in FY 2016, $530 million in FY 2017 and $370 million in FY 2018, amounting to a cumulative budget gap of $2 billion over three years.

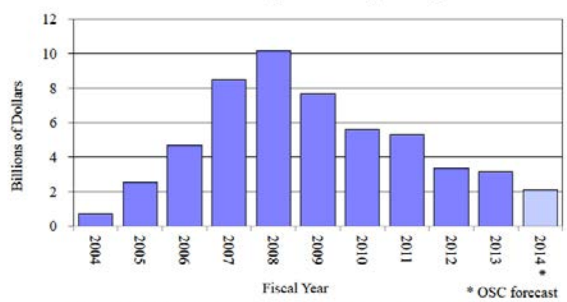
The dramatic improvement over the past two and a half years results from a number of developments, including continued improvement in the local economy, a drawdown of reserves, low interest rates that permitted the City to refinance outstanding debt at lower cost, expiring labor agreements and agency cost-reduction initiatives.

All of the labor agreements with the municipal workforce have expired, some as long ago as 2008. The unions representing the municipal workers are seeking retroactive wage increases, as well as annual wage increases during the financial plan period. While the cost and structure of future agreements are still unknown, they are likely to have a significant impact on the City's projected budget gaps.

The City has a long history of identifying and implementing agency cost-reduction initiatives. The resources these initiatives generate have contributed to budget surpluses, which have helped balance future budgets. Historically, the Mayor's preliminary budget has included an agency program to close the budget gap for the following year. The February Plan does not include an agency program because the City balanced the FY 2015 budget in November 2013. (This was the earliest point at which the City eliminated a budget gap for the next fiscal year since it adopted a four-year financial planning process after the fiscal crisis of the 1970s.) To help close future budget gaps, the City should resume the process for identifying cost efficiencies as soon as is practicable to help close future budget gaps.

Figure 9

Cumulative Operating Surplus



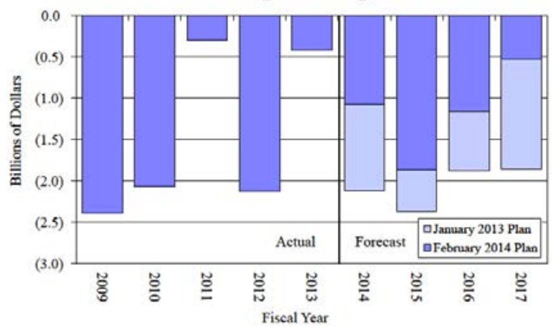
Notes: Adjusted for surplus transfers, TFA, TSASC, and discretionary actions. Estimates include the balance of Retiree Health Benefits Trust reserves for each fiscal year ended June 30.

Sources: NYC Office of Management and Budget; NYC OPEB Plan; OSC analysis

Since FY 1981 the City has balanced its budget each year in accordance with generally accepted accounting principles as required by law,[10] but in most years it has relied heavily on surplus resources generated in prior years. During the last economic expansion, the City accumulated large surplus resources as revenue growth outpaced spending. The cumulative operating surplus peaked in FY 2008 at $10.2 billion. As shown in Figure 9, the City began to draw on these resources beginning in FY 2009 to help navigate the Great Recession while maintaining municipal services.

Figure 10 shows the sizable deficits that would have resulted during the recent recession without the benefit of surplus resources from prior years (i.e., the current-year deficit). In addition to prior-year resources, the City has relied on other nonrecurring resources, such as savings from debt refinancings, to balance the operating budget. While Figure 10 shows that the current-year deficits projected for fiscal years 2014 through 2017 are considerably smaller than projected one year ago, the gaps are understated because they do not yet reflect the impact of unfinished labor negotiations.[11]

Figure 10
Annual Operating Deficit



Note: Adjusted for surplus transfers, TFA, TSASC, and discretionary actions.
Sources: NYC Office of Management and Budget; OSC analysis

10 Since FY 2009 the City's budget has been balanced in accordance with generally accepted accounting principles except for the application of GASB 49, which effectively prohibits the City from using bond proceeds to fund certain pollution remediation costs. The Financial Control Board approved a two-year waiver in 2008 and State law was amended in 2010 to permit the continued use of bond proceeds.

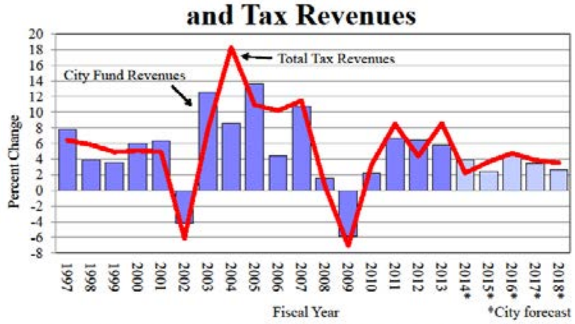
11 The City estimated that the cost of providing retroactive wage increases to all employees (without offsetting savings), as well as wage increases at the local inflation rate, would total $7.8 billion in FY 2014 and more than $3 billion annually thereafter.

V. Revenue Trends

Since June 2013, the City has raised its tax revenue forecast by $5.1 billion for fiscal years 2014 through 2018 because economic growth has been better than the City anticipated. More than half of the new revenue comes from the real property tax ($2.8 billion), reflecting growth in property values that is much stronger than expected. The remainder comes from higher personal income tax collections, generated by strong job growth and capital gains on stock transactions; a sharp rise in real estate transactions; and sales tax collections that benefited from the record number of tourists who visited the City.

Nevertheless, the City expects tax collections to grow by only 2.2 percent in FY 2014 (see Figure 11) because higher federal income tax rates that became effective in January 2013 caused some taxpayers to shift income into FY 2013 to avoid higher taxes. Tax collections are expected to strengthen in FY 2015 (3.7 percent), and the February Plan assumes that tax collections will rise by an average of 4 percent annually during fiscal years 2016 through 2018.

Figure 11
Annual Changes in City Fund Revenues and Tax Revenues



Note: Excludes the forecast for revenues associated with the City's proposed tax program. Adjusted for debt service on TFA and Tobacco Bonds, and the transfer of TSASC revenues.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

City Fund revenues, which include both tax collections and miscellaneous revenues, are expected to rise by only 2.4 percent in FY 2015 (to $53.6 billion) because $850 million in nonrecurring revenues in FY 2014 were not replaced in FY 2015. City fund revenues are projected to rise at an average annual rate of 3.5 percent in fiscal years 2016 through 2018, driven by stronger tax collections.

The February Plan includes a proposed tax program to fund universal full-day prekindergarten and additional after-school programs for middle-school children. The tax program, which requires State approval, would increase the top personal income tax rate for City residents with taxable annual incomes of more than $500,000 from 3.876 percent to 4.41 percent, yielding $530 million in FY 2015 and slightly higher amounts in subsequent years. If the program is approved, these resources would boost City fund revenue growth in FY 2015 to 3.4 percent. Revenue growth in subsequent years would continue to average 3.5 percent annually.

Our analysis suggests that revenues could be higher than the City's forecast based on our higher estimates for personal income and sales tax collections during the plan period, and transaction tax collections in FY 2015.

Details of the City's revenue forecasts are shown in Figure 12 and discussed below.

Figure 12
City Fund Revenues
(in millions)

	FY 2014	FY 2015	Annual Growth	FY 2016	FY 2017	FY 2018	Average Three-Year Growth Rate
Taxes							
Real Property Tax	$ 19,781	$ 20,782	5.1%	$ 21,815	$ 22,703	$ 23,579	4.3%
Personal Income Tax	8,663	9,151	5.6%	9,643	10,055	10,368	4.2%
Sales Tax	6,424	6,630	3.2%	6,915	7,170	7,422	3.8%
Business Taxes	5,782	5,913	2.3%	6,108	6,305	6,536	3.4%
Real Estate Transaction Taxes	2,383	2,175	-8.7%	2,392	2,535	2,671	7.1%
Other Taxes	2,988	3,081	3.1%	3,153	3,214	3,281	2.1%
Audits	710	709	-0.1%	709	709	709	0.0%
Subtotal	**46,731**	**48,441**	**3.7%**	**50,735**	**52,691**	**54,566**	**4.0%**
Miscellaneous Revenues	5,612	5,160	-8.1%	5,213	5,225	4,878	-1.9%
Grant Disallowances	(15)	(15)	NA	(15)	(15)	(15)	NA
City Funds Before Tax Program	**$ 52,328**	**$ 53,586**	**2.4%**	**$ 55,933**	**$ 57,901**	**$ 59,429**	**3.5%**
Proposed Tax Program	- - -	530	NA	533	569	594	3.9%
City Funds After Tax Program	**$ 52,328**	**$ 54,116**	**3.4%**	**$ 56,466**	**$ 58,470**	**$ 60,023**	**3.5%**

Note: Miscellaneous revenues include debt service on tobacco bonds.
Sources: NYC Office of Management and Budget; OSC analysis

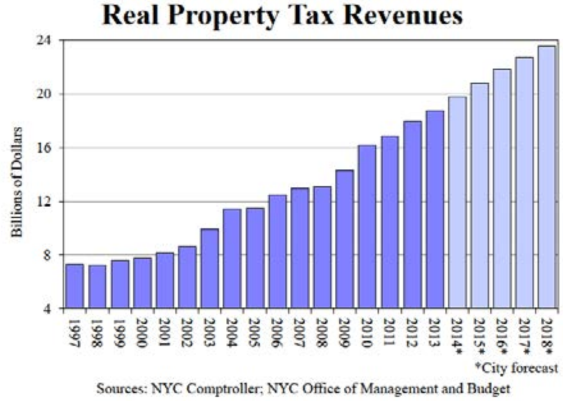
1. Real Property Tax

Real property tax collections have been growing steadily in recent years and are projected to reach $23.6 billion by FY 2018, $4.8 billion more than collected last year (see Figure 13). The City's forecast is $2.8 billion higher during the financial plan period than projected in June 2013.

The tentative roll for FY 2015 shows that the recovery in the City's real estate markets remains strong. On a preliminary basis, market values for all property in the City grew by 6.6 percent, and growth for commercial properties exceeded 10 percent.

The total value of one-, two- and three-family homes increased by almost 5 percent, while the value of larger residential properties increased by more than 7 percent.[12]

Figure 13
Real Property Tax Revenues



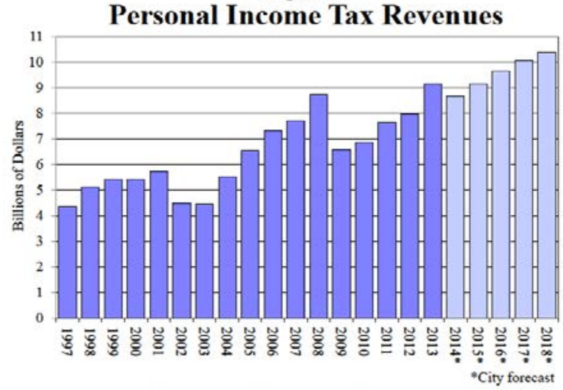
12 Revenue growth was lower than the increase in market values because market values do not reflect the impact of exemptions, credits, phase-in requirements, tax challenges and other adjustments.

The City expects rising interest rates to slow down growth in property values during fiscal years 2016 through 2018, but revenue growth will be supported by the continued phase-in of property value increases from prior years.[13] If commercial and large residential property values continue to grow at recent rates, then the City could realize significantly more tax revenue during the financial plan period.

2. Personal Income Tax

Personal income tax collections grew at a relatively fast pace (15.3 percent) in FY 2013 because of a change in taxpayer behavior, as income was accelerated into the end of 2012 to avoid higher federal tax rates that took effect January 1, 2013. Although the February Plan assumes that collections will decline in FY 2014 because of the income acceleration (see Figure 14), the reduction has been partially offset by strong year-to-date gains in payments on nonwage income (mostly capital gains) as the financial markets reached record highs in 2013. In addition, the City received payments from the State to correct a distributional shortfall in personal income tax revenue last year.[14]

Figure 14
Personal Income Tax Revenues



Sources: NYC Comptroller, NYC Office of Management and Budget

The February Plan assumes that personal income tax revenues will rise by 5.6 percent in FY 2015 to reach $9.2 billion (excluding the impact of the proposed tax program). The February Plan anticipates continued strong growth in employment during the financial plan period, though lower-paying jobs (such as those in retail trade and tourism) continue to account for a significant portion of the new jobs created. As a result, wage gains are expected to remain modest (at about 4 percent annually), leading to personal income tax revenue growth that averages 4.2 percent annually in fiscal years 2016 through 2018.

OSC's review finds that the strength in year-to-date collections will likely boost withholding and year-end payments for 2013 that are due on April 15, 2014, so that personal income tax collections could be higher than the City's forecast by $250 million in FY 2014. Collections could also be slightly higher in subsequent years.

---

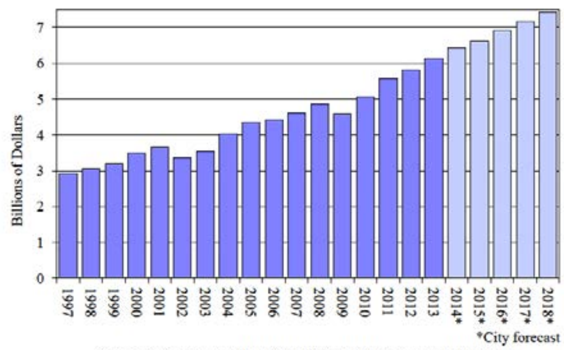
13 State law requires that changes in property values for large residential and commercial properties be phased in over five years. For one-, two- and three-family homes, increases are limited to 5 percent per year and 20 percent over a five-year period. OSC estimates that the value of commercial and large residential properties waiting to be phased in currently exceeds $20 billion, the highest level ever.

14 The State collects personal income tax revenue for the City.

3. Sales Tax

Sales tax collections are expected to grow by 4.8 percent in FY 2014, but year-to-date collections have been much stronger (rising by 6.4 percent) as tourism spending has been robust and the holiday sales season brought modest gains. The February Plan assumes that collections will increase by 3.2 percent in FY 2015 to reach $6.6 billion (see Figure 15), a slower rate of growth than forecast for FY 2014. Collections are expected to continue growing at an average annual rate of 3.8 percent during fiscal years 2016 through 2018 on the assumptions that tourism will remain strong and wage growth will average 4 percent annually during the financial plan period. OSC forecasts that sales tax collections are likely to be higher by $50 million in FY 2014 based on the strength of year-to-date collections. Collections could also be slightly higher in subsequent years.

Figure 15
Sales Tax Revenues



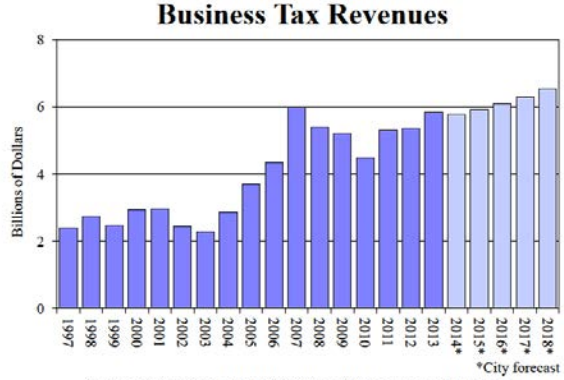
Sources: NYC Comptroller; NYC Office of Management and Budget

4. Business Taxes

New York City collects about $6 billion annually from three types of business taxes, which cover general corporations, banking corporations and unincorporated businesses (i.e., partnerships and sole proprietorships). Overall, financial firms account for about half of all business tax collections (and securities industry firms account for slightly less than half of the financial share), while one-fifth of business tax collections comes from firms that provide business and professional services (e.g., accounting or law firms), and nearly one-tenth comes from firms in the transportation and trade sector.

The February Plan assumes that business tax collections will decline by 1.3 percent in FY 2014, the first reduction in collections since FY 2010 (see Figure 16). The decline largely reflects lower collections from financial firms as a result of lower profits for Wall Street firms in 2013, the impact of legal settlements related to the financial crisis, and reductions in mortgage refinance activity at commercial banks caused by increases in interest rates. The City expects growth to resume (2.3 percent) in FY 2015 and to continue during the financial plan period (at an average annual rate of 3.4 percent).

Figure 16
Business Tax Revenues



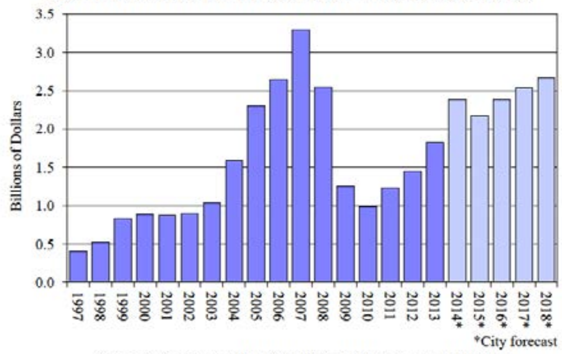
Sources: NYC Comptroller; NYC Office of Management and Budget

5. Real Estate Transaction Taxes

The City imposes two taxes on real estate transactions: the mortgage recording tax and the real property transfer tax. In recent years, there has been an increase in transaction activity as the real estate markets have improved.

Figure 17

Real Estate Transaction Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

In FY 2014, the City expects greater sales volumes and higher prices for real estate transactions to raise transaction tax revenues by 30.4 percent, which would be the fastest rate of growth since FY 2005. Collections are forecast to reach nearly $2.4 billion, significantly higher than forecasts in June 2013 but still well below levels before the recession (see Figure 17). Activity has been particularly strong for large commercial properties and high-end Manhattan residential properties, reflecting an influx of foreign investors and investors looking to complete transactions while interest rates remain low.

The February Plan assumes that transaction activity will fall off dramatically in late 2014 and early 2015 because of higher interest rates and the completion of large commercial projects. As a result, the City expects real estate transaction tax revenue to decline by 8.7 percent in FY 2015. Although mortgage rates rose during the summer of 2013, they have since stabilized at a slightly higher level. The IHS Global Insight forecast in February 2014 projects that interest rates will rise at a slightly slower rate than the City expects. As a result, OSC expects that the decline in transaction activity could be less dramatic, yielding $175 million more in transaction tax revenues in FY 2015 than anticipated in the February Plan.

6. Miscellaneous Revenues

Miscellaneous revenues (from sources such as charges for services, licenses, permits, fines, fees and investment income) are expected to total $5.6 billion in FY 2014, almost $900 million more than in FY 2013. Virtually all of this growth will come from nonrecurring resources, including proceeds from the sale of taxi medallions ($364 million), asset sales ($243 million) and a refund in health insurance premiums ($104 million). Since the February Plan assumes that most of these resources will not recur in FY 2015,[15] the City assumes that miscellaneous revenues will decline by 8.1 percent that year. In subsequent years of the financial plan period, collections are forecast to decline by 1.9 percent annually (excluding nonrecurring items).

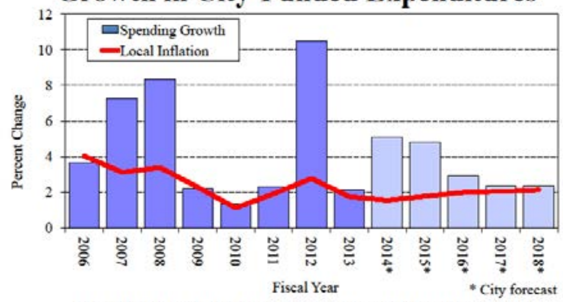
[15] Only the sale of the taxi medallions is expected to generate revenues in fiscal years 2015 through 2017.

VI. Expenditure Trends

City-funded expenditures are projected to grow by nearly 4.8 percent ($2.6 billion) to reach $56 billion in FY 2015 (see Figure 18), driven in large measure by higher costs for debt service, salaries and wages, and health insurance.[16] Together, debt service and health insurance are projected to grow by $4.6 billion (47 percent) between fiscal years 2013 through 2018, consuming 24 percent of City fund revenue by FY 2018. The February Plan also assumes that the State will approve the Mayor's proposal to increase the personal income tax on the City's highest earners to fund universal full-day prekindergarten and additional after-school program for middle-school children. The City estimates that these initiatives would cost $530 million in FY 2015 and slightly higher amounts in subsequent years.

Figure 18

Growth in City-Funded Expenditures



Note: Adjusted for surplus transfers, TFA, TSASC, and discretionary actions. City-funded expenditures grew by 10.5 percent in FY 2012 because the City replaced expiring federal stimulus aid ($1.8 billion) and a cut in State education aid ($812 million) with City funds.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

The contracts with all of the City's 152 labor unions expired years ago, and the City has begun discussing new contracts with the municipal unions. The February Plan makes no provision for retroactive wage increases and includes resources in fiscal years 2014 through 2018 to fund annual wage increases of 1.25 percent.

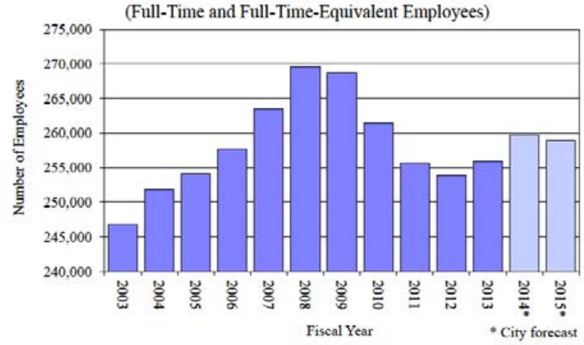
Although City-funded spending is projected to exceed City fund revenues by nearly $1.2 billion in FY 2014 and by $1.9 billion in FY 2015, the budget will be balanced with surplus resources from prior years. By our estimate, the FY 2014 budget includes a total of $2.5 billion in nonrecurring resources, and the FY 2015 budget includes $2.6 billion in nonrecurring resources (for more information, see Appendix A).

The City-funded workforce grew between fiscal years 2003 and 2008 (see Figure 19) as the economy expanded, but contracted by 15,666 employees over the next four years as budget cuts were imposed to help weather the Great

Figure 19

City-Funded Staffing Levels

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



Note: Staffing levels are as of June 30 of each fiscal year.
Sources: NYC Office of Management and Budget; OSC analysis

16 City-funded expenditure estimates are adjusted for surplus transfers and debt defeasances, and include debt service on bonds issued by TSASC.

Recession. Staffing levels rose by 2,003 employees last year, and while the City plans to add 3,859 employees during FY 2014 (see Appendix B), staffing levels would remain below the prerecession peak.

The February Plan is based on the trends shown in Figure 20 and discussed below.

Figure 20
Estimated City-Funded Expenditures
(Adjusted for Surplus Transfers and TSASC)
(in millions)

	FY 2014	FY 2015	Annual Growth	FY 2016	FY 2017	FY 2018	Average Three-Year Growth Rate
Salaries and Wages	$ 13,455	$ 13,936	3.6%	$ 14,149	$ 14,252	$ 14,267	0.8%
Pension Contributions	8,165	8,173	0.1%	8,292	8,396	8,573	1.6%
Medicaid	6,272	6,353	1.3%	6,322	6,322	6,322	-0.2%
Debt Service	5,593	6,610	18.2%	7,176	7,407	7,622	4.9%
Health Insurance	4,805	5,153	7.2%	5,711	6,330	6,966	10.6%
Other Fringe Benefits	2,977	3,094	3.9%	3,199	3,300	3,439	3.6%
Energy	932	950	1.9%	937	947	974	0.8%
Judgments and Claims	663	674	1.7%	710	746	782	5.1%
Public Assistance	558	571	2.3%	571	575	575	0.2%
General Reserve	150	600	NA	600	600	600	NA
Other	9,833	9,871	0.4%	9,961	10,126	10,282	1.4%
Total	**$ 53,403**	**$ 55,985**	**4.8%**	**$ 57,628**	**$ 59,001**	**$ 60,402**	**2.6%**

Sources: NYC Office of Management and Budget; OSC analysis

1. Collective Bargaining

All of the labor agreements between the City and the municipal unions have expired. Some of the agreements expired as long ago as 2008; the labor agreement with the United Federation of Teachers, which represents the City's teachers and paraprofessionals (37 percent of the City workforce), expired in November 2009; and the agreements with most other unions expired in 2010. Although the City had set aside resources to fund two annual wage increases of 4 percent in calendar years 2009 and 2010 for teachers and principals (similar to increases negotiated with the City's other unions), the City later redirected those resources to offset a sharp reduction in State education aid.

The new administration has indicated that settling these contracts will be a priority, and that it will seek cost savings and other efficiencies from the unions to help fund the cost of new labor agreements. The February Plan does not include any resources to fund retroactive wage increases, but includes a reserve to fund annual wage increases of 1.25 percent during the financial plan period, which is lower than the projected inflation rate. The City had estimated that the cost of providing retroactive wage increases to all employees (without offsetting savings), as well as wage increases at the local inflation rate, would total $7.8 billion in FY 2014 (including $3.2 billion for City teachers) and more than $3 billion annually thereafter.

In February 2014, the City reached a labor agreement with the union that represents environmental police officers at the Department of Environmental Protection. The agreement is based on a January 2012 binding arbitration award that provided retroactive wage increases of 5 percent for 2005 and 4 percent for each of 2006 and 2007. The wage increases are equivalent to those provided to City police officers. The cost of the agreement was funded by the New York City Water Board through higher water and sewer fees implemented in prior years, and not from the City's budget.

In early 2010, the State Public Employment Relations Board (PERB) found that negotiations between the City and the United Federation of Teachers had reached an impasse. The PERB appointed a mediator to facilitate negotiations, but mediation was unsuccessful. In the fall of 2012, the PERB established a fact-finding panel to determine the underlying causes of the impasse. Hearings commenced in May 2013, and were expected to conclude in December 2013, but have been extended to allow the new mayoral administration to present its position on the issues. Although the findings of the fact-finding panel are nonbinding, they could serve as a framework for a new labor agreement.[17]

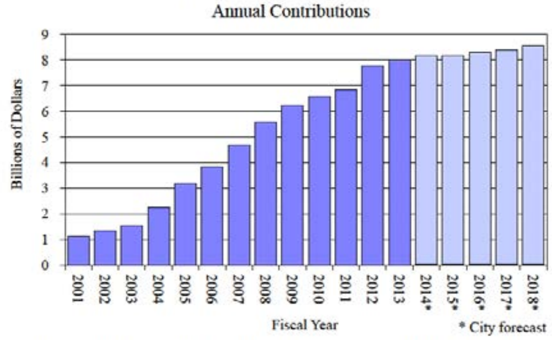
2. Pension Contributions

After rising rapidly over the past decade, the growth in pension contributions has begun to slow, and is projected to rise gradually during the financial plan period from $8.2 billion in FY 2014 to $8.6 billion in FY 2018 (see Figure 21). The City's estimates, however, do not reflect the potential impact of wage increases from new labor agreements that are currently under discussion with the unions that represent the municipal workforce, which could significantly increase the City's forecasts for pension contributions.

Figure 21

New York City Pension Systems

Annual Contributions



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

[17] In 2013, the New York City Office of Collective Bargaining commenced binding arbitration proceedings for the unions representing medical professionals at the Health and Hospitals Corporation. The proceedings have not yet concluded and their completion date has not been made public. In 1998, the State transferred the responsibility for handling police officer and firefighter contract disputes from the Office of Collective Bargaining to the PERB, and any arbitration award made by the PERB for police officers and firefighters is binding on both parties. The unions representing police officers and firefighters have not filed for binding arbitration.

The City's projections do reflect recent changes in the assumptions and methodologies used to calculate City pension contributions, which were recommended by the City Actuary and approved by the boards of trustees of the City's five pension systems in 2012, and (where necessary) enacted into law by the State in January 2013.

The changes include a reduction in the investment earnings assumption from 8 percent to 7 percent; a different methodology to determine the projected cost of future pension benefits; a market value restart;[18] and a longer amortization period, which will help free up resources during the financial plan period but also will result in higher costs over the longer term. The City has engaged the services of an independent actuarial consultant, as required under the City Charter, to conduct a biennial audit of the pension systems. The audits, which are expected to be released during FY 2014, may recommend additional changes to the actuarial assumptions and methodologies that are used to calculate City pension contributions, which could increase (or decrease) planned City pension contributions.

The City's projections also reflect the impact of better-than-expected investment gains during FY 2013. The City's pension systems earned 12.1 percent on their investments during FY 2013 (compared to an expected annual return of 7 percent). As of February 21, 2014, the City's pension systems have earned an estimated 10 percent on their investments.

As of June 30, 2011 (the most recent date of pension valuation data reported by the City Actuary), the City's five pension systems had sufficient assets to fund, on average, 61 percent of their accrued liabilities. The New York City Employees' Retirement System, for example, had assets to cover 65 percent of its liabilities, while the New York City Fire Pension Fund had assets to fund 50 percent of its liabilities.

3. Health Insurance

For the first time since FY 1998, health insurance premiums for active employees will be held flat in FY 2015 because the City's primary insurer, EmblemHealth, did not seek a premium rate increase for FY 2015 (after the former Mayor announced his intention to seek new carriers for the City's health insurance plans for municipal employees).[19] Despite the rate freeze for active employees, health insurance costs will grow by 7.2 percent in FY 2015 (see Figure 22) because costs for retired employees

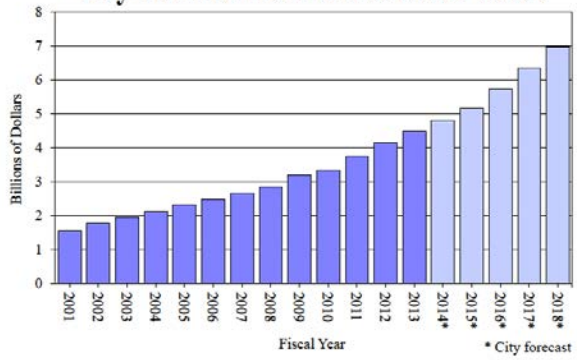
[18] Under a market value restart, the actuarial value of assets is reset to the market value rather than phasing in gains and losses over a six-year period.

[19] EmblemHealth is composed of HIP Health Plan of New York plus Group Health Incorporated, and insures about 95 percent of City employees and their dependents.

are expected to rise, reflecting a growing population of retirees as well as higher health insurance premiums.[20]

The February Plan assumes that health insurance premiums for active employees will resume growing in FY 2016 (by 9 percent annually), and that City-funded health insurance costs will grow from $5.2 billion in FY 2015 to $7 billion in FY 2018, an average of 10.6 percent annually.

Figure 22
City-Funded Health Insurance Costs



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

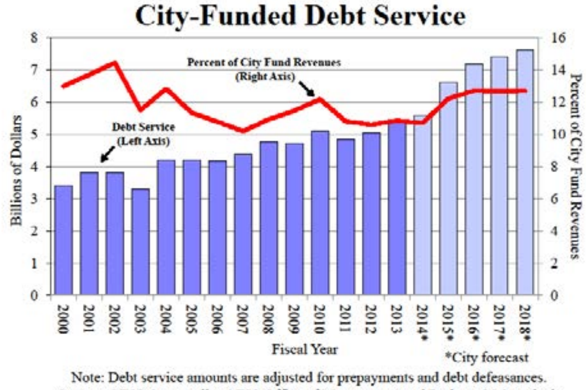
As part of its collective bargaining proposals, the City has suggested that employees share in the cost of their health insurance; such agreements have been successfully negotiated in the past. Some past agreements have increased employee copayments and limited benefits, but significant resources have come from freeing up unneeded funds held in the Health Stabilization Fund (HSF). The HSF was established in 1986 pursuant to collective bargaining. Under the agreement the City pays $35 million annually into the HSF, and contributes additional amounts for each fiscal year in which the rate approved for the HIP exceeds the rates for GHI and Blue Cross Blue Shield. As of February 2013, the HSF held assets totaling $1.1 billion.

4. Debt Service

In recent years, the City has taken advantage of historically low interest rates to refinance outstanding debt. Since FY 2008, the City has refinanced more than $20 billion in debt (about 30 percent of all bonds outstanding) for cumulative savings of $1.5 billion through FY 2014, including more than $500 million in FY 2014 alone. In addition to generating budgetary savings, the City's refinancings have followed prudent debt management practices.

The February Plan assumes that City-funded debt service (adjusted for surplus transfers) will grow from $5.6 billion in FY 2014 to $7.6 billion by FY 2018 (see Figure 23), an increase of 36 percent in four years. The debt service burden (i.e., debt service as a percent of City fund

Figure 23
City-Funded Debt Service



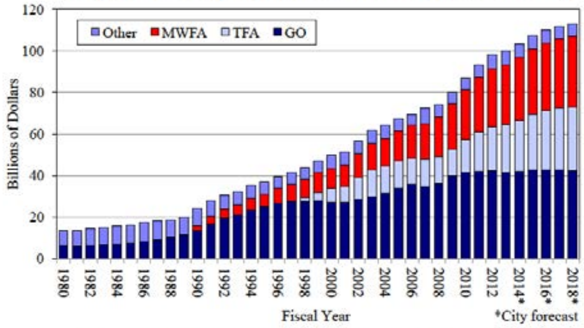
Note: Debt service amounts are adjusted for prepayments and debt defeasances.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

[20] The City expects premiums for Medicare-eligible retirees to rise by 8 percent annually starting in FY 2015.

revenues) is projected to rise from 10.7 percent in FY 2014 to 12.7 percent by FY 2016. The burden would remain at that level through FY 2018, as revenues and debt service are projected to grow at similar rates during those years.

However, the City's debt service estimates are based on conservative interest rate assumptions. Although long-term interest rates have risen from historic lows during 2012, rates remain below the City's forecast. The City realized savings of more than $200 million in FY 2014 from lower interest costs on variable rate debt, and could realize similar savings in FY 2015 if rates stay low.

Figure 24
City and City-Related Debt Outstanding



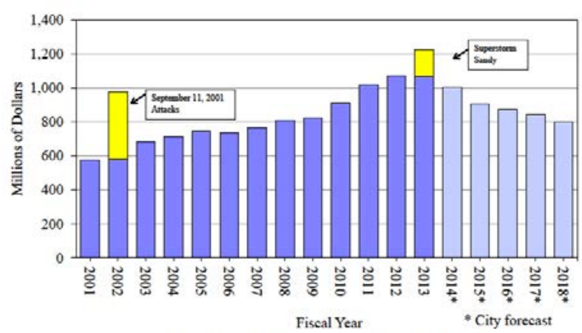
Note: TFA excludes Building Aid Revenue Bonds; "Other" includes lease and guaranteed debt, and HYIC, TSASC, FSC, JSDC and MAC debt.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

The outstanding debt of the City and City-related entities has risen steadily over the past three decades to fund the City's capital program.[21] Debt outstanding reached $100 billion at the end of FY 2013, an increase of 56 percent over the past decade (see Figure 24). The amount of debt outstanding at the end of FY 2013 was about $12,000 per capita, or $4,000 more than ten years earlier.

5. Uniformed Agencies

Overtime costs in the uniformed agencies (i.e., the Police, Fire, Correction and Sanitation departments) grew by 30 percent between fiscal years 2009 and 2012 (see Figure 25), largely as a result of staff shortages in the Fire and Correction departments. Excluding overtime costs associated with Superstorm Sandy, overtime declined slightly in FY 2013 because certain public events, such as the New York City Marathon, were cancelled as a result of the storm.

Figure 25
Overtime Spending in Uniformed Agencies



Sources: NYC Office of Management and Budget; OSC analysis

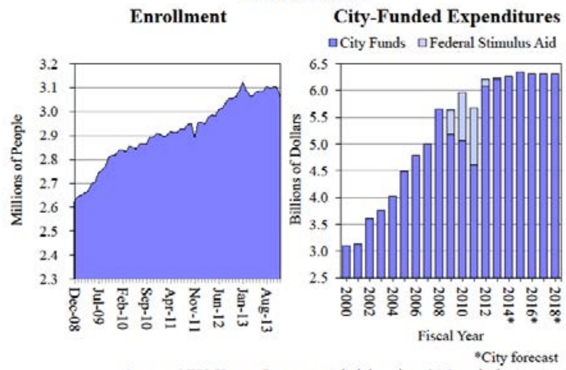
[21] City and City-related debt includes general obligation (GO) debt, Municipal Water Finance Authority (MWFA) debt, TFA-PIT debt, lease and guaranteed debt, and debt of the Hudson Yards Infrastructure Corporation (HYIC), TSASC, the Fiscal Year 2005 Securitization Corporation (FSC), the Jay Street Development Corporation (JSDC) and the Municipal Assistance Corporation (MAC).

The February Plan assumes that overtime will decline by $62 million in FY 2014 and by another $98 million in FY 2015 as a result of increased staffing levels at the Department of Correction and the Fire Department; and overtime reduction initiatives at the Police Department. The Fire Department had been prevented from hiring for three years (until January 2013) because a federal court found that the department's hiring practices were biased against certain minorities. In January 2014, the Fire Department hired its third new class of firefighters since the ban was lifted; also, the Department of Correction placed 342 new officers on active posts. Nevertheless, overtime costs are running above the levels predicted by the City, and this could result in unplanned costs of $50 million in FY 2014 and $100 million annually thereafter.

6. Medicaid

Since December 2008, enrollment in the Medicaid program rose by 16 percent to reach almost 3.1 million people as of December 2013 (see Figure 26), amounting to about one of every three New York City residents. Enrollment over the past year has increased, but at a slower rate than five years ago as the economy has slowly improved and unemployment has gradually declined. Enrollment growth is largely attributed to the recent recession, and will continue under the Affordable Care Act, which expanded Medicaid eligibility.

Figure 26
Medicaid



Sources: NYC Human Resources Administration; OSC analysis

Despite the expected growth in enrollment, the City-funded cost of Medicaid will remain relatively flat because of actions taken by the State to provide financial relief to localities. The February Plan assumes that the cost of this program will grow slowly and then level off at $6.3 billion in FY 2016 as the State completes a three-year takeover in the growth in the local share of Medicaid.

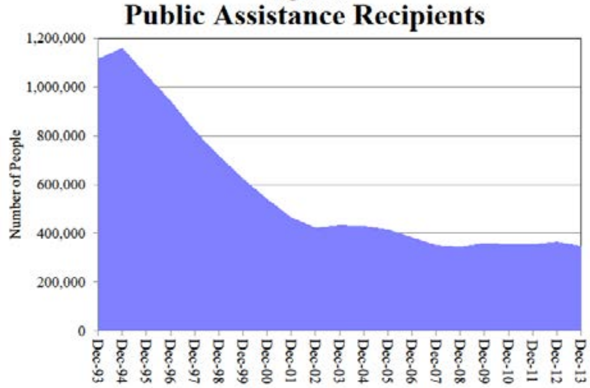
7. Public Assistance

The public assistance caseload grew by only 6 percent between December 2008 and December 2012, despite the recent recession, and then declined by almost 5 percent over the past year to total 346,398 recipients in December 2013 (see Figure 27).[22] The February Plan assumes that City-funded expenditures for public assistance will total $571 million in FY 2015, including $17 million for a new intitiative to provide rent relief to public assistance recipients living with HIV/AIDS. The City expects that the caseload will increase to 350,297 by June 2014, with no further growth expected through 2018.

[22] The December 2013 caseload was almost 815,000 lower than the peak in March 1995, largely as a result of federal welfare reform measures implemented in the late 1990s that enforced work requirements.

In 2012 (the most recent year for which data are available), 21 percent of the City's population lived below the federal poverty line, and about one in every five City residents received public assistance and/or Supplemental Nutrition Assistance Program (SNAP) benefits. In response to the economic downturn, the American Recovery and Reinvestment Act of 2009 temporarily increased SNAP benefits (i.e., food stamps) for all households, but this increase expired on November 1, 2013. Furthermore, on February 7, 2014, Congress passed and the President signed a farm bill that will cut $8.7 billion in food stamp benefits over the next ten years. The Governor has reallocated federal funds in a way that would mitigate the impact in New York State.

Figure 27
Public Assistance Recipients



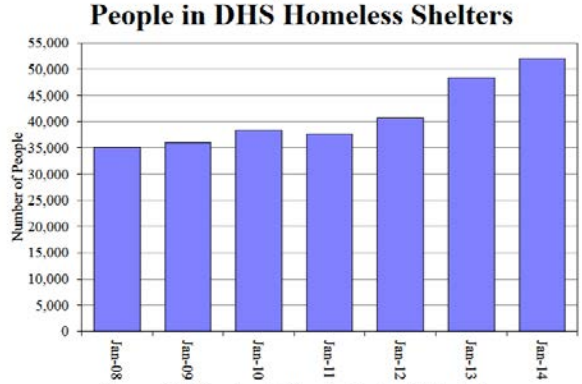
Sources: NYC Human Resources Administration; OSC analysis

8. Homeless Services

The February Plan estimates that the City-funded cost of providing services to the City's homeless people in facilities managed by the Department of Homeless Services (DHS) will average $410 million annually through FY 2018.[23] The population of homeless people in DHS shelters reached record-high levels in January 2014, at 51,909 people (see Figure 28), or 28 percent higher than two years earlier. In January 2014, the City established a new policy that guarantees shelter to homeless families (regardless of their eligibility) on the coldest nights of the year.

The growth in the homeless population results in part from the City's termination of a rental subsidy program for homeless families and individuals after the State withdrew its support. The new mayoral adminstration has discussed the possibility of an alternative rent subsidy program with the State.

Figure 28
People in DHS Homeless Shelters



Sources: NYC Department of Homeless Services; OSC analysis

[23] The DHS also provides funding for short-term housing and overnight shelters, which are operated by community-based and faith-based organizations, for about 1,500 single adults in special needs populations.

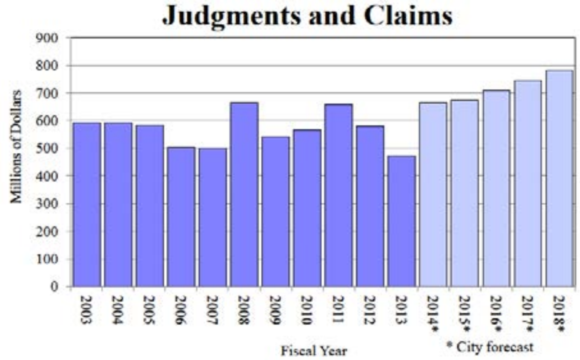
The New York City Human Resources Administration shelters more than 2,500 people in facilities for victims of domestic violence, and another 2,000 people in facilities for homeless people with HIV/AIDS. The City's Department of Housing Preservation and Development provides emergency housing to about 2,000 people who have become homeless as a result of extraordinary circumstances, such as fires. The February Plan adds funding for an additional 76 shelter beds (for a total of 326 shelter beds) operated by community-based and faith-based organizations for runaway and homeless youths aged 16 to 21.

According to a 2013 federal assessment, among the 50 largest cities in the United States, New York City had the largest homeless population (both sheltered and unsheltered) in 2013, which increased by 13 percent from 2012. This was the second-highest rate of increase in a major city behind Los Angeles, which showed a 27 percent increase in its homeless population.

9. Judgments and Claims

The cost of judgments and claims against the City totaled $474 million in FY 2013, $185 million less than the recent high of $659 million in FY 2011 (see Figure 29). The City attributes the decline to lower settlement costs for medical malpractice, injuries incurred in the City's schools, and civil rights violations.

Figure 29



Sources: NYC Comptroller, NYC Office of Management and Budget; OSC analysis

The February Plan, however, assumes that such costs will grow by 40 percent in FY 2014 ($189 million) and then increase slowly in subsequent years.[24] Although the costs have not risen during the first half of the fiscal year, there could be a number of high-cost settlements during the second half of the fiscal year.

[24] The City's Comprehensive Annual Financial Report shows that the cost of judgments and claims attributable to FY 2013 totaled $524 million, but savings from an overestimation of the amounts paid in prior years reduced the net cost to $474 million in FY 2013. The February Plan anticipates that the cost of judgments and claims that is attributable to FY 2014 will total $663 million, 27 percent more than the amount attributable to FY 2013.

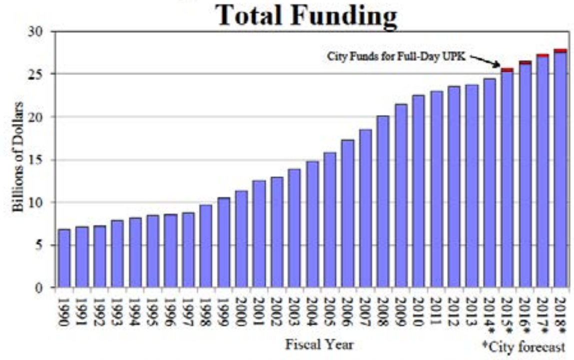
VII. Semi-Autonomous Entities

As discussed below, a number of public authorities have a financial relationship with the City.

1. Department of Education

The February Plan allocates $25.3 billion to the Department of Education in FY 2015, which is $860 million (4 percent) more than budgeted in FY 2014 (see Figure 30). The increase largely reflects higher costs for special education, debt service and fringe benefits. The February Plan allocates another $340 million in FY 2015 to the Department of Education (rising to $381 million by FY 2018) to make full-day universal prekindergarten available to all four-year-old children. (The Mayor has also proposed allocating $190 million to the Department of Youth and Community Development in FY 2015, along with similar amounts in subsequent years, to expand after-school programs for middle-school children.)

Figure 30
Department of Education Total Funding



Sources: NYC Office of Management and Budget; OSC analysis

The City currently provides full-day prekindergarten services to about 19,500 children and part-day services to another 39,000 children. Under the Mayor's proposal, the City would secure additional classroom space and hire 1,900 teachers and paraprofessionals in order to provide high-quality full-day prekindergarten services to 73,250 children by January 2016. In the first phase, the City would provide full-day services to 53,600 children by September 2014. According to a recent City report, community-based organizations have submitted proposals to provide 20,000 potential seats and public elementary schools have submitted applications to provide an additional 9,000 seats, amounting to more than the 21,000 seats needed for the first phase of the proposal.

The Mayor has proposed funding his full-day universal prekindergarten and after-school initiatives by raising the top personal income tax rate for City residents with taxable annual incomes of more than $500,000 from 3.876 percent to 4.41 percent, yielding $530 million in FY 2015 and slightly higher amounts in subsequent years. Raising the City's personal income tax, however, requires State approval. The Governor has instead proposed investing more than $2.2 billion over five years to support a phase-in of universal full-day prekindergarten programs and an expansion of after-school programs throughout the State.

Although not reflected in the February Plan, the City is seeking an additional $500 million in State education aid on top of the $234 million increase recommended by the Governor for the City in FY 2015. In making the case for additional aid, the City points to the State's failure to fulfill a 2007 promise to increase State education aid to the City by $3.2 billion over a four-year period as part of the resolution of the Campaign for Fiscal Equity (CFE) lawsuit.[25] The State was unable to fulfill its commitment because of severe budgetary pressures resulting from the Great Recession. If the State had kept its pledge, the City estimates that State education aid to the City would have been $2.7 billion more than recommended by the Governor in his executive budget.[26]

A series of federal audits, beginning in 2005, found that the State and City failed to properly document Medicaid reimbursement claims for students with special needs. As a result, in July 2009 the State, City and federal government reached an agreement that called for the State to repay $440 million to the federal government and the City to repay $100 million. The settlement also required the State and City to reform the documentation process.

At the beginning of FY 2013, the City anticipated $167 million in Medicaid reimbursement, but it received only $15 million because the Department of Education had not overcome all of its problems in preparing adequately documented claims. The Department of Education now believes it has solved the problem, and the City anticipates Medicaid reimbursements of $50 million in FY 2014, $137 million in FY 2015 and $167 million annually in subsequent years. Until the Department of Education demonstrates that it has solved the problems in the reimbursement process, the amounts above last year's level remain at risk.

2. Metropolitan Transportation Authority

In September 2013, OSC issued a report on the July 2013 financial plan of the Metropolitan Transportation Authority (MTA). The report found that the MTA's financial outlook was much improved compared to just seven months before, and estimated that the MTA had realized $1.9 billion in unanticipated resources over the course of the financial plan period compared with estimates in the MTA's February 2013 financial plan. The MTA proposed using the additional resources to balance the

[25] In June 2003, the New York State Court of Appeals overturned an appellate court decision and ruled that New York State failed to fulfill its State constitutional mandate to provide a sound, basic education to New York City schoolchildren.

[26] In February 2014, a group of parents and education advocates filed a lawsuit against the State claiming that the State has failed to meet the funding commitments it made to school districts in response to the CFE resolution. The lawsuit also contends that the State has underfunded schools statewide (including in New York City) by a total of $4 billion.

2014 budget and narrow the out-year budget gaps; to increase the amount of operating funds set aside to fund the capital program on a pay-as-you-go basis; to pay down some long-term liabilities; and to improve services. The proposed uses for the new resources did not include reducing the two 7.5 percent fare and toll increases planned for 2015 and 2017.

While OSC's report recognized that funding the next capital program and improving services were critically important, it also recommended that the MTA consider reducing the size of planned fare and toll hikes. In addition, the report recommended that the MTA refocus its efforts on reducing waste, as the value of new cost-reduction initiatives in areas other than paratransit have been modest since 2010. The MTA then released its November 2013 financial plan, which showed a reduction of the planned fare and toll increases from 7.5 percent to 4 percent as the result of an additional $1.2 billion in new resources identified over the financial plan period. The MTA also plans to increase its cost-cutting program by $500 million over the last four years of the financial plan.

Despite these positive developments, the MTA still faces significant fiscal challenges, including the outcome of ongoing labor negotiations. The MTA's financial plan assumes three years of net-zero wage increases for represented employees, followed by wage increases at the projected inflation rate. According to the MTA, wage increases in the first three years may be granted if the cost is offset by savings from work rules and other concessions.

In February 2014, the MTA reached a seven-year agreement with the union that represents its police officers. The agreement includes annual wage increases that are partially offset by work-rule and pay offsets. The MTA reports the net contract cost is 10.6 percent of the union's wage base, and is consistent with the MTA's financial plan assumptions.

All of the unionized employees of the Long Island Rail Road (LIRR) have been without a contract since 2010. In December 2013, a federal emergency board recommended wage increases of 18.4 percent (compounded) over a six-year period for most of the LIRR's represented employees and that employees contribute to the cost of their health insurance. The MTA rejected the recommendation because it did not conform to its budgetary assumptions. On March 5, 2014, the MTA requested that the President appoint another emergency board to assist the parties in reaching an agreement. The contract with the Transport Workers Union, the MTA's largest union, expired on January 15, 2012, and talks have progressed slowly.

The MTA is also in the process of developing its 2015-2019 capital program, and estimates that it would need to spend $26.6 billion during those five years just to maintain and modernize the existing transportation system. Additional resources would be needed to complete the East Side Access project (which the MTA reports is again over budget and behind schedule) and to begin the next phase of the Second Avenue Subway. The MTA has indicated, however, that the next capital program will be roughly $24 billion (the same size as its current capital program, excluding costs associated with Superstorm Sandy). The MTA has identified $6.5 billion to help fund the next capital program, but additional resources will be needed. Given the budget constraints facing the federal government, the MTA can be expected to look to the State and the City for new sources of funding for the capital program.

3. Health and Hospitals Corporation

The Health and Hospitals Corporation (HHC) is the largest municipal hospital system in the country, and is the single-largest provider of health care to uninsured New York City residents, serving almost 476,000 uninsured patients in FY 2013. The HHC also relies heavily on Medicaid (74 percent of total patient revenue), and is significantly affected by State and federal government actions that impact Medicaid.

The HHC benefited from large, nonrecurring Medicaid reimbursements as recently as FY 2007, when it ended the fiscal year with a cash balance of more than $1 billion (its highest ever). Since then, however, the HHC has drawn on these reserves to balance its budget. The HHC ended December 2013 with $194 million, or enough cash to allow the HHC to pay its bills for just 12 days. Without sufficient cash reserves, the HHC is especially sensitive to the timing of supplemental Medicaid payments that it receives for providing services to Medicaid patients and uninsured patients.

In recent years, the HHC has responded to significant fiscal challenges by instituting cost-saving measures, including a hiring freeze that reduced staff by about 3,700, and by renegotiating affiliation contracts. In spite of these efforts, the HHC has yet to solve its underlying structural imbalance. The HHC expects its operating revenues to decline by 3.5 percent from FY 2014 through FY 2018, while operating expenses are expected to grow by 11 percent during the same period.

A number of recent developments will benefit the HHC. Enrollment deadlines stipulated in the Affordable Care Act (which requires people under age 62 to obtain health insurance or pay a fine) are likely to significantly increase enrollment in the HHC's MetroPlus Health Plan (a Medicaid managed care plan), and the HHC's financial plan assumes that this will raise annual premium revenue by $120 million.

In February 2014, the U.S. Centers for Medicare and Medicaid Services (CMS) approved a waiver that will allow New York State to reinvest $8 billion in federal savings generated by recommendations from the State's Medicaid redesign team.

Reinvestment will occur over five years and will aim to transform the health care system and preserve vital health services in Brooklyn and other parts of the State. Though the federal funds are less than the $10 billion authorization that the State requested in August 2012, they will be crucial to restructuring financially distressed health care facilities in the State. The HHC's financial plan counts on the receipt of $400 million annually (for five years) from the Medicaid waiver starting in FY 2015, which seems likely to occur since the waiver has been approved by the federal government.

The HHC also will benefit in the short term from a recent federal budget agreement that rescinds a prior cut to supplemental Medicaid payments of $56.5 million in each of FY 2014 and FY 2015. However, the agreement doubles the cut for FY 2016, resulting in a decrease of $56.5 million that year.

Despite these favorable developments, the HHC's financial plan is still precarious, for it anticipates the receipt of $1.6 billion from several prior-year supplemental Medicaid payments, which have yet to be approved by the federal government.[27] If approved, the HHC projects a year-end cash balance of $735 million in FY 2014. If not, it is possible that the HHC will look to the City for financial assistance as it did last year.

4. New York City Housing Authority

The New York City Housing Authority (NYCHA) is a critical component of the City's current supply of affordable housing. As the City's largest landlord, NYCHA manages approximately 179,000 apartments with more than 400,000 residents (including 176,000 families). In total, these units account for more than 8 percent of the rental units citywide. NYCHA also manages the nation's largest Section 8 housing program, which provides rent subsidies at 93,000 private apartments that house 225,000 residents. NYCHA apartments rent for an average of $436 a month, and more than 167,000 families are on the waiting list for a NYCHA apartment.

Over the years, NYCHA has faced significant fiscal and management challenges that have threatened its ability to provide safe and affordable housing. For example, NYCHA has experienced significant cuts in federal subsidies, which make up nearly 70 percent of its revenue base, and has had a long history of being unable to make timely repairs to its apartments. NYCHA has taken steps to improve its budget process, but it still projects operating budget gaps of $200 million in 2014, rising to $300 million by 2018. The Mayor's new management team will be developing a strategy to balance NYCHA's budget and improve service. In the meantime, the February Plan provides NYCHA with $53 million in budget relief in 2014, which is expected to be used to reduce the backlog of work orders and to improve inspections.

[27] In response to the delayed payment, the State agreed to advance the HHC a Medicaid payment of $530 million in January 2014.

The lack of affordable housing in New York City remains a serious challenge despite efforts made by prior mayoral administrations over the past 30 years to create and preserve affordable housing units. In a recent report, OSC found that housing had become even less affordable for lower- and middle-income households because rents continue to rise but income growth has stagnated. Nearly 30 percent of City households faced a severe rent burden (i.e., rent exceeded half of household income) in 2011. Even with government rent subsidies taken into account, one of every five City households paid more than half of their household income to rent that year.[28]

In an effort to address this problem, the Mayor has called for the creation and preservation of 200,000 affordable housing units. Though details on this plan are not expected to be released until May 2014, the Mayor has suggested, for example, that developers be required to include affordable housing units in residential projects that receive City subsidies and zoning variances.

[28] Office of the State Deputy Comptroller, Report 3-2014, *The Continued Decline in Affordable Housing in New York City*, June 2013.

VIII. Other Issues

As discussed below, there are a number of other issues that could affect the February Plan.

1. Sale of Taxi Medallions

After a yearlong legal battle, in June 2013 the New York State Court of Appeals upheld a State law authorizing the City to sell new taxi medallions and create a new class of street-hail livery licenses. The law, which intends to increase access to the City's yellow taxicabs and livery cars for passengers who are disabled or who live outside Manhattan's central business district, was first signed by the Governor in December 2011 on the condition that it would be amended (which occurred in February 2012) to include extra provisions to improve accessibility for people with disabilities.

The law authorizes the City to sell up to 2,000 new taxi medallions, with their use restricted to vehicles that are wheelchair-accessible.[29] The law also permits the creation of up to 18,000 new hail licenses over a three-year period. These licenses would allow designated livery cars, known as green boro taxis, to pick up passengers via street hails in Upper Manhattan and the other four boroughs (excluding the airports), with 20 percent of the licenses designated for vehicles that are accessible to passengers with disabilities.[30]

The City has sold all 6,000 street-hail licenses and nearly all of the 400 taxi medallions it is allowed to sell before the State Department of Transportation must approve a disabled accessibility plan (DAP).[31] The DAP, which must be submitted no later than June 2014, will outline how the Taxi and Limousine Commission (TLC) plans to achieve meaningful accessibility for disabled passengers throughout the City, with a gradual phase-in of accessible vehicles among the medallion taxi fleet as well as among radio-dispatch livery cars and the new green boro taxis.

The DAP will be developed with input from various stakeholders, including disability rights advocates, and will be reviewed by the City Council. Once the DAP is submitted, the law stipulates that the State may "recommend changes or amendments to the TLC as a condition of its approval and must approve or reject the disabled accessibility plan within sixty days of submission by the TLC."

[29] When the law was passed, fewer than 2 percent of the City's yellow taxis were wheelchair-accessible. If all of the additional 2,000 medallions are sold, nearly one in five yellow taxis will be wheelchair-accessible.

[30] The new green boro taxis can pick up passengers by prearrangement anywhere (including airports), except in Manhattan south of West 110th Street and East 96th Street.

[31] By the end of FY 2014, the City expects to have sold all 400 medallions; it plans to hold an auction for the remaining portion on March 25, 2014.

On December 6, 2013, the City announced a settlement agreement which, if approved by the TLC and the U.S. District Court, would resolve outstanding legal issues regarding accessibility in the City's taxi medallion fleet. The agreement would require that half of the taxi fleet be wheelchair-accessible by 2020, and could serve as the principle component of the DAP.

The February Plan anticipates the receipt of $364 million in FY 2014 from the sale of the first 400 taxi medallions, an amount that will be exceeded given the results of recent auctions. The February Plan anticipates the receipt of $1.2 billion over the next three fiscal years from the sale of an additional 1,600 medallions, but these proceeds (which could exceed $1.5 billion) are contingent upon the timely submission of the DAP and its approval by the State.

2. Impact of the State Budget

On January 21, 2014, the Governor proposed his executive budget for State fiscal year (SFY) 2014-2015 along with an associated financial plan. The State Division of the Budget estimates that the executive budget would benefit the City by $246 million in City fiscal year (CFY) 2015, $607 million in CFY 2016 and nearly $1 billion in CFY 2017 (see Figure 31). The benefits are largely the result of projected incremental increases in education aid, which are reflected in the City's February Plan.[32]

Figure 31
Impact of the SFY 2014-15 Executive Budget on New York City
(in millions)

	FY 2015	FY 2016	FY 2017
Education Aid	$ 233.8	$ 563.5	$ 972.5
All Other Actions	12.3	43.5	25.5
Total Impact	**$ 246.1**	**$ 607.0**	**$ 998.0**

Source: NYS Division of the Budget

In addition, the Governor has proposed investing more than $2.2 billion over five years to support a phase-in of universal full-day prekindergarten programs and an expansion of after-school programs throughout the State, which could benefit New York City. (The February Plan assumes that the State will approve an increase in the personal income tax for the City's highest earners to fund an expansion of full-day prekindergarten and after-school programs in the City.) The City also could benefit from the Governor's proposed Smart Schools Bond Act, which, if approved by voters in November 2014, would allocate $2 billion statewide for technology investments in schools and to fund space for new prekindergarten and after-school programs.[33]

32 The executive budget includes a proposal that would provide rent relief to public assistance recipients with HIV/AIDS. The February Plan assumes this initiative will receive State approval and already includes the anticipated cost to the City ($17 million).

33 The City's capital plan anticipates the receipt of $800 million as a result of the Governor's bond proposal.

3. Impact of the Federal Budget

In an effort to reduce the federal deficit, in August 2011 the U.S. government implemented across-the-board spending cuts (known as the sequester), which became effective on March 1, 2013. These cuts reduced funding to the City's budget by a total of $148 million in federal fiscal year (FFY) 2013, which affected City fiscal years 2013 and 2014.[34] In May 2013, the City revised its four-year financial plan to reflect the impact of these cuts on the City's budget, and mitigated most of the impact with City, State and other federal funds. In some cases the City chose not to mitigate the impact of federal budget cuts, and some programs, such as Head Start and certain health services (e.g., services for people living with HIV/AIDS, disease control and immunizations), experienced a loss in funding and reduced services.

Congress was unable to reach agreement on a new budget for FFY 2014, which began on October 1, 2013, and this resulted in a government shutdown that lasted 16 days. Government operations resumed only after Congress approved an appropriations bill that funded operations at last year's level through January 15, 2014.

In December 2013, a two-year budget agreement revised discretionary spending caps, rescinding two-thirds ($22 billion) of the cuts scheduled to take effect in FFY 2014.[35] The agreement maintains federal spending at that level through FFY 2015, but it does not rescind budget cuts planned for subsequent years.

The February Plan does not reflect further federal budget cuts because congressional appropriations for FFY 2014 have largely restored discretionary spending for programs that affect the City's financial plan. Cuts to discretionary spending in FFY 2015 and subsequent years, however, will have to be determined by future federal budget negotiations, and could be larger or smaller than those in FFY 2013. The agreement also does not extend unemployment benefits for some 1.3 million people who have been out of work for more than six months (including approximately 73,000 New York City residents), and whose benefits expired on December 31, 2013.

[34] These estimates exclude the impact of federal budget cuts to programs and agencies outside of the City's financial plan, such as the New York City Housing Authority and the New York City Health and Hospitals Corporation.

[35] The agreement maintains cuts in spending for mandatory programs; these are programs required by law to provide certain benefits (rather than discretionary spending, which is determined by the annual congressional budget process). The February Plan estimates a loss of $20 million annually because of the cuts to mandatory programs that affect the City of New York.

4. Federal Assistance for Superstorm Sandy Recovery

According to the City's most recent estimates, Superstorm Sandy could cost the City about $5.1 billion. Of this amount, approximately $1.8 billion represents storm-related operating expenses, such as emergency repairs, debris removal and overtime, and $3.3 billion represents capital funding for long-term permanent work to repair damaged infrastructure. The February Plan assumes that all of the costs related to the storm will be funded from non-City sources, primarily the federal government.

New York City will be required to contribute 10 percent of the cost of any claim deemed eligible for reimbursement by the Federal Emergency Management Agency (FEMA). So far, FEMA has agreed to reimburse the City $1.3 billion (mostly for operating expenses), approximately $500 million less than the estimate of storm-related operating expenses. Although the reimbursement process for capital projects is proceeding more slowly, the City will be required to cover approximately $330 million of the estimated capital repair costs even if all claims are deemed eligible for reimbursement by FEMA.

The City has been allocated $3.2 billion in Community Development Block Grant-Disaster Relief funding, $855 million of which would be available to fill gaps in FEMA funding. The City, however, has already used $183 million of these resources to cover the cost of storm-related services provided by the Health and Hospitals Corporation. In addition, the federal government reduced FEMA's nationwide disaster relief fund by more than $900 million, which could affect the level of capital reimbursement to the City.

The City has indicated that the reimbursement process is complicated and will take some time to complete, but it is working with FEMA and other federal agencies to maximize reimbursement to the City. The City also notes that it could incur flood insurance costs for certain properties, and is in the process of analyzing this potential liability.

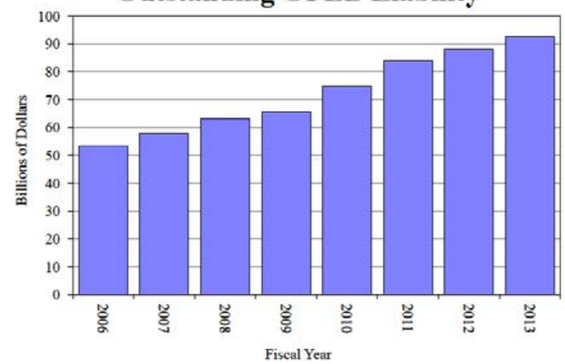
5. Other Post-Employment Benefits

In June 2004, the Governmental Accounting Standards Board (GASB) issued Statement No. 45, which establishes standards for measuring and reporting the expense and related liabilities of other post-employment benefits (OPEBs), such as health insurance, on an actuarial basis.

Although GASB 45 does not require entities to fund these costs on an actuarial basis, entities could realize significant long-term savings if they did so. As shown in Figure 32, the City's outstanding OPEB liability for past employee service reached $92.5 billion as of FY 2013, an increase of $39 billion since FY 2006 (the first OPEB valuation year reported by the City), and $5.5 billion more than in the prior year.

Figure 32

Outstanding OPEB Liability



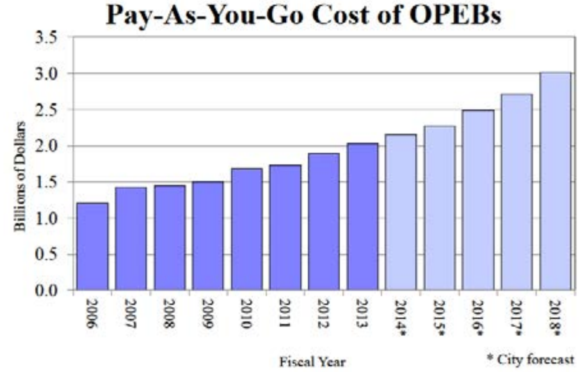
Sources: NYC Actuary; OSC analysis

Although the City is required to fund pension costs on an actuarial basis to ensure that current taxpayers pay their fair share of services, the City is not required to fund OPEBs on a similar basis. In FY 2013, the City paid less than a third of the present value of obligations ($3.8 billion) that is attributed, on an actuarial basis, to services received that fiscal year, deferring nearly $2.6 billion to future taxpayers. The City, like many employers, pays the annual cost of benefits provided to current retirees on a pay-as-you-go (PAYGO) basis. OPEB costs, on a PAYGO basis, are projected to rise from $2 billion in FY 2013 to $3 billion in FY 2018 (see Figure 33), an increase of nearly 49 percent in five years.

In FY 2006 the City established the Retiree Health Benefits Trust (RHBT), and over two years deposited $2.5 billion of surplus resources into the trust to help fund the future cost of OPEBs. These resources were invested and have earned interest.

Figure 33

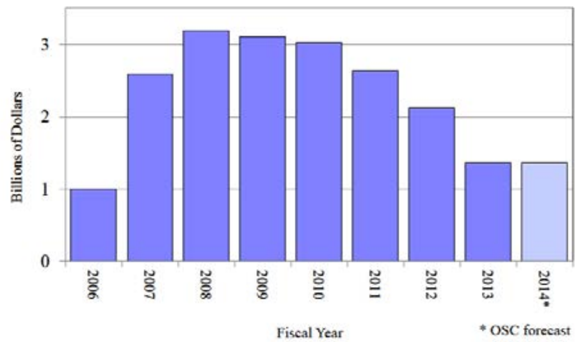
Pay-As-You-Go Cost of OPEBs



Sources: NYC Actuary; NYC Office of Management and Budget; OSC analysis

Although these resources were intended to help fund a future liability, the City has instead used the RHBT as a rainy-day fund to help balance the budget. The City drew down much of the resources in the RHBT during fiscal years 2009 through 2013 (see Figure 34), leaving future taxpayers to fund the full cost of services provided in those years. The City had planned to transfer $1 billion from the RHBT to help balance the FY 2014 budget, but the February Plan rescinds the planned transfer because revenues have grown much faster than the City anticipated at the beginning of the fiscal year, leaving a balance of $1.4 billion in the RHBT.

Figure 34
Balance of RHBT Resources



Sources: NYC Actuary; NYC Office of Management and Budget; OSC analysis

Appendix A:
Nonrecurring Resources

In recent years, the City has relied heavily on nonrecurring resources to balance the budget. The FY 2014 budget includes an estimated $2.5 billion in such resources, and the FY 2015 budget includes $2.6 billion in nonrecurring resources, as shown in Figure 35 and discussed below.

Figure 35
Nonrecurring Resources
(in millions)

	FY 2014	**FY 2015**
Net Surplus Transfers	$ 1,068	$ 1,770
Debt Refinancings–Net	554	208
Taxi Medallion Sales	364	481
Sale of City-Owned Buildings	243	- - -
Health Insurance Refunds	103	- - -
Verizon Settlement	50	- - -
Uncashed Paychecks	44	- - -
Educational Construction Fund	32	- - -
TFA Debt Redemption	7	99
Total	**$ 2,465**	**$ 2,558**

Sources: NYC Office of Management and Budget; OSC analysis

- Surplus resources accumulated in prior years have been used to help balance the FY 2014 and FY 2015 budgets.
- Historically low interest rates in recent years have permitted the City to refinance outstanding debt, generating savings of $554 million in FY 2014 and $208 million in FY 2015.
- The sale of additional taxi medallions is expected to generate $364 million in FY 2014, $481 million in FY 2015, $360 million in FY 2016 and $400 million in FY 2017, for a total of $1.6 billion.
- As part of a plan to consolidate City-owned real estate, the City expects to generate $243 million in FY 2014 from the sale of two buildings in Lower Manhattan.
- The City anticipates a refund of $103 million in health insurance premiums in FY 2014 as a result of the lower-than-expected use of medical services.
- Verizon has agreed to pay the City $50 million in FY 2014 to settle cost overruns resulting from delays to the upgrade of the City’s 911 system.
- The City expects $44 million in FY 2014 from paychecks that have not been cashed in more than six years.

- The Educational Construction Fund will transfer $32 million in surplus funds to the Department of Education in FY 2014.
- The City used $196 million in resources generated in FY 2013 to redeem TFA debt due in future years, which lowers debt service by $7 million in FY 2014, $99 million in FY 2015 and $103 million in FY 2016.

Appendix B:
Staffing Levels

(Full-Time and Full-Time-Equivalents)

Additions/(Reductions)

		Actual		City Forecast		Variance		
		June 2013	Dec. 2013	June 2014	June 2015	June 2013 to Dec. 2013	June 2013 to June 2014	June 2014 to June 2015
Public Safety		**80,700**	**80,998**	**80,626**	**80,477**	**298**	**(74)**	**(149)**
Police	Uniformed	34,708	34,824	34,483	34,483	116	(225)	0
	Civilian	15,598	15,626	15,898	15,770	28	300	(128)
Fire	Uniformed	10,178	10,231	10,779	10,779	53	601	0
	Civilian	5,293	5,168	5,073	5,073	(125)	(220)	0
Correction	Uniformed	8,970	9,126	8,882	8,873	156	(88)	(9)
	Civilian	1,383	1,389	1,627	1,626	6	244	(1)
District Attorneys & Prosecutors		3,825	3,853	3,138	3,138	28	(687)	0
Probation		730	765	730	718	35	0	(12)
Board of Correction		15	16	16	17	1	1	1
Health & Welfare		**22,430**	**22,179**	**23,622**	**22,988**	**(251)**	**1,192**	**(634)**
Social Services		10,103	10,066	10,151	9,553	(37)	48	(598)
Children's Services		5,957	5,803	6,461	6,461	(154)	504	0
Health & Mental Hygiene		4,224	4,157	4,611	4,569	(67)	387	(42)
Homeless Services		1,760	1,783	1,983	1,949	23	223	(34)
Other		386	370	416	456	(16)	30	40
Environment & Infrastructure		**17,614**	**16,046**	**17,752**	**17,796**	**(1,568)**	**138**	**44**
Sanitation	Uniformed	7,020	7,232	7,118	7,172	212	98	54
	Civilian	1,867	1,838	2,089	2,127	(29)	222	38
Transportation		1,938	1,964	2,031	2,106	26	93	75
Parks & Recreation		6,580	4,807	6,292	6,172	(1,773)	(288)	(120)
Other		209	205	222	219	(4)	13	(3)
General Government		**9,254**	**9,469**	**11,644**	**10,816**	**215**	**2,390**	**(828)**
Finance		1,802	1,867	1,976	1,980	65	174	4
Law		1,397	1,382	1,388	1,361	(15)	(9)	(27)
Citywide Administrative Services		1,338	1,307	1,470	1,529	(31)	132	59
Taxi & Limousine Commission		514	539	621	656	25	107	35
Investigations		197	208	267	257	11	70	(10)
Board of Elections		669	716	1,980	1,053	47	1,311	(927)
IT & Telecommunications		1,007	1,072	1,187	1,229	65	180	42
Other		2,330	2,378	2,755	2,751	48	425	(4)
Housing		**1,503**	**1,522**	**1,692**	**1,667**	**19**	**189**	**(25)**
Buildings		1,039	1,057	1,180	1,163	18	141	(17)
Housing Preservation		464	465	512	504	1	48	(8)
Department of Education		**113,717**	**114,728**	**114,335**	**115,155**	**1,011**	**618**	**820**
	Pedagogues	92,486	93,414	93,362	94,560	928	876	1,198
	Non-Pedagogues	21,231	21,314	20,973	20,595	83	(258)	(378)
City University of New York		**8,399**	**8,060**	**7,768**	**7,736**	**(339)**	**(631)**	**(32)**
	Pedagogues	5,387	5,022	5,028	5,028	(365)	(359)	0
	Non-Pedagogues	3,012	3,038	2,740	2,708	26	(272)	(32)
Elected Officials		**2,318**	**2,224**	**2,355**	**2,322**	**(94)**	**37**	**(33)**
Total		**255,935**	**255,226**	**259,794**	**258,957**	**(709)**	**3,859**	**(837)**

Sources: NYC Office of Management and Budget; OSC analysis