Review of the Financial Plan of the City of New York

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New York State
Office of the State Comptroller
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I. Executive Summary

On November 25, 2014, the City of New York submitted to the New York State Financial Control Board a revised four-year financial plan (the "November Plan") covering fiscal years 2015 through 2018 (see Figure 1). The November Plan incorporates developments during the first quarter of the current fiscal year, including higher-than-expected tax collections and agency spending. The November Plan shows substantially smaller out-year gaps than projected by the City in June 2014, mostly because of savings from better-than-expected pension fund investment earnings in FY 2014 and additional debt refinancings.

In the past seven months, the City has reached new labor agreements with 71 percent of its workforce. In May 2014, the City reached an agreement with the United Federation of Teachers (UFT), which has set the pattern for civilian employees. On December 9, 2014, the City announced a tentative agreement with a coalition of unions that represent superior officers in the four uniformed agencies, the first agreement with uniformed employees. The union that represents the City's police officers has not yet reached agreement with the City and the parties have begun binding arbitration.

In May, the City also reached an agreement with the unions to reduce the cost of health insurance by $3.4 billion through FY 2018, of which $1.3 billion would be recurring savings. The anticipated savings would be used to help fund the new labor agreements. The City reports that it is on track to meet the savings targets for fiscal years 2015 and 2016.

In June 2014, the City projected budget gaps of $2.6 billion in FY 2016, $1.9 billion in FY 2017 and $3.1 billion in FY 2018, which were much larger than those projected in February 2014 because of higher collective bargaining costs and new programmatic initiatives. Nevertheless, the gaps were still significantly smaller than the historical average over the past 35 years when measured as a share of City fund revenues.

Since then, the City has increased its revenue forecast by more than $1.1 billion for fiscal years 2015 through 2018, and has lowered its expenditure forecast by $1.7 billion. These resources permitted the City to reduce the out-year gaps in the November Plan to $1.8 billion in FY 2016, $1.2 billion in FY 2017 and $1.8 billion in FY 2018. The budget gaps are relatively small (averaging 2.8 percent of City fund revenues) and the financial plan includes an annual general reserve of $750 million, the largest amount ever, and the City also has other reserves it can draw upon if needed.

The reduction in the out-year gaps (averaging more than 36 percent) resulted mostly from refinancing outstanding debt in the current fiscal year and much-better-than-expected pension fund investment earnings in FY 2014. The City reports that its five pension systems had sufficient assets to fund, on average, 72.5 percent of their accrued pension liabilities as of June 30, 2014. Although the City made a large discretionary contribution to the Retiree Health Benefits Trust in FY 2014, its liability for post-employment benefits other than pensions remains mostly unfunded ($89.5 billion).[1]

1 Unlike pensions, the City is not required to fund other post-employment benefits on an actuarial basis. Instead, these costs are funded on a pay-as-you-go basis.

The Office of the State Comptroller (OSC) estimates that City-funded spending grew by 10.2 percent in FY 2014 (after adjusting for surplus transfers) and will increase by another 4.2 percent in FY 2015. Although the City is relying on nonrecurring resources of $3.4 billion to balance the FY 2015 budget, the FY 2016 budget includes less than $1 billion in nonrecurring resources.

In our last report, OSC expressed concern about the size of the budget gaps in years beyond the financial plan period because the cost of new labor agreements will be greatest in those years. The City's 2015-2019 financial plan is not scheduled to be released before the end of January 2015, but the FY 2019 budget will benefit from the sale of taxi medallions (now that the City has spread the sale over additional years) and recurring savings from better-than-expected pension fund investment earnings in FY 2014.

As part of the preparations for the Mayor's preliminary and executive budgets for FY 2016 (and the associated four-year financial plans), the budget director has asked agency heads to identify savings from implementing management and productivity improvements, eliminating or reducing ineffective programs, consolidating or restructuring programs, and reducing the use of consultants or outside contracting. Any resources resulting from this exercise could fund new agency initiatives or help close the projected budget gaps.

Economic growth in New York City has been strong for the past four years, driven by historically high levels of job growth, a booming tourism sector and strengthening real estate markets. The City has added 86,400 jobs so far this year, an annual growth rate of 2.3 percent. Wage growth, however, has been slow because many of the new jobs have been in low-wage industries. The high-wage securities industry is much smaller today than before the financial crisis, although it remains profitable and continues to be a major contributor to the City's economy.

While the City's financial outlook continues to improve, the Health and Hospitals Corporation (HHC) is still experiencing financial difficulties, resulting in additional financial assistance from the City. The City covered $300 million of the HHC's obligations in FY 2013 and still has not been reimbursed for $450 million of such costs in FY 2014. The City has also set aside $1.4 billion to fund new labor agreements at the HHC.

In conclusion, the City projects a surplus of $105 million in FY 2015, which is likely to grow as the fiscal year progresses given the City's conservative economic and revenue assumptions, and the continued strength of the local economy (see Figure 2). The City is also making good progress in reducing the size of the out-year budget gaps, and it has resumed the process of examining agency operations for cost savings. While there is the potential for an economic setback during the financial plan period, the City has substantial reserves, which would cushion the impact.

Figure 1
New York City Financial Plan
(in millions)

REVENUES	FY 2015	FY 2016	FY 2017	FY 2018
Taxes				
General Property Tax	$ 20,968	$ 21,969	$ 22,919	$ 23,859
Other Taxes	27,505	28,466	29,433	30,368
Tax Audit Revenue	911	709	709	709
Subtotal: Taxes	$ 49,384	$ 51,144	$ 53,061	$ 54,936
Miscellaneous Revenues	7,665	6,981	6,840	6,900
Unrestricted Intergovernmental Aid	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(1,924)	(1,835)	(1,845)	(1,856)
Disallowances Against Categorical Grants	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 55,110	$ 56,275	$ 58,041	$ 59,965
Other Categorical Grants	848	877	873	869
Inter-Fund Revenues	545	533	540	542
Federal Categorical Grants	7,967	6,432	6,381	6,378
State Categorical Grants	12,467	12,841	13,323	13,843
Total Revenues	**$ 76,937**	**$ 76,958**	**$ 79,158**	**$ 81,597**
EXPENDITURES				
Personal Service				
Salaries and Wages	$ 23,778	$ 24,501	$ 24,721	$ 26,061
Pensions	8,587	8,628	8,492	8,793
Fringe Benefits	8,707	9,116	9,599	10,180
Subtotal: Personal Service	$ 41,072	$ 42,245	$ 42,812	$ 45,034
Other Than Personal Service				
Medical Assistance	$ 6,447	$ 6,415	$ 6,415	$ 6,415
Public Assistance	1,460	1,407	1,413	1,413
All Other	24,575	23,080	23,532	24,066
Subtotal: Other Than Personal Service	$ 32,482	$ 30,902	$ 31,360	$ 31,894
Debt Service[2,3]	$ 6,458	$ 6,836	$ 7,271	$ 7,546
FY 2014 Budget Stabilization[2]	(2,006)	- - -	- - -	- - -
FY 2015 Budget Stabilization[3]	105	(105)	- - -	- - -
General Reserve	750	750	750	750
Subtotal	$ 78,861	$ 80,628	$ 82,193	$ 85,224
Less: Intra-City Expenses	(1,924)	(1,835)	(1,845)	(1,856)
Total Expenditures	**$ 76,937**	**$ 78,793**	**$ 80,348**	**$ 83,368**
Gap to Be Closed	**- - -**	**$ (1,835)**	**$ (1,190)**	**$ (1,771)**

Source: NYC Office of Management and Budget

2 Fiscal Year 2014 Budget Stabilization totals $2.006 billion, including GO of $621 million, TFA of $1.362 billion, and net equity contribution in bond refunding of $23 million.

3 Fiscal Year 2015 Budget Stabilization totals $105 million.

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

	Better/(Worse)			
	FY 2015	**FY 2016**	**FY 2017**	**FY 2018**
Surplus/(Gaps) Per November Plan	**$ - - -**	**$ (1,835)**	**$ (1,190)**	**$ (1,771)**
Tax Revenue	650	400	400	400
Debt Service	150	- - -	- - -	- - -
Medicaid Reimbursement	(50)	(80)	(80)	(80)
Uniformed Overtime	(75)	(100)	(100)	(100)
Collective Bargaining[4]	(84)	(59)	(36)	(38)
OSC Baseline Risk Assessment	**591**	**161**	**184**	**182**
Surplus/(Gaps) Per OSC[5]	**$ 591**	**$ (1,674)**	**$ (1,006)**	**$ (1,589)**

[4] In December 2014, the City reached tentative agreements with the Council of School Supervisors and Administrators, and a coalition of eight unions that represent superior officers in the uniformed agencies (the first agreement with unions that represent uniformed employees). These agreements are expected to cost more than anticipated in the November Plan. The agreement with the superior officers, for example, increases wages by 11 percent over seven years, or one percentage point more than assumed in the November Plan. The City would incur additional costs of $465 million during the financial plan period if the economic terms of the recent agreement with the superior officers are applied to all other uniformed employees.

[5] The November Plan includes a general reserve of $750 million in each of fiscal years 2015 through 2018, which if not needed, could be used to help close the projected budget gaps. In addition, the City's financial plan excludes savings from overestimating prior years' expenses, which have averaged $432 million annually over the past ten years. The Retiree Health Benefits Trust, which the City has used in the past as a rainy-day fund, has a balance of $2.4 billion.

II. Economic Trends

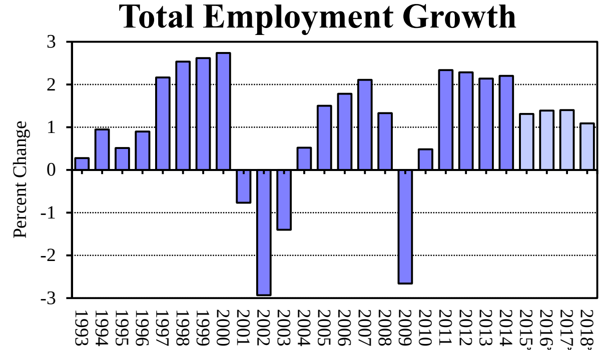
The national economy contracted sharply in the first quarter of 2014 due to severe weather, but growth was very strong during the second and third quarters (averaging 4.2 percent). For all of 2014, the national economy is expected to grow by 2.2 percent, about the same annual pace as in the two prior years. Job growth has accelerated and the nation has now added more jobs (119 percent) than it lost during the recession. While the unemployment rate has fallen from its recessionary peak of 10 percent to 5.8 percent, many workers have been unable to find full-time jobs or have been without jobs for an extended period of time. Many others have become discouraged and left the labor force, resulting in the lowest labor force participation rate in three decades.

In October 2014, the Federal Reserve indicated that economic conditions had improved sufficiently to allow it to end its bond purchasing program (i.e., quantitative easing). While the central bank has also reaffirmed its commitment to keep short-term interest rates near zero for some time, most economists believe the Federal Reserve will begin to raise interest during the third quarter of 2015 (the beginning of FY 2016).

Unlike in the nation, economic growth in New York City has been strong for the past four years, driven by historically high levels of job growth, a booming tourism sector and strengthening real estate markets. Nonetheless, there are still weaknesses in parts of the labor market, wage growth has been slow and housing is still unaffordable for many residents.

As shown in Figure 3, job growth in New York City has been consistently strong for the past four years, averaging nearly 2.3 percent annually from 2011 through 2014 (private sector growth has been even stronger, averaging about 2.7 percent annually). The only period in the past half-century when job growth was stronger was the boom in the late 1990s. Employment in the City is at a record level and is approaching 4.1 million jobs.

Figure 3
Total Employment Growth



Note: 2014 growth is year-to-date. *City forecast
Sources: NYS Department of Labor; NYC Office of Management and Budget; OSC analysis

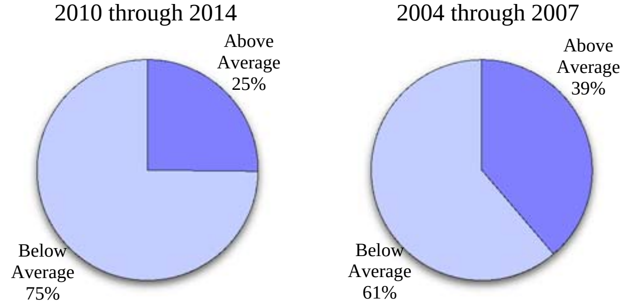
Wage growth, however, has been weak, averaging 3.3 percent annually since 2010, or less than half the growth rate during each of the past two expansions. The slow rate of wage growth reflects both the large number of lower-paying jobs that have been created in the City compared to prior recoveries and job losses in the high-paying securities industry.

Figure 4 shows that three quarters of the private sector jobs added during the current economic recovery have been in industries that pay less than the citywide average, a larger share than in the 2004-2007 recovery (61 percent). These lower-paying industries include restaurants, retail trade and health care. One third of the jobs created during the current recovery have been in industries with average salaries of less than $40,000.

Figure 4

Distribution of New Jobs in the City

Above or Below the Private Sector Average



Sources: NYS Department of Labor; OSC analysis

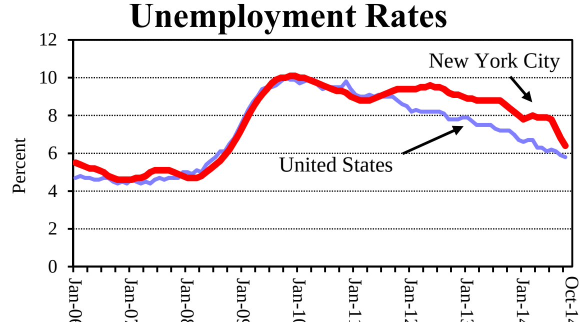
Only one quarter of the jobs added during the current recovery were in industries that pay more than the citywide average salary. The high-paying securities industry has not contributed to the current job recovery, though it was a major factor in the prior recovery. Since 2010, the average salary in the private sector has declined (after adjusting for inflation) to $81,200 in 2013, and has declined by more than $10,000 from the prerecession peak in 2007.

The November Plan assumes that job growth will ease from an annual average of 2.3 percent in recent years to 1.3 percent annually during calendar years 2015 through 2018. The City also expects that the bulk of the new jobs will continue to be created in lower-paying industries. As a result, wages are expected to grow at an average annual rate of 3.7 percent during this period.

The City's unemployment rate has fallen from its recessionary peak of 10.1 percent to 6.4 percent in October 2014 (see Figure 5). Over the past 12 months, the unemployment rate has fallen by two percentage points, the largest 12-month decline in nearly two decades. Nevertheless, the unemployment rate in New York City remains slightly higher than the national unemployment rate, and is much higher for certain segments of the labor force and in some parts of the City.

Figure 5

Unemployment Rates



Note: Data have been seasonally adjusted.

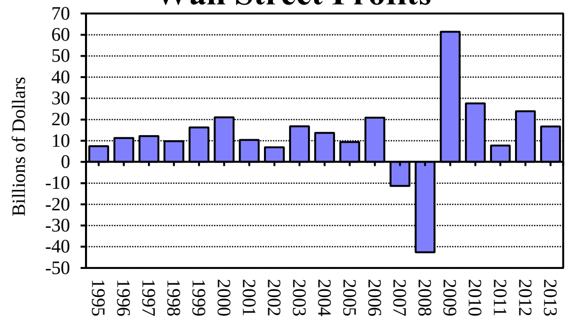
Sources: U.S. Bureau of Labor Statistics; NYS Department of Labor; OSC analysis

Wall Street is one of the City's economic engines and a major source of tax revenues. In the six years since the financial crisis, Wall Street has been adapting to changes in its regulatory and business environment. While the securities industry has been profitable (see Figure 6), rising non-compensation expenses (including payments to settle legal actions related to the financial crisis) have constrained profitability during the past two years.

In 2013, the broker/dealer profits of the member firms of the New York Stock Exchange declined by 30 percent to $16.7 billion. During the first three quarters of 2014, profits totaled $11.7 billion, which was 13.5 percent less than the same period last year. The November Plan assumes that industry profits will total $14 billion in all of 2014, and while OSC also expects profits to be less than last year, profits could exceed $15 billion in 2014.

Figure 6

Wall Street Profits



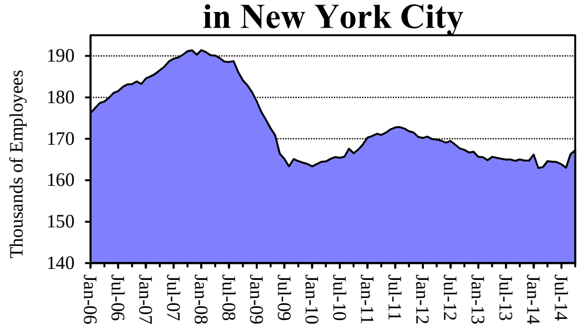
Note: Results are for broker/dealer operations of the NYSE member firms.
Sources: Securities Industry and Financial Markets Association; NYSE/Intercontinental Exchange

While the securities industry has been profitable for the past five years, industry employment in New York City continues to decline. As of August 2014, there were 15 percent fewer securities industry jobs in the City than before the financial crisis (see Figure 7). Employment data for September and October showed some job gains, but it would be premature to conclude that the industry is expanding again. The data are still preliminary and appear inconsistent with recent reports from the major firms. Although the industry is significantly smaller, it remains well-compensated, with an average salary (including bonuses) of $355,900 in 2013, five times higher than the average salary of all other private sector jobs in the City.

OSC estimated that bonuses for securities industry employees in the City increased by 15 percent in 2013 to an average of $164,530, the third-highest level ever. While the November Plan assumes that bonuses (both cash payments and bonuses deferred from prior years) will decline in 2014, compensation trends suggest a modest increase.

Figure 7

Securities Industry Employment in New York City

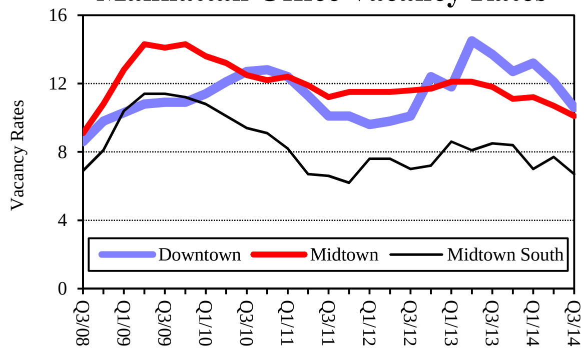


Note: Data have been seasonally adjusted.
Sources: NYS Department of Labor; OSC analysis

The City's tourism industry plays a large role in the local economy, with visitors spending nearly $40 billion in 2013. NYC & Company (the City's tourism organization) estimates that the total number of visitors will reach 55.8 million in 2014, which would be the fifth-consecutive record year. The hotel occupancy rate is also expected to reach a record 88.6 percent in 2014 (the third-consecutive record year), with the average daily room rate reaching $298 (close to a record).

The City's commercial real estate market is the largest in the nation and is also among the strongest. According to Jones Lang LaSalle, Manhattan's vacancy rate was 9.7 percent in the third quarter, the lowest rate among the nation's largest cities. As shown in Figure 8, among the three major Manhattan office markets, Midtown South had the lowest vacancy rate (6.7 percent), driven by technology, media and information companies.

Figure 8
Manhattan Office Vacancy Rates



Source: Jones Lang LaSalle

Real estate transaction activity and property values have increased significantly in recent years. Data from the New York City Department of Finance show that in FY 2014 the dollar value of sales of large Manhattan office buildings (those valued at more than $50 million) had reached the highest level since the recession. Residential sales throughout the City have also been increasing, and in FY 2014 the dollar value of sales had exceeded prerecession levels. Both residential and commercial sales have been supported by foreign investors, attracted by the security and rising values of properties in the City compared to other investments.

The City's economy is strong today, but the possibility of an economic setback increases with each year. Changes in the business cycle are inevitable, and the City is not immune to difficulties in the national and international economies. Economic growth in many Asian and European countries has weakened in recent quarters, contributing to the rise in the value of the dollar, which could impact trade and tourism. While the Federal Reserve is not expected to begin raising interest rates before the summer of 2015, the magnitude and timing of rate increases will affect businesses and consumers throughout the economy.

III. Changes Since the June 2014 Plan

In June 2014, the City projected gaps of $2.6 billion in FY 2016, $1.9 billion in FY 2017 and $3.1 billion in FY 2018. Since then, the City has increased its revenue forecast by more than $1.1 billion during the financial plan period and has lowered its expenditure forecast by $1.7 billion. These unanticipated resources permitted the City to reduce the out-year gaps by an average of more than 36 percent to $1.8 billion in FY 2016, $1.2 billion in FY 2017 and $1.8 billion in FY 2018, even though the City has stretched out the anticipated receipt of proceeds from the sale of taxi medallions and also has funded new agency needs (see Figure 9). The projected gaps are relatively small (averaging 2.8 percent of City fund revenues) and the City has substantial reserves.

Figure 9
Financial Plan Reconciliation–City Funds
November 2014 Plan vs. June 2014 Plan
(in millions)

		Better/(Worse)		
	FY 2015	**FY 2016**	**FY 2017**	**FY 2018**
Surplus/(Gaps) Per June 2014	**$ - - -**	**$ (2,625)**	**$ (1,871)**	**$ (3,093)**
Revenue Reestimates				
Taxes				
Personal Income	215	137	142	148
Real Property	189	115	120	125
Real Estate Transactions	85			
Other Taxes	75	- - -	- - -	- - -
Audits	202	- - -	- - -	- - -
Subtotal	**766**	**252**	**262**	**273**
Taxi Medallions	(506)	(48)	(161)	256
All Other	24	20	(7)	(6)
Total	**284**	**224**	**94**	**523**
Expenditure Reestimates				
Debt Service	95	405	311	293
Pension Contributions	8	205	408	615
Agency New Needs	(237)	(207)	(197)	(183)
All Other	(45)	58	65	74
Total	**(179)**	**461**	**587**	**799**
Net Change During FY 2015	**105**	**685**	**681**	**1,322**
Surplus/(Gap)	**$ 105**	**$ (1,940)**	**$ (1,190)**	**$ (1,771)**
Surplus Transfer	(105)	105	- - -	- - -
Gaps Per November 2014 Plan	**$ - - -**	**$ (1,835)**	**$ (1,190)**	**$ (1,771)**

Sources: NYC Office of Management and Budget; OSC analysis

Tax collections are now expected to be higher than projected at the beginning of the fiscal year by $766 million in FY 2015, because strong job and wage growth is increasing personal income tax collections faster than the City had expected; property tax delinquencies have been lower; and a number of large audits were completed during the first part of the fiscal year. Tax collections are projected to be higher than previously forecast by about $260 million annually in subsequent years.

Debt refinancings, combined with the City’s strong cash position that negated the need for short-term borrowing, resulted in debt service savings of $1.1 billion during the financial plan period (for more detail, see “Debt Service” in Section V). Better-than-expected pension fund investment earnings in FY 2014 permitted the City to reduce its planned contributions by $1.2 billion during the financial plan period. The City’s pension systems earned nearly 17.5 percent on their investments, far more than the 7 percent expected rate of return.

The improved financial outlook enabled the City to reschedule the sale of taxi medallions, which postponed the receipt of $506 million from FY 2015 to future years, and to fund new agency needs, which averaged more than $200 million annually. These new needs include training NYPD officers in community engagement techniques, additional mental health services to the City’s inmate population, and increases in the homeless shelter population and programs to prevent homelessness.

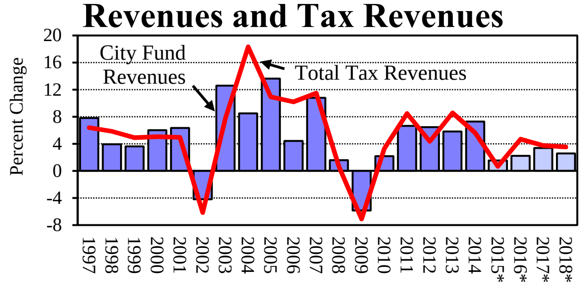
As part of the preparations for the Mayor’s preliminary budget for FY 2016 and the associated four-year financial plan, the City’s budget director has asked agency heads to identify savings from implementing management and productivity improvements, eliminating or reducing ineffective programs, consolidating or restructuring programs, and reducing the use of consultants or outside contracting. These savings may be used to address future agency needs or reduce the projected budget gaps.

IV. Revenue Trends

The November Plan assumes that City fund revenues will increase by 2.3 percent in FY 2015, about one-third the average annual rate of growth (6.5 percent) in fiscal years 2011 through 2014 (see Figure 10). The relatively slow rate of growth for FY 2015 reflects the City's assumptions that job growth will slow, Wall Street bonuses will decline and interest rates will rise.

However, job growth remains strong, securities industry compensation trends suggest that bonuses will increase, and the Federal Reserve has renewed its commitment to keep short-term interest rates near zero for some time. Most economists do not expect the Federal Reserve to begin to raise rates until FY 2016. If tax revenues were to grow at the average annual rate of the past four years, the City could realize more than $2 billion in additional revenue in FY 2015. Based on year-to-date collection trends, OSC conservatively forecasts that tax collections will be $650 million higher than the City forecasts in FY 2015.

Figure 10
Annual Changes in City Fund Revenues and Tax Revenues



Note: Adjusted for debt service on TFA Bonds and tobacco settlement revenues used to pay TSASC debt service.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

The City could also benefit from an $8.9 billion penalty to be paid by French bank BNP Paribas to settle federal and state criminal charges. The City's share could total $900 million, but the use would be restricted to law enforcement activities.

Details of the City's revenue forecasts are shown in Figure 11 and discussed below.

Figure 11
City Fund Revenues
(in millions)

	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Taxes					
Real Property Tax	$ 19,977	$ 20,968	$ 21,969	$ 22,919	$ 23,859
Personal Income Tax	9,539	9,406	9,754	10,090	10,368
Sales Tax	6,494	6,681	6,946	7,260	7,556
Business Taxes	5,876	5,990	6,149	6,312	6,530
Real Estate Transaction Taxes	2,488	2,311	2,467	2,561	2,638
Other Taxes	3,090	3,117	3,150	3,210	3,276
Audits	911	911	709	709	709
Subtotal	**48,375**	**49,384**	**51,144**	**53,061**	**54,936**
Miscellaneous Revenues	5,569	5,815	5,220	5,069	5,126
Grant Disallowances	(18)	(15)	(15)	(15)	(15)
Total	**$ 53,926**	**$ 55,184**	**$ 56,349**	**$ 58,115**	**$ 60,047**

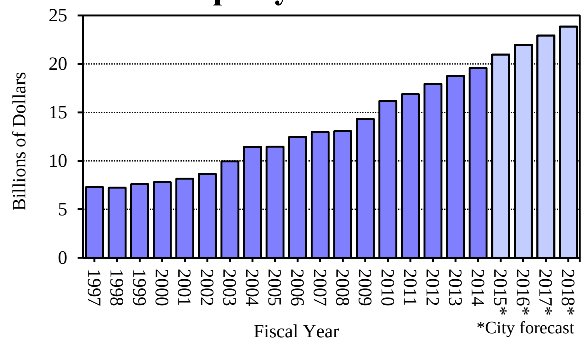
Note: Miscellaneous revenues include tobacco settlement revenues used to pay TSASC debt service.
Sources: NYC Office of Management and Budget; OSC analysis

1. Real Property Tax

Real property tax growth remains strong, driven primarily by rising values of commercial real estate. Real property tax collections are forecast to increase by 5 percent in FY 2015, to $21 billion (see Figure 12). This is consistent with the average annual gains of 5.4 percent since FY 2010 (the last year in which property tax rates were raised). Overall, collections will be nearly one-third higher in FY 2015 than they were in FY 2010.

Figure 12

Real Property Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

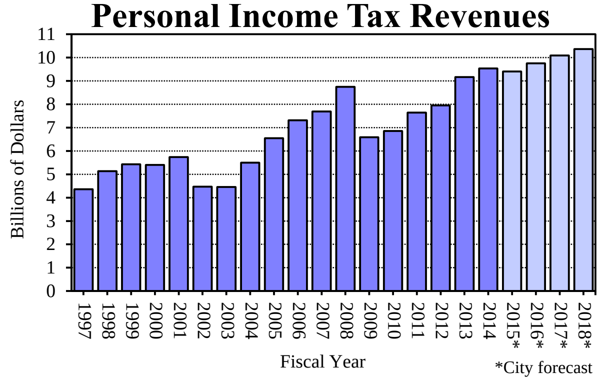
The November Plan assumes that assessed values for both commercial and residential properties will increase at an average annual rate of 4.6 percent during fiscal years 2016 through 2018, compared with 5.1 percent in recent years. The City's forecast assumes that long-term interest rates (which affect property valuation) will rise sharply during the latter part of the financial plan period, holding down the growth in assessed values. If long-term interest rates rise at a slower rate, growth in property values could exceed the City's forecast, yielding additional revenues.

2. Personal Income Tax

Personal income tax collections have increased at an average annual rate of 7.7 percent during the past five years, driven by strong job gains and higher Wall Street bonuses, to reach $9.5 billion in FY 2014 (see Figure 13). While the City has increased its personal income tax forecast for the financial plan period, the November Plan still assumes that collections will decline by 1.4 percent in FY 2015, which would be the first reduction since the recession.[6]

Figure 13

Personal Income Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

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6 The November Plan reflects the State Legislature's recent extension of the 14 percent personal income tax surcharge through December 31, 2017, and assumes that the surcharge will be extended through the balance of the financial plan period. The surcharge, valued at more than $1 billion annually, was first enacted in 1991 and has been extended every two to three years since then.

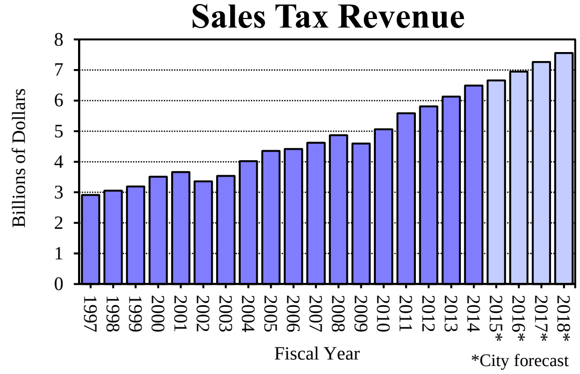
Personal income tax collections are likely to be higher than the City's forecast for FY 2015 because job growth remains strong and Wall Street bonuses are unlikely to be lower than last year. If collections were to increase at the average annual rate of the past five years (7.7 percent), the City would receive an additional $850 million. In fact, personal income tax collections grew by 9 percent during the first five months of the fiscal year. OSC conservatively estimates that collections could be higher by $400 million in FY 2015. While the City has more realistic forecasts for subsequent years, it could also realize additional revenues in those years in the absence of a significant economic setback.

3. Sales Tax

The largest sources of sales tax collections are the industries that benefit from tourism, such as retail stores, hotels and restaurants. Tourists spent nearly $40 billion in 2013, and the City anticipates that 2014 will be another record-breaking year for tourist spending. Over the past three years, sales tax collections have grown at an average annual rate of 5.1 percent. The November Plan assumes, however, that sales tax collections will increase by only 2.9 percent in FY 2015 to reach $6.7 billion (see Figure 14). The November Plan assumes that sales tax collections will grow at a faster rate during fiscal years 2016 through 2018 (an average annual rate of 4.2 percent).

Figure 14

Sales Tax Revenue



Sources: NYC Comptroller; NYC Office of Management and Budget

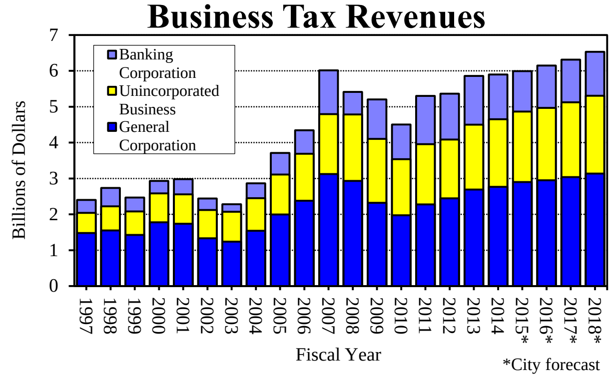
Year-to-date collections and economic trends indicate that collections could higher than the forecast in the November Plan be at least $50 million in FY 2015 and similar amounts in subsequent years.

4. Business Taxes

The November Plan assumes that aggregate collections from the three business taxes (the general corporation, banking corporation and unincorporated business taxes) will increase by 1.9 percent to nearly $6 billion in FY 2015 (see Figure 15). The relatively slow rate of growth reflects a decline in bank tax collections, which fell by 9.6 percent in FY 2014 and are projected to decline by another 8.2 percent in FY 2015, bringing them to the lowest level since FY 2010. These declines reflect the banking industry's continued restructuring due to changing regulatory and market conditions, as well as the impact of legal settlements primarily related to its activities during the financial crisis.

Bank tax collections are expected to resume growing in FY 2016. While compliance costs are expected to continue to constrain profitability for financial firms, the November Plan expects that rising interest rates will help boost earnings. The Federal Reserve, however, may not increase interest rates as soon as the City expects. Profits from business and professional service industries (the second-largest payer of business taxes after the financial industry) are expected to remain strong. The November Plan assumes that the growth in business tax collections will average 2.9 percent during fiscal years 2016 through 2018.

Figure 15
Business Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

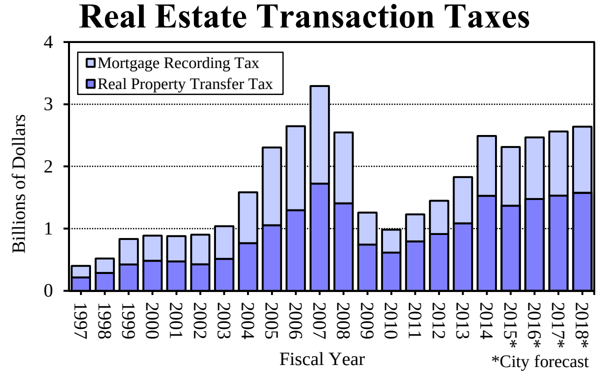
These estimates exclude the results of tax audits. Last year, the City realized $911 million from tax audits, of which nearly 90 percent represented underpayment of business taxes. The City completed a number of large audits of financial firms during the first quarter of the current fiscal year, causing the City to raise its audit forecast by $202 million to last year's level.

5. Real Estate Transaction Taxes

The City's commercial and residential real estate markets continue to show strength with a rising number of transactions, fueled by low interest rates and overseas investors. In FY 2014, collections from the real estate transaction taxes (i.e., the mortgage recording tax and the real property transfer tax) reached nearly $2.5 billion (see Figure 16). While less than the peak reached in FY 2007, it was still among the best years on record.

The increase in collections was driven by activity in Manhattan. Last year, for example, sales of large Manhattan office buildings (valued at more than $50 million) reached their highest level since the recession ($10.8 billion), driven by a 40 percent increase in transactions.

Figure 16
Real Estate Transaction Taxes



Sources: NYC Comptroller; NYC Office of Management and Budget

The November Plan assumes that interest rates will begin to increase during FY 2015, and as a result collections will decline by $177 million (7.1 percent). However, four months into the fiscal year, interest rates have remained at historically low levels, and revenues from the two taxes were 10.8 percent higher than the level during the same period last fiscal year. OSC forecasts that collections from these taxes could be $200 million higher than the City's forecast for FY 2015 based on the strength in year-to-date collections. In recent months a number of large sales have been announced but have not yet closed, including the sale of the Waldorf-Astoria ($2 billion) and 1095 Sixth Avenue ($2.3 billion).

6. Miscellaneous Revenues

Miscellaneous revenues are projected to total $5.8 billion in FY 2015 (see Figure 17), including a transfer of $1 billion from the Health Stabilization Fund pursuant to a May 2014 agreement with the municipal unions. The amount anticipated from recurring sources (i.e., excluding proceeds from the sale of taxi medallions and the transfer from the Health Stabilization Fund) is expected to remain relatively stable at about $4.8 billion during the financial plan period.

Figure 17
Miscellaneous Revenues
(in millions)

	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Water and Sewer Charges	$ 1,491	$ 1,565	$ 1,580	$ 1,538	$ 1,542
Charges for Services	951	920	927	926	926
Fines and Forfeitures	892	803	788	788	788
Licenses, Franchises, Etc.	648	583	591	568	565
Rental Income	311	270	270	270	270
Interest Income	16	17	45	134	163
Other	922	610	707	606	616
Subtotal	**5,231**	**4,768**	**4,908**	**4,830**	**4,870**
Sales of Taxi Medallions	338	47	312	239	256
Health Stabilization Fund	0	1,000	0	0	0
Total	**$ 5,569**	**$ 5,815**	**$ 5,220**	**$ 5,069**	**$ 5,126**

Note: Other includes tobacco settlement revenues used to pay TSASC debt service.
Sources: NYC Office of Management and Budget; OSC analysis

The City has overcome a number of legal and procedural obstacles to the sale of 2,000 new yellow taxi medallions for wheelchair-accessible vehicles.[7] The City sold 350 medallions in FY 2014, generating $338 million in that year. The November Plan assumes that the sale of the remaining 1,650 medallions will be spread out through

[7] In August 2014, the last procedural issue was resolved when the New York State Department of Transportation approved the City's disabled accessibility plan (DAP).

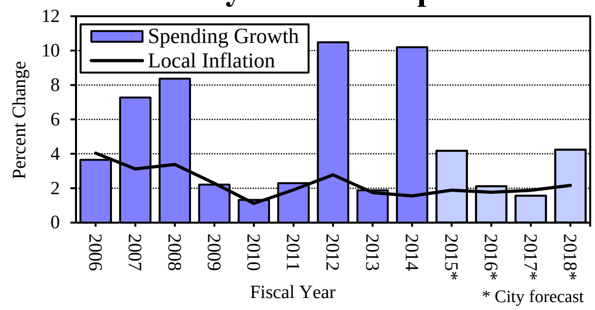
FY 2019 (a longer period of time than previously anticipated). Changing market conditions, such as the growing presence of electronic hailing services through smartphone applications like Uber, have recently hurt the market value of current medallions and could affect the value of new medallions at auction.

V. Expenditure Trends

City-funded expenditures grew by 10.2 percent in FY 2014 largely because of the cost of new labor agreements, which increased costs by $2 billion in that year (see Figure 18).[8] Spending is projected to increase by another 4.2 percent in FY 2015 (more than twice the projected inflation rate) to reach nearly $57.2 billion, reflecting a large projected increase in debt service ($938 million) and a general reserve of $750 million, which is the largest ever. City-funded spending is projected to grow more slowly during fiscal years 2016 and 2017 (an average of less than 2 percent), but then resume growing at more than 4 percent in FY 2018, mostly because of higher collective bargaining costs pursuant to recent agreements.

Figure 18

Growth in City-Funded Expenditures



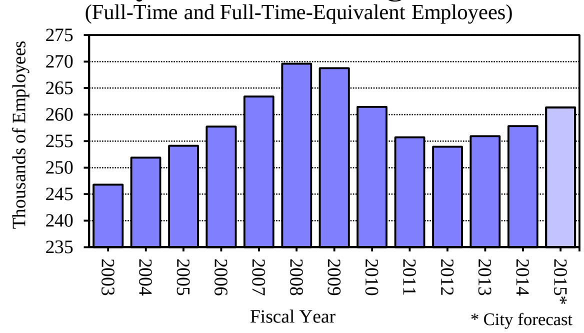
Note: Adjusted for surplus transfers, TFA, TSASC and discretionary actions. City-funded expenditures grew by 10.5 percent in FY 2012 because the City replaced expiring federal stimulus aid ($1.8 billion) and a cut in State education aid ($812 million) with City funds.
Sources: NYC Office of Management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

The City-funded workforce grew by 22,800 employees between fiscal years 2003 and 2008 (see Figure 19), but contracted by 15,666 employees over the next four years as agency cost-reduction initiatives were implemented to help weather the Great Recession. Since FY 2012 staffing levels have been increasing, growing by about 2,000 employees in each of fiscal years 2013 and 2014. The November Plan assumes that City-funded staffing (both full-time and full-time-equivalents) will increase by 3,495 employees during FY 2015 (excluding temporary hires) to reach 261,341 (for details, see Appendix B), which is still well below the prerecession peak.[9] The City is also adding another 3,031 employees (mostly for education and social service programs) that will be funded with non-City funds (e.g., federal and State grants).

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

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8 OSC adjusts City-funded expenditures for surplus transfers and debt defeasances, and includes debt service on bonds issued by TSASC.

9 The City plans to add 3,495 employees between June 30, 2014, and June 30, 2015.

The November 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 Debt Service)
(in millions)

	FY 2014	FY 2015	Annual Growth	FY 2016	FY 2017	FY 2018	Average Three-Year Growth Rate
Salaries and Wages	$ 16,185	$ 15,702	-3.0%	$ 16,479	$ 16,705	$ 18,000	4.7%
Pension Contributions	8,109	8,429	3.9%	8,467	8,330	8,632	0.8%
Medicaid	6,272	6,353	1.3%	6,322	6,322	6,322	-0.2%
Debt Service	5,436	6,374	17.3%	6,719	7,054	7,343	4.8%
Health Insurance	4,280	4,290	0.2%	4,556	4,773	4,999	5.2%
Other Fringe Benefits	2,533	2,743	8.3%	2,851	2,928	3,000	3.0%
Energy	947	920	-2.9%	912	922	965	1.6%
Judgments and Claims	603	572	-5.1%	570	606	642	3.9%
Public Assistance	561	614	9.4%	582	585	585	-1.6%
General Reserve	- - -	750	NA	750	750	750	NA
Retiree Health Benefits Trust	864	- - -	NA	- - -	- - -	- - -	NA
Prior Years' Expenses	(821)	- - -	NA	- - -	- - -	- - -	NA
Other	9,923	10,437	5.2%	10,184	10,330	10,580	0.5%
Total	**$ 54,892**	**$ 57,184**	**4.2%**	**$ 58,392**	**$ 59,305**	**$ 61,818**	**2.6%**

Note: Debt service has been adjusted for surplus transfers and redemptions.
Sources: NYC Office of Management and Budget; OSC analysis

1. Collective Bargaining

In May 2014, the City and the United Federation of Teachers (UFT), which represents the City's teachers and paraprofessionals (33 percent of the workforce), reached a nine-year labor agreement. The UFT agreement compensates teachers and other UFT members for two annual wage increases of 4 percent that were provided to most other municipal unions in 2009 and 2010 but not to members of the UFT.[10] The agreement also increases wages by 10 percent over a seven-year period. The November Plan assumes that these terms will set the wage pattern for all municipal unions with expired labor agreements.

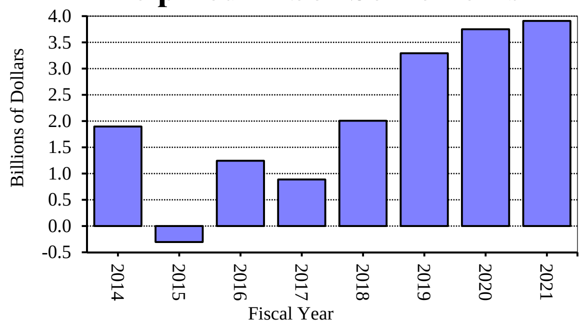
The City estimates that these agreements will cost $13.6 billion during fiscal years 2014 through 2018, but that the cost will be partially offset by resources that had been set aside by the City in its labor reserve prior to reaching the UFT agreement ($3.5 billion), and by new resources ($4.4 billion) that are expected to result from a separate agreement between the City and its unions (see "Health Insurance" later in this section).

[10] The City had set aside resources to increase the wages for members of the UFT by 4 percent in each of calendar years 2009 and 2010, but the City redirected those resources in 2010 to offset a sharp reduction in State education aid, which resulted from the State's efforts to balance its budget during the recession.

The net budgetary impact during fiscal years 2014 through 2018 is expected to total $5.7 billion. The largest budgetary impact will be during fiscal years 2019 through 2021 (see Figure 21). The cost continues to rise after the expiration of the contracts because of lump-sum payments scheduled for those years to compensate members of the UFT and other employees for the time they went without wage increases, as well as the full impact of wage increases granted in prior years.[11]

Figure 21

Net Budgetary Impact of Anticipated Labor Settlements



Sources: NYC Office of Management and Budget; OSC analysis

The City has reached new labor agreements with 71 percent of its unionized workforce, including District Council 37, which represents most civilian employees. The City recently reached tentative agreements with the Council of School Supervisors and Administrators (CSA), and a coalition of eight unions that represent superior uniformed officers. While the CSA agreement is consistent with the economic terms of the UFT agreement, it will cost the City $82 million more than planned through FY 2021 because the City has agreed to compensate employees for the time they worked in nonsupervisory positions (e.g., as teachers). These employees were not compensated under the UFT agreement because they were no longer members of that union.

The agreement with superior officers will increase wages by 11 percent over seven years, one percentage point more than the UFT pattern for this period. The City estimates that this agreement will cost $145 million more than planned during the financial plan period. The Patrolmen's Benevolent Association (which represents police officers) has not yet reached agreement with the City, and the parties have begun binding arbitration.[12]

The UFT agreement also established the Structured Retiree Claims Settlement Fund to settle all claims by retirees who retired between November 1, 2009, and June 30, 2014. Under the agreement, the City's liability is limited to $180 million regardless of the number of retirees. Nearly 17,900 UFT members retired during fiscal years 2010 through 2014, which was more than had been expected. The UFT estimates that an additional $60 million would be needed to fully compensate these retirees for the time they went without pay raises, and the UFT has hired an arbitrator to help identify sources of funding.

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[11] The City estimates that lump-sum payments will total $7.2 billion during fiscal years 2014 through 2021, of which $4.2 billion will be included in the budgets for fiscal years 2019 through 2021 after most contracts expire in 2018.

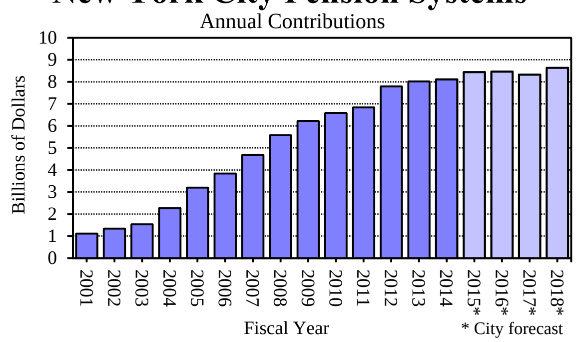
[12] The City would incur additional costs of $465 million during the financial plan period if the economic terms of the agreement with the superior officers was applied to all other uniformed employees.

2. Pension Contributions

After rising rapidly over the past decade, the growth in City-funded pension contributions has slowed significantly in recent years. The slowdown reflects the impact of changes in assumptions and methodologies used to calculate City pension contributions,[13] stronger-than-expected investment returns over the past five years, and savings from the State enactment of new pension plans for City employees hired after March 31, 2012. Nevertheless, pension contributions are projected to increase from $8.1 billion in FY 2014 to nearly $8.6 billion in FY 2018 (see Figure 22), largely because of wage increases to be provided to City employees during this period.

Figure 22

New York City Pension Systems



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

As a result of the Great Recession, the assets of the City's pension funds declined by 23 percent over two years to $85.9 billion in FY 2009. Since then, the assets have nearly doubled to $160.6 billion as of the end of FY 2014. Investment returns have exceeded the expected gains in four of the past five years, and last year the pension systems earned, on average, nearly 17.5 percent on their investments (compared to an expected return of 7 percent). As a result, the City was able to reduce its planned pension contributions in the November Plan by $208 million in FY 2016, $415 million in FY 2017 and $623 million in FY 2018.

The City has implemented new financial reporting standards for state and local government pension plans that were promulgated by the Governmental Accounting Standards Board, one year earlier than required. The City reports that its five pension systems had sufficient assets to fund, on average, 72.5 percent of their accrued pension liabilities as of June 30, 2014. This is an improvement from the prior fiscal year, largely as a result of strong investment earnings in FY 2014.

An independent actuarial consultant recently completed a biennial audit of the pension systems as required by the City Charter. The audit focused on demographic trends, but deferred making any recommendations until a final review is completed in 2015.

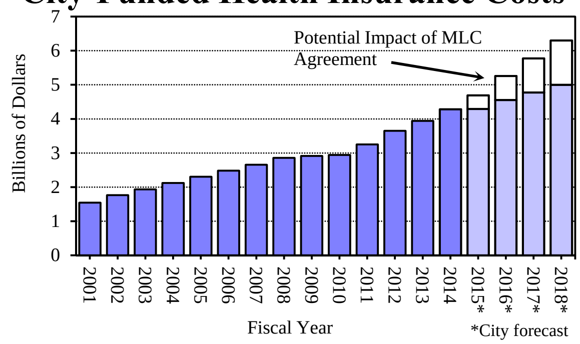
13 These include a longer amortization period for unfunded liabilities, which held down contributions during the financial plan period but will result in higher costs over the longer term.

3. Health Insurance

An agreement between the City and the Municipal Labor Committee (MLC), which represents the City's unions, is expected to generate health insurance savings of $400 million in FY 2015, $700 million in FY 2016, $1 billion in FY 2017 and $1.3 billion in FY 2018, with recurring savings of $1.3 billion. The savings would be used by the City to help fund wage increases for its employees. If the savings are realized as planned, the growth in health insurance costs between fiscal years 2014 and 2018 would slow from a projected average annual rate of 10.1 percent to 4 percent. Nevertheless, health insurance costs would still reach $5 billion by FY 2018 (see Figure 23), which is 27 percent more than the cost in FY 2013.

Figure 23

City-Funded Health Insurance Costs



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

The City reports that it is on track to meet the savings targets for fiscal years 2015 and 2016. Pursuant to the MLC agreement, a joint labor-management committee was formed to identify actions to reduce the cost of health care while at the same time improving the quality of care. The City and the MLC have each hired independent health care actuaries to measure the savings anticipated from agreed-upon initiatives. A number of cost-reduction initiatives have already been implemented and a number of additional actions are planned for the future. Working with a health care cost-management professional, the City has developed a detailed plan of possible actions to achieve, or even exceed, the planned savings target of $3.4 billion during the financial plan period.

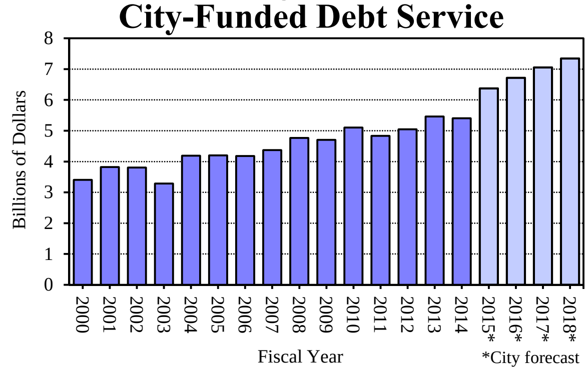
Under the MLC agreement, savings from lower-than-planned increases in health insurance premiums would also be credited toward meeting the targets of the agreement. For example, the City had assumed that health insurance premiums for active employees would grow at an annual rate of 9 percent, which was consistent with historical trends. In the fall of 2014, the State approved an increase in health insurance premiums for FY 2016 of less than 2.9 percent for the Health Insurance Plan of Greater New York (the City's principal insurer). OSC estimates that the lower-than-expected premium increase will generate savings of $335 million in FY 2016, $367 million in FY 2017 and $403 million in FY 2018.

4. Debt Service

In 2003, the City created the Sales Tax Asset Receivable (STAR) Corporation to refinance outstanding debt of the Municipal Assistance Corporation by securitizing annual payments from the New York Local Government Assistance Corporation, which provided budgetary relief of $2.5 billion during fiscal years 2005 through 2008. In October 2014, the City refinanced outstanding STAR debt, which generated debt service savings of about $200 million annually during fiscal years 2016 through 2018.[14] The City will also realize more than $130 million in savings during the financial plan period from refinancing general obligation debt, and will save $75 million in FY 2015 because it will not need to borrow for cash flow purposes given its large cash balance. In total, debt service is expected to be $1.1 billion less during the financial plan period than forecast in June 2014.

Despite these savings, the November Plan assumes that City-funded debt service (adjusted for surplus transfers) will grow by more than $900 million between fiscal years 2014 and 2015 to reach $6.4 billion (see Figure 24), and will reach $7.3 billion by FY 2018. These estimates, however, assume that interest rates for both variable-rate and fixed-rate debt will remain considerably higher than current market conditions, but most economists believe that interest rates will not begin to rise until the beginning of FY 2016. OSC estimates that the City could realize at least $150 million in savings in FY 2015 because interest rates on variable rate debt have averaged less than 1 percent, much less than assumed in the November Plan.

Figure 24
City-Funded Debt Service



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

[14] This refinancing permitted the STAR to transfer $637 million in excess funds to the Transitional Finance Authority, which it used to defease debt due in fiscal years 2016 through 2018.

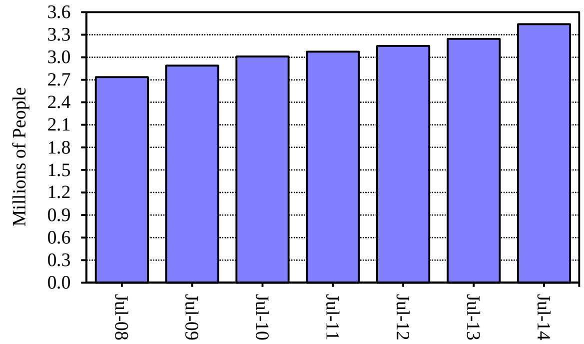
5. Medicaid

After growing steadily since the recession, enrollment in the federal Medicaid program in New York City reached 3.4 million people in July 2014 (see Figure 25). Growth accelerated after January 1, 2014, when provisions of the federal Affordable Care Act (ACA) that require health insurance coverage for most individuals became effective. The November Plan assumes that the City's share of the cost of Medicaid will level off at $6.3 billion in FY 2016 as the State completes a three-year takeover in the growth of the local share of Medicaid.

In October 2014, the United States filed a civil lawsuit against New York City and a computer services vendor, alleging that computer programs were altering billing data, resulting in millions of dollars in fraudulent Medicaid claims. The lawsuit seeks triple damages and penalties, but the potential financial impact on the City has not yet been determined.

Figure 25

Medicaid Enrollment



Sources: NYS Department of Health; OSC analysis

6. Public Assistance

For the past ten years the City's public assistance caseload has remained relatively stable, through recession and recovery, at an average of less than 350,000.[15] This level is less than one-third of the peak reached in 1995, prior to national welfare reform (see Figure 26). At that time, President Clinton signed into law sweeping changes to the nation's welfare system, including placing a time limit on benefits and imposing a work requirement on many recipients.[16] These changes led to dramatic reductions in public assistance enrollment. New York passed the State Welfare Reform Act of 1997 to come into compliance with federal regulations, and New York City greatly expanded the City's Work Experience Program (WEP), which provides work assignments (mainly in City agencies) to people receiving public assistance benefits. The November Plan assumes that enrollment in the public assistance program will remain steady throughout the financial plan period, and that City-funded expenditures for public assistance will average slightly less than $600 million annually.

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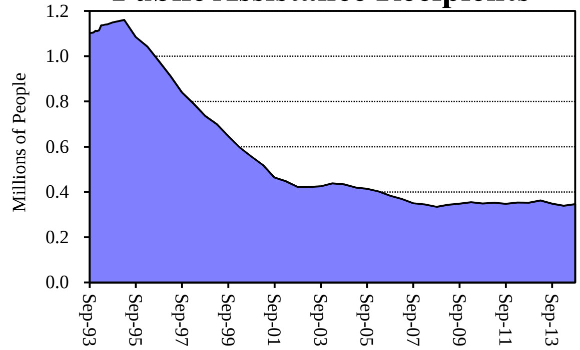
[15] Public assistance consists of temporary cash grants for shelter, utilities and other expenses. Benefits are awarded to eligible clients based on income and resources, household composition and citizenship status. Most recipients are required to engage in work activities.

[16] The 2006 reauthorization of Temporary Assistance to Needy Families (TANF) continued the law's emphasis on work, and imposed financial penalties on states for not meeting required work participation rates.

The City has recently enacted a series of changes to the public assistance program. These include implementing an automated system to remind recipients of mandated appointments, increasing the amount of time clients have to find child care, and developing online systems that will allow recertification of benefits. In October 2014, the Commissioner of the New York City Human Resources Administration also announced a series of changes to the City's employment programs. The changes comply with federal requirements, but allow more education and training programs to count toward work requirements.

Figure 26

Public Assistance Recipients



Source: NYC Human Resources Administration; OSC analysis

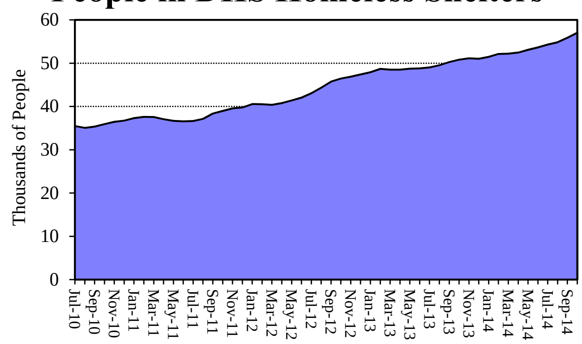
7. Homeless Services

A recent federal assessment found that New York City had the largest homeless population (both sheltered and unsheltered) among the 50 largest cities in the United States in 2014, and one of the highest ratios of homelessness on a per-capita basis.[17] While the number of homeless people declined by 2 percent nationally, it increased by 6 percent in New York City. However, New York City experienced the largest decline (54 percent) in the number of homeless veterans.

In October 2014, more than 57,000 people (see Figure 27), on average, were residing in shelters operated by the Department of Homeless Service (DHS), and nearly half of them were children. This represents an increase of 59 percent in the shelter population in just four years and an increase of 12 percent over the 12 prior months. Much of the growth resulted from the termination of a rent subsidy program for homeless families and individuals by the City in April 2011, following the State's withdrawal of funding.

Figure 27

People in DHS Homeless Shelters



Sources: NYC Human Resources Administration; OSC analysis

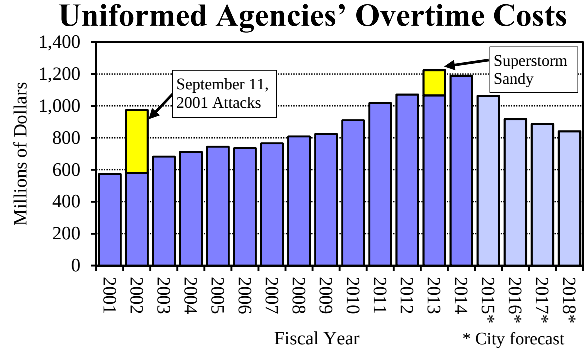
17 The federal assessment estimates are based on one-night counts of sheltered and unsheltered individuals conducted in late January of each year.

Since January 2014, the City has announced a number of initiatives to prevent homelessness and to reduce the number of people in shelters. For example, the DHS has expanded the Homebase prevention program, which provides assistance to families and individuals at risk of homelessness, and those that have recently left the shelter system. In addition, the New York City Housing Authority has given priority to families in shelters (reinstituting a policy that was terminated in 2005), and has already met its annual goal of placing 750 families. Working together, the City and the State have developed three programs that provide temporary rental assistance to help families in homeless or domestic violence shelters. Despite these initiatives, the number of people in homeless shelters continues to rise. The November Plan assumes that the City-funded cost of sheltering homeless people in DHS facilities will reach $445 million in FY 2015, including an additional $36 million to cover the cost of more people residing in shelters. The City expects these costs to then decrease to an average of $416 million annually through FY 2018 based on the assumption that the homeless shelter caseload will decline in those years.

8. Uniformed Agencies

Overtime in the uniformed agencies (i.e., the Police, Fire, Correction and Sanitation departments) set a record of $1.2 billion in FY 2014 (see Figure 28), excluding costs associated with Superstorm Sandy in FY 2013. Overtime exceeded the City's initial forecast by $234 million in FY 2014, and exceeded the City's forecast for the first quarter of the current fiscal year. Even after considering the potential for additional federal grants and savings in other personal service costs, overtime could be higher by $75 million in FY 2015 and by $100 million thereafter.

Figure 28
Uniformed Agencies' Overtime Costs



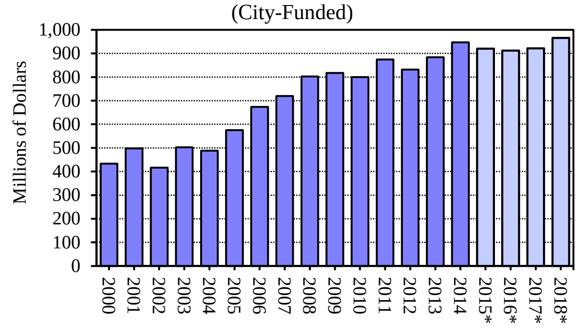
Sources: NYC Comptroller, NYC Office of Management and Budget; OSC analysis

9. Energy

Energy costs (i.e., electricity, fuel and heat) rose sharply between fiscal years 2004 and 2008, mostly as a result of higher prices for oil and natural gas (see Figure 29). Costs remained relatively stable during the next two years, then rose by 9 percent in FY 2011, reflecting a harsh winter. Another cold winter during FY 2014 contributed to record-high costs of $947 million.

The November Plan assumes that energy costs will decline slightly in FY 2015 to $920 million, mostly as a result of lower electric and natural gas prices. In fact, energy costs have declined faster than the City had anticipated during the first five months of the current fiscal year. The City could realize savings if these trends continue, but the actual amount of savings will depend on the severity of the upcoming winter. The November Plan also assumes a slight decline in energy costs in FY 2016, but that costs will begin to rise in FY 2017.

Figure 29
Energy Costs
(City-Funded)

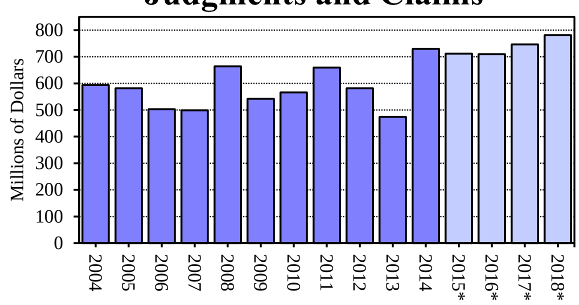


Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

10. Judgments and Claims

The cost of judgments and claims against the City reached a record $730 million in FY 2014 ($603 million excluding costs associated with the Health and Hospitals Corporation), which is nearly 29 percent more than the average annual cost over the ten prior years. Most of the increase comes from claims related to medical malpractice at the City's municipal hospitals, as well as claims related to civil rights violations and police actions. In FY 2014, the City settled a number of long-standing and costly cases, including litigation related to discrimination in the hiring of firefighters, and the Central Park Five case. The November Plan assumes that the cost of judgments and claims will decline slightly in fiscal years 2015 and 2016 before growing to $782 million by FY 2018 (see Figure 30).

Figure 30
Judgments and Claims



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

VI. Semi-Autonomous Entities

As discussed below, a number of semi-autonomous entities have a financial relationship with the City.

1. Department of Education

The November Plan allocates $26.3 billion to the Department of Education (DOE) in FY 2015, which includes the cost of the recent labor agreement with the United Federation of Teachers (UFT). Also included are the Mayor's initiatives to expand full-day prekindergarten and after-school programs for middle-school students, which are funded by the largest increase in State education aid since FY 2008. The City reports that more than 53,000 children were enrolled in full-day prekindergarten programs at the beginning of the current school year, 33,000 more than last year.

Total enrollment at schools operated by the DOE has remained steady over the past five years, at about 1 million students. While enrollment in special education programs has grown, the increase has been offset by a decline in general education enrollment. Nearly 71,000 students were enrolled in charter schools last year, and the City projects that charter school enrollment will increase by more than 10,000 students in the current school year.

The November Plan assumes the receipt of $67 million in federal Medicaid reimbursement in FY 2015 ($97 million annually thereafter) for certain services provided by the DOE to students with special needs. Last year, the DOE anticipated $50 million in Medicaid reimbursements, but now anticipates $15 million because of problems documenting claims.[18] While the DOE submitted $10 million in claims during the first four months of FY 2015, it is too early to conclude that it has overcome problems documenting claims and that it will meet its annual target.

The new UFT labor agreement grants the DOE additional flexibility to reduce the number of teachers assigned to the absent teacher reserve (ATR). The ATR is comprised mostly of teachers who have been displaced from their full-time assignments for various reasons (e.g., school closings and pending disciplinary actions). In July 2014, the DOE offered financial incentives to employees in the ATR to voluntarily leave the payroll. The DOE reports that 115 employees took the incentive and that it also encouraged principals to consider placing ATR teachers back in classrooms. There were 258 fewer employees in the ATR in December 2014 than one year earlier, but the DOE has not yet quantified the budgetary impact.

[18] 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.

2. Health and Hospitals Corporation

The Health and Hospitals Corporation (HHC), the largest municipal hospital system in the country and the largest provider of health care to uninsured City residents, faces serious financial challenges. The HHC relies heavily on Medicaid (which provides 64 percent of total patient revenue), and is significantly affected by State and federal government actions that impact Medicaid.

The HHC has faced a significant structural imbalance in its finances for years, and despite efforts to solve the underlying imbalance, the situation is projected to worsen during the financial plan period unless corrective measures are successfully implemented. The HHC ended FY 2014 with enough cash ($287 million) to meet its needs for 18 days, and operating revenues are projected to grow by 3 percent between fiscal years 2014 and 2018, while operating expenses are expected to grow much faster at 22 percent.

In light of the HHC's poor cash position, the City has provided additional financial assistance. The City covered $750 million of the HHC's financial obligations during fiscal years 2013 and 2014, including the cost of debt service on City bonds issued on the HHC's behalf and the cost of medical malpractice. The City has agreed to forgo repayment of $300 million for FY 2013, and it still has not been reimbursed $450 million for FY 2014. The City has also set aside $1.4 billion to fund new labor agreements at the HHC.

The HHC is counting on the receipt of $1.3 billion in retroactive Medicaid reimbursement in FY 2015, but the claims have not yet been approved by the federal government. It is also counting on the receipt of $2 billion in federal funds over five years (including $384 million in FY 2015) in exchange for reducing utilization of inpatient and emergency room services.[19] The federal government has approved a proposal by New York State that will allow the State to reinvest the federal government's share of savings ($8 billion over five years) anticipated from State actions to lower the cost of Medicaid-related health care. Although the HHC has yet to submit a plan for the State to review (the deadline has been extended to December 22, 2014), implementation is scheduled for April 2015. The HHC will have to meet performance goals to continue to receive funding.

The HHC's Bellevue Hospital Center in Manhattan is one of ten hospitals in the State designated to treat potential patients with Ebola virus, and it treated the first person in New York City to test positive for Ebola (the patient has since recovered and been released). The City is seeking $32 million in federal funding (including $20 million for the HHC) to reimburse for costs related to treating and monitoring Ebola.

[19] The HHC received $152 million in FY 2015 from this pool of funds to provide short-term financial relief.

3. Metropolitan Transportation Authority

In October 2014, OSC issued a report on the July 2014 financial plan of the Metropolitan Transportation Authority (MTA). The report found that the MTA's short-term financial outlook continues to improve with the economy, mostly due to higher-than-anticipated tax revenues and increasing subway ridership as well as to slower growth in costs related to fringe benefits, debt service and energy. As a result, the MTA has been able to reduce its operating budget gaps, reach new labor agreements without raising fares and tolls any faster than already planned, and fund new transit services. The MTA's November Plan shows further improvement in the MTA's finances as subway ridership continues to reach record levels and commercial real estate transaction tax collections continue to rebound. The November Plan projects a balanced budget for calendar years 2014 through 2017, and a budget gap of $322 million in 2018.

Nevertheless, the MTA still faces challenges, perhaps none greater than adequately funding its next capital program without putting the financial burden on riders. The MTA's proposed $32.1 billion capital program for 2015-2019 has a $15.2 billion funding gap. In the absence of new resources, the MTA could be required to close the gap through a combination of program reductions and increased borrowing, which is how it closed most of the funding gap in the current capital program. Each $1 billion borrowed would increase debt service by an amount comparable to a 1 percent increase in fares and tolls. In the months ahead, the MTA will be working closely with its funding partners to fully fund the capital program at an appropriate level.

4. New York City Housing Authority

The New York City Housing Authority (NYCHA) is a critical component of the City's supply of affordable housing. As the City's largest landlord, NYCHA manages approximately 180,000 apartments with more than 400,000 residents. 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 for more than 91,000 private apartments that house 235,000 residents. On average, NYCHA residents pay 30 percent or less of their annual incomes on rent. Currently, more than 247,000 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 subsides (which make up 50 percent of its operating budget and 70 percent of its capital budget) and difficulties making timely repairs. This past year, the City has dedicated more than $210 million to increase safety and improve maintenance operations in NYCHA developments. The strategy includes increasing funding for repairs, targeting law enforcement, improving security lighting and cameras, extending the hours of community and senior centers, and expanding community programs. NYCHA reports that the backlog of work orders for maintenance and repairs has been greatly reduced.

NYCHA reports that it adopted a five-year financial plan on November 26, 2014, and at that time it projected a budget gap of $98 million for calendar year 2015, along with larger gaps in subsequent years. NYCHA is currently in negotiations to sell a stake in certain NYCHA-owned apartment buildings, which is expected to generate several hundred million dollars to help close operating budget gaps and help fund capital improvements.

VII. Other Issues

As discussed below, a number of other issues could affect the November Plan.

1. Superstorm Sandy Recovery

According to the City's most recent estimates, the effects of Superstorm Sandy could cost about $8.4 billion. Of this amount, $2.3 billion represents storm-related operating expenses (such as emergency repairs, debris removal and overtime), and $6.1 billion represents capital costs for permanent work to repair or replace damaged infrastructure, and to mitigate future risks. These estimates include costs for the New York City Health and Hospitals Corporation and the New York City Housing Authority.

So far, the Federal Emergency Management Agency (FEMA), along with other federal agencies, have agreed to reimburse the City $2.2 billion, mostly for operating expenses. The reimbursement process for capital repairs and mitigation is proceeding more slowly, and will require a local match of $610 million even if all claims are deemed eligible for reimbursement by FEMA and insurance. The City is working with FEMA and other federal agencies to maximize reimbursement.

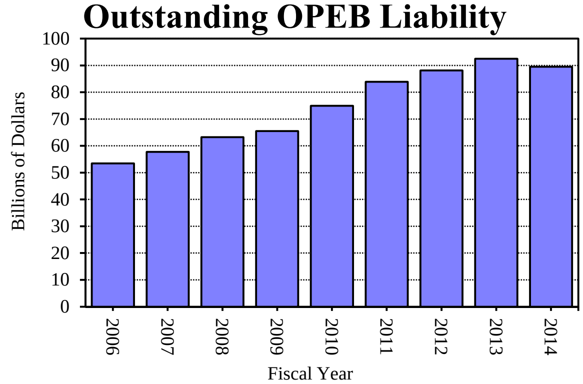
The City also has been allocated $4.2 billion in Community Development Block Grant-Disaster Recovery funding. While the City intends to use most of these funds for housing recovery and infrastructure resiliency projects, about one-quarter has been set aside to fill gaps in FEMA funding. While the November Plan assumes that all of the costs related to the storm will be covered with federal funds, no assurance has been given that the City will be reimbursed for all of its costs.

2. Other Post-Employment Benefits

The City estimates that its unfunded liability for post-employment benefits other than pensions (OPEBs) declined by $3 billion to $89.5 billion in FY 2014, the first decline since the City began reporting its liability in 2006 (see Figure 31). The decline reflects lower-than-expected growth in health insurance premiums and an increase in the City's contribution to the OPEB trust during FY 2014.

Figure 31

Outstanding OPEB Liability



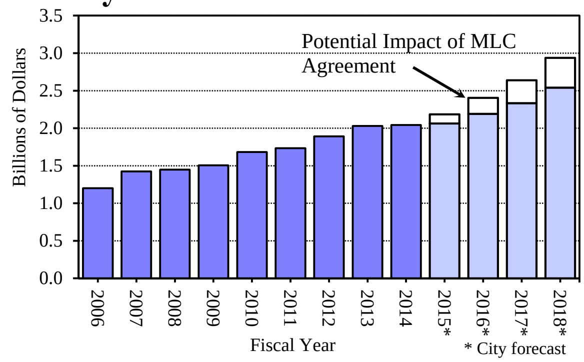
Sources: NYC Actuary; OSC analysis

However, the Governmental Accounting Standards Board (GASB) is considering two draft statements that, if implemented, could increase the City's OPEB liability. The proposed changes would conform the standards for measuring OPEB liabilities with those for pension liabilities. In addition, entities that do not fund their OPEB liabilities on an actuarial basis would be required to discount future costs using an interest rate that is lower than the entity's assumed rate of return on investments.

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 nearly $2.5 billion in FY 2018 (see Figure 32), an increase of 25 percent in five years. These estimates reflect the City's expectation that an agreement between the City and the municipal unions to reduce the cost of municipal health insurance will also reduce the rate of growth in the cost of OPEBs.

Figure 32

Pay-As-You-Go Cost of OPEBs

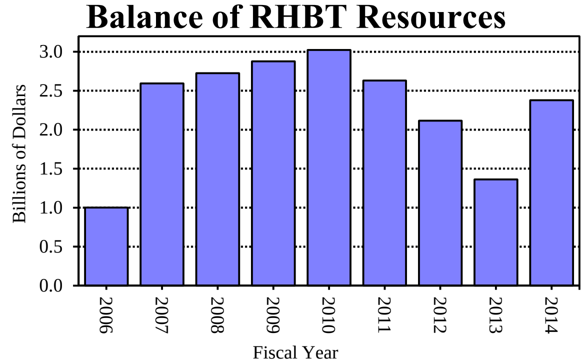


Sources: NYC Office of Management and Budget; OSC analysis

In FY 2006 the City established the Retiree Health Benefits Trust (RHBT) and deposited $2.5 billion of surplus resources into the trust in fiscal years 2006 and 2007 to help fund the future cost of OPEBs. These resources were invested and earned interest, with the balance peaking at more than $3 billion in FY 2010 (see Figure 33). Although the RHBT was intended to help fund a future liability, the City has used it as a rainy-day fund to help balance the budget. The City drew down much of the resources in the RHBT during fiscal years 2011 through 2013, 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 revenues grew much faster than the City had anticipated at the beginning of the fiscal year, which permitted the City to rescind the planned transfer and to add $864 million (leaving a balance of $2.4 billion at the end of FY 2014).

Figure 33

Balance of RHBT Resources



Note: Adjusted for prepayments.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

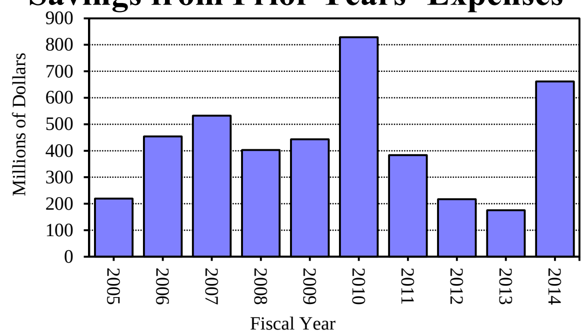
3. Prior Years' Expenses

At the end of each fiscal year, the City estimates the amount of expenses that have been incurred but not yet paid, and the amount of revenues earned but not yet received. The City generally makes conservative estimates because an unfunded liability has a budgetary impact in the current fiscal year. Over the past ten years, the City has realized net resources averaging $432 million annually from overestimating prior years' expenses and from underestimating prior years' receivables. The November Plan does not anticipate any resources from this source during the financial plan period.

In FY 2014, the City realized a net benefit of $662 million (see Figure 34). The benefit resulted largely from an overestimation of prior years' expenses in the Department of Education (nearly $1.4 billion), mostly for contractual special education services, partly offset by a reduction in associated federal and state categorical education aid ($612 million). The net benefit was further reduced when the City wrote off $300 million that the Health and Hospitals Corporation (HHC) owed the City for payments made on the HHC's behalf in FY 2013 (largely for debt service and medical malpractice reimbursement) because the HHC continues to experience cash flow difficulties.

Figure 34

Savings from Prior Years' Expenses



Note: Adjusted for annual changes in prior-year receivables.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

4. Rent Stabilization

The City's rent stabilization laws are set to expire on June 15, 2015. While these laws have been extended many times, the State Legislature has made modifications in the past. In 1993, the Legislature passed a provision that allowed units to be removed from rent stabilization based upon the income of the tenant or the rent level of the apartment. In 2011, the last time the laws were extended, the State Legislature raised the deregulation annual income threshold to $200,000 and the monthly rent threshold to $2,500. According to the New York City Rent Guidelines Board, deregulation has contributed to the loss of at least 139,000 rent-stabilized units from 1994 to 2013.

Appendix A: Nonrecurring Resources

As shown in Figure 35 and discussed below, OSC estimates that the November Plan includes nonrecurring resources of $3.4 billion in FY 2015 and $966 million in FY 2016.

Figure 35
Nonrecurring Resources
(in millions)

	FY 2015	FY 2016
Surplus Transfers (Net)	$ 1,901	$ 105
Health Stabilization Fund	1,000	- - -
Debt Refinancings (Net)	369	112
TFA Redemption	99	103
Taxi Medallion Sales	47	312
STAR Refinancing	16	234
HPD Mortgage Sale	- - -	100
Total	**$ 3,432**	**$ 966**

Sources: NYC Office of Management and Budget; OSC analysis

- Surplus resources accumulated in prior years will be used to help balance the budget in fiscal years 2015 and 2016.
- The City plans to transfer $1 billion from the Health Stabilization Fund to help fund the cost of labor settlements.
- Historically low interest rates in recent years have permitted the City to refinance outstanding debt, generating savings of $369 million in FY 2015 and $112 million in FY 2016.
- The City used $196 million in resources generated in FY 2013 to redeem Transitional Finance Authority debt due in future years, which lowered debt service by $99 million in FY 2015 and $103 million in FY 2016.
- The sale of taxi medallions is expected to generate $47 million in FY 2015 and $312 million in FY 2016.
- Refinancing debt of the Sales Tax Asset Receivable Corporation generated savings of $16 million in FY 2015 and $234 million in FY 2016.
- The Department of Housing Preservation and Development (HPD) plans to sell $100 million in mortgages to the Housing Development Corporation in FY 2016.

Appendix B:
Staffing Levels

Between fiscal years 2008 and 2012, the City-funded workforce (full-time and full-time-equivalent employees) declined by 15,666 employees (5.8 percent), reflecting the impact of agency cost-reduction initiatives in response to the recession. Staffing levels rose by about 2,000 employees in each of fiscal years 2013 and 2014, concentrated mainly in education. The City plans to add an additional 3,495 employees during FY 2015 (excluding temporary employees), which would increase staffing to 261,341 employees by the end of the fiscal year (see Figure 36). Most of the additions are planned for the following agencies.

- The health and welfare agencies plan to add 1,933 employees during FY 2015, including 700 employees at the Administration for Children's Services, 535 employees at the Department of Health and Mental Hygiene, and 333 employees at the Department of Social Services. However, these agencies added 790 fewer employees than planned during the first quarter of the fiscal year.
- The Department of Correction plans to add 592 employees (286 uniformed and 306 civilians), mainly to improve security and inmate discharge planning.
- The Fire Department plans to add 463 employees to increase uniformed staffing to 10,780 positions (the highest level since February 2011).
- The Department of Education plans to add 540 pedagogues, mostly to staff special education programs. (The department also added more than 900 employees to staff an expansion of full-day prekindergarten and after-school programs, which will be funded by an increase in State education aid.)
- The Police Department plans to add 298 civilians, including administrative aides to allow police officers to be redeployed to patrol functions and traffic enforcement agents for the Mayor's Vision Zero initiative. The police force will average nearly 34,500 officers during the financial plan period, nearly 1,300 fewer officers than on June 30, 2006, before force levels began to decline.
- The November Plan also assumes that the City's district attorneys will reduce their staffing levels by 716 employees during FY 2015.

Figure 36
City-Funded Staffing Levels
(Full-Time and Full-Time-Equivalents)

Additions (Reductions)

		Actual		*Forecast*	*Variance*	
		June 2012	June 2014	June 2015	June 2012 to June 2014	June 2014 to June 2015
Public Safety		**79,883**	**80,869**	**81,571**	**986**	**702**
Police	Uniformed	34,406	34,440	34,483	34	43
	Civilian	15,679	15,993	16,291	314	298
Fire	Uniformed	10,254	10,317	10,780	63	463
	Civilian	5,110	5,190	5,195	80	5
Correction	Uniformed	8,519	8,922	9,208	403	286
	Civilian	1,447	1,390	1,696	(57)	306
District Attorneys & Prosecutors		3,690	3,852	3,136	162	(716)
Probation		766	749	761	(17)	12
Board of Correction		12	16	21	4	5
Health and Welfare		**22,598**	**22,134**	**24,067**	**(464)**	**1,933**
Social Services		10,090	10,038	10,371	(52)	333
Children’s Services		6,097	5,773	6,473	(324)	700
Health & Mental Hygiene		4,268	4,148	4,683	(120)	535
Homeless Services		1,762	1,759	1,977	(3)	218
Other		381	416	563	35	147
Environmental & Infrastructure		**17,085**	**17,940**	**18,424**	**855**	**484**
Sanitation	Uniformed	6,882	7,081	7,239	199	158
	Civilian	1,888	1,896	2,189	8	293
Transportation		2,005	2,001	2,258	(4)	257
Parks & Recreation		6,092	6,760	6,504	668	(256)
Other		218	202	234	(16)	32
General Government		**9,148**	**9,593**	**10,620**	**445**	**1,027**
Finance		1,814	1,870	2,035	56	165
Law		1,348	1,451	1,392	103	(59)
Citywide Administrative Services		1,397	1,352	1,666	(45)	314
Taxi & Limousine Commission		461	592	722	131	130
Investigations		192	212	291	20	79
Board of Elections		768	624	360	(144)	(264)
IT & Telecommunications		963	1,071	1,320	108	249
Other		2,205	2,421	2,834	216	413
Housing		**1,522**	**1,528**	**1,702**	**6**	**174**
Buildings		1,067	1,073	1,177	6	104
Housing Preservation		455	455	525	0	70
Department of Education		**113,584**	**114,896**	**114,661**	**1,312**	**(235)**
	Pedagogues	91,841	93,344	93,884	1,503	540
	Non-Pedagogues	21,743	21,552	20,777	(191)	(775)
City University of New York		**7,815**	**8,633**	**7,828**	**818**	**(805)**
	Pedagogues	5,048	5,544	5,116	496	(428)
	Non-Pedagogues	2,767	3,089	2,712	322	(377)
Elected Officials		**2,297**	**2,253**	**2,468**	**(44)**	**215**
Total		**253,932**	**257,846**	**261,341**	**3,914**	**3,495**

Note: Excludes 1,115 temporary employees at the Board of Elections who have already left the payroll.
Sources: NYC Office of Management and Budget; OSC analysis