Review of the Financial Plan of the City of New York

Report 10-2019

OFFICE OF THE NEW YORK STATE COMPTROLLER
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Message from the Comptroller

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As the State's chief financial officer, I have a constitutional and statutory responsibility to monitor the finances of the City of New York.

This report discusses the economic, fiscal and social challenges facing New York City in an effort to promote an informed discussion. I encourage every City stakeholder to learn more about these issues and to participate fully in the public debate.

Thomas P. DiNapoli
State Comptroller

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I. Executive Summary

New York City's economy continues to set records, although external risks are growing. A total of 820,400 jobs were added between 2009 and 2018, the largest and longest job expansion in the post–World War II period. Employment set an annual record of 4.55 million in 2018, 721,800 higher than the prerecession level in 2008.

The unemployment rate fell to 4.1 percent in 2018, the lowest annual rate on record. In addition, tourism set a new record, consumer confidence is at an 18-year high and wages continue to rise (helped by the increase in the minimum wage).

Preliminary employment data had suggested that the pace of job growth in New York City had slowed, but revised data shows that job growth remains strong. In 2018, the City added 86,600 jobs (14,000 more than previously reported), on par with gains in the two prior years. However, the City expects job growth to slow.

The February Plan projects a surplus of $3.2 billion in FY 2019 (see Figure 1), which will be used to balance the FY 2020 budget. The surplus results mostly from a drawdown of unneeded reserves in the current fiscal year, resources from the citywide savings program and higher-than-expected revenues.

Since June 2018, the City has raised its revenue forecast for FY 2019 by $969 million, driven mostly by higher tax collections ($604 million), despite a large shortfall in estimated personal income tax payments.

Estimated payments on nonwage income fell by $1.2 billion in December and January. While the City had anticipated much of the decline, collections were still short by $433 million. New York State and other jurisdictions with high tax burdens had similar experiences.

Many believe that changes in federal tax policies, such as a cap on the deductibility of state and local taxes, may have encouraged high-income taxpayers (who are responsible for a large share of personal income tax collections) to utilize strategies, such as a change in residency, to reduce their state and local tax liabilities. Other factors, such as the record drop in the financial markets in December 2018, could have contributed to the falloff in estimated payments.

The City believes nearly half of the shortfall will be recovered by the end of the current fiscal year and that other sources of personal income tax revenue will more than offset the remaining shortfall. Changes in taxpayer behavior in response to revisions in federal tax policies are difficult to predict, increasing the level of uncertainty in the City's tax projections.

Although the City has closed the FY 2020 budget gap, it projects budget gaps of $3.5 billion in FY 2021, $2.9 billion in FY 2022 and $3.3 billion in FY 2023. The gaps reflect the cost of wage increases for the municipal work force, higher costs for debt service and health insurance, and an anticipated slowdown in job growth and tax collections. While sizable, the out-year budget gaps are manageable under current conditions.

City-funded spending is projected to increase by 3.4 percent in FY 2020 (excluding reserves), faster than the local inflation rate. While the revenue and expenditure projections in the February Plan are generally reasonable (see Figure 2), there are risks that the City may need to address during the financial plan period.

The most immediate risk is the potential impact of the State budget. On January 15, 2019, the Governor released his executive budget for State fiscal year (SFY) 2019-2020. The budget includes a number of proposals that could have an adverse impact on the City's financial plan. The City estimates that the impact could total as much as $589 million in FY 2020.

The largest risk to the City's financial plan remains the potential for an economic setback. While the City's economy remains strong, the national economy appears more vulnerable than in recent years, and an economic setback could make closing the out-year budget gaps more difficult. Another risk is the possibility of federal budget cuts during the financial plan period given the growing federal deficit, which is projected to exceed $1 trillion in the coming years.

In addition, City pension fund investment earnings have trailed expectations for most of the fiscal year. A shortfall could require the City to increase its contributions to the pension funds beginning in FY 2021.

The regional transportation system operated by the Metropolitan Transportation Authority (MTA) is critically important to the City's economy. However, it is facing its greatest crisis in decades. Service has deteriorated and subway ridership has fallen despite the largest job expansion in the City's history.

The MTA projects a balanced operating budget for 2019, but it projects out-year budget gaps that grow from $467 million in 2020 to nearly $1 billion in 2022. The gaps remain even after planned fare and toll increases of 4 percent in 2019 and 2021.

While the MTA is seeking new sources of funding from the State to help close the projected budget gaps, it recently directed its agencies to identify $500 million in recurring savings beginning in 2020. In addition, the MTA has warned that it may need to reduce services or increase fares and tolls more than planned to close the projected budget gaps in its operating budget. The MTA is also seeking additional funding for its capital program.

The Governor and the Mayor recently announced an agreement to transform and fund the MTA. The agreement calls for the consolidation and streamlining of all common functions; congestion pricing and other new sources of funding for the MTA's capital program; limiting mass transit fare increases to 2 percent per year through cost-containment; increased efforts to combat fare evasion; and increased oversight of the MTA's capital program. It remains to be seen whether these initiatives will be sufficient to close the out-year budget gaps and fund the MTA's capital needs.

The City's financial plan for fiscal years 2020 through 2023 includes a general reserve of $1 billion annually and a capital stabilization reserve of $250 million annually. Given the risks facing the City and the size of the out-year budget gaps, the Mayor has asked the agencies to identify an additional $750 million in recurring savings. These resources could be used to mitigate the impact of adverse developments or to narrow the projected budget gaps.

FIGURE 1
New York City Financial Plan
(in millions)

	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
Revenues					
Taxes					
General Property Tax	$ 27,865	$ 29,529	$ 30,909	$ 32,150	$ 33,110
Other Taxes	31,759	32,389	33,138	34,059	35,064
Tax Audit Revenue	1,057	998	721	721	721
Subtotal: Taxes	$ 60,681	$ 62,916	$ 64,768	$ 66,930	$ 68,895
Miscellaneous Revenues	7,633	6,799	6,772	6,747	6,735
Unrestricted Intergovernmental Aid	151	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(2,154)	(1,794)	(1,796)	(1,794)	(1,792)
Disallowances Against Categorical Grants	91	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 66,402	$ 67,906	$ 69,729	$ 71,868	$ 73,823
Other Categorical Grants	1,198	926	868	862	862
Inter-Fund Revenues	690	661	662	661	661
Federal Categorical Grants	8,471	7,327	7,205	7,133	7,120
State Categorical Grants	15,258	15,390	15,837	16,305	16,353
Total Revenues	**$ 92,019**	**$ 92,210**	**$ 94,301**	**$ 96,829**	**$ 98,819**
Expenditures					
Personal Service					
Salaries and Wages	$ 29,016	$ 30,240	$ 31,258	$ 31,115	$ 31,642
Pensions	9,850	9,951	10,418	10,864	11,070
Fringe Benefits	10,643	11,536	12,028	12,705	13,385
Subtotal: Personal Service	$ 49,509	$ 51,727	$ 53,704	$ 54,684	$ 56,097
Other Than Personal Service					
Medical Assistance	5,915	5,915	5,915	5,915	5,915
Public Assistance	1,595	1,617	1,617	1,617	1,617
All Other	31,524	29,319	29,469	29,759	29,942
Subtotal: Other Than Personal Service	$ 39,034	$ 36,851	$ 37,001	$ 37,291	$ 37,474
Debt Service	6,737	7,345	7,658	8,337	9,086
FY 2018 Budget Stabilization & Discretionary Transfers	(4,576)	- - -	- - -	- - -	- - -
FY 2019 Budget Stabilization	3,169	(3,169)	- - -	- - -	- - -
Capital Stabilization Reserve	- - -	250	250	250	250
General Reserve	300	1,000	1,000	1,000	1,000
Less: Intra-City Expenses	(2,154)	(1,794)	(1,796)	(1,794)	(1,792)
Total Expenditures	**$ 92,019**	**$ 92,210**	**$ 97,817**	**$ 99,768**	**$ 102,115**
Gap to be Closed	**$ - - -**	**$ - - -**	**$ (3,516)**	**$ (2,939)**	**$ (3,296)**

Source: NYC Office of Management and Budget

FIGURE 2
Office of the State Comptroller (OSC)
Risk Assessment of the New York City Financial Plan
(in millions)

	Better/(Worse)				
	FY 2019	**FY 2020**	**FY 2021**	**FY 2022**	**FY 2023**
Gaps Per NYC Financial Plan	**$ - - -**	**$ - - -**	**$ (3,516)**	**$ (2,939)**	**$ (3,296)**
Tax Revenues	225	125	- - -	- - -	- - -
Miscellaneous Revenues	75	125	125	125	125
Debt Service	- - -	50	- - -	- - -	- - -
Uniformed Agency Overtime	(70)	(70)	(70)	(70)	(70)
Pension Contributions	(105)	(105)	- - -	- - -	- - -
Department of Education	(170)	(170)	(170)	(170)	(170)
Fair Fares	- - -	- - -	(212)	(212)	(212)
OSC Risk Assessment	**(45)**	**(45)**	**(327)**	**(327)**	**(327)**
Potential Gaps Per OSC[1,2]	**$ (45)**	**$ (45)**	**$ (3,843)**	**$ (3,266)**	**$ (3,623)**

[1] The February Plan includes a general reserve of $300 million in FY 2019 and $1 billion in each of fiscal years 2020 through 2022. In addition, the Capital Stabilization Reserve has a balance of $250 million in each of fiscal years 2020 through 2023. If not needed, these resources could be used to help close the projected budget gaps. The February Plan also includes reserves ($100 million in each of fiscal years 2019 and 2020, rising to $400 million beginning in FY 2021) to fund potential changes in the actuarial assumptions and methodologies used to calculate employer pension contributions.

[2] The Retiree Health Benefits Trust, which the City has used in the past as a rainy-day fund, has a balance of nearly $4.5 billion (net of any prepayments).

II. Changes Since the Beginning of the Fiscal Year

The City has made a number of changes to its revenue and expenditure forecasts since the budget was adopted in June 2018. As a result, the City now projects a surplus of $3.2 billion in FY 2019, mostly from a drawdown of unneeded reserves, resources from the citywide savings program and an increase in its revenue forecast (see Figure 3, next page).

Since July 1, 2018, the City has freed up nearly $1.2 billion in reserves in FY 2019 by reducing the general reserve (by $825 million) and the reserve for federal and State disallowances (by $106 million), and by eliminating the capital stabilization reserve ($250 million). The City also anticipates savings from overestimating prior years' expenses ($400 million).

The citywide savings program is expected to generate $1.1 billion in FY 2019 (including a one-time reimbursement of $372 million from the Health and Hospitals Corporation) and about half that amount in subsequent years. The Mayor has announced that he will expand the savings program by $750 million in his executive budget.

The mayoral agencies are expected to contribute $493 million in FY 2019 and smaller amounts in subsequent years. Most of these savings are expected to come from not filling vacant positions and from procurement savings. Savings from lower debt service are expected to generate $234 million in FY 2019 and nearly $800 million through FY 2022. Efficiencies are only a small part of the savings program.

Since June 2018, the City has raised its revenue forecast by $969 million, driven mostly by higher tax collections. While the City has benefited from a number of one-time actions ($257 million), tax collections are expected to be $604 million higher than forecast at the start of the fiscal year.

Although estimated personal income tax payments were down by $1.2 billion in December and January, much of the decline was anticipated by the City. While collections still fell short of expectations, the City believes nearly half of the shortfall will be recovered by the end of the fiscal year and that other sources of personal income tax payments will more than offset the remaining shortfall. Thus, despite the adverse development, the personal income tax collections are expected to be $67 million higher than projected at the start of the fiscal year.

The combination of unneeded reserves, the citywide savings program and higher revenues was more than enough to offset the impact of higher labor costs in fiscal years 2019 and 2020 (for more detail, see Section V, "Expenditure Trends") and to fund some relatively small agency needs (mostly for social services and education). The City also funded a new initiative to provide care to New Yorkers without health insurance ($25 million in FY 2020, rising to $100 million annually by FY 2022).

The City also benefited from better-than-expected pension fund investment earnings in FY 2018. Last year, the funds earned 8.7 percent on their investments, compared to an expected gain of 7 percent. As a result, the City was able to reduce its planned pension contributions by $50 million in FY 2020, $92 million in FY 2021 and $151 million by FY 2022. However, investments in the current year are trailing behind the actuarial expectation for the year.

On March 1, 2019, Moody's Investors Service upgraded the City's credit rating on general obligation bonds to Aa1 from Aa2, reflecting the strength and the diversification of the economy.

The February Plan projects budget gaps of $3.5 billion in FY 2021 and $2.9 billion in FY 2022, as well as a budget gap of $3.3 billion in FY 2023. These gaps are still relatively small as a share of City fund revenues (averaging 4.5 percent), but they do not reflect the potential impact of federal and State actions. The budgets for these years each include a general reserve of $1 billion ($300 million remains in FY 2019) and a capital stabilization reserve of $250 million, which, if not needed for other purposes, could be used to narrow the gaps.

FIGURE 3
Financial Plan Reconciliation—City Funds
February 2019 Plan vs. June 2018 Plan
(in millions)

	Better/(Worse)			
	FY 2019	FY 2020	FY 2021	FY 2022
Projected Gaps Per June 2018 Plan	**$ - - -**	**$ (3,260)**	**$ (2,889)**	**$ (2,285)**
Tax Reestimates				
Real Estate Transactions	228	15	(33)	(51)
Business Taxes	90	3	(21)	76
General Property Taxes	76	234	198	448
Personal Income	67	24	(81)	12
Sales Taxes	47	2	(52)	(39)
Tax Audits	- - -	275	- - -	- - -
Other Taxes	96	12	(5)	(11)
Subtotal	**604**	**565**	**6**	**435**
Other Revenue Reestimates				
Proceeds from Sale of City Property	118	- - -	- - -	- - -
Bank Settlement	78	- - -	- - -	- - -
Federal Reimbursement for NYPD Protective Service for the United Nations	61	- - -	- - -	- - -
All Other	107	(11)	(14)	(16)
Subtotal	**365**	**(11)**	**(14)**	**(16)**
Total Revenue Reestimates	**969**	**554**	**(8)**	**419**
Citywide Savings Program				
Agency Actions	493	406	341	317
Health and Hospitals Corporation Reimbursement	372	- - -	- - -	- - -
Debt Service	234	129	198	223
Total	**1,099**	**535**	**539**	**540**
Reserves				
General Reserve	825	- - -	- - -	- - -
Capital Stabilization Reserve	250	- - -	- - -	- - -
Disallowances of Federal and State Aid	106	- - -	- - -	- - -
Total	**1,181**	- - -	- - -	- - -
Net Cost of Collective Bargaining	**(227)**	**(704)**	**(967)**	**(1,444)**
Expenditure Reestimates				
New Agency Needs	(213)	(333)	(275)	(298)
Pension Contributions	- - -	50	92	151
Prior-Years' Expenses	400	- - -	- - -	- - -
All Other	(39)	(12)	(9)	(23)
Net Change During FY 2019	**3,169**	**90**	**(628)**	**(655)**
Surplus/(Gap)	**$ 3,169**	**$ (3,169)**	**$ (3,516)**	**$ (2,939)**
Surplus Transfer	(3,169)	3,169	- - -	- - -
Projected Gaps Per February 2019 Plan	**$ - - -**	**$ - - -**	**$ (3,516)**	**$ (2,939)**

Note: Columns may not add due to rounding.

Sources: NYC Office of Management and Budget; OSC analysis

III. Potential Impact of State and Federal Actions

On January 15, 2019, the Governor released his executive budget for State fiscal year (SFY) 2019-2020. The budget includes a number of proposals that could have an adverse impact on the City's financial plan. The City estimates that this could total as much as $589 million in FY 2020 (see Figure 4).[3]

FIGURE 4

City Assessment of Governor's Executive Budget

(City funds in millions) Better (Worse)

	FY 2020
School Aid	$ (300)
Cost Shifts	(197)
Election Reforms	(120)
Lead-Based Paint Inspections	(60)
Speed Cameras	(41)
Other Costs	(41)
Tax on Internet Sales	170
Net Change	**$ (589)**

Sources: NYC Office of Management and Budget

After the initial release of the Governor's proposed budget, State tax collections for January fell far short of expectations. To help mitigate the impact, the Governor proposed statewide reductions in Medicaid ($1 billion over the next two fiscal years). In mid-March, the State budget director indicated that these cuts will not be pursued in final budget negotiations with the Legislature.

In addition, the Governor has proposed authorizing the budget director to reduce State aid to localities by up to 3 percent in the event that State tax receipts fall short of the executive budget forecast for SFY 2019-2020 by more than $500 million. Certain programs, such as most education aid, public assistance and Medicaid, would be exempt from the cuts. The budget director would continue to be authorized to take certain steps to manage significant reductions in federal aid should they arise.

The executive budget recommends increasing State education aid to New York City by $282 million in FY 2020, $148 million less than the February Plan assumes. The City would be eligible to apply for a share of $50 million in statewide competitive grants and $157 million in fiscal stabilization grants.

The Governor proposes requiring school districts, including New York City, to dedicate an amount equal to up to 75 percent of the increase in foundation aid to underfunded high-needs schools ($152 million). Although similar to the City's Fair Student Funding program, the initiative could limit the City's budgetary flexibility.

The executive budget also includes a number of actions that would shift financial responsibility from the State to the City. For example, the Governor has proposed reducing the State reimbursement for certain public health programs from 36 percent to 20 percent. The State and the City estimate that this change could increase the City's costs by between $54 million and $59 million annually.

The Governor's budget would also require the City to fund 10 percent of the cost of the Family Assistance program. The State and the City, however, have not reached a consensus on the possible budgetary impact. The State believes the initiative could increase the City's costs by $72 million, while the City believes the impact could total $125 million annually.

The City has indicated that the Governor's proposed budget includes a number of new unfunded mandates. For example, the Governor would require employers to provide employees with up to three hours of paid leave to vote in any election. The City estimates that the loss of productive time could cost $120 million annually, but the budgetary impact could be much lower.

[3] The Governor and the Mayor subsequently agreed to allocate a portion of the revenue from a proposed tax on internet sales to the Metropolitan Transportation Authority.

The executive budget also would require owners of residential rental property constructed prior to January 1, 1978, to ensure that their property is certified to meet certain minimum standards for lead-based paint to be promulgated by the State's Health Commissioner. While the City's Department of Housing Preservation and Development would be responsible for enforcing the proposed law, it is unclear who would bear the cost of inspections. The City estimates that its costs could increase by $60 million annually if it is required to perform the inspections.

While the executive budget would authorize the City to install speed cameras in an additional 150 school speed zones (for a total of 290 zones), the revenue would be remitted to the Metropolitan Transportation Authority (MTA), and the cost of installing and maintaining the cameras would be borne by the City.

The Governor's budget would also require internet marketplace providers (such as Amazon and eBay) to collect sales taxes from third-party sellers that use their platforms. This initiative will generate an additional $160 million in sales tax revenues for the City in FY 2020 and similar amounts in subsequent years.[4]

Both the State and the City had assumed that these resources would be available to mitigate the adverse impact of other State initiatives. However, subsequent to the release of the 30-day amendments, the Governor and the Mayor announced an agreement to transform and fund the MTA. Under the agreement, some of the revenues from the new tax on internet sales would be devoted to the MTA's capital program.

The State would also remind certain out-of-state internet retailers (those whose sales in New York exceed $300,000 or 100 transactions) that they are required under current State law to collect and remit sales taxes on transactions that originate in New York State. This enforcement action, which does not require legislative approval, will generate $48 million for the City in FY 2020, according to State estimates.

Under a State law enacted two years ago, the age of criminal responsibility for most crimes was raised from 16 years to 17 years beginning on October 1, 2018, and will be raised to 18 years on October 1, 2019. The City estimates the cost of implementing the initiative at $108 million in FY 2019, reaching $131 million in FY 2020. Last year, the State appropriated $100 million for State and local costs associated with the initiative, and the City submitted an application for partial reimbursement. The Governor's executive budget includes $200 million in SFY 2019-2020 for the same purpose.

Last year, the State budget required the City to match the State's $50 million capital contribution to the Hudson River Park for SFY 2018-2019. The Governor is proposing that the City match the State's additional capital contribution of $23 million for SFY 2019-2020.

The February Plan does not reflect future increases in per-pupil charter-school tuition rates mandated by State law. The City estimates that these changes could increase its costs by $119 million in FY 2020, $281 million in FY 2021, $478 million in FY 2022, and $758 million in FY 2023 if not offset by increases in State education aid. The City's estimates are based on preliminary data and are subject to change.

The City also receives significant funding from the federal government. At various times, federal officials have proposed changes in federal law and programs that could have had an adverse impact on the City. The President's proposed budget for the coming federal fiscal year, for example, would cut total funding for social safety net and nondefense discretionary programs.

[4] The effective date of this proposal was advanced by three months in the Governor's 30-day amendments, raising the expected amount to $160 million from $122 million.

IV. Revenue Trends

The City added 820,400 jobs between 2009 and 2018, the largest and longest job expansion in the post–World War II period. Employment reached a record of 4.55 million in 2018, 721,800 higher than the prerecession level.

The unemployment rate fell to 4.1 percent in 2018, the lowest rate since the current series began in 1976. In addition, tourism set a new record in 2018, consumer confidence is at an 18-year high and wages continue to rise (helped by the increase in the minimum wage).

Preliminary employment data had suggested that the pace of job growth in New York City had slowed, but revised data shows that job growth remains strong. In 2018, the City added 86,600 jobs (14,000 more than previously reported), on par with gains in the two prior years. The February Plan assumes job growth will slow to 54,800 jobs in 2019, which would be the smallest gain since 2010.

Revenues, including federal and State categorical aid, are projected to reach $92.2 billion in FY 2020. Locally generated revenues (i.e., City funds) are projected to total $67.9 billion, of which $62.9 billion would come from tax revenues.

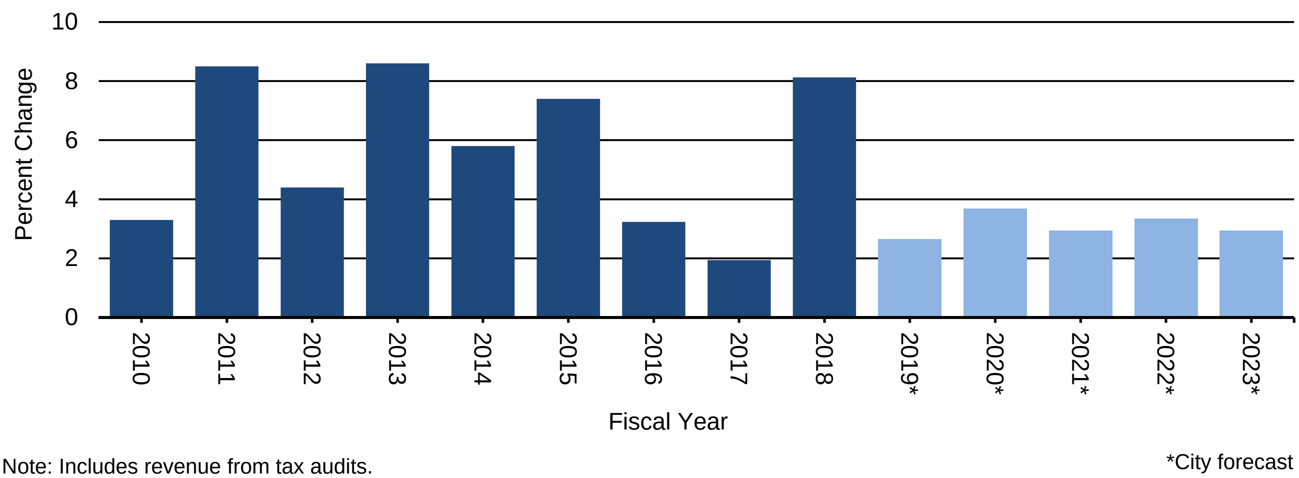
The growth in City fund revenues is projected to slow from 6.5 percent in FY 2018 to 3.3 percent in FY 2019 and then to 2.3 percent in FY 2020. The slowdown is primarily driven by an expected weakness in tax collections, which had surged by 8.1 percent in FY 2018 (see Figure 5).

The surge in tax collections in FY 2018 was driven by strong job gains, higher bonuses and capital gains, and changes in federal tax policy that affected taxpayer behavior. While the City expected personal income tax collections to be lower than last year in December and January, the decline was greater than expected.

Despite the adverse development, tax collections are still expected to be $604 million higher in FY 2019 than projected at the beginning of the fiscal year. Tax collections are now expected to increase by 2.7 percent in FY 2019 and by 3.7 percent in FY 2020.

Based on current trends, OSC expects tax revenue collections to exceed the City's expectations by $225 million in FY 2019 and $125 million in FY 2020. In addition, miscellaneous revenues are likely to exceed the City's expectations by $75 million in FY 2019 and $125 million beginning in FY 2020.

FIGURE 5
Annual Change in Tax Revenues



Note: Includes revenue from tax audits.
Sources: NYC Office of Management and Budget; OSC analysis

FIGURE 6
Trends in City Fund Revenues
(in millions)

	FY 2019	FY 2020	Annual Growth	FY 2021	FY 2022	FY 2023	Average Three-Year Growth Rate
General Property Tax	$ 27,865	$ 29,529	6.0%	$ 30,909	$ 32,150	$ 33,110	3.9%
Personal Income Tax	12,445	12,993	4.4%	13,309	13,734	14,209	3.0%
Sales Tax	7,809	8,169	4.6%	8,439	8,740	9,022	3.4%
Business Taxes	5,954	5,981	0.5%	6,087	6,170	6,299	1.7%
Real Estate Transaction Taxes	2,625	2,374	-9.6%	2,404	2,460	2,530	2.1%
Other Taxes	2,926	2,872	-1.8%	2,899	2,955	3,004	1.5%
Tax Audits	1,057	998	-5.6%	721	721	721	-10.3%
Subtotal: Taxes	**60,681**	**62,916**	**3.7%**	**64,768**	**66,930**	**68,895**	**3.1%**
Miscellaneous Revenues	5,479	5,005	-8.7%	4,976	4,953	4,943	-0.4%
Unrestricted Intergovernmental Aid	151	0	NA	0	0	0	0.0%
Grant Disallowances	91	(15)	NA	(15)	(15)	(15)	0.0%
Total	**66,402**	**67,906**	**2.3%**	**69,729**	**71,868**	**73,823**	**2.8%**

Sources: NYC Office of Management and Budget; OSC analysis

The February Plan is based on the trends shown in Figure 6 and discussed below.

1. General Property Tax

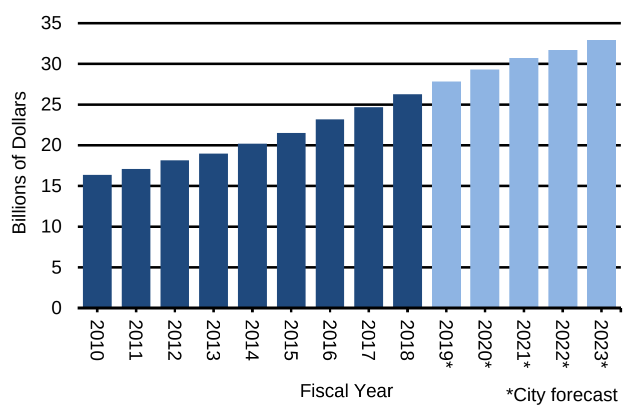
Rising property values have fueled the growth in property tax collections during the current economic expansion even as the average tax rate has remained unchanged. Since FY 2010, the average property tax bill for Class 1 properties (i.e., single-family and small multifamily homes) has risen by 67 percent, while the average bill for Class 4 properties (i.e., commercial properties) rose by 57 percent.

Collections increased by $10 billion between fiscal years 2010 and 2018, accounting for nearly half of the increase in City tax collections (excluding audits) during this period. In FY 2019, property tax collections are projected to increase by $1.6 billion, accounting for most (89 percent) of the expected gain in tax collections.

The preliminary property tax roll for FY 2020, which was released in January 2019, shows that the market value of properties in the City rose by 5.8 percent, the slowest rate of growth in five years. Despite the slower growth, market values reached a record $1.3 trillion. Slower growth in residential property values (which account for nearly three-quarters of the market value of all properties in the City) held down the rate of growth.

Based on the preliminary roll, the City raised its revenue forecast by $234 million in FY 2020, $198 million in FY 2021 and $448 million in FY 2022. Collections are now expected to total $29.5 billion in FY 2020 (see Figure 7), an increase of 6 percent ($1.7 billion).

FIGURE 7
Property Tax Collections



Sources: NYC Office of Management and Budget

The City expects slower growth in property values during the remainder of the financial plan period on the assumption of rising interest rates. As a result, the February Plan assumes that growth in property tax collections will slow, averaging 3.9 percent during fiscal years 2021 and 2023. The Federal Reserve, however, has indicated that short-term interest rates may rise more slowly than previously expected given muted inflation and recent global economic and financial developments.

At the beginning of FY 2019, the City set aside $1.8 billion as a reserve for delinquencies, refunds and tax abatements, $274 million more than was needed in FY 2018. While the City reduced the reserve by $76 million in the February Plan, OSC believes another $150 million may become available as the year progresses.

On April 24, 2017, Tax Equity Now New York (a coalition of advocates, property owners and tenants) filed suit against the State and the City claiming that the current real property tax system in New York City violates the State and federal constitution and the Fair Housing Act.

The lawsuit alleges that the City's property tax system imposes unequal tax burdens on similarly valued properties within the same property class, and imposes disproportionate financial burdens on racial minorities. On September 24, 2018, the court dismissed all but two of the claims against the State, but did not dismiss any of the 16 claims against the City. The City and the State have appealed this decision.

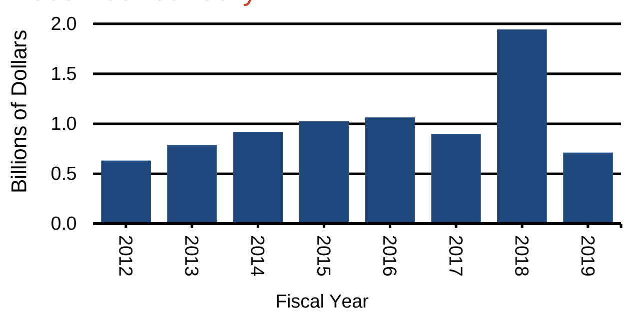
In June 2018, the Mayor and City Council Speaker established an advisory commission to develop recommendations to make the City's property tax system simpler, clearer and fairer, while ensuring that there is no reduction in the revenue used to fund essential City services. The commission is currently holding public hearings, which are expected to continue through the spring.

2. Personal Income Tax

Personal income tax collections surged by 15.8 percent in FY 2018 in response to strong job growth, higher bonuses and capital gains, and changes in federal tax policies that affected taxpayer behavior.[5]

In FY 2018, estimated personal income tax payments on nonwage income totaled $1.9 billion during December and January, more than twice the amount during the same two-month period in the prior fiscal year (see Figure 8). In FY 2019, estimated payments fell by $1.2 billion in December and January. While the City had anticipated much of the decline, collections were still short by $433 million.

FIGURE 8
Estimated Personal Income Tax Payments, December-January



Sources: NYS Department of Taxation and Finance; OSC analysis

This development was not unique to New York City. Estimated payments during the two-month period declined by 55 percent in New York State, 55 percent in Connecticut, 50 percent in Massachusetts and 35 percent in New Jersey.

[5] The growth in personal income tax has been adjusted for changes in the administration of the New York State School Tax Relief Program.

Officials in these states believe that the passage of the Tax Cuts and Jobs Act of 2017, which capped the deductibility of state and local taxes at $10,000, may have encouraged high-income taxpayers to utilize strategies (such as a change in residency) to reduce their tax liabilities. According to the New York City Independent Budget Office, the top 1 percent of personal income taxpayers are responsible for 43 percent of the revenue collected by the City. Other factors, such as the sharp drop in the financial markets in December 2018, could have contributed to the falloff in estimated payments.

As shown in Figure 9, the City reduced its forecast for quarterly estimated payments in the February Plan by $433 million to reflect the weakness in December-January payments. The City, however, believes that some of the loss may be due to timing, and that $201 million will be recovered in April from estimated payments made by taxpayers seeking extensions to file their taxes. It notes that the Congressional Budget Office expects growth in federal personal income tax collections and capital gains in 2018.

FIGURE 9
Changes in the Personal Income Tax Forecast
February Plan vs. November Plan
(in millions)

	FY 2019	FY 2020
Withholding	$ (12)	$ (30)
Estimated Payments	(232)	(23)
Quarterly Payments	(433)	(292)
Extension Payments	201	269
Final Returns	(69)	(55)
Assessments	25	0
Distribution Payments	160	51
Charges	0	0
Refunds	(48)	80
Total	**$ (177)**	**$ 24**

Note: Totals may not add due to rounding
Sources: NYC Office of Management and Budget; OSC analysis

The City also raised its forecast for State distribution payments by $160 million based on year-to-date trends. The State administers the City's personal income tax and remits to the City an estimate of its share each month. The State subsequently reviews the results and makes adjustments as necessary.

Although the City increased its forecast for State distribution payments, payments are still likely to exceed the City's forecast by $75 million annually in fiscal years 2019 and 2020 based on current trends and projections by the State Division of the Budget.

Although the City reduced its forecast in the February Plan by a net of $177 million, collections are still expected to be higher than the forecast at the beginning of the fiscal year by $67 million. Nonetheless, collections are still projected to decline in FY 2019 (by $749 million, or 5.7 percent).

The February Plan assumes that personal income tax collections will grow by 4.4 percent in FY 2020. The City expects capital gains to increase, helping to boost estimated payments. A slower rate of job growth, however, is expected to constrain the growth in withholding (e.g., the amount of tax taken from employee paychecks).

The February Plan expects personal income tax collections to increase at an average annual rate of 3 percent during fiscal years 2021 through 2023 on the assumptions that job and wage growth will remain weak.

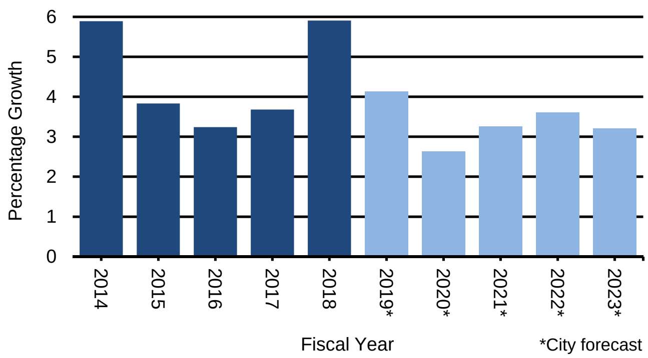
3. Sales Tax

Sales tax collections grew by 5.9 percent in FY 2018 (see Figure 10). This was the strongest rate of growth since FY 2014, when collections also rose by 5.9 percent. Collections remained strong during the first seven months of FY 2019, increasing by 4.7 percent compared to the same period last year. (A recent OSC report found that sales tax collections in calendar year 2018 were strong throughout New York State.)

The February Plan assumes the growth in sales tax collections will slow to 4.1 percent in FY 2019 and then to 2.6 percent in FY 2020 as job and wage growth slow. Based on current collection trends, as well as expectations of stronger job growth, OSC estimates that sales tax collections could be higher by $50 million in FY 2020.

Higher consumer confidence has contributed to the strength in sales tax collections. According to the Siena College consumer sentiment indices for the State and the City, conducted in early December 2018, consumer confidence was at its highest point since 2000. The strong labor market and rising wages are contributing factors.

FIGURE 10
Growth in Sales Tax Collections



Note: Adjusted for STARC repayments in fiscal years 2016-2019.
Sources: NYC Office of Management and Budget; OSC analysis

Tourism has helped boost sales tax collections. According to NYC & Company (the City's tourism agency), the City reached another historic record for tourism in 2018, with 65.2 million visitors, its ninth consecutive year of growth. International visitors, who tend to spend more than domestic visitors, totaled 13.5 million, growing by 3.1 percent from the previous year. The City expects the number of total visitors to exceed 67 million in 2019.

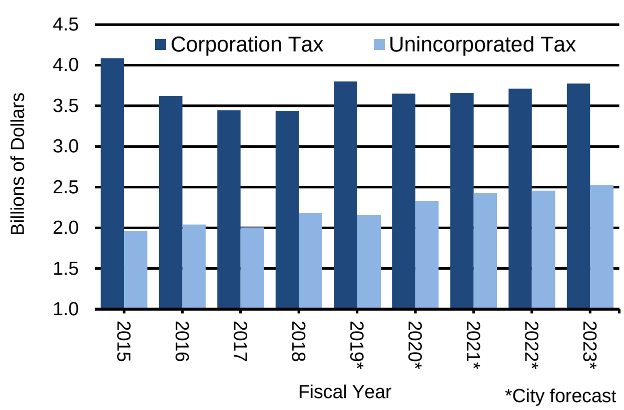
The record number of visitors has boosted hotel occupancy and average daily room rates, and has helped Broadway attendance reach a record of 14.3 million in 2018.

The Governor's executive budget includes enhanced enforcement of taxation on internet sales to New York residents, and a proposal to require internet marketplace providers to collect sales taxes when they facilitate third-party sales. The City could realize additional sales tax revenue from these State budget initiatives (see Section III, "Potential Impact of State and Federal Actions").

4. Business Taxes

In April 2015, the State enacted legislation that combined the City's banking and general corporation taxes. The change was expected to be revenue-neutral, but business corporation tax collections declined for three consecutive years, falling short of the City's expectations. However, collections are expected to increase in FY 2019, suggesting a turning point (see Figure 11).

FIGURE 11
Business Tax Collections



Sources: NYC Office of Management and Budget; OSC analysis

During the first seven months of FY 2019, business corporation tax collections were 18.3 percent higher than during the same period last year. The City believes that corporations have adjusted to the new tax law and that payment patterns have normalized as overpayments made during the transition to the new law have been drawn down.

As a result, the City increased its forecast for business corporation tax collections in the February Plan by $174 million. Collections are now projected to increase by 10.5 percent for all of FY 2019. For the remainder of the financial plan period, the City expects growth to slow significantly in response to an economic slowdown.

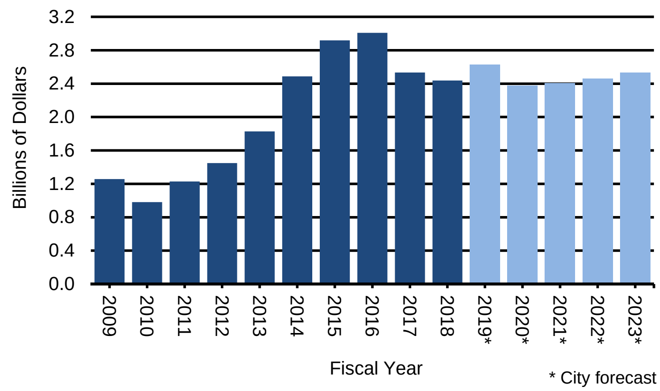
Collections for the unincorporated business tax were boosted in FY 2018 by higher business earnings and one-time factors, including the repatriation of overseas income by December 31, 2017, as required by a 2008 federal law. With the loss of these one-time benefits in FY 2019, along with poor performance at many hedge funds, collections from the unincorporated business tax during the first seven months of FY 2019 declined by 16.7 percent ($211 million). The City expects collections to rebound in FY 2020, growing by 8.1 percent.

Securities industry profits increased by 11 percent in 2018 to $27.3 billion. (The February Plan had assumed that industry profitability would decline by 12.6 percent in 2018.) The February Plan assumes bonuses paid to industry workers in New York City will decline by 9.2 percent in 2018.

5. Real Estate Transaction Taxes

After two years of decline, collections from the real estate transaction taxes (the mortgage recording tax and real property transfer tax) are expected to increase in FY 2019, reflecting stronger-than-expected commercial sales and an acceleration of mortgage refinancing activity. The February Plan assumes collections will reach $2.6 billion in FY 2019, a gain of 7.7 percent.

FIGURE 12
Real Estate Transaction Tax Collections



Source: NYC Office of Management and Budget

However, the February Plan also assumes that collections will decline by 9.6 percent to $2.4 billion in FY 2020 as a result of slowing in the global economy, the cumulative effects of Federal Reserve tightening, diminishing foreign investment and political uncertainty. The City expects modest growth during fiscal years 2021 through 2023 (see Figure 12).

Recent large commercial transactions have included sales of the Terminal Stores building on 11th Avenue for $880 million, 425 Lexington Avenue for $701 million, and two hotels for $615 million (the Parker Hotel and Hilton Embassy Suites).

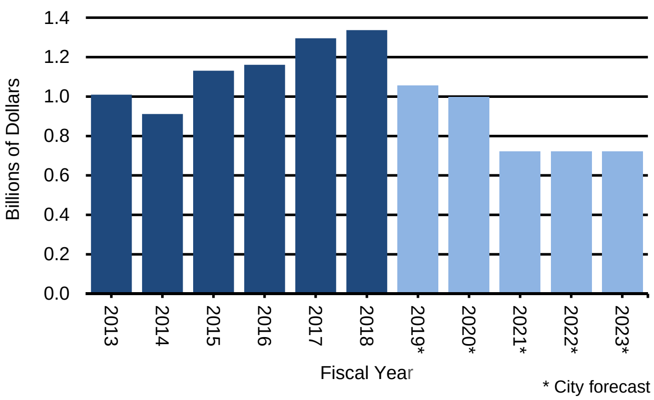
While the commercial market remains strong, the residential market has weakened, especially for higher-priced properties. Along with concerns over pricing and access to financing, real estate firms believe that the recent tax law changes have had a dampening effect on sales activity.

6. Audit Revenues

Each year, the Department of Finance conducts audits of individuals and businesses to ensure compliance with the tax code. In FY 2018, audit revenue exceeded $1.3 billion (see Figure 13), driven by business tax audits.

Although the City raised its forecast for audit revenue in the February Plan by $275 million in FY 2020 (to $1 billion), the City still assumes collections will decline sharply during the remainder of the financial plan period (averaging $721 million). By comparison, collections averaged $1.1 billion annually during fiscal years 2013 through 2018. Therefore, it is likely that audit revenue will be higher in the later years of the financial plan period.

FIGURE 13
Audit Revenue



Source: NYC Office of Management and Budget

7. Miscellaneous Revenues

The February Plan assumes that miscellaneous revenues will total $5.5 billion in FY 2019, but then drop to $5 billion in FY 2020 and remain at that level.

Although the City raised its forecast in the February Plan by $444 million in FY 2019, the increase primarily reflects one-time revenues, including a reimbursement from the New York City Health and Hospitals Corporation ($152 million),[6] an asset sale ($118 million) and restitution from a bank settlement ($78 million).

Excluding these one-time revenues, the February Plan assumes that recurring miscellaneous revenues (i.e., fines, fees, licenses, water and sewer charges, and other sources) will total $4.6 billion in FY 2019, $116 million higher than the forecast at the beginning of the fiscal year.

In recent years, miscellaneous revenues have exceeded the City's initial forecast by more than $200 million annually. Fines and licenses accounted for about two-thirds of this additional revenue in the past two fiscal years. In FY 2019, collections from these two categories have increased by 7 percent during the first seven months of the fiscal year. In contrast, the February Plan assumes a 5 percent decline.

OSC estimates that miscellaneous revenues could exceed the City's forecast by at least $75 million in FY 2019 and by $125 million annually in subsequent years based on current trends.

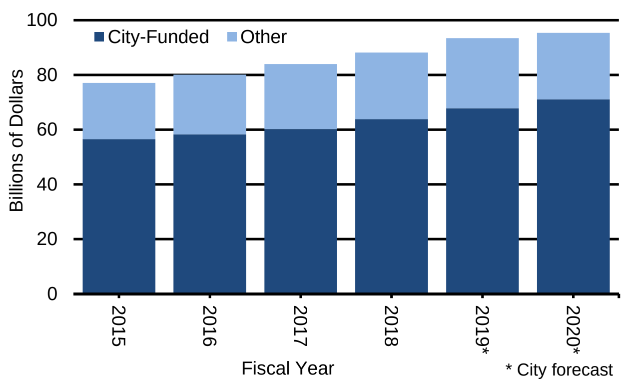
[6] The balance of the $372 million reimbursement from the Health and Hospitals Corporation is reflected in other categorical funds.

V. Expenditure Trends

The February Plan assumes expenditures will total nearly $92.2 billion in FY 2020, including programs funded with federal and State categorical grants. The portion funded with locally generated revenue (i.e., City funds) is expected to total $67.9 billion.

After adjusting for surplus transfers, which can mask trends, City-funded spending is projected to grow by 4.8 percent in FY 2020 to $71.1 billion (see Figure 14). Excluding reserves, spending would increase by 3.4 percent, which is faster than the projected inflation rate (2.4 percent).

FIGURE 14
City-Funded Expenditures



Note: Adjusted for surplus transfers.
Sources: NYC Office of Management and Budget; OSC analysis

City-funded spending increased by 6.1 percent in FY 2018 and is expected to rise at a similar pace in FY 2019 (5.7 percent, excluding reserves), driven by the cost of collective bargaining, higher agency spending, rising health insurance and debt service costs, and a State-mandated increase in City support for the MTA in FY2019.

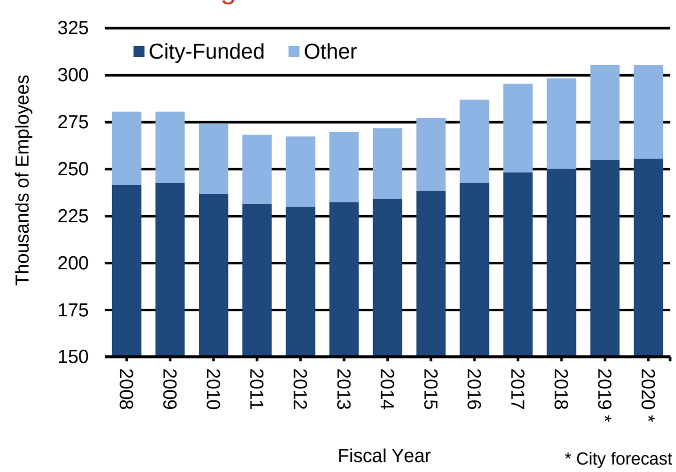
In FY 2020, spending will be driven by the continued cost of the 2010-2017 round of collective bargaining, which will peak in FY 2021, and the City's expectation that the remainder of the work force will reach agreements in the current round of negotiations that conform to the pattern established by District Council 37 and the United Federation of Teachers.

The growth in City-funded spending also reflects the continued rise in health insurance and debt service costs. Despite a new agreement between the City and the Municipal Labor Committee to generate $1.7 billion in health insurance savings to help pay for wage increases, health insurance costs are projected to increase at an annual rate of 7.9 percent during fiscal years 2020 through 2023. Debt service is projected to grow at an annual rate of 7.7 percent.

Since FY 2012, the City's full-time work force (including positions funded by federal and State categorical grants) has increased by 30,947 employees to reach 298,370 in June 2018, the highest level since the 1975 fiscal crisis (including a record 250,105 City-funded employees; see Figure 15).

The February Plan assumes the addition of 7,585 employees during FY 2019, with hiring concentrated in the health and welfare agencies. However, the City fell far short of its hiring target during the first half of FY 2019 (by 4,353 positions). The City is implementing an expansion of a hiring freeze to be included in the executive budget for FY 2020, which could generate significant personal service savings.

FIGURE 15
Full-Time Staffing Levels



Sources: NYC Office of Management and Budget; OSC analysis

FIGURE 16
Trends in City-Funded Spending
(in millions)

	FY 2019	FY 2020	Annual Growth	FY 2021	FY 2022	FY 2023	Average Three-Year Growth Rate
Salaries and Wages	$ 20,194	$ 21,504	6.5%	$ 22,278	$ 21,736	$ 22,270	1.2%
Pension Contributions	9,706	9,807	1.0%	10,273	10,720	10,925	3.7%
Debt Service	6,494	7,093	9.2%	7,414	8,097	8,851	7.7%
Medicaid	5,813	5,813	0.0%	5,813	5,813	5,813	0.0%
Health Insurance	5,011	5,576	11.3%	5,966	6,490	7,012	7.9%
Other Fringe Benefits	3,070	3,353	9.2%	3,489	3,639	3,798	4.2%
Energy	785	800	1.9%	824	843	862	2.5%
Judgments and Claims	557	572	2.7%	587	602	618	2.6%
Public Assistance	640	719	12.3%	719	719	719	0.0%
Other	15,639	14,588	-6.7%	14,632	14,898	15,001	0.9%
Subtotal	**67,909**	**69,825**	**2.8%**	**71,995**	**73,557**	**75,869**	**2.8%**
Prior Years' Expenses	(400)	- - -	NA	- - -	- - -	- - -	NA
General Reserve	300	1,000	NA	1,000	1,000	1,000	NA
Capital Stabilization Reserve	- - -	250	NA	250	250	250	NA
Total	**$ 67,809**	**$ 71,075**	**4.8%**	**$ 73,245**	**$ 74,807**	**$ 77,119**	**2.8%**

Note: Debt service and totals have been adjusted for surplus transfers. Judgments and claims excludes a prior-year reimbursement from the Health and Hospitals Corporation in FY 2019.
Sources: NYC Office of Management and Budget; OSC analysis

The February Plan is based on the trends shown in Figure 16 and discussed below.

1. Collective Bargaining

As of March 2019, almost two-thirds of the municipal work force had reached new labor agreements with the City for the 2017-2021 round of bargaining. In August 2018, the rank-and-file members of District Council 37 (DC 37), which represents about one-quarter of the municipal work force, approved an agreement that calls for wages to increase by 7.4 percent (compounded) over a 44-month period.[7]

In October 2018, the rank-and-file members of the United Federation of Teachers (UFT), which represents more than one-third of the municipal work force, approved a similar agreement. The UFT agreement also includes financial incentives ($5,000 to $8,000 annually) for members who transfer to hard-to-staff positions at high-needs schools.

The City has a long history of pattern bargaining, and it expects the agreements with DC 37 and the UFT to set the framework for negotiations with the remainder of the municipal work force for the 2017-2021 round of negotiation. Similar wage agreements with the entire work force would cost a total of $8.8 billion during fiscal years 2018 through 2022, according to the City's estimates.

At the same time the City announced the agreement with DC 37, it announced that it had

[7] The first wage increase of 2 percent, retroactive to September 2017, was paid shortly after the agreement was approved by union members. The second wage increase of 2.25 percent was paid in October 2018. The agreement also calls for a wage increase of 3 percent in October 2019. The pattern also provides funding equal to 0.25 percent of wages to be used to fund benefit items.

reached a second agreement with the Municipal Labor Committee (MLC) to generate health insurance savings to fund wage increases. The February Plan assumes the latest agreement will generate savings of $200 million in FY 2019, $300 million in FY 2020 and $600 million in FY 2021, plus recurring savings of $633 million beginning in FY 2022.[8]

According to the agreement, the savings are guaranteed and are enforceable through arbitration. In addition, the annual savings targets could be met with nonrecurring savings that may include drawing down resources from the health stabilization fund, which currently has a balance of $1.6 billion.

A committee including representatives from the City and the MLC, plus an independent arbitrator, will be established to recommend modifications in the way health care is currently provided or funded.

After taking into account the savings anticipated in the health insurance agreement and funding that was previously set aside in the City's labor reserve, the net cost of the 2017-2021 round of bargaining would grow from $142 million in FY 2018 to $1.3 billion in FY 2022 (see Figure 17). These costs are in addition to those incurred from the 2010-2017 round of bargaining.

None of the unions that represent uniformed employees have reached new agreements with the City. In March 2018, the Patrolmen's Benevolent Association (PBA), which represents police officers, filed a petition with the New York State Public Employment Relations Board requesting the appointment of a three-member arbitration panel. Although the panel has been selected, the proceedings have been delayed pending the outcome of a lawsuit by the PBA objecting to the City's appointment to the panel. According to State law, arbitration awards for disputes between the City and police officers are binding on both parties and limited to two years.

2. Health Insurance

In May 2014, the City and the MLC reached the first of two agreements to generate health insurance savings to help fund wage increases for municipal employees. Under the first agreement, the City and the unions agreed to generate a cumulative total of $3.4 billion during fiscal years 2015 through 2018, and $1.3 billion in recurring savings beginning in FY 2019.

In October 2018, the Commissioner of Labor Relations reported that the City exceeded the cumulative four-year target by $86 million. These savings were credited toward the second health insurance savings agreement that was announced in June 2018.

FIGURE 17
Budgetary Impact of Pattern Labor Settlements
(in millions)

	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
Pattern Cost (2017-2021 Contract Period)	**$ (255)**	**$ (781)**	**$ (1,730)**	**$ (2,657)**	**$ (3,390)**
Offsets					
Labor Reserve	113	354	726	1,128	1,413
Anticipated Health Insurance Savings	- - -	200	300	600	633
Total Offsets	**113**	**554**	**1,026**	**1,728**	**2,046**
Net Budgetary Impact	**$ (142)**	**$ (227)**	**$ (704)**	**$ (929)**	**$ (1,344)**

Sources: NYC Office of Management and Budget; OSC analysis

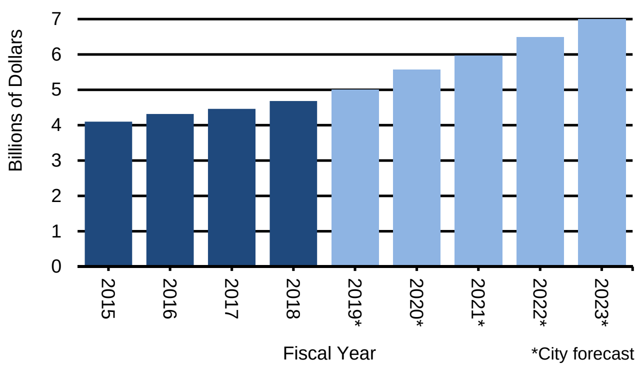
[8] The MLC agreement calls for recurring savings of $600 million beginning in FY 2022.

More than three-quarters of the cumulative savings from the first agreement came from lower-than-planned increases in health insurance premiums and other administrative actions. Cost-containment initiatives accounted for one-fifth of the savings ($723 million), mostly from higher co-payments.

In total, the two agreements are expected to generate cumulative savings of $10.3 billion through FY 2022 and recurring savings of $1.9 billion beginning in FY 2022. Despite the savings, health insurance costs could still reach $7 billion by FY 2023 (see Figure 18), 50 percent more than in FY 2018.

FIGURE 18

Health Insurance Costs
City-Funded



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

In December 2018, the Commissioner of the Office of Labor Relations announced that the City has reached agreement with its primary insurer to increase health insurance premiums for active employees by 3.5 percent in FY 2020 and by 3 percent in FY 2021. The increases are about half of those the City assumed prior to the agreement, which will generate significant savings that will be credited against the savings targets in the second agreement.

In FY 2006, the City established the Retiree Health Benefits Trust (RHBT) to help fund the future cost of post-employment benefits other than pensions (OPEBs). While the RHBT was intended to help fund future OPEB liabilities, it has been used as a rainy-day fund in the past. The balance in the RHBT now totals nearly $4.5 billion (net of any prepayments), the highest amount ever. The City's unfunded OPEB liability totaled $98.5 billion at the end of FY 2018.

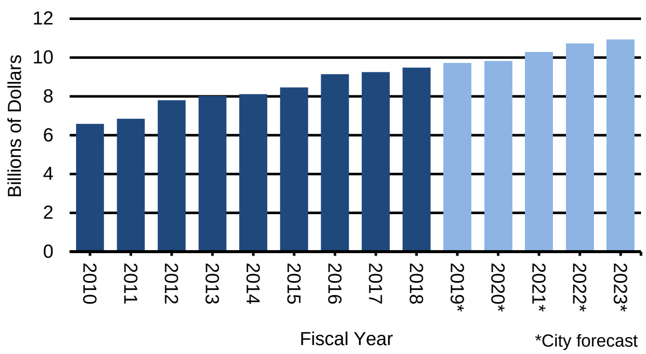
The City, like many employers, does not fund its OPEB liabilities on an actuarial basis but rather pays the annual cost of benefits to current retirees on a pay-as-you-go (PAYGO) basis. OPEB costs, on a PAYGO basis, are projected to rise from $2.4 billion in FY 2018 to $3 billion in FY 2023, an increase of 25 percent over five years.

3. Pension Contributions

After rising rapidly between fiscal years 2003 and 2012, the growth in City-funded pension contributions slowed, averaging 3.3 percent annually through 2018. The slower rate of growth reflected the impact of changes in assumptions and methodologies used to calculate City pension contributions, savings from lower-cost pension plans for employees hired after March 31, 2012, and better-than-expected investment earnings. The pension funds have earned, on average, 8 percent on their investments since the earnings assumptions were lowered to 7 percent beginning in FY 2012.

As shown in Figure 19, the February Plan assumes that pension contributions will continue to grow slowly in fiscal years 2019 and 2020, but then pick up beginning in FY 2021 as a reflection of the impact of labor agreements for the 2017-2021 round of bargaining. By FY 2023, pension contributions are projected to total $10.9 billion, accounting for 15 percent of City fund revenues.

FIGURE 19
Pension Contributions
City-Funded



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

Subsequent to the release of the February Plan, the City indicated that pension contributions could be higher by about $175 million annually because of a calculation error.[9] In addition, the City Actuary has proposed changes in the assumptions and methodologies used to calculate pension liabilities, which could require the City to increase its contribution to the pension funds by $30 million annually. Taken together, pension contributions could be higher-than-planned by about $205 million annually.

The February Plan includes pension reserves of $100 million in each of fiscal years 2019 and 2020, rising to $400 million beginning in FY 2021 for such contingencies. While not sufficient to cover the full cost of these developments in fiscal years 2019 and 2020, the reserves are more than adequate in subsequent years.

However, the balance in the reserves (about $195 million annually beginning in FY 2021) could be needed to cover a shortfall in pension fund investment earnings in the current fiscal year. As of February 28, 2019, the pension funds have earned about 2 percent, five percentage points short of the expected annual return of 7 percent. While there is still time to mitigate the shortfall, each percentage-point difference from the expected annual return could increase (or decrease) pension contributions by about $30 million in FY 2021, $60 million in FY 2022, and $90 million in FY 2023.

In the five years since the City adopted new, more transparent financial reporting standards for pension liabilities in FY 2014, the financial condition of the City's five actuarial pension systems has improved. In the aggregate, the pension systems had enough assets to fund (on a market-value basis) 76 percent of their accrued pension liabilities as of the end of FY 2018 (see Figure 20). During this period, the unfunded net liability for all five systems declined by $12.1 billion to $47.8 billion.

FIGURE 20
Funded Status of the NYC Retirement Systems
(As of June 30, 2018)

Pension System	Funded Status
Board of Education Retirement System	90%
New York City Employees' Retirement System	78%
Police Pension Fund	79%
Teachers' Retirement System	74%
Fire Pension Fund	65%
All Systems	**76%**

Sources: NYC Retirement Systems; NYC Comptroller; OSC analysis

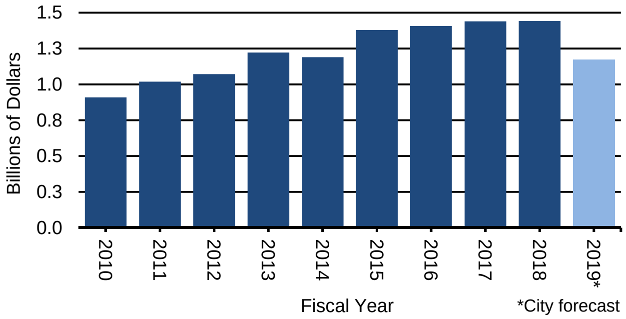
4. Uniformed Overtime

The growth in overtime at the uniformed agencies has slowed over the past three fiscal years (see Figure 21), after rising by 52 percent between fiscal years 2010 and 2015. Overtime reached a record of $1.4 billion in FY 2018 (only $3 million more than in the prior year).

After nearly doubling between fiscal years 2014 and 2016, overtime at the Department of Correction declined with the hiring of 1,897 additional correction officers. The February Plan assumes overtime at the department will decline by 29 percent to $157 million in FY 2019.

[9] The City estimates the cost of these developments at between $150 million and $200 million annually.

FIGURE 21
Uniformed Agency Overtime



Sources: NYC Financial Management System; NYC Office of Management and Budget; OSC analysis

The February Plan assumes that overtime will decline to $1.2 billion in FY 2019, a reduction of $256 million (17.7 percent). Although overtime was lower during the first eight months of FY 2019 compared to the same period last year, it exceeded the City's forecast by $119 million.

While overtime is likely to exceed the City's forecast for FY 2019, these unplanned costs could be partly offset, as in past years, by savings in other personal service costs or by the receipt of unplanned federal and State categorical grants. Still, OSC estimates that the uniformed agencies could require as much as $70 million in additional City funding to cover unplanned overtime.

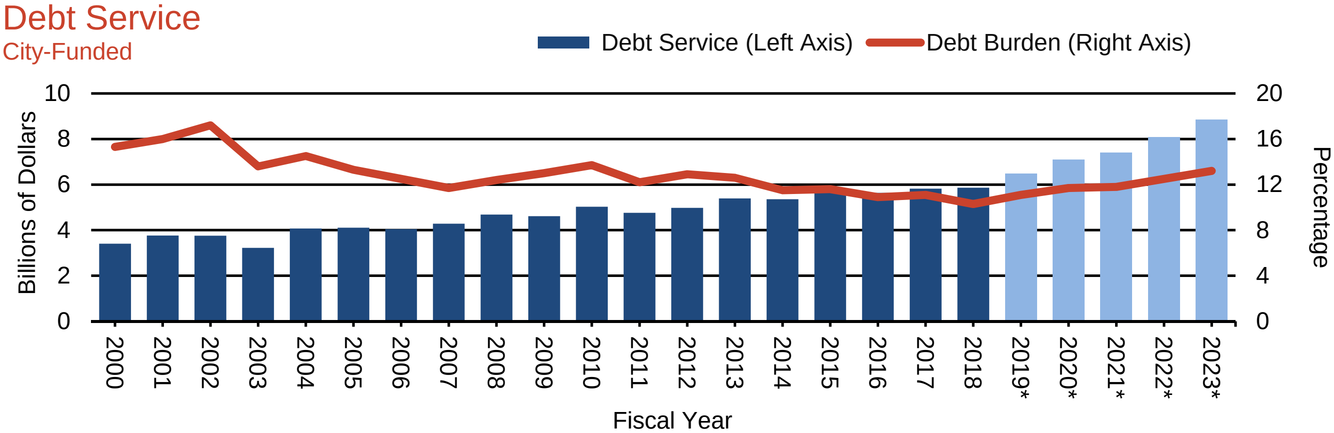
5. Debt Service

City-funded debt service increased at an average annual rate of only 2.3 percent during fiscal years 2014 through 2018 because of historically low interest rates that reduced the cost of new issuances and created opportunities to refinance outstanding debt. During the past four fiscal years, debt service was lower than the City's estimates at the beginning of the fiscal year by an average of $537 million annually. So far, the City has realized budgetary savings of $234 million in FY 2019.

The February Plan assumes debt service will grow by 51 percent (nearly $3 billion) between fiscal years 2018 and 2023 to reach $8.9 billion (see Figure 22). Although debt service may grow more slowly, opportunities for future savings may be reduced compared to recent years because of the expanding capital program and greater uncertainty regarding future interest rates.

The City will likely continue to realize savings, at least in the near term, because interest rates are likely to remain below the City's assumptions and capital commitments are likely to fall short of the City's ambitious targets. Last year, City-funded capital commitments totaled $10.8 billion, 27 percent less than planned at the beginning of the year. In FY 2019, City-funded commitments

FIGURE 22
Debt Service
City-Funded



Note: Debt service has been adjusted for prepayments and defeasances.
*City forecast
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

are projected to total $12.2 billion. While less than the amount planned for FY 2018, it is still 12 percent more than the amount committed last year. The City expects commitments to reach $15.5 billion by FY 2020.

Debt service as a share of tax revenue (i.e., the debt burden) has fallen from a post-recession peak of 13.7 percent in FY 2010 to 10.3 percent in FY 2018. The February Plan assumes that the debt burden will rise to 13.2 percent by FY 2023, but this estimate is based on conservative assumptions for tax collections, interest rates and capital commitments.

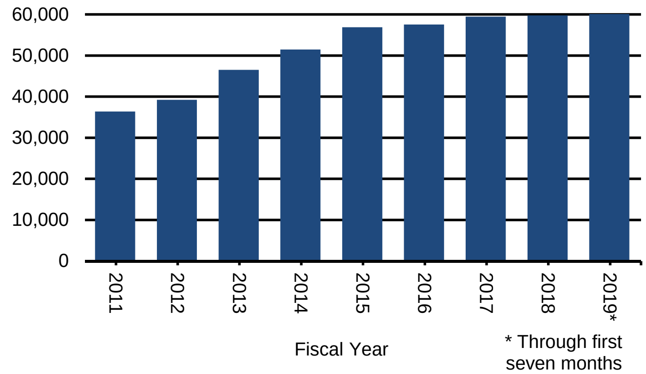
Although debt service is projected to account for a larger share of tax revenue, the share would remain well below 15 percent, a level that is considered high. To prevent the debt burden from rising too quickly in the event of a rapid hike in interest rates or a sharp decline in tax revenue, the City established a capital stabilization reserve in FY 2016. The reserve is valued at $250 million annually during fiscal years 2020 through 2023.

6. Homeless Services

The number of homeless people residing in shelters operated by the Department of Homeless Services (DHS) reached nearly 60,000 during FY 2018 (see Figure 23), an increase of 64 percent since 2011. In January 2019, the caseload reached a new record despite efforts to prevent homelessness and to create permanent housing.

The shelter population averaged 60,334 during the first seven months of FY 2019, slightly higher than during the same period last year. Although the number of individuals in the family program (which accounts for three-quarters of the shelter population) declined by 2 percent, the single-adult population grew by 10 percent. The single-adult population rose by 31 percent between fiscal years 2015 and 2018, while enrollment in the family program declined slightly.

FIGURE 23
Homeless Shelter Population



Sources: NYC Department of Homeless Services; OSC analysis

The cost of homeless services has increased from $1 billion in FY 2014 to a record of more than $2.1 billion in FY 2018 ($1.2 billion in City funds). The City attributes the increase to the higher shelter population, as well as to security and service improvements. The February Plan assumes that the cost of housing single adults will decline by 4.3 percent in FY 2019, but this seems unlikely given the growth in the single-adult population during the first part of FY 2019.

The City intends to reduce its reliance on hotels and cluster sites, where families are temporarily placed in apartments owned by private landlords. These facilities are expensive and often lack access to support services. The City intends to build 90 new shelters by the first quarter of 2022 so it can eliminate the use of hotels and cluster sites. As of January 31, 2019, a total of 21 new shelters have opened.

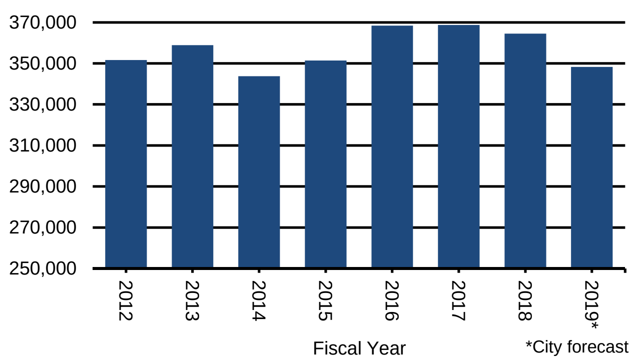
7. Public Assistance

The largest public assistance programs in New York State are the Family Assistance (FA) and Safety Net Assistance (SNA) programs. The FA program, which is federally funded, provides five years of lifetime benefits to low-income families with children. The SNA program, which is funded by the State, the City and counties outside of the City, provides benefits to families who have exhausted their federal benefits and to low-income individuals ineligible for federal benefits.

In FY 2017, the public assistance caseload reached its highest level in 10 years. The caseload fell by 1 percent in FY 2018 and is projected by the City to decline by another 4 percent in FY 2019 (see Figure 24). In December 2018, the caseload totaled 346,145, the lowest level in more than four years.

While the public assistance caseload has been declining, costs increased by 11 percent between fiscal years 2016 and 2018. The growth is attributed mostly to an expansion in eviction-prevention programs. However, the City could realize some modest savings since costs during the first half of FY 2019 were lower than last year. The City-funded share of public assistance is projected to total $640 million in FY 2019.

FIGURE 24
Public Assistance Caseload



Source: NYC Human Resources Administration

On October 10, 2018, the U.S. Department of Homeland Security issued a proposed rule that would change the standard used to determine whether certain immigrants seeking visas or status as lawful permanent residents are likely at any time in the future to become public charges (i.e., individuals who receive certain public income, housing, food and medical benefits) and could be prohibited from entering or remaining in the United States. The public had until December 10, 2018, to comment, and the department is still reviewing the comments.

Participation in federally funded programs such as cash assistance, the Supplemental Nutrition Assistance Program (SNAP, also known as food stamps), Medicaid, the Medicare Part D low-income subsidy, subsidized long-term care and housing assistance could decline if immigrants and their family members discontinue receiving federal benefits or do not apply for these programs out of fear of being denied legal resident status.

8. Fair Fares

On January 4, 2019, the City launched a pilot program known as Fair Fares to provide half-fares to low-income New Yorkers who use the subway or bus systems operated by the Metropolitan Transportation Authority (MTA).

Under an agreement with the City, the MTA created a special Fair Fares MetroCard that allows the purchase of half-priced 7-day or 30-day unlimited passes at MTA vending machines and subway station booths. The City is paying for half of the cost of the new MetroCards, and eligible participants will be required to pay the other half. The City is working with the MTA to phase in a pay-per-ride option, which it expects to launch in March 2019.

An estimated 30,000 working New Yorkers who receive cash assistance benefits are now eligible to participate. An additional 130,000 working New Yorkers who receive SNAP benefits will become eligible by April 2019.

The Mayor and the Speaker of the City Council recently announced that eligibility will be expanded later this year to include eligible residents at the New York City Housing Authority, enrolled students at the City University of New York and veterans at or below the federal poverty line.

In January 2020, the City intends to launch an open enrollment process for eligible New Yorkers at or below the federal poverty line who do not have discounted transportation from the MTA or the City.

The February Plan includes $106 million in each of fiscal years 2019 and 2020, but does not fund the program in subsequent years. In addition, the City Council had previously estimated the cost of Fair Fares at $212 million annually when fully implemented. The Mayor announced in February 2019 that the City will publish monthly enrollment reports so the expansion of the program can be monitored. As of March 2019, the City has conducted outreach efforts to more than 45,000 eligible New Yorkers.

9. Medical Assistance

Medicaid provides health insurance to low-income children and adults, and pays more toward long-term-care costs than any other entity. Medicaid also provides subsidies to health care providers (such as the Health and Hospitals Corporation) that serve large numbers of low-income patients and uninsured patients.

The City's Medicaid caseload grew steadily after the recession and accelerated after January 1, 2014, when Medicaid eligibility expanded under the federal Affordable Care Act (ACA). Enrollment reached almost 3.7 million people in December 2015, an increase of 510,000 people since December 2013.

In January 2016, the caseload fell by 134,000 as the State transferred certain immigrants who were ineligible for federal Medicaid to the Essential Plan (funded by federal and State resources). Since then, the Medicaid caseload has gradually declined to less than 3.5 million as of June 2018 (the latest data available). Of the people enrolled in Medicaid, 81 percent are in managed care plans.

A provision in the ACA increased the federal reimbursement rate to the states that had expanded coverage to certain childless adults prior to the ACA (from 50 percent to 90 percent in 2018). The City's savings have reached $389 million annually, which has been used largely to provide the City with fiscal relief and additional financial support to the Health and Hospitals Corporation. The City will further benefit when the rate increases to 93 percent in 2019. In subsequent years, the rate will return to 90 percent.

The City-funded share of Medicaid will total $5.8 billion in FY 2019 (9 percent of City fund revenues) and remain at that level because the State has assumed financial responsibility for the growth in the local share. These estimates assume there will be no changes in federal and State policies.

VI. Preliminary Ten-Year Capital Strategy

In February 2019, the City released its biennial preliminary ten-year capital strategy, which totals $104.1 billion. The proposed strategy is $14.5 billion (16 percent) larger than the preliminary strategy released two years ago, with most of the increase concentrated in housing and education. The City will fund $98.3 billion of the cost (an increase of $15.1 billion), with the balance funded by the federal and State governments.

The current preliminary capital strategy is the largest on record and twice as large (on an inflation-adjusted basis) as the strategy released in February 2011 (see Figure 25). More than half of the increase ($52 billion) has been devoted to housing ($9.2 billion), transportation ($7.7 billion), education ($6.2 billion) and environmental protection ($6.1 billion). Much of the remainder is devoted to resiliency and technology projects ($5.6 billion).

More than one-fifth of the current capital strategy ($23 billion) would be devoted to education, mostly to support the construction of new schools and the rehabilitation and expansion of existing schools ($16.4 billion). The remainder would support emergency repairs, administrative costs, technology upgrades and enhanced security systems ($6.6 billion).

Environmental protection projects ($19.7 billion) would focus on maintaining and protecting the City's water supply, including sewers, pollution control, and maintenance and upkeep of the water supply and distribution system. The strategy would allocate $939 million to complete construction on the City's third water tunnel, which delivers water from upstate reservoirs.

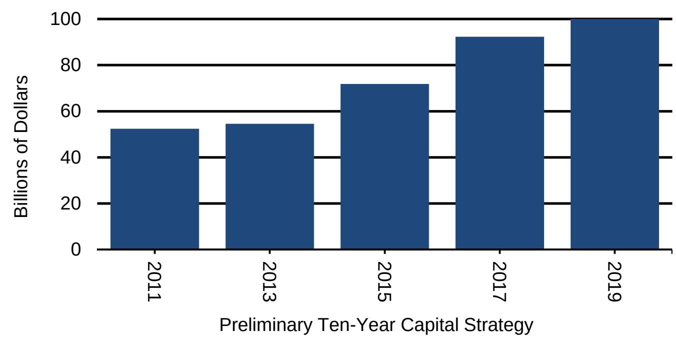
Of the $15.6 billion allocated to transportation, nearly $8 billion would support the reconstruction and rehabilitation of bridges, including $2 billion for the Brooklyn-Queens Expressway and the East River bridges. Another $6.1 billion would fund street and sidewalk reconstruction, such as resurfacing 6,300 lane miles.

The strategy provides the MTA with $429 million over the next 10 years. The City has not yet included $1.8 billion of its $2.7 billion commitment to fund the MTA's 2015-2019 capital program. The remaining funds are expected to come from development deals and bond proceeds that will be provided concurrently with additional State funds.

Housing projects would receive $13 billion, compared with $3.8 billion in 2011. The largest portion ($9.1 billion) would be used to fund the construction and preservation of affordable and special-needs housing to help reach the City's goal of creating or preserving 300,000 affordable housing units by 2026. The New York City Housing Authority would receive $3 billion for roof replacement, lead abatement, pest mitigation and upgrades to heating components as agreed to by the City under its agreement with the Department of Housing and Urban Development.

Public safety projects would receive $6.5 billion for the Police, Correction and Fire departments and the courts. While the City allocated $1.1 billion (including amounts in FY 2019) for the replacement of the Rikers Island jail complex with a system of borough-based jails, the City has indicated that the ultimate cost is likely to be significantly higher than the cost included in the preliminary ten-year strategy.

FIGURE 25
Planned Capital Spending



Note: Totals expressed in 2019 dollars.
Sources: NYC Office of Management and Budget; OSC analysis

VII. Semi-Autonomous Entities

1. Department of Education

The February Plan allocates $33.9 billion to the Department of Education in FY 2020, an increase of $713 million from FY 2019.[10] New York City is expected to fund $19.3 billion (57 percent) of the total cost, with the remainder funded by the State (36 percent) and the federal government and other sources (7 percent).

The Governor's executive budget would increase State education aid to New York City by $282 million, about $150 million less than assumed in the February Plan. Historically, the adopted State budget includes more education aid than initially proposed by the Governor, but a shortfall in State tax receipts could constrain further increases in education aid.

Under federal law, school districts are required to provide appropriate services to students with disabilities through individualized education programs (IEPs). If the district cannot provide the required services itself, it must reimburse parents for private schools and/or outside services that are included in the IEP. Additionally, if a parent challenges the district's evaluation of their child in the IEP, the district may be required by an independent arbiter to fund additional services.

The February Plan assumes that the cost of these services will decline by $170 million to $293 million in FY 2019. However, such costs have increased in each of the past five fiscal years. Accordingly, it is likely that the City will be called upon to increase its funding for these services by at least $170 million beginning in FY 2019.

2. Metropolitan Transportation Authority

The Metropolitan Transportation Authority is facing its greatest crisis in decades. Service has deteriorated on the City's subways, buses and commuter railroads, and the MTA has large funding gaps in its operating and capital budgets. Subway ridership has fallen for three consecutive years, and the MTA anticipates a further decline in 2019. Fare evasion has increased and is responsible for more than $200 million in lost revenue, according to the MTA.

While the MTA projects a balanced operating budget for 2019, it projects out-year gaps that grow from $467 million in 2020 to $976 million in 2022. These estimates assume fare and toll increases of 4 percent in 2019 and 2021.[11]

While the MTA is seeking new sources of funding from the State to help close the projected budget gaps, it recently directed its agencies to identify $500 million in recurring savings beginning in 2020.[12] The MTA has also warned that it may become necessary to reduce services or increase fares and tolls more than planned to close the projected budget gaps.

The MTA has also indicated that it has large unfunded capital needs, although it has not yet released its 20-year capital needs assessment. The president of New York City Transit (which operates the City's subways and buses) estimates that about $40 billion will be needed over the next 10 years to modernize the subway and bus system.

The Governor's executive budget would authorize the MTA to establish a congestion tolling program in Manhattan's Central Business District (defined as 60th Street and below, excluding FDR Drive) to help fund the capital

[10] This estimate includes debt service and pension contributions.

[11] On February 27, 2019, the MTA approved fare and toll increases to raise revenue from this source by 4 percent.

[12] Nonreimbursable costs would be reduced by $350 million annually and capital reimbursable costs by $150 million annually.

program. If approved, implementation could not begin before December 31, 2020.

The program would require the MTA to establish a congestion tolling capital lockbox fund. The MTA could pledge congestion toll revenue from the fund to secure bonds, notes or other obligations for any MTA capital projects within the 2020-2024 capital program, or any successor program, or to pay the cost of capital projects, debt service and reserve requirements.

For-hire vehicles (which are subject to a separate congestion toll established last year), as well as emergency vehicles, would be exempt from the congestion toll. Vehicles using the Queens Midtown Tunnel, the Hugh Carey Tunnel, the Holland Tunnel, the Lincoln Tunnel or the Henry Hudson Bridge would be credited an amount equal to the toll for the crossing prior to entering the congestion zone.

The Governor's proposed budget would require the MTA to develop a reorganization plan that could, in whole or in part, include the assignment, transfer, sharing or consolidation of powers, functions or activities of the MTA. A majority of the MTA Board would have to approve any reforms before they could be implemented. However, the MTA is not authorized to implement any reforms that would impair the rights of the MTA's bondholders or violate any labor agreements.

The proposed budget would establish a mass transit expert panel, consisting of six members, to oversee the preparation of a performance and financial audit of the capital and operating budgets of the MTA. The proposed legislation does not indicate who would appoint the members of the panel or their terms of service.

The oversight panel would also be required to review and approve the capital and operating budgets of the MTA; review and approve the MTA's 2020-24 capital plan and successor plans; review and approve the MTA's reorganization plan; assess fiscal and programmatic risk; and improve work force management. The panel would also determine the congestion toll amounts, which would include a variable pricing structure. The panel would be required to ensure that net revenues (i.e., after operating costs) would be sufficient to fund at least $15 billion for MTA capital projects over the next 10 years.

In addition, the budget would authorize the City to install, over three years, 150 additional speed cameras in school zones. The revenue generated by the additional cameras would be paid to New York City Transit to support capital initiatives for improvements to system safety.

The Governor's proposed budget appropriates the final $1.5 billion installment of the State's $7.3 billion commitment for the MTA's 2015-2019 capital plan, but it makes payment of any of the $7.3 billion contingent on the State Legislature passing the bills on congestion pricing, the mass transit expert panel, MTA reform and school-zone speed cameras. In addition, the State would make payment after the MTA has effectively exhausted all other MTA sources of capital funding, or when MTA capital resources planned for the capital program are not available, but no later than SFY 2025-26 or the completion of the 2015-2019 capital program.

Subsequent to the release of the 30-day amendments, the Governor and the Mayor announced an agreement to transform and fund the MTA. The 10-point agreement calls for the consolidation and streamlining of all common functions (e.g., procurement); implementation of congestion pricing and other new sources of revenue to help fund the MTA's capital program; limiting mass transit fare increases to 2 percent per year through cost-containment; increased efforts to combat fare evasion; the completion of an independent audit by January 2020; all major construction projects to be pursued as design-build; and the expedited completion of the Subway Action Plan.

In addition to revenue from congestion pricing, the agreement dedicates to the MTA's capital program a fixed amount of revenue from the proposed tax on internet sales within New York City (with a growth factor), as well as a percentage of the State and City revenue from the proposed cannabis excise tax. Despite these new resources, it remains to be seen whether the State or the City will be required to increase their contributions to the MTA's capital program since the MTA has not yet its proposed five-year capital program for 2020-2024.

Under the agreement, the capital program will be reviewed by a new committee of transportation, engineering and government experts appointed by the Governor, the Mayor, the State Assembly and Senate, and organizations representing subway riders and driving commuters. The committee will also review the toll and fare increases proposed by the MTA as necessary to fund the capital program. It is unclear at this time how the committee would interact with the MTA Board and the Capital Program Review Board, which also approves the capital program.

In addition, all major construction projects will be reviewed by construction and engineering experts not affiliated with the MTA or its consultants. The Governor and the Mayor also pledged to work closely with the Legislature to effectuate the provisions in the agreement.

3. New York City Housing Authority

The New York City Housing Authority (NYCHA) is an important component of the City's supply of affordable housing. NYCHA manages approximately 176,000 apartments that house nearly 400,000 residents, which amounts to 8 percent of the City's rental apartments.

According to NYCHA, federal funds make up 60 percent ($2.1 billion) of NYCHA's operating budget and 86 percent of the portion that is not funded with rent proceeds. As a result of inadequate federal funding coupled with mismanagement, the City's public housing properties have fallen into disrepair.

On January 31, 2019, the City and the U.S. Department of Housing and Urban Development (HUD) signed a voluntary agreement to remedy the deficient physical conditions in NYCHA properties, ensure that NYCHA complies with its obligations under federal law, and reform the management structure of NYCHA.

The agreement requires the City to provide the $2 billion in capital funding to NYCHA that was originally planned during the City's capital plan for fiscal years 2018 through 2027. The City will also be required to supplement these capital funds with an additional $1 billion during fiscal years 2020 through 2023, and then $200 million annually thereafter beginning in FY 2024.

The City is also required to provide nearly $1 billion in operating assistance to NYCHA during fiscal years 2018 and 2027, and to not impose any payment requirements on NYCHA. The February Plan includes the agreed-upon capital and operating funding during the financial plan period.

In addition, the agreement requires the City, HUD and the Southern District to jointly agree on the selection of a permanent chairman and CEO for NYCHA. HUD and the Southern District will also appoint a monitor in consultation with NYCHA and the City. The monitor will approve or reject action plans developed by NYCHA to achieve sustained compliance with milestones detailed in the agreement to remedy lead paint conditions as well as to resolve deficiencies related to heat, mold, elevators and pests.

The City is required to pay for the costs of the monitor as well as the cost of a consultant to propose organizational reforms at NYCHA. These costs have not been included in the February Plan.

NYCHA estimates that its capital needs will total $31.8 billion over the next five years and $45.2 billion over the next 20 years. Despite the commitment of additional City and State funding, the amount of capital resources currently available to NYCHA over the next five years is less than $8 billion, a fraction of the total.[13]

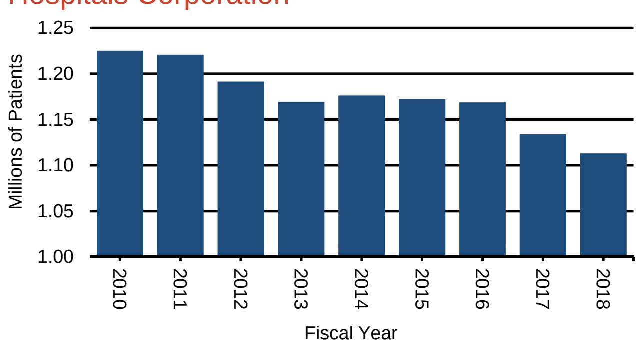
On December 12, 2018, the City announced a proposal that, if fully realized, could address an additional $16 billion of NYCHA's capital needs over the next 10 years. The proposal requires the participation of private developers and an expansion of the federal Rental Assistance Demonstration program.

4. Health and Hospitals Corporation

The Health and Hospitals Corporation provides health and mental health services to more than 1.1 million City residents. The Corporation faces significant challenges, including the declining use of services and a large share (more than one-third) of patients who lack health insurance.

Since FY 2010, the Corporation has attempted to restructure and transform itself. The Corporation has implemented initiatives to increase revenues and reduce costs (including staff reductions), but a structural imbalance between revenues and expenses persists.

FIGURE 26
Total Patients Served at the Health and Hospitals Corporation

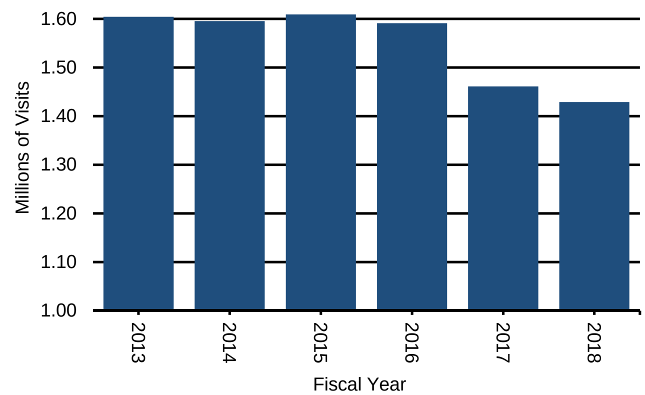


Source: NYC Mayor's Management Report

[13] NYCHA expects the State to provide it with $450 million in capital funding in 2019, but the State has not agreed to provide the funding.

As shown in Figure 26, the number of patients served by the Corporation declined by 112,000 patients (9 percent) between fiscal years 2010 and 2018. Industrywide, patient care has shifted to less costly outpatient settings, but the Corporation has not kept pace with this trend. For example, primary care visits (a subset of outpatient visits) declined by 11 percent between fiscal years 2015 and 2018 (see Figure 27). During the first quarter of FY 2019, primary care visits continued to decline.

FIGURE 27
Patient Primary Care Visits



Sources: NYC Health and Hospitals Corporation; OSC analysis

The City expects to increase its financial support from $1.1 billion in FY 2014 to $2 billion by FY 2022. The February Plan includes additional funding for the Corporation to increase enrollment in health insurance programs and to provide free or subsidized services to those who cannot afford coverage.

Although the Affordable Care Act reduced the number of residents without health insurance by nearly half, about 600,000 still lack coverage. Beginning this summer, Bronx residents ineligible for coverage will be able to enroll in NYC Care, a new City-funded program that guarantees care (including a primary care physician) at one of the Corporation's facilities. In 2021, the program will be expanded citywide.

The Corporation's financial plan projects a large cash balance for FY 2020 ($885 million). However, it also projects annual losses that grow from $99 million in FY 2021 to $399 million in FY 2023. As a result, the cash balance is projected to decline to $114 million by FY 2023. Moreover, these estimates assume successful implementation of future gap-closing actions (e.g., $1.6 billion in FY 2021), which obscures the size of the underlying budget gaps.

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