Review of the Financial Plan of the City of New York

Report 3-2017

OFFICE OF THE NEW YORK STATE COMPTROLLER
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August 2016

Message from the Comptroller

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As the State's chief financial officer, I have a constitutional and statutory responsibility to oversee 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 citizen 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

On June 14, 2016, the City of New York submitted a four-year financial plan (the “June Plan”) covering fiscal years 2017 through 2020 (see Figure 1) to the New York State Financial Control Board.

The City ended FY 2016 with a projected surplus of $4 billion (the largest since FY 2008), which was used to balance the FY 2017 budget. The surplus resulted from unanticipated tax revenues, debt service savings and a drawdown of unneeded reserves. The June Plan also reflects the citywide savings program, which is expected to generate $6 billion through FY 2020, the largest program in five years.

Despite these favorable developments, the FY 2018 budget gap has grown by more than $900 million over the past year to $2.8 billion and the FY 2019 budget gap is essentially unchanged at $2.9 billion. The City projects a budget gap of $2.3 billion for FY 2020.

Nonetheless, the out-year budget gaps are relatively small as a share of City fund revenues (averaging 4.2 percent), and are manageable under current conditions. The budgets for those years also include a general reserve of $1 billion, which, if unneeded for other purposes, could be used to narrow the gaps. In addition, the City intends to expand the citywide savings program in November 2016, which could reduce the size of the projected budget gaps.

Balancing New York City’s budget in recent years has been aided by strong economic growth and the City’s conservative approach to forecasting tax revenues. While the City’s economy is doing well today, there are reasons to be concerned about the future.

Downward pressure on the economy is still mounting in China, and the United Kingdom’s intention to exit the European Union shook global financial markets and has increased uncertainty.

While the nation continues to add jobs, job growth during the first half of 2016 was the slowest start of any year since 2010. Moreover, the U.S. economy grew by only a modest 2.6 percent in 2015, and most economists expect growth to slow to less than 2 percent in 2016.

Although job growth may exceed the City’s expectations in 2016, it is slowing after record job gains over the past two years. The tourism and retail sectors have been affected by the stronger dollar and weakened global economies, and after two years of job growth the securities industry has resumed downsizing. The City also expects securities industry profitability to decline for the fourth consecutive year.

In addition, the growth in City tax collections has been slowing. Collections slowed to 3.6 percent in FY 2016 after growing at an average rate of 6.9 percent during the five prior fiscal years. The June Plan assumes that collections will slow to 1.8 percent in FY 2017. While property tax collections continue to grow, nonproperty tax collections are expected to decline by 0.8 percent in FY 2017.

The City’s cautious approach to FY 2017 is warranted given the elevated economic risks. The City’s revenue forecasts for subsequent years, however, are less conservative and more vulnerable to an economic setback.

City-funded spending is projected to grow by 4.2 percent annually during the financial plan period, more than twice the inflation rate.

Debt service is projected to increase by 38 percent by FY 2020, reflecting a large increase in the capital program and the City’s conservative interest rate assumptions. Despite the City’s efforts to slow the growth of health insurance costs, these costs are projected to rise by 34 percent.

The City has also made targeted investments in education, health and homeless services that have contributed to the growth in spending.

The FY 2017 budget is balanced, but the Office of the State Comptroller (OSC) has identified budget risks that could increase the projected budget gaps by a net of more than $1 billion by FY 2020 (see Figure 2). While the City's tax forecasts are generally reasonable, the slowing of the City's economy raises concerns.

Each year, overtime costs exceed the amount budgeted by the City, and FY 2017 is unlikely to be an exception. The June Plan assumes these costs will decline by $180 million in FY 2017, but that estimate seems optimistic.

The June Plan does not reflect the full impact of the State budget. The State intends to recoup, over 36 months, $600 million in savings that accrued to the City when it refinanced bonds of the Sales Tax Asset Receivable Corporation at lower interest rates. The June Plan reflects the impact for only the first 12 months. Thus, sales tax collections are likely to be lower by $400 million during the financial plan period.

Pension fund investment earnings fell short of target in FY 2016, largely because of volatility in the equity markets. As a result, the City could be required to increase its planned pension contributions beginning in FY 2018 to make up for the shortfall.

The homeless shelter population increased by 57 percent in the five years since the State and the prior mayoral administration cut funding for rental assistance. More recently, the City has made a significant investment to improve shelter conditions and increase homeless services. The shelter population, however, may not decline as rapidly as anticipated in the June Plan.

The City anticipates $731 million from the sale of taxi medallions during fiscal years 2018 through 2020, but the sale has been repeatedly delayed and market conditions remain unsettled.

The City has reached new labor agreements with nearly all of its unions, but most of those agreements expire in FY 2018. While the City has set aside resources to fund annual wage increases of 1 percent after the agreements expire, the actual cost could be greater.

In addition, the Health and Hospitals Corporation continues to face serious financial challenges. The City has increased its support to $2 billion (more than one-quarter of total receipts), but the Corporation still projects budget gaps that reach $1.8 billion by FY 2020. Although the Corporation has proposed an ambitious gap-closing program, it relies heavily on actions that have fallen short of target in the past. If the program is unsuccessful, the City could be called upon to increase its support.

To its credit, the City continues to add to its reserves. In FY 2015 it raised the general reserve to a record level of $1 billion, and last year it created a $500 million Capital Stabilization Reserve.

The City has also replenished the Retiree Health Benefits Trust, which was drawn down by the prior administration to help the City navigate through the Great Recession. In FY 2016, the City deposited an additional $500 million, raising the balance to a record $3.9 billion.

In conclusion, the economy is slowing and there are a number of budget risks that could increase the size of the out-year budget gaps. At the same time, the City has entered a period of heightened economic uncertainty. To its credit, the City has prudently increased its reserves to historic levels, which will provide a cushion against any adverse development.

FIGURE 1

New York City Financial Plan

(in millions)

	FY 2017	FY 2018	FY 2019	FY 2020
Revenues				
Taxes				
General Property Tax	$ 24,025	$ 25,410	$ 26,920	$ 28,191
Other Taxes	29,904	31,092	32,081	33,182
Tax Audit Revenue	714	714	714	714
Subtotal: Taxes	$ 54,643	$ 57,216	$ 59,715	$ 62,087
Miscellaneous Revenues	6,407	6,434	6,678	6,777
Unrestricted Intergovernmental Aid	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(1,764)	(1,764)	(1,759)	(1,765)
Disallowances Against Categorical Grants	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 59,271	$ 61,871	$ 64,619	$ 67,084
Other Categorical Grants	853	837	835	831
Inter-Fund Revenues	646	644	582	581
Federal Categorical Grants	7,673	6,811	6,680	6,618
State Categorical Grants	13,673	14,293	14,763	15,249
Total Revenues	**$ 82,116**	**$ 84,456**	**$ 87,479**	**$ 90,363**
Expenditures				
Personal Service				
Salaries and Wages	$ 25,745	$ 27,213	$ 28,749	$ 29,582
Pensions	9,422	9,710	9,852	9,783
Fringe Benefits	9,679	10,254	10,932	11,879
Retiree Health Benefits Trust	- - -	- - -	- - -	- - -
Subtotal: Personal Service	$ 44,846	$ 47,177	$ 49,533	$ 51,244
Other Than Personal Service				
Medical Assistance	5,915	5,915	5,915	5,915
Public Assistance	1,584	1,602	1,613	1,624
All Other	27,450	26,393	26,666	26,556
Subtotal: Other Than Personal Service	$ 34,949	$ 33,910	$ 34,194	$ 34,095
Debt Service[1]	6,579	6,949	7,456	8,115
FY 2016 Budget Stabilization[1]	(3,994)	- - -	- - -	- - -
Capital Stabilization Reserve	500	- - -	- - -	- - -
General Reserve	1,000	1,000	1,000	1,000
Subtotal	$ 83,880	$ 89,036	$ 92,183	$ 94,454
Less: Intra-City Expenses	(1,764)	(1,764)	(1,759)	(1,765)
Total Expenditures	**$ 82,116**	**$ 87,272**	**$ 90,424**	**$ 92,689**
Gap to be Closed	**$ - - -**	**$ (2,816)**	**$ (2,945)**	**$ (2,326)**

Source: NYC Office of Management and Budget

[1] The FY 2016 Budget Stabilization totals $3.994 billion, including GO of $1.760 billion, TFA-PIT of $1.734 billion, lease debt service of $100 million, and subsidies of $400 million.

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

	Better/(Worse)			
	FY 2017	**FY 2018**	**FY 2019**	**FY 2020**
Surplus/(Gaps) Per NYC Financial Plan	**$ - - -**	**$ (2,816)**	**$ (2,945)**	**$ (2,326)**
Tax Revenues	(50)	(50)	(50)	(50)
Uniformed Agency Overtime	(150)	(150)	(150)	(150)
Sales Tax Asset Receivable Corporation	(50)	(200)	(150)	- - -
Special Education Medicaid Reimbursement	(22)	(79)	(79)	(79)
Pension Fund Investment Earnings	- - -	(122)	(244)	(366)
Debt Service	200	- - -	- - -	- - -
Miscellaneous Revenues	100	100	100	100
Homeless Shelters	- - -	(125)	(125)	(125)
Sale of Taxi Medallions	- - -	(107)	(257)	(367)
Revenue from Development Opportunities	- - -	- - -	- - -	(100)
OSC Risk Assessment	**28**	**(733)**	**(955)**	**(1,137)**
Potential Surplus/(Gaps) Per OSC[2]	**$ 28**	**$ (3,549)**	**$ (3,900)**	**$ (3,463)**

[2] The June Plan includes a general reserve of $1 billion in each of fiscal years 2017 through 2020, which, if not needed, could be used to help close the projected budget gaps. In addition, the Capital Stabilization Reserve has a balance of $500 million in FY 2017, and the Retiree Health Benefits Trust, which the City has used in the past as a rainy-day fund, has a projected balance of $3.9 billion.

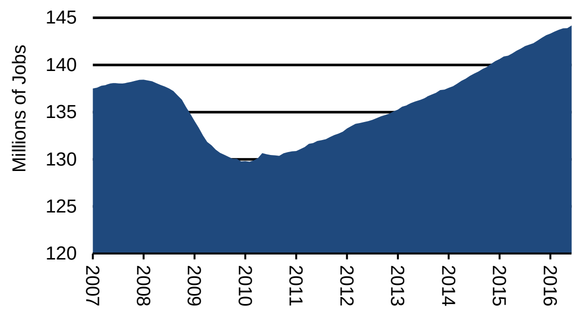
II. Economic Trends

The global economy is weakening and the United Kingdom's intention to exit the European Union has heightened uncertainties. Although the U.S. economy is slowing, it is outperforming most other nations. New York City's economic expansion is also slowing.

The National Economy

The United States added 2.9 million jobs in 2015, the most since 1999, but job growth has slowed in 2016. While the nation has added jobs for 69 consecutive months, the increase during the first half of 2016 was the slowest start of any year since 2010. The nation has added 14.4 million jobs since the end of the recession (5.7 million more than were lost during the recession), and set a new record of 144.2 million jobs in June 2016 (see Figure 3).

FIGURE 3
U.S. Employment



Note: Data are seasonally adjusted.
Source: U.S. Bureau of Labor Statistics

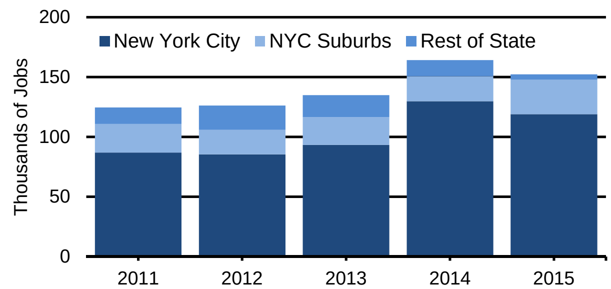
Despite the large increase in employment, wage growth remains sluggish and inflation remains well below the target set by the Federal Reserve. The national economy grew by only a modest 2.6 percent in 2015, and it is increasingly likely that growth will slow further in 2016. In December 2015, the Federal Reserve raised interest rates for the first time in nearly a decade, but economic developments have caused the Fed to postpone its plans for further rate increases.

New York Employment Trends

Between 2009 and 2015, New York State added 706,500 jobs, 469,200 more than were lost during the recession. Only California, Texas and Florida added more jobs. However, the rate of job growth has begun to slow, increasing by 1.8 percent in 2014, 1.7 percent in 2015 and 1.3 percent during the first half of 2016.

Moreover, job growth has not been uniform across the state. In 2015, New York City and its suburbs (Nassau, Suffolk, Westchester, Rockland and Orange counties) added 147,700 jobs (see Figure 4), accounting for 97 percent of the jobs added in the state that year. (Since 2009, the City and its suburbs have accounted for 92 percent of the statewide job gains.) Job growth remained strong in the downstate region during the first half of 2016 (growing by 2.1 percent), but it weakened in the rest of the State.

FIGURE 4
State Job Growth Concentrated in New York City and Its Suburbs



Sources: NYS Department of Labor; OSC analysis

Some areas, like Buffalo, continue to add jobs, but Albany and Rochester had small job losses during the first half of 2016. Some upstate regions, such as Syracuse, have not recovered all of the jobs lost during the recession, while other areas, such as Binghamton, have continued to lose jobs even during the recovery.

Since 2009, New York City has added 532,000 jobs, with nearly half added in the last two years alone. The June Plan assumes that growth will slow from 119,000 jobs in 2015 to 53,000 in 2016. Although job growth is slowing, OSC expects it to slow more gradually than assumed in the June Plan, with the City adding 80,000 jobs in 2016.

The business, health care and construction sectors continue to exhibit strong job growth during the first half of 2016. However, weakness in the global economy has dampened visitor spending and thus job growth has slowed in tourism-related industries (i.e., restaurants and hotels) and the retail sector has lost jobs.

Unemployment

The national unemployment rate was 4.9 percent in June 2016, half its recessionary peak. New claims for unemployment benefits have declined from the recessionary peak of 665,000 to less than 300,000 for 73 consecutive weeks.

New York State's unemployment rate fell from its recessionary peak (8.9 percent) to 4.7 percent in June 2016, slightly less than the national rate and only slightly higher than the prerecession level.

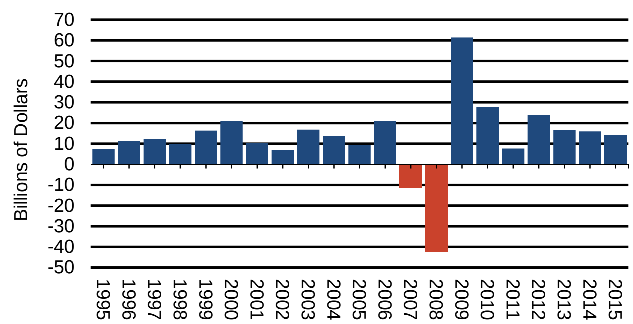
The City's unemployment rate is now half its recessionary peak (10.2 percent), falling to 5 percent in June 2016 (the lowest since 2007). Despite this progress, some workers have much higher rates of unemployment. For example, the unemployment rate for those without a high school diploma was 13.3 percent in 2015. In addition, more than one-third of the City's unemployed have been out of the work force for six months or more, compared to one-fourth before the recession.

Securities Industry

The securities industry is an important part of the City's economy. Even though it accounts for less than 5 percent of the jobs, it accounts for 21 percent of all private sector wages.

Pre-tax profits for the broker/dealer operations of New York Stock Exchange (NYSE) member firms (the traditional measure of industry profitability) declined in 2015 for the third consecutive year to $14.3 billion (see Figure 5). Despite a strong first quarter, profitability deteriorated as the year progressed, with the fourth quarter bringing the first loss since 2011.

FIGURE 5
Securities Industry Profits



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

Current trends also do not bode well for the securities industry in 2016. Profits totaled $3.4 billion in the first quarter, nearly 50 percent less than last year, and revenues declined by 10 percent, the largest drop since the fourth quarter of 2011. The City expects profits to decline by 26 percent in 2016 to $10.6 billion, which would be the fourth year of lower profits.

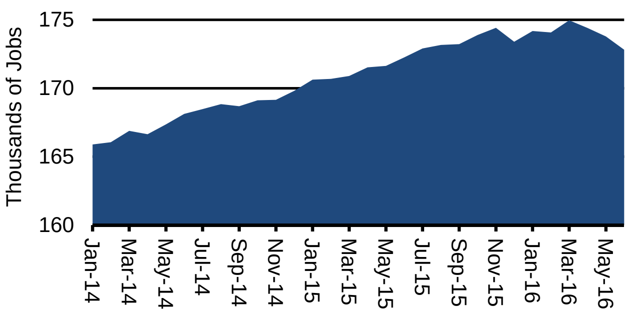
Ongoing weaknesses in the global economy and market volatility are likely to lead to lower bonuses in 2016 as well. OSC estimated that the bonus pool for securities industry employees who work in New York City declined in 2015 (by 6 percent) for the second consecutive year.

Also, federal regulators recently proposed rules to restrict excessive risk-taking by regulating bonus payments at financial institutions, which could affect bonuses in the future. The rules would require the largest firms to defer at least half of the bonus payments for top executives and significant risk-takers for a minimum of four years (one year longer than industry practice). These changes could reduce the amount of tax revenue the City would otherwise realize from securities industry bonuses.

Over the past two years the securities industry in New York City has added 6,900 jobs, the first time since the financial crisis that the industry has added jobs for two consecutive years. Despite the job gains, the industry was still 8 percent smaller than before the 2008 financial crisis and the industry has resumed downsizing.

After adding jobs at a strong pace for most of 2015, job growth in the securities industry in New York City began languishing late in the year, and by April 2016 the industry had begun to shed jobs (see Figure 6). A number of large financial firms have announced plans to reduce costs to improve profitability, which could lead to further job losses in New York City.

FIGURE 6
Securities Industry Job Growth



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

Tourism

NYC & Company, the official tourism and marketing organization of New York City, estimates that a record 58.3 million visitors came to the City in 2015, an increase of 33 percent since 2006. As the number of visitors has increased over the past decade, the hotel industry has added more than 34,000 new hotel rooms and more than 11,000 jobs. In 2015, occupancy and room rates eased as the supply of rooms increased and tourist spending slowed.

Real Estate

New York City's commercial and residential real estate markets have grown significantly over the past six years, with rising property values and larger transaction volumes boosting tax collections. The average price of transactions has grown by 14.2 percent since 2009, with commercial prices (23.4 percent) growing at a significantly higher rate than residential prices (10.4 percent), according to data from the City's Department of Finance.

In 2015, sales of large Manhattan commercial buildings (priced at $50 million or more) totaled $26.7 billion, the highest level since 2007.[3] Residential sales volume reached an all-time high of $73 billion in 2015. In total, sales increased by 14 percent in 2015.

While the total number of transactions during the first quarter of 2016 increased slightly, the value of these sales declined by 12.5 percent. The value of commercial sales fell sharply, by 37.6 percent.

[3] Large commercial sales in Brooklyn reached a record $907 million (the previous high was $718 million in 2012).

Wages

Job growth in the City has been strong, but wage growth has lagged. Much of the job growth has been in lower-wage sectors, for jobs such as restaurant workers, retail store workers and home health aides. Since 2007, median household income in New York City has declined by 4.6 percent (after adjusting for inflation).

In an effort to boost income for the lowest-paying jobs, New York State plans to raise the statewide minimum wage from $9 per hour to $15 per hour. For workers in New York City employed by large businesses (those with at least 11 employees), the minimum hourly wage would rise to $11 at the end of 2016, then by another $2 each year until reaching $15 on December 31, 2018. For small businesses in New York City (those with 10 employees or fewer), the minimum wage would rise to $15 an hour by December 31, 2019.[4]

The wage increase is expected to impact more than 900,000 New York City residents who currently earn less than $15 per hour, according to the State Department of Labor. Workers in the retail trade and leisure and hospitality sectors will receive the largest benefit. U.S. Census Bureau data show that more than half of these workers earned less than $15 per hour in 2014.

Conclusion

China's slowdown and weak commodity prices have taken a deep toll on emerging markets, and growth in other advanced nations has been sluggish since the financial crisis. The United Kingdom's referendum to leave the European Union increases uncertainties. Job growth in the U.S. is slowing, corporate profits are under pressure and industrial production has declined for the past ten months.

New York City is still doing well, but there are signs the economic expansion is slowing. Job growth has tapered off from last year's record pace. In addition, a strong dollar and weakness in overseas economies have dampened visitor spending, which has affected restaurants, retail shops and other businesses that rely on tourism.

Although the City has become more diversified and less reliant on Wall Street since the financial crisis, the securities industry is still an important part of the local economy. Results for the first quarter suggest that 2016 could be a difficult year for the industry.

The national economic recovery has already lasted much longer than the average length for recoveries during the post–World War II era. New York City has experienced six consecutive years of job growth and the June Plan anticipates another five years of growth, which would exceed the current record of eight years.

Changes in the business cycle are inevitable, but predicting the turning point is always difficult. While a downturn may not be imminent, the economy is slowing and risks are elevated.

4 Wages in Long Island will reach $15 an hour by 2021, and the timeline for the rest of the State will be determined based on an annual analysis of the regional economies.

III. Changes Since the Beginning of the Fiscal Year

In June 2015, the City projected a balanced budget for FY 2016 and a budget gap of $1.5 billion in FY 2017 (see Figure 7). One year later, the City estimates that it ended FY 2016 with a $4 billion surplus (the largest since the 2008 financial crisis) and projects a balanced budget for FY 2017.

Despite favorable developments that led to the improvement in the City's short-term financial outlook, the budget gap for FY 2018 has grown by $909 million to $2.8 billion and the FY 2019 budget gap is unchanged at $2.9 billion. (The City projects a gap of $2.3 billion for FY 2020.)

The out-year gaps are relatively small as a share of City fund revenues (averaging 4.2 percent). The budgets for those years also include a historic general reserve of $1 billion, which, if unneeded, could be used to narrow the gaps.[5]

The City continues to benefit from its conservative approach to forecasting tax revenues. Over the past 12 months, the City raised its tax revenue forecast by nearly $5 billion through FY 2019, including $1.6 billion in FY 2016. Most of the additional revenue is expected to come from real estate and personal income taxes, partly offset by lower business tax collections. The City also expects to realize $4.9 billion from the citywide savings program, including nearly $1.2 billion in debt service savings. Given these favorable developments, the City freed up nearly $2 billion in unneeded reserves in FY 2016.

In total, the City identified cumulative resources of nearly $12.1 billion through FY 2019. Most of the resources were used to fund increased spending ($10.5 billion), and the balance was used to offset the impact of the State budget and to relieve the Water Board of an annual rental payment to the City.

The City also deposited $500 million into the Retiree Health Benefits Trust, raising the year-end balance to a record $3.9 billion, and maintained the Capital Stabilization Reserve at $500 million.

Nearly one-third of the additional spending ($3.1 billion) stems from an increase in planned pension contributions, mostly to make up for an investment shortfall in FY 2015 and the use of updated mortality tables.

The City also funded a number of new agency needs, which total nearly $8.3 billion through 2019 (about $2.1 billion annually). For example, funding for homeless services was increased by nearly $1.3 billion through FY 2019, and City funding to the Department of Education grew by more than $1.2 billion.

The Health and Hospitals Corporation has been allocated more than $1 billion ($497 million in FY 2016 alone) and funding for the uniformed agencies has increased by $953 million, largely to improve security at the Department of Correction and to staff additional ambulance tours at the Fire Department.

The June Plan also reflects costs associated with a number of City Council initiatives, which are funded only in FY 2017 ($352 million). In addition, the City also added funding during the entire financial plan period to a number of public health programs (e.g., mental health services) and to other City Council priorities (e.g., summer youth employment and six-day public library service) during the budget adoption process for FY 2017.

[5] In FY 2016, the City began budgeting for an annual general reserve of $1 billion. At this level, it is the largest ever, both in absolute dollars and as a share of City-funded expenditures.

FIGURE 7
Financial Plan Reconciliation—City Funds
June 2016 Plan vs. June 2015 Plan
(in millions)

	Better/(Worse)			
	FY 2016	FY 2017	FY 2018	FY 2019
Projected Gaps Per June 2015 Plan	**$ - - -**	**$ (1,465)**	**$ (1,907)**	**$ (2,853)**
Revenue Reestimate				
Real Estate Transaction Taxes	590	66	25	36
General Property Tax	531	532	907	1,351
Personal Income Tax	256	374	447	524
Business Taxes	(173)	(360)	(216)	(349)
Sales Tax	(28)	(54)	(60)	(6)
Other Taxes	95	28	36	57
Tax Audits	349	3	3	3
Subtotal: Taxes	**1,620**	**589**	**1,142**	**1,616**
Taxi Medallion Sales	- - -	(107)	(150)	(110)
All Other	619	116	86	216
Total	**2,239**	**598**	**1,078**	**1,722**
Citywide Savings Program				
Agency Actions	1,102	990	817	860
Debt Service	539	143	247	249
Total	**1,641**	**1,133**	**1,064**	**1,109**
Reserves				
General Reserve	980	- - -	- - -	- - -
Capital Stabilization Reserve	500	(500)	- - -	- - -
Prior-Year Payable	500	- - -	- - -	- - -
Total	**1,980**	**(500)**	**- - -**	**- - -**
Expenditure Reestimates				
Energy	- - -	49	42	26
Debt Service	32	86	(26)	(1)
Technical Adjustments	155	(124)	(24)	(7)
All Other	475	(51)	17	222
Total	**662**	**(40)**	**9**	**240**
New Needs				
Pension Contributions	(530)	(703)	(933)	(975)
Health and Hospitals Corporation	(497)	(180)	(173)	(179)
Uniformed Agencies	(241)	(286)	(214)	(212)
Services for the Homeless	(204)	(401)	(305)	(352)
Department of Education	(162)	(343)	(358)	(364)
Other Health and Social Services	(13)	(277)	(275)	(292)
City Council Initiatives	- - -	(352)	- - -	- - -
All Other	(311)	(894)	(686)	(693)
Total	**(1,958)**	**(3,436)**	**(2,944)**	**(3,067)**
Other				
Retiree Health Trust Fund	(500)	- - -	- - - -	- - -
State Budget Impact	(50)	(150)	- - -	- - -
Water Board Rental Payment	(20)	(134)	(116)	(96)
Net Change During FY 2016	**3,994**	**(2,529)**	**(909)**	**(92)**
Surplus/(Gap)	**$ 3,994**	**$ (3,994)**	**$ (2,816)**	**$ (2,945)**
Surplus Transfer	(3,994)	3,994	- - -	- - -
Projected Gaps Per June 2016 Plan	**$ - - -**	**$ - - -**	**$ (2,816)**	**$ (2,945)**

Sources: NYC Office of Management and Budget; OSC analysis

IV. Impact of State Actions

The State budget for fiscal year 2016-2017 increases education aid to New York City by $525 million in FY 2017, which is reflected in the June Plan. However, the City has not reflected the full impact of an initiative that was advanced by the Governor and approved by the State Legislature that will cost the City $600 million over three years.

In October 2014, the Sales Tax Asset Receivable Corporation refinanced bonds at lower interest rates, realizing significant savings that benefited the City. The Governor and the State Legislature believe that the State should have benefited from the refinancing since the debt service on the bonds is paid by the State.

To provide the State with the benefit of the refinancing, State law requires the State Comptroller to intercept $16.7 million each month in sales tax receipts intended for the City for a period of 36 months (a total of $600 million). The City's financial plan, however, only reflects the cost for the first 12 months ($50 million in FY 2016 and $150 million in FY 2017). Under current law, the City will lose an additional $400 million during fiscal years 2017 through 2019.

The State budget excludes two proposals that were made by the Governor in January 2016 that would have shifted a larger share of the cost of Medicaid and the senior colleges of the City University of New York (CUNY) to the City's budget. These proposals would have cost the City $785 million in FY 2017 and much larger amounts in subsequent years.

The State approved a personal income tax reduction program that will lower tax rates over a seven-year period beginning in 2018. The State Division of the Budget estimates that more than 2 million New York City taxpayers will save a total of $1.3 billion annually beginning in 2025 (saving each taxpayer an average of $653).

The State appropriated $1 billion to help cover the cost of expanding the Jacob K. Javits Convention Center on the far West Side of Manhattan. Javits is the busiest convention center in the nation, but it ranks 13th for prime exhibit space. When completed, the project could generate an estimated 200,000 additional hotel room stays annually, an increase of 42 percent over the current level.

The State also appropriated $2 billion over five years for a statewide housing program. The State budget director and legislative leaders have reached an agreement on the allocation of the first $150 million, which will be used to finance and operate supportive housing units. The amount dedicated to New York City projects remains undetermined.

In addition to the budget, the State also approved a plan to raise the minimum wage for private sector workers over the next few years. For workers in New York City employed by large businesses (those with at least 11 employees), the minimum hourly wage would rise from $9 to $15 by December 31, 2018. For small businesses, the minimum wage would reach $15 per hour by December 31, 2019.

In June 2016, after the budget was adopted, the State extended mayoral control of New York City schools for one year. The Mayor had initially sought a seven-year extension.

The State Legislature also approved a bill that would require the State to assume the entire cost of providing legal services to indigent people over a seven-year period beginning on April 1, 2017. Currently, the State's 62 counties spend more than $500 million a year, and the State reimburses about one-third of these costs. If the bill is signed into law by the Governor, New York City could realize savings of more than $300 million during the financial plan period.

V. The Citywide Savings Program

In January 2016, the Mayor announced a citywide savings program that was designed to generate $1.8 billion during fiscal years 2016 through 2020. The program was expanded in April and again in June, and is now expected to generate nearly $6 billion (see Figure 8), the largest program in five years.

Of this amount, more than three-quarters (nearly $4.7 billion) will come from agency actions, with the balance ($1.3 billion) coming from lower debt service. As discussed below and shown in Figure 8, agency actions include funding shifts, reestimates, administrative efficiencies and revenue initiatives.

The largest initiative involves Medicaid savings of more than $1.5 billion through FY 2020. Beginning in 2014, the Affordable Care Act (ACA) offered states the option of expanding Medicaid eligibility to low-income individuals, with the federal government funding the entire cost for the first three years. For states that had expanded coverage prior to the law, such as New York, the reimbursement rate will gradually increase to 90 percent by 2020.

Since the City's financial plan had not previously reflected the impact of the ACA, the City realized annual savings of $305 million beginning in FY 2016. It is likely that the City will realize additional savings as the reimbursement rate increases from 85 percent to 90 percent.

The City anticipates savings of nearly $1.6 billion through FY 2020 from cost reestimates, including $454 million in FY 2016. More than half of the savings ($851 million) result from slower than anticipated growth in staffing and supplemental welfare fund benefits. Additional savings ($297 million) will come from an expected decline in the cost of judgments and claims.

Administrative efficiencies are expected to save $1 billion through FY 2020. One-fifth of the savings will come from eliminating the reserve that offsets the impact of inflation on procurement. Inflation is expected to remain low, and agencies will be expected to offset the loss through efficiencies to maintain service levels.

A new legal case management system is expected to reduce the cost of judgments and claims by $143 million through FY 2020. A Law Department pilot program in the Bronx assigned cases to one attorney (instead of a team of attorneys) who was responsible for all legal preparation, court proceedings, and appeals. The program is now being expanded to all cases in the Bronx and Brooklyn.

FIGURE 8
Citywide Savings Program
(in millions)

	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020	Total
Agency Actions						
Medicaid Reestimate	$ 305	$ 305	$ 305	$ 305	$ 305	$ 1,526
Cost Reestimates	454	391	227	243	275	1,592
Funding Shifts	283	44	34	34	34	429
Administrative Efficiencies	31	221	237	265	274	1,028
Revenue	27	27	13	12	12	91
Subtotal	**1,101**	**989**	**817**	**860**	**900**	**4,667**
Debt Service	**540**	**143**	**247**	**249**	**132**	**1,311**
Total	**$ 1,641**	**$ 1,132**	**$ 1,064**	**$ 1,108**	**$ 1,032**	**$ 5,978**

Note: Totals may not add as a result of rounding.
Sources: NYC Office of Management and Budget; OSC analysis

Consolidating administrative functions and implementing programmatic changes at the Human Resources Administration (HRA) is expected to generate $321 million in administrative efficiencies. For example, the management of the Department of Homeless Services will be folded into the HRA (for savings of $165 million). In addition, the HRA intends to increase homeless prevention services and supportive housing placements, which is expected to reduce the demand for shelters (saving $156 million).

The City realized estimated savings of $283 million in FY 2016 from shifting financial responsibility from the City to the federal and State governments. Most of the savings in FY 2016 came from an increase in federal and State reimbursements for fringe benefits associated with social services programs. Additional savings of $146 million is expected in subsequent years, mostly from higher State reimbursements for child welfare services.

Revenue initiatives are expected to generate $91 million through FY 2020. Nearly all of the resources would come from fees and fines (e.g., franchise fees on cable subscriptions, fines for unsafe sidewalk conditions, and fees for the use of public street space by utilities).

Nearly one-quarter of the savings in the citywide savings program ($1.3 billion) will come from lower debt service. The City realized savings of $540 million in FY 2016, mostly from lower-cost variable rate debt (from both lower interest rates and fees). Additional savings in subsequent years will come from delays in capital commitments in FY 2016 and from refinancing debt at lower interest rates.

The citywide savings program includes some initiatives that may fall short of target. In the event that this occurs, the State Comptroller recommends that the City be prepared with alternative initiatives.

The Mayor has stated that he intends to announce a new round of cost-saving actions in November 2016 with the release of the first-quarter financial plan modification. These initiatives could reduce the budget gaps projected for fiscal years 2018 through 2020.

VI. Revenue Trends

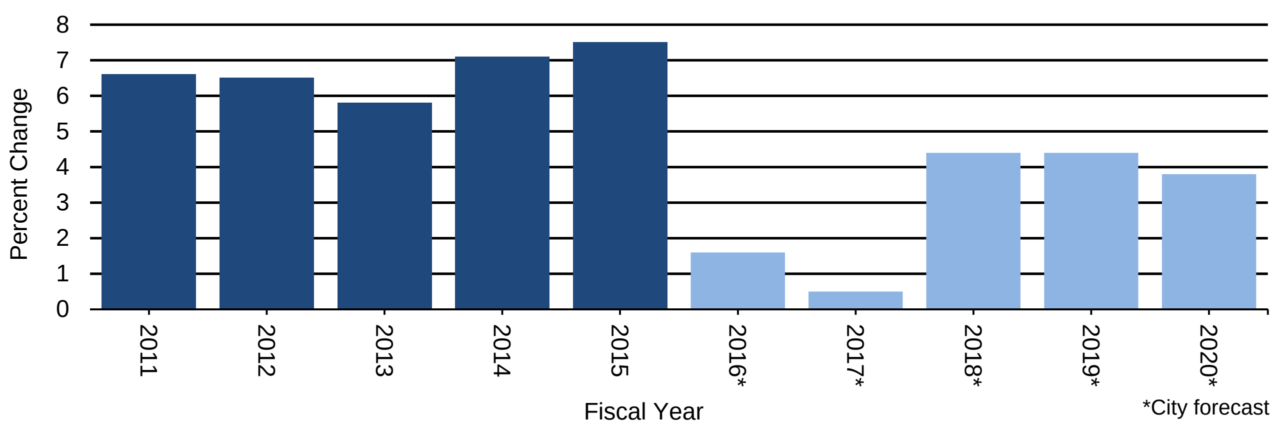
After increasing at an average annual rate of 6.7 percent during the past five fiscal years, City fund revenues grew by an estimated 1.6 percent in FY 2016 (see Figure 9). The June Plan assumes that City fund revenues will slow even further to 0.5 percent in FY 2017.

While property tax collections continue to show strong gains, the City expects nonproperty tax collections to decline by 0.8 percent in FY 2017 in response to weaker business profits, declines in the financial markets and lower tourism spending.

The City's cautious approach to FY 2017 is warranted given current collection trends and recent economic developments. The June Plan assumes that growth in nonproperty tax collections will rebound during fiscal years 2018 through 2020 (averaging 3.4 percent annually), but that assumption may be optimistic.

In addition, the June Plan anticipates $731 million during fiscal years 2018 through 2020 from the sale of taxi medallions, and $100 million in FY 2020 from development opportunities at properties leased to the Health and Hospitals Corporation. As discussed later in this report, the receipt of these resources is uncertain. As previously discussed, the City has not fully reflected the impact of the State budget. As a result, sales tax collections could be $400 million lower than assumed in the June Plan.

FIGURE 9
Annual Change in City Fund Revenues



Sources: NYC Office of Management and Budget; OSC analysis

FIGURE 10
City Fund Revenues
(in millions)

	FY 2016	FY 2017	Annual Growth	FY 2018	FY 2019	FY 2020	Average Three-Year Growth Rate
General Property Tax	$ 22,913	$ 24,025	4.9%	$ 25,410	$ 26,920	$ 28,191	5.5%
Personal Income Tax	11,038	11,225	1.7%	11,553	11,971	12,436	3.5%
Sales Tax	6,998	7,266	3.8%	7,557	7,880	8,216	4.2%
Business Taxes	5,961	6,009	0.8%	6,344	6,442	6,596	3.2%
Real Estate Transaction Taxes	2,923	2,643	-9.6%	2,678	2,760	2,836	2.4%
Other Taxes	2,946	2,911	-1.2%	2,960	3,028	3,098	2.1%
Tax Audits	1,060	714	-32.6%	714	714	714	0.0%
Subtotal: Taxes	**53,839**	**54,793**	**1.8%**	**57,216**	**59,715**	**62,087**	**4.3%**
Sales Tax Intercept	(50)	(150)	NA	- - -	- - -	- - -	NA
Miscellaneous Revenues	5,224	4,643	-11.1%	4,670	4,919	5,012	2.6%
Grant Disallowances	(15)	(15)	0.0%	(15)	(15)	(15)	0.0%
Total	**58,998**	**59,271**	**0.5%**	**61,871**	**64,619**	**67,084**	**4.2%**

Note: OSC has adjusted FY 2016 for changes in the School Tax Relief program to make it comparable to the City's financial plan forecasts.
Sources: NYC Office of Management and Budget; OSC analysis

The June Plan is based on the trends shown in Figure 10 and discussed below.

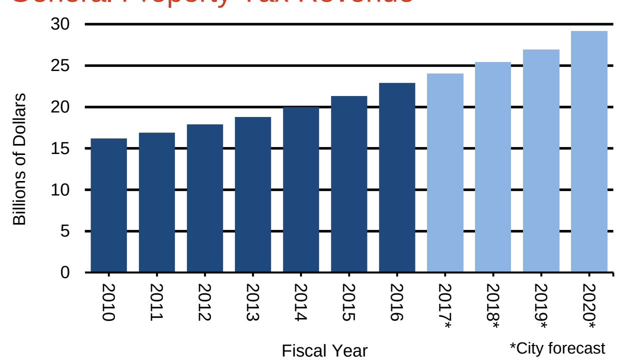
1. General Property Tax

Property taxes are the City's largest revenue source, accounting for 44 percent of tax revenues in FY 2017. Collections are projected to grow by 4.9 percent in FY 2017 to reach $24 billion (see Figure 11). Growth is forecast to be slower than in FY 2016, when the City lowered the property tax reserve and collections rose by 7.5 percent.

In May, the City released the final property tax roll for FY 2017, which shows that property values surged by 9.8 percent to reach $1 trillion, stronger than last year's growth rate (7 percent). Property value growth was strongest for one-, two- and three-family homes, at 12.2 percent. Values for large residential and commercial properties, which are based on market conditions in prior years, grew by 9.5 percent and 6.5 percent, respectively.

Between FY 2010 and FY 2017, collections have grown by $7.8 billion (an average annual growth rate of 5.8 percent) as a result of strong growth in commercial and residential property values. During this time, average tax bills have increased by $27,000 for commercial properties and by $1,500 for home owners, though the overall tax rate has remained unchanged during this period.

FIGURE 11
General Property Tax Revenue



Sources: NYC Comptroller; NYC Office of Management and Budget

State law requires changes in assessed values for commercial and large residential properties to be phased in over five years. The amount of revenue from the pipeline is expected to remain relatively constant during the financial plan period (averaging $900 million annually), creating a cushion against an economic slowdown that might impact property values. During the Great Recession, the five-year phase-in prevented a decline in property tax collections.

2. Personal Income Tax

Between fiscal years 2009 and 2015, personal income tax collections increased at an average annual rate of 8.3 percent as the economy expanded, employment increased at record rates and the stock market rebounded after the financial crisis.

Despite record job gains, collections slowed during FY 2016 as wage growth weakened, Wall Street bonuses declined and volatility in the financial markets led to lower capital gains. As a result, personal income tax collections were forecast by the City to increase by only 1.6 percent in FY 2016, the slowest rate in seven years. However, actual collections were weaker than expected.

Personal income tax collections, which account for one-fifth of tax collections, are projected to increase by only $187 million in FY 2017, an increase of 1.7 percent.[6] This forecast is less conservative now than it would have been a few months ago given recent economic developments. The June Plan assumes collections will accelerate, averaging 3.5 percent during fiscal years 2018 through 2020, but that assumption may be optimistic.

3. Sales Tax

Sales tax collections have risen steadily in recent years, boosted by spending from a robust local economy and a record number of tourists visiting New York City. Since FY 2009, sales tax revenue grew by an average of 6.6 percent annually, but growth began to slow in FY 2015, as weakness in the global economy and a strong dollar have dampened visitor spending.

Sales tax collections grew at an estimated 3.8 percent in FY 2016, and the June Plan assumes a similar rate of growth in FY 2017 (after adjusting for the effects of the State intercept of sales tax revenue). The June Plan assumes that the growth in sales tax collections will pick up slightly during the remainder of the financial plan, averaging 4.2 percent annually.

OSC estimates that collections could be lower by $50 million annually beginning in FY 2017 because the City's top three countries for overseas tourism (the United Kingdom, Brazil and China) are facing economic uncertainties.

As previously discussed, sales tax collections could be lower by $400 million during the financial plan period ($50 million in FY 2017, $200 million in FY 2018 and $150 million in FY 2019) because the State intends to recoup savings that accrued to the City from refinancing bonds of the Sales Tax Asset Receivable Corporation at lower interest rates.

[6] Beginning in FY 2017, the State has changed how it reimburses the City for benefits provided to home owners and renters under the School Tax Relief Program. To better understand personal income tax trends, OSC has adjusted FY 2016 so it is comparable to the City's financial plan forecasts.

4. Real Estate Transaction Taxes

Revenues from the real estate transaction taxes have grown rapidly during the recovery, rising from $1 billion in FY 2010 to $2.9 billion in FY 2015 (see Figure 12). Despite the extraordinary growth, revenues did not reach the prerecession peak of $3.3 billion (in FY 2007). In FY 2016, however, the growth in collections ended. The June Plan assumes that collections will decline by $280 million in FY 2017 as the economy slows, but it assumes growth will resume in subsequent years.

5. Business Taxes

In April 2015, the State combined the City's banking and general corporation taxes. While the change is expected to be revenue-neutral, collections were trending below expectations during the fourth quarter of FY 2016, which could have implications for subsequent years.

Business tax collections were forecast by the City to decline by 1.5 percent in FY 2016, ending five years of growth. The decline reflects lower Wall Street profits and only moderate growth in nonfinancial sectors. The City expects collections to increase by 0.8 percent in FY 2017, but 2016 is shaping up to be another difficult year for Wall Street.

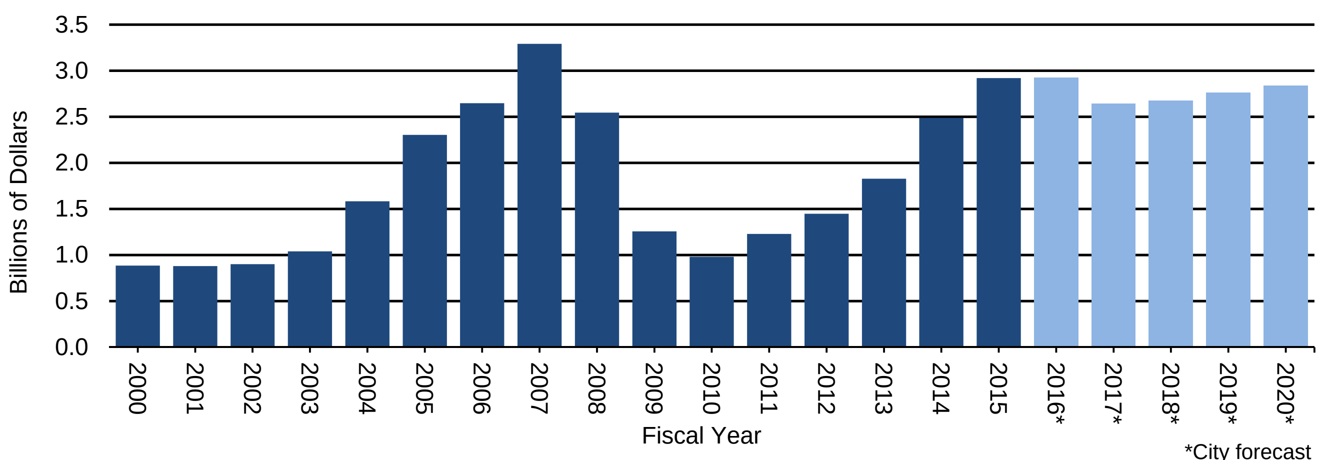
6. Miscellaneous Revenues

Miscellaneous revenues (e.g., fines, fees and proceeds from the sale of City property) are projected to total $4.7 billion in FY 2017. OSC estimates that revenues from fines, rental payments and charges for services could be higher by $100 million annually beginning in FY 2017 based on collections in FY 2016.

The June Plan also anticipates revenue from the sale of taxi medallions ($107 million in FY 2018, $257 million in FY 2019 and $367 million in FY 2020). However, the sale has been repeatedly delayed and market conditions remain unsettled. The growing presence of alternatives to taxis (including services such as Uber and Lyft) has lowered demand for taxi medallions. Consequently, OSC believes these revenues could be at risk.

The City also expects $100 million in FY 2020 from development opportunities at properties leased to the Health and Hospitals Corporation. The City intends to transfer the proceeds to the Corporation to help balance its budget. In the event of a shortfall, the City may be called upon to make up the difference or the Corporation may be required to cut more than already planned.

Figure 12
Real Estate Transaction Taxes Revenue



Sources: NYC Comptroller; NYC Office of Management and Budget

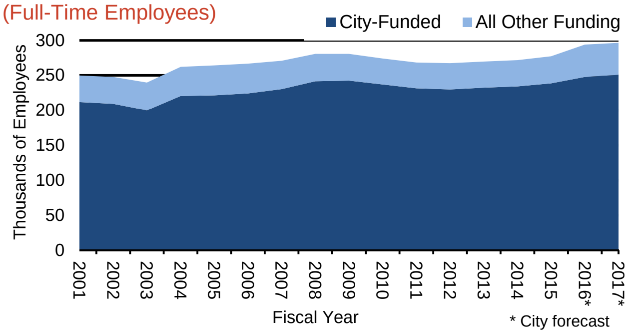
VII. Expenditure Trends

The adopted budget for FY 2017 totals $82.1 billion, including spending funded by federal and State grants. The portion of the budget funded with locally generated revenue (i.e., City funds) is projected to total nearly $59.3 billion. After adjusting for surplus transfers and debt defeasances, which can mask expenditure trends, City-funded spending is projected to reach $63.3 billion in FY 2017 (see Figure 13), an increase of 7.9 percent (5.4 percent excluding reserves).

City-funded spending is projected to grow at an average annual rate of 4.2 percent during the financial plan period (more than twice the projected inflation rate) to reach $69.4 billion by FY 2020. This represents an increase of $19.7 billion (nearly 40 percent) since FY 2013. Growth is driven by the cost of recent labor agreements, higher costs for employee fringe benefits and debt service, and new programmatic initiatives.

The City's full-time work force (including jobs fully funded by the federal and State governments) grew by 9,750 employees between fiscal years 2012 and 2015. The June Plan anticipated the addition of another 16,845 employees during FY 2016 (see Figure 14), but many of these positions remained vacant.

FIGURE 14
Staffing
(Full-Time Employees)

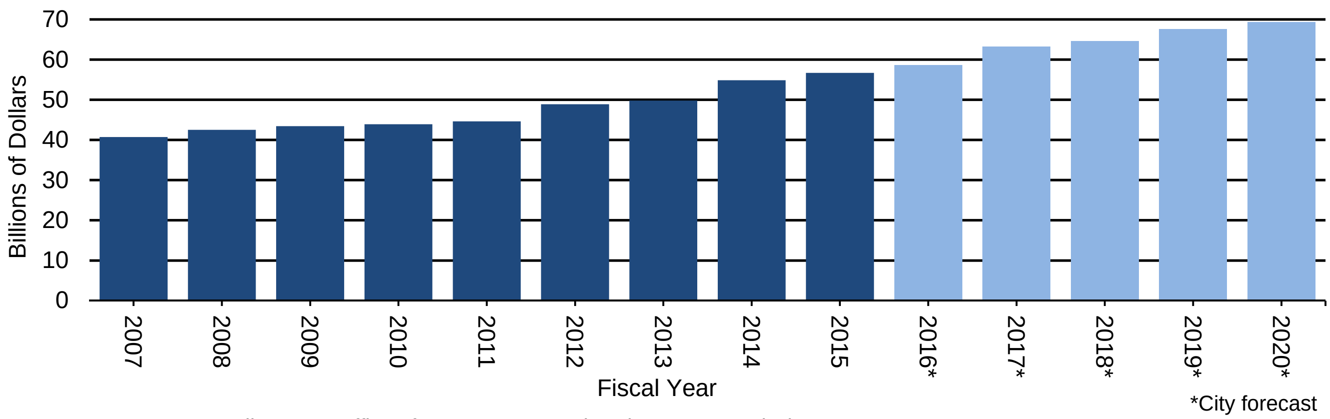


Note: Staffing levels are as of June 30 of each fiscal year.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

As of May 2016, the City had added 8,791 full-time employees, half of the number planned for the year. (Teachers, police officers and correction officers accounted for nearly two-thirds of the new hires in FY 2016.) Even so, it is the largest one-year increase since FY 2008, and the work force exceeded the prerecession level by 5,315 employees.

The June Plan assumes that the FY 2016 vacancies will be filled by the end of FY 2017 and that the City will add another 2,470 employees. If all of the positions are filled as planned, the full-time work force would reach 296,488 employees by the end of FY 2017, which would be 15,839 more than the prerecession level.

FIGURE 13
Growth in City-Funded Expenditures



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

FIGURE 15
City-Funded Expenditures
(in millions)

	FY 2016	FY 2017	Annual Growth	FY 2018	FY 2019	FY 2020	Average Three-Year Growth Rate
Salaries and Wages	$ 16,834	$ 17,468	3.8%	$ 18,801	$ 20,196	$ 20,912	6.2%
Pension Contributions	9,141	9,278	1.5%	9,566	9,708	9,639	1.3%
Medicaid	5,715	5,813	1.7%	5,813	5,813	5,813	0.0%
Debt Service	5,695	6,315	10.9%	6,685	7,199	7,864	7.6%
Health Insurance	4,466	4,813	7.8%	5,094	5,503	5,979	7.5%
Other Fringe Benefits	2,797	2,783	-0.5%	2,845	3,060	3,355	6.4%
Energy	689	738	7.1%	791	842	873	5.8%
Judgments and Claims	515	536	4.1%	552	567	585	3.0%
Public Assistance	650	703	8.2%	713	718	724	1.0%
Other	12,109	13,318	10.0%	12,827	12,958	12,666	-1.7%
Subtotal	**58,611**	**61,765**	**5.4%**	**63,687**	**66,564**	**68,410**	**3.5%**
Retiree Health Benefits Trust	500	- - -	NA	- - -	- - -	- - -	NA
General Reserve	20	1,000	NA	1,000	1,000	1,000	NA
Prior Year's Expenses	(500)	- - -	NA	- - -	- - -	- - -	NA
Capital Stabilization Reserve	- - -	500	NA	- - -	- - -	- - -	NA
Total	**$ 58,631**	**$ 63,265**	**7.9%**	**$ 64,687**	**$ 67,564**	**$ 69,410**	**3.1%**

Note: Debt service has been adjusted for surplus transfers and redemptions. The cost of judgments and claims excludes medical malpractice claims filed against the Health and Hospitals Corporation.
Sources: NYC Office of Management and Budget; OSC analysis

The June Plan is based on the trends shown in Figure 15 and discussed below.

1. Collective Bargaining

As of July 2016, the City had reached new labor agreements with nearly all of the municipal unions. The agreements call for wage increases of 10 percent over seven years for civilian employees and 11 percent over seven years for uniformed employees. The City expects the remaining unions with expired contracts to reach conforming agreements.

The agreements also compensate members of the United Federation of Teachers (UFT) and other employees for two annual wage increases of 4 percent that were provided to most other municipal unions in 2009 and 2010 but not to these employees.

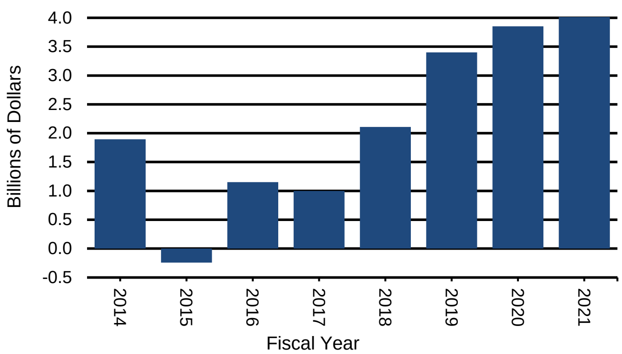
The City and the Patrolmen's Benevolent Association (PBA) have not been able to reach a negotiated agreement. In November 2015, a three-member arbitration panel awarded police officers two annual wage increases of 1 percent for 2011 and 2012, which was consistent with the City's financial plan. The PBA has petitioned the Public Employment Relations Board to declare an impasse in the current negotiations and to appoint a mediator. If mediation fails, the dispute could be resolved through binding arbitration.

The City estimates that recently negotiated and anticipated agreements will cost $13.8 billion during fiscal years 2014 through 2018 (the end of the contract period), 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 new wage agreements ($3.5 billion), and from health insurance savings ($4.4 billion) that are expected to result from a separate agreement between the City and its unions. The net budgetary impact during fiscal years 2014 through 2018 will total $5.9 billion.

The budgetary impact will be greatest during fiscal years 2018 through 2021, and will peak at $4 billion in FY 2021 (see Figure 16). Beginning in FY 2018, the cost continues to rise after the expiration of the contracts because of lump-sum payments 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.

FIGURE 16

Net Budgetary Impact of Labor Settlements



Sources: NYC Office of Management and Budget; OSC analysis

The June Plan includes resources to fund annual wage increases of 1 percent after the expiration of the current round of collective bargaining, which for most employees would be during FY 2018. The actual cost of the next round of collective bargaining will be determined through negotiation or arbitration, and could be higher than assumed in the June Plan. Wage increases at the projected inflation rate, for example, would increase costs by an additional $166 million in FY 2018, $507 million in FY 2019 and $1.1 billion in FY 2020.

2. Pension Contributions

After rising rapidly between fiscal years 2003 and 2012, the growth in City-funded pension contributions slowed over the next three years. The slower rate of growth reflects the impact of changes in assumptions and methodologies used to calculate City pension contributions,[7] better-than-expected investment returns,[8] and savings from lower-cost pension plans for City employees hired after March 31, 2012.

Pursuant to a biennial review mandated by the City Charter, an independent actuarial consultant recommended (in October 2015) a number of changes in the actuarial assumptions used to calculate contributions to the five pension funds.

Upon the recommendation of the City Actuary, the boards of trustees of the five pension systems implemented the consultant's recommendation to utilize updated mortality tables. The recommendation required the City to increase its planned pension contributions by about $600 million annually beginning in FY 2016. The consultant offered other recommendations, but these are still under review by the City Actuary.[9]

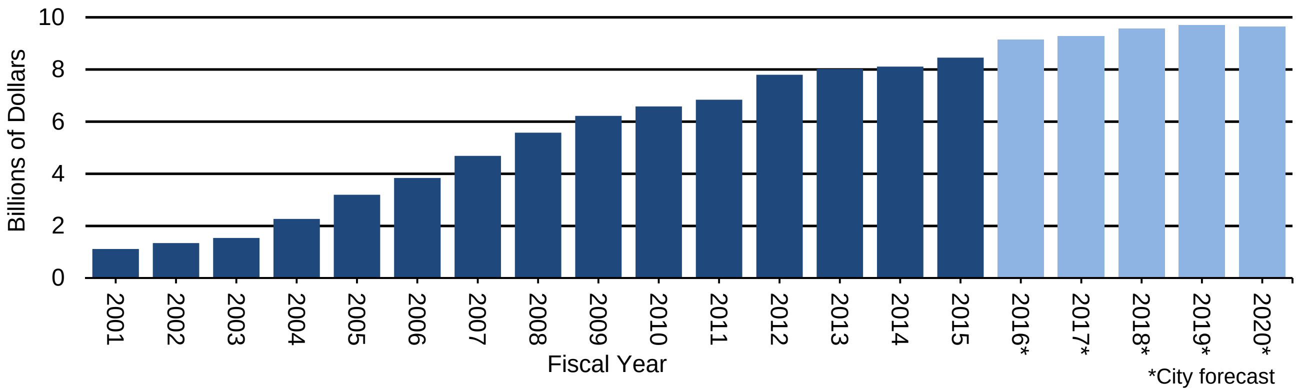
The June Plan shows that pension contributions will reach $9.6 billion by FY 2020 (see Figure 17), accounting for 14.4 percent of City fund revenues. These estimates assume that the pension funds earn, on average, 7 percent on their investments each year. However, investment earnings have fallen short of expectations for the past two fiscal years.

[7] 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.

[8] The pension funds earned, on average, 13.4 percent annually on their investments during fiscal years 2010 through 2014, compared to the expected annual return of 7 percent.

[9] If the independent actuarial consultant's other recommendations are adopted as proposed, pension contributions would increase by an additional $300 million annually. Most of the increase would come from higher overtime costs.

FIGURE 17
Pension Contributions
City-Funded



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

In FY 2015, the pension funds earned less than half of the expected gain. Consequently, the unfunded net pension liability rose to $52 billion, and future contributions to the pension funds will increase faster than previously planned to make up for the shortfall.[10]

Pension fund investment earnings fell short of expectations in FY 2016 as well, even though the stock market rebounded from heavy losses earlier in the year. According to the City Comptroller, the City's five pension funds earned less than 1.5 percent on their investments during FY 2016, a significant shortfall from the expected return of 7 percent. As a result, the City could be required to increase its pension contributions by $122 million in FY 2018, $244 million in 2019, and by $366 million in FY 2020.

The State Legislature recently approved a bill that would increase disability pension benefits for firefighters hired after June 30, 2009. Under the bill, these employees will be eligible for disability payments equal to 75 percent of the five consecutive years that produce the highest average salary.[11] The cost of the enhanced benefit will be shared between the City and the employees. The City estimates that its share of the cost will total $48 million through FY 2021.

The City has also agreed to increase the benefits of uniformed members of the Department of Correction and the Sanitation Department hired after March 31, 2012. State approval is not required for these employees since the cost will be paid by employees who elect to receive the additional benefit. The City and the union representing police officers have not reached agreement on a proposal to increase disability benefits to police officers hired after June 30, 2009.

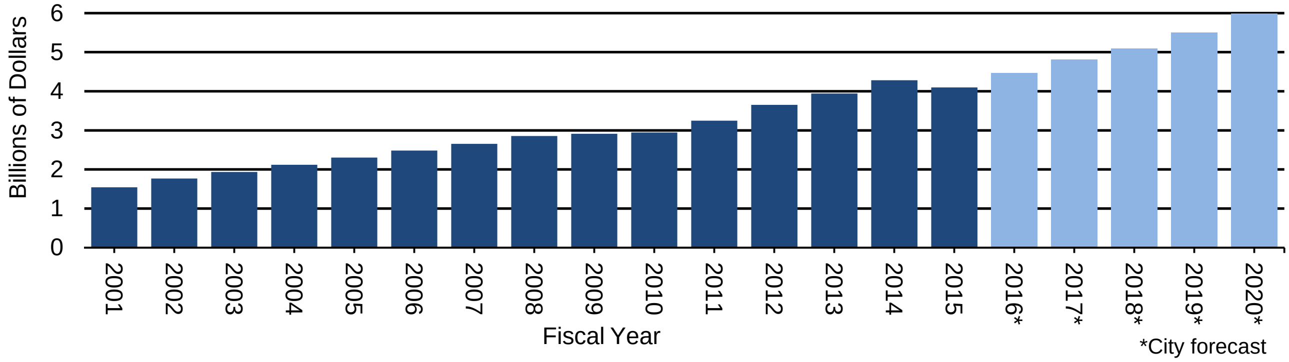
3. Health Insurance

As part of the current round of collective bargaining, the City and the Municipal Labor Committee reached agreement in May 2014 to identify savings that could be used to help fund wage increases for municipal employees.

[10] The pension systems had sufficient assets to fund, on a market value basis, 70.5 percent of their accrued pension liabilities as of June 30, 2015, two percentage points less than in the prior year.

[11] Currently, these employees are eligible for half of the five-year average, less 50 percent of their Social Security Disability Insurance benefits.

FIGURE 18
Health Insurance Costs
City-Funded



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

The agreement calls for 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 in subsequent years. The agreement includes provisions that provide incentives to both the City and the unions to exceed the planned targets. The City is confident that it has reached the $700 million savings target for FY 2016 and that it is on track to meet the $1 billion savings target for FY 2017.

Thus far, more than three-quarters of the $3.4 billion in savings ($2.7 billion over four years) has come from administrative actions and lower-than-planned increases in health insurance premiums. Cost-containment initiatives are expected to save $454 million, 13 percent of the total. The City has yet to identify the sources of the remaining $232 million in savings.

The City and unions are working together to expand the number of cost-containment initiatives. Discouraging the use of higher-cost health services by increasing co-pays for emergency room, urgent care and specialty care is expected to save $170 million. Imposing a $10 co-pay for the use of "nonpreferred" health providers is expected to save $128 million.

Despite the anticipated savings from the agreement with the Municipal Labor Committee, City-funded health insurance costs are projected to reach $6 billion by FY 2020 (see Figure 18), $1.7 billion (40 percent) more than in FY 2014.

4. Debt Service

Since July 1, 2015, the City's financial plan has benefited by $1.3 billion in debt service savings, with most of the benefit accruing to fiscal years 2016 and 2017. Much of the savings resulted from favorable short-term interest rates ($382 million) and refinancing long-term bonds at lower interest rates ($381 million). The City also did not need to borrow to meet its cash flow needs given its large cash reserves, saving $64 million in FY 2016.

Since the start of FY 2016, the City has increased its capital program by $7.6 billion, mostly for investments in environmental protection, road and bridge repairs (including the Ed Koch Queensboro Bridge), and public schools. The City also added funding to complete construction of the third water tunnel in Brooklyn and Queens by 2025.

In total, the City now plans to commit $67 billion during fiscal years 2016 through 2020 (more than twice the amount in the prior five-year period). Of this amount, $14.2 billion (21 percent) would be devoted to public schools, $12.3 billion (18 percent) to environmental protection, $10.7 billion (16 percent) to transportation and $7 billion (10 percent) to affordable housing.

City-funded debt service will rise by $2.2 billion (38 percent) to $7.9 billion between fiscal years 2016 and 2020 (see Figure 19). Borrowing is expected to more than double as the City expands its capital program. By FY 2020, debt outstanding will reach $85 billion, $15.7 billion more than in FY 2015.

Figure 19 also shows that debt service as a share of tax revenue (i.e., the debt burden) would rise from 11.6 percent in FY 2015 to 13.1 percent in FY 2020. Debt service would account for a larger share of tax revenue by FY 2020, but the share would remain below 15 percent, a level that is considered high.

The June Plan is based on a number of assumptions, which may increase or decrease the debt burden. For example, it assumes that the City will meet its annual capital commitment target, which has been a problem in the past.

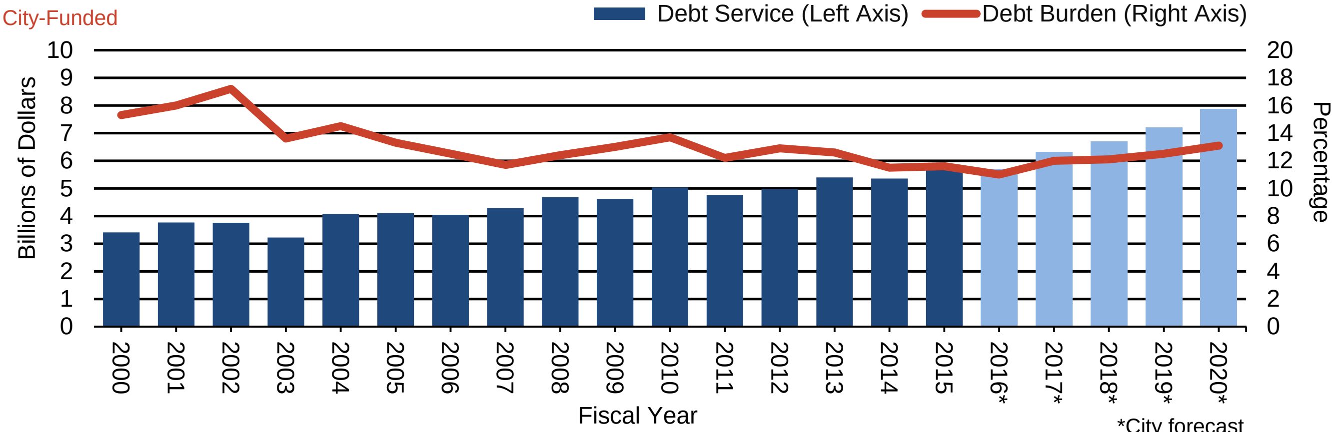
The City assumes that capital commitments will average more than $12.7 billion during fiscal years 2017 through 2020, even though actual commitments in the past five years have averaged $7.7 billion. As of April 2016, agencies had committed only slightly more than half (53 percent) of the FY 2016 year-end target.

Debt service is also dependent on interest rates, and it is likely that interest rates for fixed and variable rate debt will be well below the levels assumed in the June Plan. Given the City's conservative interest rate assumptions and the unlikelihood that the City will need to borrow to meet its cash flow needs, OSC estimates that the City could realize debt service savings of $200 million in FY 2017.

The debt burden is also dependent on tax collections. While the City's forecast for FY 2017 was conservative a few months ago, recent economic developments suggest revenues could be lower than projected by the City for FY 2017.

To prevent debt service from rising too quickly as a share of tax revenues, the City has established a $500 million Capital Stabilization Reserve. The reserve could be used to defease debt to hold down the rise in debt service.

FIGURE 19
Debt Service
City-Funded



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

5. Homeless Services

The number of homeless people residing in shelters operated by the Department of Homeless Services reached a record level of 58,745 in December 2014 (see Figure 20), an increase of 57 percent in five years. The City attributes the increase to several factors, including the elimination of State and City funding for the Advantage rental assistance program and a lack of affordable housing.

In May 2016, the shelter population totaled 57,891 individuals, only slightly less than the December 2014 record. Even though the City is moving more families into permanent housing, the shelter population remains high because more families are entering the system. The number of individuals in the adult family and single adult programs set new records in the spring of 2016.

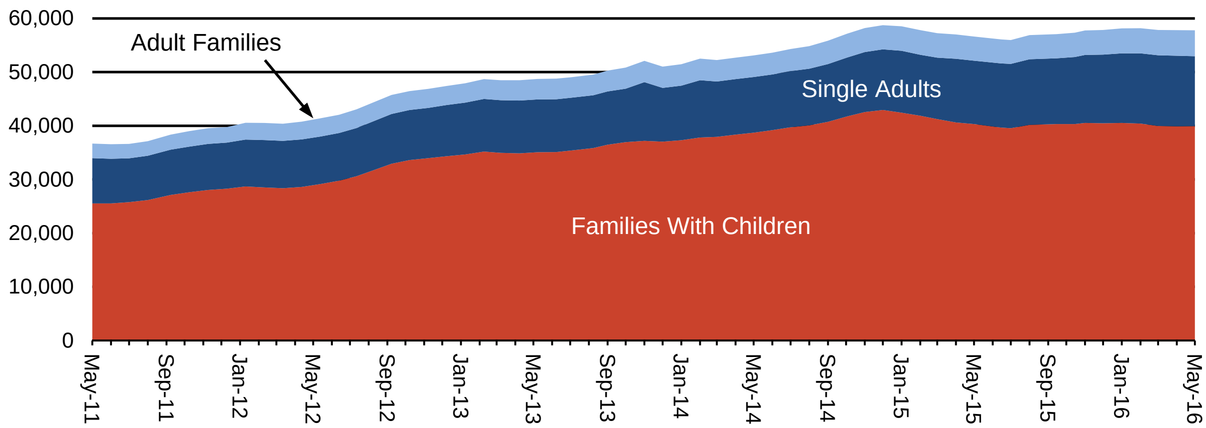
The City recently completed a review of its homeless programs and is planning a number of changes, including improvements in security and shelter conditions. The June Plan dedicates $66 million in FY 2017 for improvements, which will be partly offset by $38 million in savings anticipated from integrating the management of the Department of Homeless Services with the Human Resources Administration.

OSC estimates that the citywide cost of homeless services increased by $677 million (48 percent) between fiscal years 2013 and 2016 to nearly $2.1 billion. The City funded more than two-thirds of the increased costs, while the federal government funded one-fifth and the State funded one-tenth. The June Plan assumes that these costs will reach nearly $2.2 billion in FY 2017.

The City expects that the shelter population will remain at the May 2016 level through FY 2017, but then expects that the family shelter population will decline in FY 2018 as more families are moved into permanent housing. As a result, the City expects the cost of family shelters to decline by 5 percent in FY 2018.

The June Plan expects the cost of sheltering single adults to decline by 24 percent in FY 2018 as hundreds of adults are moved into supportive housing. However, the adult shelter population reached record levels during FY 2016, despite the City's increased efforts. OSC estimates that even without further growth in the adult shelter population, the cost of providing shelter could exceed the City's estimates by $125 million annually beginning in FY 2018.

FIGURE 20
People in Homeless Shelters



Source: NYC Department of Homeless Services

6. Uniformed Agencies

Overtime costs in the uniformed agencies (both for uniformed and civilian employees) are projected to reach $1.3 billion in FY 2016, only $109 million less than the record set in FY 2015 (see Figure 21). The Police Department accounts for about half of the total cost.

The amount of overtime in FY 2015 was the highest level on record and nearly 52 percent higher than five years earlier. The Police, Correction and Sanitation departments each set new records in FY 2015, and overtime costs in the Fire Department were only slightly below the record set in FY 2014.

Each of the uniformed agencies has been dealing with issues that have increased overtime in recent years, such as antiterrorism efforts in the Police Department and staff shortages in the Fire and Correction departments. The City allocated additional resources to the agencies at the start of the fiscal year so they could better manage their overtime budgets.

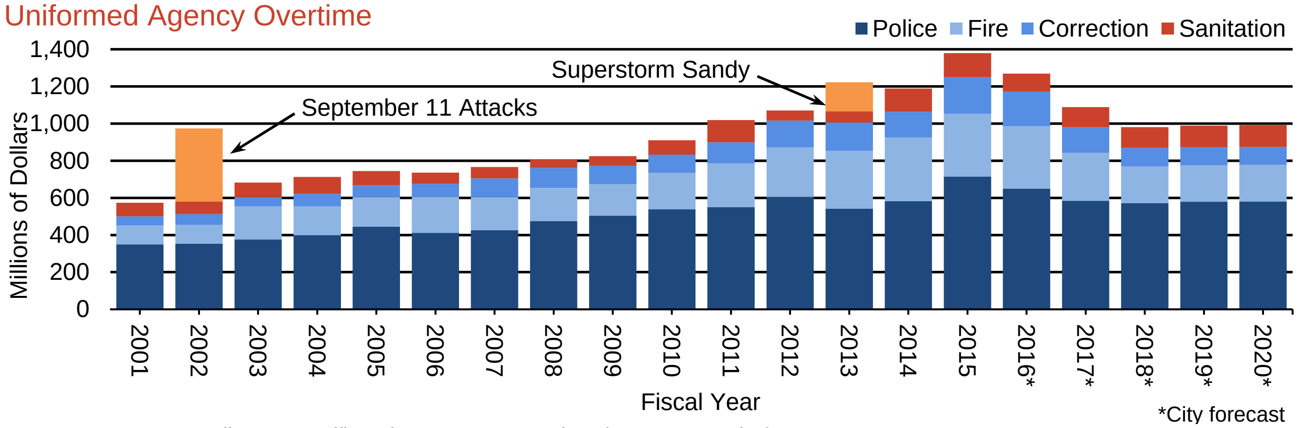
The City increased the size of the police force by 1,297 officers in FY 2016. Most of these officers were dedicated to community policing, but about 350 were assigned to antiterrorism efforts. The Police Department had planned to hire 415 civilians to perform desk work to free up police officers for patrol, but it filled only 122 of these positions as of May 2016.

In light of the additional resources allocated to the Police Department, the Mayor placed a cap on the City-funded share of overtime for uniformed employees, which may be exceeded only in the event of an emergency (such as Superstorm Sandy). The June Plan assumes that the Police Department will adhere to the mayoral cap.

While the Department of Sanitation stayed within its initial overtime allocation, the Fire and Correction departments exceeded their allocations by a total of $187 million in FY 2016, mostly as a result of continued staff shortages. About two-thirds of the unplanned costs were offset by savings from delays in hiring.

The June Plan assumes that overtime at the uniformed agencies will decline by $180 million in FY 2017, and then by another $107 million in FY 2018. Based on current trends, overtime could exceed the City's estimates by $150 million during fiscal years 2017 through 2020. Some of these costs could be offset by federal grants and savings from other personal services.

FIGURE 21
Uniformed Agency Overtime



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

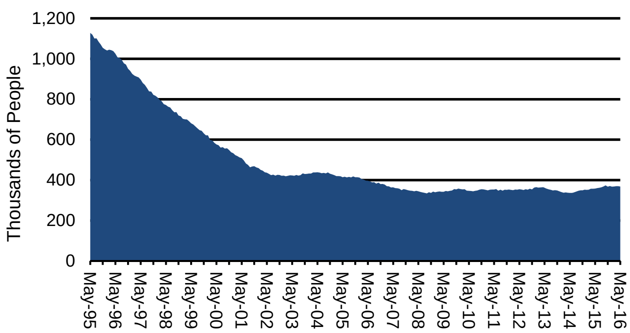
7. Public Assistance

The public assistance caseload fell from more than 1 million in 1995 to 330,000 in 2008 in response to welfare reforms that were implemented in the 1990s that established work requirements. In New York City, about half of the caseload is exempt because of medical or mental health disabilities, or age.

The City's public assistance caseload has remained relatively stable since 2008 (see Figure 22), but recently it increased by 9.5 percent over a two-year period, reaching 368,430 individuals in May 2016. The City attributes most of the increase to changes in policies rather than economic conditions.

FIGURE 22

Public Assistance Caseload



Source: NYC Human Resources Administration

For example, the City has granted recipients greater flexibility in scheduling appointments, which has reduced the number of people who lose their benefits for not meeting administrative requirements. The City also increased the amount of education and training hours that can be applied to a recipient's work requirements, which has allowed more low-income students to receive benefits.

The City plans to provide rental assistance payments to additional low-income families to prevent evictions and homelessness. In addition, the State has adopted new policies that will prevent public assistance recipients from being removed from the caseload for administrative reasons. As a result, the June Plan assumes that the caseload will increase by 5 percent to 388,600 by the end of FY 2017.

City-funded public assistance expenditures are projected to grow by 8 percent to $703 million in FY 2017 to fund an increase in the caseload and to provide enhanced benefits for people living with HIV. Costs are projected to grow slowly in subsequent years.

8. Medicaid

Enrollment in the federal Medicaid program in New York City grew slowly in the years following the recession, but then accelerated with the implementation of the federal Affordable Care Act (ACA) in January 2014. The ACA expands Medicaid eligibility to millions of Americans who were previously ineligible for this program.

In New York City, Medicaid enrollment exceeded 3.7 million people in December 2015, an increase of 16 percent since December 2013. In December 2015, 44 percent of the City's population was enrolled in Medicaid.

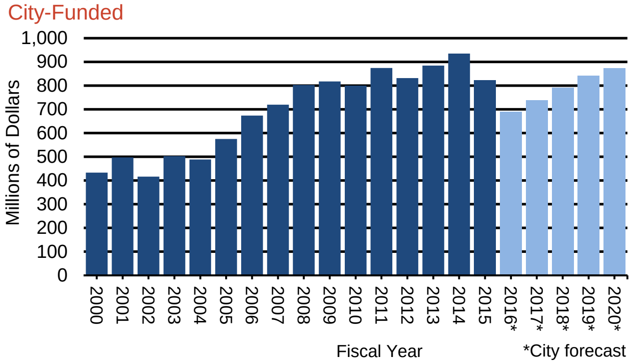
The June Plan assumes that the City's share of the cost of Medicaid will level off at $5.8 billion in FY 2017 (10 percent of City-funded revenue) because the State has completed a three-year phased takeover in the growth in the local share of Medicaid.

The City also realized savings of $305 million annually from a provision in the ACA that increases the federal reimbursement rate to states that expand Medicaid eligibility. For states that had expanded coverage prior to the ACA, such as New York, the reimbursement rate will increase to 90 percent by 2020. The City's financial plan had not previously anticipated the impact of the law, but the City will likely realize additional savings as the reimbursement rate increases from 85 percent to 90 percent.

9. Energy

Energy costs (i.e., electricity, fuel and heat) reached a record high of $935 million in FY 2014 (see Figure 23), mainly because of a harsh winter. In FY 2015, energy costs declined by 12 percent to $822 million (despite another harsh winter), mostly as a result of lower prices for electricity, fuel and heat.

Figure 23
Energy Costs
City-Funded



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

This past winter was relatively mild compared to the two prior years (with the exception of one large snowstorm), and fuel costs have remained low. As a result, energy costs are projected to decline to $689 million in FY 2016, 16 percent less than last year and $100 million lower than forecast at the beginning of the fiscal year. The June Plan assumes that energy costs will increase by 7 percent to $738 million in FY 2017, and will continue to increase to $873 million by FY 2020.

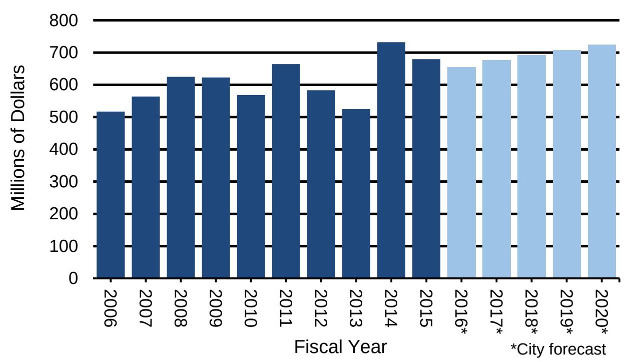
10. Judgments and Claims

The cost of judgments and claims against the City for personal injury, property damage and to resolve contract disputes peaked at $732 million in FY 2014 when a number of costly, high-profile cases were settled. While the cost declined in FY 2015, it remained elevated. The Police Department ($274 million) and the Health and Hospitals Corporation ($127 million) accounted for 60 percent of the cost in FY 2015.

Although the cost of judgments and claims declined for the second consecutive year in FY 2016, the City expects it to increase by 3 percent in FY 2017 to $676 million (see Figure 24). The June Plan assumes that these costs will continue to rise slowly (by 2 percent annually), reaching $725 million by FY 2020.

The June Plan does not reflect the cost of a recent judgment that awarded $183 million to the families of five firefighters who were killed or injured in a Bronx apartment building fire in 2005 ($140 million was attributed to the City). The City is appealing this decision.

FIGURE 24
Judgments and Claims



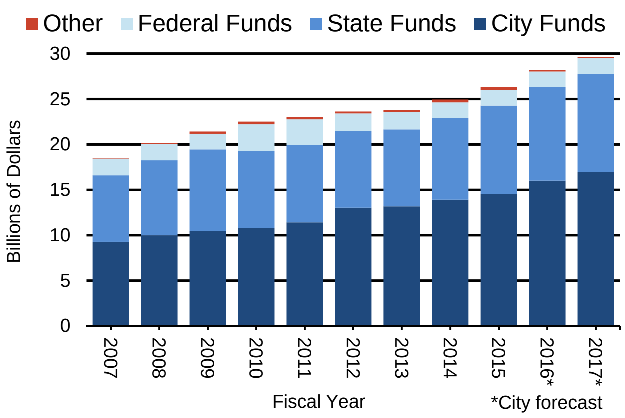
Sources: NYC Comptroller; NYC Office of Management and Budget

VIII. Department of Education

New York City has the largest public school system in the nation, operating more than 1,800 schools and serving more than 1.1 million students. The June Plan allocates $29.7 billion to the Department of Education for FY 2017, $1.5 billion more than forecast for FY 2016. Of this amount, $16.9 billion (57 percent) would come from the City and $10.8 billion (37 percent) would come from the State, with $2 billion (6 percent) coming from the federal government.

Following the Campaign for Fiscal Equity lawsuit, funding for the City's public schools has grown by $11 billion (59 percent) since FY 2007 (see Figure 25). City funding has increased by $7.6 billion, while State funding increased by $3.5 billion (since FY 2013, State funding has increased by $2.4 billion as the State recovered from the Great Recession). Federal funding for the City's schools has declined by 17 percent since FY 2007 after accounting for inflation.

FIGURE 25
Education Funding by Source



Sources: NYC Office of Management and Budget; OSC analysis

The State budget increased education aid to the City by $525 million in FY 2017. The City intends to use $161 million of this amount to help bridge the equity gap among schools. In addition, the State continues to allocate $300 million to New York City to provide prekindergarten services to all four-year-old children.

The City will increase funding for education by $936 million in FY 2017, mostly to cover higher debt service and pension contributions, but also to fund programmatic initiatives, such as the Equity and Excellence program, and to expand physical education and universal prekindergarten programs.

The City's capital plan allocates $14.2 billion to the Department between fiscal years 2016 and 2020, or 23 percent more than was committed during the previous five years. The City will now fund a much higher share of the Department's capital commitments (89 percent) than in the previous five years (53 percent) because the Transitional Finance Authority (a City-created entity that issues debt to fund portions of the City's capital plan) is approaching the State cap on bonds backed by State building aid.

Most of the increase in the capital program is devoted to addressing mandates (such as asbestos removal) and school overcrowding. The Department estimates that an additional 83,000 seats are needed to bring the system into compliance with its standards. The capital program would add 44,300 seats, or about half of the estimated need.

Each year, the Department submits claims to the federal government for Medicaid reimbursement for services provided to students with special needs. The Department, however, has a long history of being unable to properly document such claims. An outside consultant with experience in this area has been hired to help the Department better document claims.

The June Plan assumes Medicaid payments of $18 million in FY 2016, $40 million in FY 2017 and $97 million beginning in FY 2018. Until the Department demonstrates that it can adequately document such claims, OSC considers the receipt of $22 million in FY 2017 and $79 million annually thereafter to be uncertain.

IX. Health and Hospitals Corporation

The Health and Hospitals Corporation, which is the largest municipal hospital system in the country and serves 1.2 million patients, faces serious financial challenges. Factors contributing to the crisis include large numbers of uninsured patients, competition for Medicaid patients, reduced federal funding and high overhead costs.

The Corporation provides services to everyone who needs care, regardless of their ability to pay. Hospitals are reimbursed for emergency care to uninsured undocumented immigrants, but not for primary care and ambulatory care services.

Medicaid and uninsured patients represent nearly 70 percent of hospital stays, compared to 40 percent for other City hospitals. Although the Affordable Care Act has reduced the number of uninsured, the Corporation served 421,650 uninsured patients last year.

The Corporation depends heavily on supplemental Medicaid payments for services to the uninsured and Medicaid patients. However, these payments will decline beginning in federal fiscal year 2018 under the assumption that most people will have health insurance as a result of the Affordable Care Act. The statewide shift to Medicaid managed care will further reduce supplemental Medicaid payments. Together, federal and State Medicaid funding is expected to decline by $800 million by FY 2020.

The Corporation is losing the competition for paying patients. Medicaid managed care hospital stays declined by 3 percent, while other major hospital systems gained 5 percent. In 2014, 5 of the Corporation's 11 hospitals had more than a third of their beds empty.

MetroPlus, a health insurance plan owned by the Corporation, has also lost market share. MetroPlus Medicaid enrollment grew by 17 percent between 2009 and 2015, while the overall market grew by 27 percent. Most of the Corporation's own employees choose health insurance plans other than MetroPlus.

According to the City, it has increased its financial support to the Corporation from an average of $1.3 billion during fiscal years 2012 through 2015 to $2 billion (more than one-quarter of total receipts).[12] Nevertheless, disbursements are projected to exceed receipts by $785 million in FY 2017. By FY 2020, the difference is projected to widen to nearly $1.8 billion (or 28 percent of total revenue).

To balance the budget, the Corporation is developing initiatives that would reduce costs and increase revenues. Cost-reduction initiatives are expected to generate cumulative savings of $1.8 billion through FY 2020. Most would come from personnel actions ($1.3 billion), but such savings have been difficult to achieve in the past.

Revenue-generating initiatives are expected to total $3.9 billion. Nearly three-quarters ($2.9 billion) would come from increases in federal and State aid, which may be difficult to achieve given fiscal constraints.[13] Another $1 billion is expected from health insurance initiatives, including $373 million from a 35 percent increase in MetroPlus enrollment.

Improving the Corporation's finances will be challenging and will require the cooperation of all stakeholders. The Corporation expects its revenue-enhancement and cost-reduction program to generate $779 million in FY 2017. If it falls short, the Corporation could be required to impose deeper cuts or the City could be called upon to further increase its support.

[12] In FY 2016, the City also prepaid $400 million in subsidies that were due in FY 2017, which gave the Corporation flexibility in managing the FY 2016 budget.

[13] Some of these initiatives require a contribution from the City, but the cost is expected to be offset by savings from increases in the federal reimbursement rate to states that have expanded Medicaid eligibility.

X. Metropolitan Transportation Authority

The Metropolitan Transportation Authority (MTA) projects positive year-end cash balances through calendar year 2019, but a $371 million budget gap for 2020. These estimates assume continued growth in the regional economy and in the use of MTA services, as well as fare and toll increases of 4 percent in 2017 and 2019.

The current economic expansion has greatly benefited the MTA's budget, but the expansion is beginning to slow. The MTA's finances are dependent on economically sensitive revenues and an economic setback would have a negative impact on the budget, possibly requiring larger fare and toll hikes than currently planned.

The enacted State budget provides the MTA with an estimated $4.5 billion in dedicated tax revenues and State subsidies in 2016, which is consistent with the amount anticipated in the MTA's operating budget.

The State budget also commits the State and the City to provide a total of $10.8 billion to the MTA's $29.5 billion capital program for 2015 through 2019 ($26.6 billion excluding bridges and tunnels), which is consistent with the agreement reached between the Governor and the Mayor in October 2015.

Last year, the State appropriated $1 billion for the MTA's 2015-2019 capital program and the City included $657 million in its five-year capital program. The State and City have not yet identified the sources of their remaining contributions ($7.3 billion in State funding and $1.8 billion in City funding).

The State and the City intend to provide the MTA with the remaining $9.2 billion after the MTA has effectively exhausted all other existing MTA-supported sources of capital funding, but no later than State fiscal year 2025-26 or by the completion of the 2015-2019 capital program.

While the State could provide direct capital grants to the MTA (and the State budget has appropriated $2.9 billion if the State elects to do so, although the sources of funding have not been identified), the MTA could issue its own bonds backed by an existing or new State revenue source.

The State increased the MTA's bond cap by $13.6 billion, which permits it to move forward with the capital program until State and City funds become available, and to cover, if needed, the State's remaining share of $7.3 billion.

The State also authorized the MTA to issue, with approval from the Director of the Budget, anticipation notes or other obligations secured solely by the State's commitment to provide additional funding if the MTA requires funds and other resources have been exhausted.

At the State's request, the MTA has agreed to request at least $500 million in additional federal funds for the next phase of the Second Avenue Subway as part of the 2015-2019 capital program. The State's enacted transportation plan includes additional commitments for priority projects that extend one year beyond the MTA's capital program (including another $443 million for the Second Avenue Subway), but the sources of this funding have not yet been identified.

The MTA has also agreed to accelerate replacement of the MetroCard system with a contactless payment system beginning in 2018; increase the number of projects that enhance subway station conditions; and move forward with environmental work and preliminary design of a controversial third mainline railroad track between Floral Park and Hicksville.

On April 20, 2016, the MTA Board approved the revised 2015-2019 capital program. The transit and commuter rail portions, which are subject to review by the Capital Program Review Board (CPRB), were approved by the CPRB in May.

XI. New York City Housing Authority

The New York City Housing Authority is an important component of the City's supply of affordable housing. The Authority manages approximately 180,000 apartments that house more than 400,000 residents, representing 8 percent of the City's rental apartments and almost 5 percent of the population. However, it has a long history of fiscal and management challenges that have allowed the City's public housing properties to fall into disrepair.

In May 2015, the Authority presented a 10-year plan to close projected budget deficits and to improve the condition of its facilities. The plan was based on a number of assumptions and relied on the cooperation of the federal, State and City governments; the unions; and private developers.

The Authority had originally expected to generate $277 million during fiscal years 2016 and 2017 from cost-reduction and revenue-enhancement initiatives. However, it now expects $217 million during this period. The revised estimate reflects delays in leasing property to private developers and in reducing central-office costs.

Despite increased financial support from the City, the Authority's financial plan projects deficits of $60 million in the current calendar year and $197 million in 2017. The Authority expects to end the current year in balance, but it has not revised its financial plan since December 2015 to show how it intends to balance the budget.

Although the Authority projects smaller deficits in subsequent years, these estimates assume successful implementation of $1 billion in cost-reduction and revenue-enhancement initiatives. If these initiatives are unsuccessful, the City could be called upon to provide additional financial assistance.

The Authority prepares a five-year financial plan each December, but it does not revise the plan during the year, making it difficult to determine whether the Authority presents a financial risk to the City. (In contrast, New York City revises its financial plan at least quarterly.) The lack of transparency in the Authority's financial planning process does not instill confidence that it will achieve its financial objectives.

The Authority also has been unable to adequately fund its capital program, in part because it has used federal capital grants to help balance its operating budget. While it has identified $17 billion in capital needs, the five-year capital plan totals $5.6 billion. In the absence of adequate funding, the condition of public housing in New York City will continue to deteriorate.

The federal government is the largest contributor to the capital program. It is expected to contribute $4.6 billion, including $2.9 billion in one-time disaster recovery funds associated with Superstorm Sandy. The City plans to contribute $718 million and the State allocated $100 million in capital funds last year.

The Authority is counting on $3.1 billion in private capital by enrolling 15,000 units in the federal Rental Assistance Demonstration (RAD) program. The RAD program, which was established in 2011, allows public housing authorities to use private capital to rehabilitate facilities through partnerships with private developers.

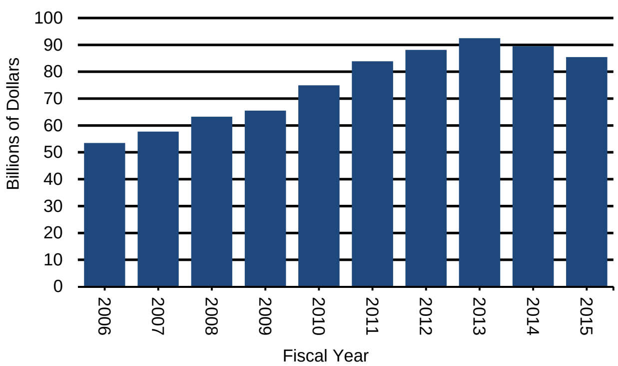
The Authority has received approval from the federal government for 1,400 RAD units, which is expected to generate $150 million in capital improvements. The Authority has applied for an additional 5,200 units, but all of the RAD slots currently available nationwide have been allocated. As a result, the receipt of the remaining $2.9 billion in private capital funds remains at risk.

XII. Other Issues

1. Post-Employment Benefits

The City's unfunded liability for post-employment benefits other than pensions (OPEBs) declined by $4 billion to $85.5 billion in FY 2015, the second consecutive decline since the City began reporting its liability in 2006 (see Figure 26). The decline reflects lower-than-expected growth in health insurance premiums and an increase in the City's contribution to the OPEB trust in FY 2015.

FIGURE 26
Unfunded OPEB Liability



Sources: NYC Actuary; OSC analysis

However, the Governmental Accounting Standards Board has approved two rules (which take effect in FY 2018) that could increase the City's OPEB liability. The changes will 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 will be required to discount future costs using an interest rate that is lower than the entity's assumed rate of return on investments.

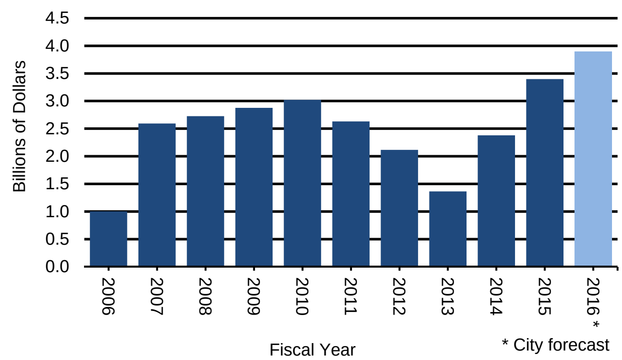
The City, like many employers, does not fund its OPEB liabilities on an actuarial basis but rather pays the annual cost of benefits to current retirees on a pay-as-you-go (PAYGO) basis. OPEB costs, on a PAYGO basis, are projected to rise from $2 billion in FY 2015 to nearly $2.9 billion in FY 2020, an increase of 44 percent in five years.

2. Retiree Health Benefits Trust

In FY 2006, to help fund the future cost of OPEBs, 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. These resources were invested and earned interest, with the balance peaking at more than $3 billion in FY 2010.

While the City's RHBT was intended to help fund future OPEB liabilities, it has been used as a rainy-day fund. The City drew down much of the resources in the RHBT during fiscal years 2011 through 2013 as it managed through the Great Recession (see Figure 27).

FIGURE 27
RHBT Year-End Balance



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

The City had planned to use $1 billion from the RHBT to help balance the FY 2014 budget, but revenues grew faster than anticipated, permitting the City to rescind the planned transfer and to contribute $864 million to the RHBT.

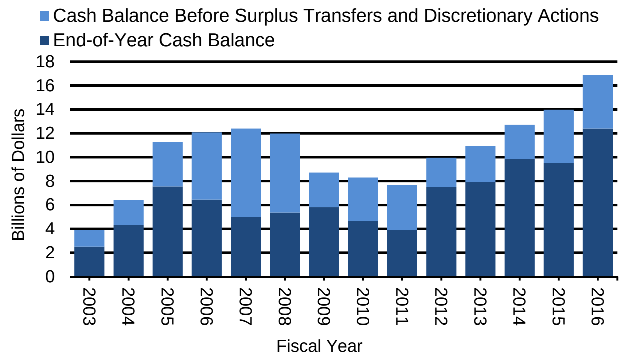
In FY 2015, revenues also grew much faster than expected, allowing the City to contribute another $955 million to the RHBT. In FY 2016, the City contributed an additional $500 million to the RHBT, which increased the year-end balance to nearly $3.9 billion, the highest amount ever.

3. Cash Flow

The City's year-end cash balance rose sharply between fiscal years 2003 and 2007, reflecting the strength of the economy, and remained at about $12 billion (before surplus transfers and other discretionary actions) through the end of FY 2008 (see Figure 28). Even though the year-end cash balance declined during the recession, the City has not needed to borrow to meet its short-term cash needs since FY 2004.

FIGURE 28

Year-End Cash Balance



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

The City's cash position has been improving since FY 2011, and in FY 2014 it exceeded the prerecession level. The New York City Office of Management and Budget estimates that the City ended FY 2016 with a record cash balance of $12.4 billion ($16.9 billion before discretionary transfers).[14] Given the amount of cash on hand, it is unlikely that the City will need to borrow to meet its cash flow needs in FY 2017, resulting in debt service savings of $75 million.

4. Credit Rating

The City-funded portion of the City's capital program is financed through General Obligation (GO) bonds secured by the City's full faith and credit, and bonds issued by the Transitional Finance Authority (TFA) secured by personal income tax and (if needed) sales tax revenues. The City's GO ratings were last upgraded in the summer of 2007, and the City was able to maintain its ratings through the recession.[15]

The City's strong credit ratings contribute to its ability to access the capital markets to meet its financing needs, and to help keep its borrowing costs at reasonable rates. The City's GO credit is rated AA by Standard & Poor's, AA by Fitch Ratings and Aa2 by Moody's Investors Service, while the TFA credit is rated higher (AAA by S&P, AAA by Fitch and Aaa by Moody's).[16] Both credits have a stable outlook from the three rating agencies.

The TFA's credit rating benefits from the strong statutory revenue streams used to secure its bonds, while GO ratings reflect the City's broad economic base, sound financial planning practices and demonstrated ability to close anticipated budget gaps. However, the rating agencies have expressed concern over the City's continued reliance on the financial services sector (although it is not as pronounced as in the past); a high debt burden; and pressure from rising nondiscretionary costs.

[14] Discretionary transfers include the FY 2016 surplus and deposits into the Retiree Health Benefits Trust.

[15] Fitch and Moody's recalibrated their ratings in April 2010 so that municipal ratings are comparable with ratings in other sectors. As a result, GO and TFA ratings were adjusted upward by one notch, though the adjustment does not reflect a change in credit quality.

[16] Fitch and S&P do not make a rating distinction between TFA senior and subordinate bonds. Moody's rates TFA subordinate bonds one notch lower (Aa1) than it rates senior bonds.

5. Constitutional Tax Limit

The amount New York City can raise from the property tax for purposes other than certain debt service and capital appropriations is subject to a constitutional tax limit. Based on information submitted by the City to OSC in October 2015, the portion of the tax limit that the City has used rose by eight and a half percentage points between fiscal years 2015 and 2016 to 97.8 percent.

The increase is not the result of higher property tax rates (as the citywide tax rate has remained unchanged). Rather, the City has indicated that the increase resulted primarily from a large prepayment in FY 2015 of debt service due in FY 2016, which resulted in a decrease in the debt service levy and an increase in the portion of the tax levy subject to the tax limit. Nevertheless, whenever a local government nears its constitutional tax limit, close attention is warranted during the annual budget process.

6. Prior-Year Payables

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 10 years, the City has realized net resources averaging $472 million annually from overestimating prior years' expenses and from underestimating prior years' receivables. The June Plan anticipates resources of $500 million in FY 2016, but none in subsequent years.

7. Water and Sewer

Revenue from water and sewer charges cover the operating cost of the water and sewer system, debt service on water and sewer capital projects, and an optional rental payment to the City for the use of the system. The City has collected the rental payment since FY 1986, and the payment totaled $214 million in FY 2014.

In FY 2015, the City implemented a plan to phase out the rental payment by FY 2023. The June Plan accelerates the phase-out, eliminating the payment by FY 2017. This action reduces revenues to the City by a total of $1.1 billion during fiscal years 2017 through 2020. (The City is not precluded from reimposing the rental payment in the future.)

In May 2016, the Water Board approved, at the Mayor's urging, a $183 water bill credit for owners of one-, two- and three-family homes. The Water Board also approved a rate increase of 2.1 percent, the lowest in 16 years. In June, a lower State court ruled that the Water Board had overstepped its authority and that its actions were invalid. The Water Board has appealed the decision.

Contact

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Prepared by the Office of the State Deputy Comptroller for the City of New York

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