Review of the Financial Plan of the City of New York

June 2014

Report 5-2015

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

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

Additional copies of this report
may be obtained from:

Office of the State Comptroller
New York City Public Information Office
59 Maiden Lane
New York, NY 10038

Telephone: (212) 383-1388

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

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

Contents

I. Executive Summary

On May 21, 2014, the City of New York revised its financial plan (the "May Plan") to update its revenue and expenditure forecasts for fiscal years 2014 through 2018 (see Figure 1). The May Plan reflects the Mayor's executive budget for FY 2015 and the recently ratified labor agreement with the United Federation of Teachers (UFT).

In our March 2014 report, the Office of the State Comptroller (OSC) concluded that the absence of new labor agreements was the greatest uncertainty facing the City's financial plan. All of the labor agreements with the City's unions had expired, some as long ago as 2008. In early May, the City announced that it had reached a nine-year labor agreement with the UFT, which represents 37 percent of the City's workforce.

The UFT agreement compensates teachers and other UFT members for two annual wage increases of 4 percent that were provided to other unions in 2009 and 2010, but withheld from the UFT by the prior mayoral administration at the onset of the recession. The agreement also increases wages by 10 percent over a seven-year period and provides employees with a $1,000 payment upon ratification of the agreement. The City, which has a long history of pattern bargaining, assumes these terms will set the wage pattern for all municipal unions. However, the union representing the City's police officers is seeking larger wage increases than those offered by the City, and has begun the process that could lead to binding arbitration.

The City estimates that the UFT agreement and the wage pattern it would set for the other unions will cost $13.6 billion during the financial plan period. These costs will be partially offset by resources previously set aside by the City in its labor reserve ($3.5 billion), and by a total of $4.4 billion in new resources that are expected to become available as the result of an approved agreement between the City and the Municipal Labor Committee (MLC), which represents the City's unions.

Under the MLC agreement, the City and the unions have agreed to work together to reduce the cost of health insurance to the City by $3.4 billion through FY 2018, of which $1.3 billion would be recurring savings. The agreement calls for arbitration to resolve differences between the City and the unions, and authorizes the arbitrator to enforce the terms of the agreement. The agreement does not rule out the possibility of higher employee insurance premiums or co-payments, but the City and the unions hope to reach the savings targets through other actions. The agreement also permits the City to use $1 billion in unneeded resources in the Health Stabilization Fund to help fund wage increases.

The agreement is unprecedented and untested, and this has raised questions about whether the savings are achievable in the amounts and in the years anticipated in the May Plan. The City has agreed to report on its progress on a regular basis, which will build confidence that the agreement is generating the anticipated savings.

The May Plan also includes a number of new programmatic initiatives, such as expansion of full-day prekindergarten and after-school programs (funded from the largest increase in State education aid in eight years), efforts to reduce and prevent homelessness, and an expansion of the capital program to fund a new affordable housing program and to reduce school overcrowding. In addition, City-funded staffing will increase by 4,300 employees during fiscal years 2014 and 2015 to reach 260,265 employees, still below the prerecession peak.

City-funded spending is projected to increase at an average annual rate of 4.6 percent between fiscal years 2013 and 2018, driven by higher labor costs and debt service. The City's unfunded obligation for post-employment benefits other than pensions grew by nearly $39 billion to $92.5 billion between fiscal years 2006 and 2013, and will likely continue to grow during the financial plan period.

The May Plan projects budget gaps of $2.6 billion in FY 2016, $1.9 billion in FY 2017 and $3.1 billion in FY 2018. These gaps are much larger than those projected by the City in February 2014, but significantly smaller than the historical average over the past 34 years when measured as a share of City revenues. The City has demonstrated in the past that gaps of this magnitude are manageable, but a significant economic setback during the financial plan period could make closing these gaps more difficult. The national economic recovery has already exceeded the average length for all recoveries since the end of World War II.

Although the budget gaps for fiscal years 2019 through 2021 could be larger because the cost of the UFT agreement (and the pattern it sets for the other unions) is higher in those years, the City has a long lead time to close these gaps. The sooner the City begins the process of identifying and implementing actions to close the budget gaps during the financial plan period, the smaller the gaps will be in fiscal years 2019 through 2021.

The City will also benefit from a continuation of its conservative approach to forecasting revenues, which has created surpluses that have helped close budget gaps and cushion the impact of adverse events. Although the City spent down most of its accumulated surplus between fiscal years 2009 and 2013, the Mayor has taken steps to increase the City's reserves by rescinding the planned transfer of $1 billion from the Retiree Health Benefits Trust into the operating budget, and by doubling the general reserve to $600 million.

The May Plan forecasts a surplus of $1.6 billion in FY 2014 (which will be used to help balance next year's budget), a balanced budget for FY 2015 and manageable out-year budget gaps. Moreover, OSC believes that revenue collections are likely to exceed the City's forecasts, particularly in the near term (see Figure 2). The City still faces challenges, however. It must conclude negotiations with the other municipal unions, complete the sale of taxi medallions ($1.2 billion), obtain planned health insurance savings ($3.4 billion) and take steps to narrow the projected budget gaps.

Figure 1
New York City Financial Plan
(in millions)

REVENUES	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Taxes					
General Property Tax	$19,969	$20,679	$21,714	$22,603	$23,478
Other Taxes	27,116	27,149	28,323	29,285	30,214
Tax Audit Revenue	860	709	709	709	709
Subtotal: Taxes	$47,945	$48,537	$50,746	$52,597	$54,401
Miscellaneous Revenues	7,347	7,063	6,994	6,986	6,622
Unrestricted Intergovernmental Aid	- - -	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(1,776)	(1,795)	(1,820)	(1,823)	(1,828)
Disallowances Against Categorical Grants	(15)	(15)	(15)	(15)	(15)
Subtotal: City Funds	$53,501	$53,790	$55,905	$57,745	$59,180
Other Categorical Grants	900	761	837	832	828
Inter-Fund Revenues	538	527	513	513	513
Federal Categorical Grants	8,303	6,377	6,333	6,310	6,299
	11,770	12,460	12,904	13,401	13,953
Total Revenues	**$75,012**	**$73,915**	**$76,492**	**$78,801**	**$80,773**
EXPENDITURES					
Personal Service					
Salaries and Wages	$24,339	$22,430	$24,231	$24,196	$25,615
Pensions	8,270	8,354	8,445	8,546	8,723
Fringe Benefits	8,737	9,058	9,722	10,444	11,240
Subtotal: Personal Service	$41,346	$39,842	$42,398	$43,186	$45,578
Other Than Personal Service					
Medical Assistance	$6,365	$6,447	$6,415	$6,415	$6,415
Public Assistance	1,379	1,428	1,407	1,413	1,413
All Other[1]	23,146	22,364	22,818	23,307	23,860
Subtotal: Other Than Personal Service	$30,890	$30,239	$30,640	$31,135	$31,688
Debt Service[1,2]	$5,704	$6,665	$7,242	$7,582	$7,840
FY 2013 Budget Stabilization & Discretionary Transfers[1]	(2,838)	- - -	- - -	- - -	- - -
FY 2014 Budget Stabilization[2]	1,636	(1,636)	- - -	- - -	- - -
General Reserve	50	600	600	600	600
Subtotal	$76,788	$75,710	$80,880	$82,503	$85,706
Less: Intra-City Expenses	(1,776)	(1,795)	(1,820)	(1,823)	(1,828)
Total Expenditures	**$75,012**	**$73,915**	**$79,060**	**$80,680**	**$83,878**
Gap to Be Closed	**- - -**	**- - -**	**$(2,568)**	**$(1,879)**	**$(3,105)**

Source: NYC Office of Management and Budget

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

2 Fiscal Year 2014 Budget Stabilization totals $1.636 billion, including GO of $274 million and TFA of $1.362 billion.

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

	Better/(Worse)				
	FY 2014	**FY 2015**	**FY 2016**	**FY 2017**	**FY 2018**
Surplus / (Gaps) Per May Plan	**$ - - -**	**$ - - -**	**$ (2,568)**	**$ (1,879)**	**$ (3,105)**
Tax Revenue	125	600	400	400	400
Debt Service	40	150	- - -	- - -	- - -
Medicaid Reimbursement	(35)	(50)	(80)	(80)	(80)
Judgments and Claims	- - -	50	50	50	50
Uniformed Overtime	- - -	(50)	(50)	(50)	(50)
OSC Baseline Risk Assessment	**130**	**700**	**320**	**320**	**320**
Surplus/(Gaps) Per OSC[3]	**$ 130**	**$ 700**	**$ (2,248)**	**$ (1,559)**	**$ (2,785)**
Additional Risks and Offsets[4]					
Taxi Medallion Sale	- - -	(481)	(360)	(400)	- - -
Health Insurance Savings	- - -	(400)	(700)	(900)	(1,300)

[3] The May Plan includes a general reserve of $50 million in FY 2014 and $600 million in each of fiscal years 2015 through 2018. The Retiree Health Benefits Trust, which the City has used in the past as a rainy-day fund, has a balance of $1.4 billion. The City also has a reserve of $1 billion for disallowances of federal and State aid, which, if not needed for that purpose, could be used to help balance the budget.

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

II. Economic Trends

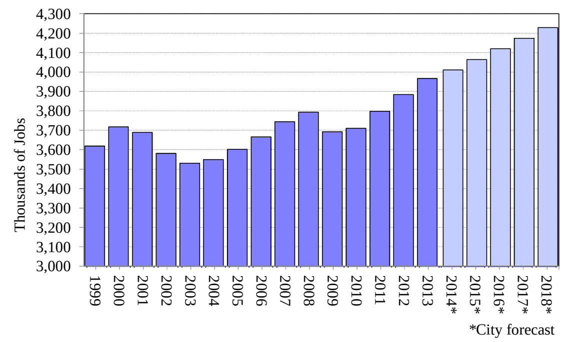
The nation's Gross Domestic Product (GDP) declined during the first quarter of 2014 (the first contraction in three years), largely as a result of severe winter weather. While the economy is expected to rebound strongly in the second quarter, growth in GDP will likely average less than 2.5 percent in 2014, well below the growth rate of past economic recoveries. The nation has regained almost all the jobs it lost during the recession, and the unemployment rate has fallen from a peak of 10 percent in October 2009 to 6.3 percent in April 2014, the lowest level since September 2008.

Citing improvements in the economy, the Federal Reserve continues to scale back its bond purchasing program, which was created to hold down long-term interest rates and stimulate economic growth. The Federal Reserve has indicated that short-term interest rates will remain near zero until there is progress toward its objectives of maximum employment and 2 percent inflation.[5] The central bank also remains concerned about the pace of the housing recovery, which has slowed in recent months.

Since the end of the recession, job growth in New York City has averaged 1.8 percent annually, nearly twice as fast as in the nation and New York State (both grew by 1 percent annually). As a result, employment in the City climbed to a record high of nearly 4 million during 2013 (see Figure 3), and the City's job gains (275,000) reached more than two and a half times the number of jobs lost during the recession.

Figure 3

Annual New York City Employment



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

Job growth in the City, however, has been concentrated in lower-paying sectors. These sectors account for more than three-quarters of all jobs created in the City since 2009, with the majority located in just three industries (home health care, accommodations and food services, and retail trade).

5 The Federal Reserve has focused on a broader range of labor market measures beyond the unemployment rate. For example, more than one-third of those unemployed have been without a job for more than 26 weeks. Many workers have also become discouraged in their job searches, resulting in the lowest labor force participation rate in three decades.

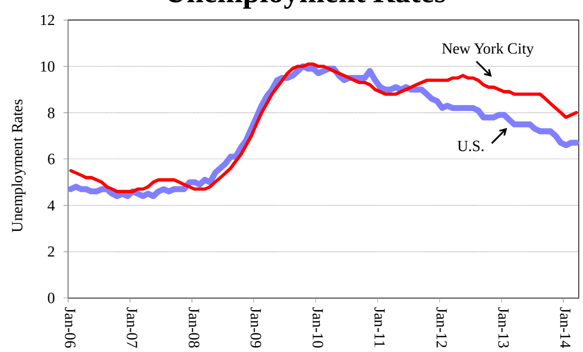
Among higher-paying sectors, job growth has been strong in professional and business services as well as in the high-tech and related creative industries. The construction sector has begun to add jobs, though employment remains well below prerecession levels. Manufacturing employment has stabilized after decades of decline, and grew by 2.4 percent in the first four months of 2014. Unlike in prior recoveries, the securities industry has lost jobs in the current recovery.

The May Plan assumes that job growth will ease but remain strong, growing by 1.5 percent in 2014 and then by 1.3 percent annually during calendar years 2015 through 2018. During the first four months of the current year, job growth averaged 2 percent. The May Plan forecasts that job growth during the financial plan period will remain concentrated in lower-paying sectors.

Although the City's unemployment rate has fallen from a peak of 10.1 percent in November 2009 to 7.9 percent in April 2014, it remains at nearly twice its prerecession level (see Figure 4). Nearly half of the unemployed people in the City have been without a job for more than six months, a share that has not changed significantly since the height of the recession (by contrast, the share declined quickly after the last recession). The number of City residents without a job for at least two years has risen sharply since the end of the recession.

Figure 4

Unemployment Rates



Note: Data have been seasonally adjusted.

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

Some of the City's boroughs, neighborhoods and segments of the population are experiencing even higher rates of unemployment. Nearly one-sixth of the City's working-age population lacks a high school diploma, and the unemployment rate among residents without a high school diploma was 11.8 percent.

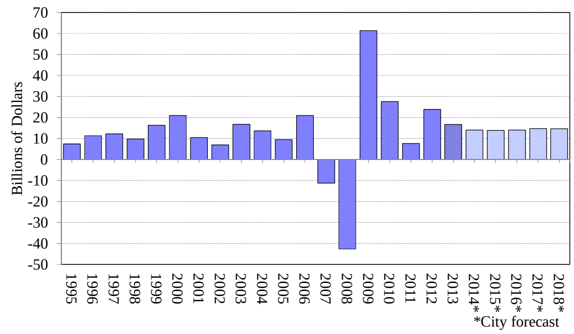
Income growth remains sluggish in the City, constrained by the high concentration of lower-paying jobs being created, small salary increases from many employers and relatively high unemployment. The City estimates that total wages grew by 3.1 percent in 2013, which was less than half the average annual rate of increase in the last economic expansion. The May Plan projects that wage growth will rise at an average annual rate of 3.9 percent through 2018.

Wall Street is one of the City's economic engines and a major source of tax revenues. The Federal Reserve's low-interest-rate policies helped Wall Street rebound from record losses in 2007 and 2008 with five consecutive years of profitability (including the three best years on record). Although the broker/dealer profits of the member firms of the New York Stock Exchange (the traditional measure of industry profitability) declined by 30 percent to $16.7 billion in 2013, profitability was still good by historical standards (see Figure 5). The City forecasts a decline in Wall Street bonuses in 2014. The City expects that several factors, including ongoing litigation, the implementation of new regulations and rising interest rates, will constrain industry profits to $14 billion in 2014 and keep them near this level over the remainder of the financial plan period.

In February 2014, OSC estimated that bonuses (including compensation deferred from prior years) for securities industry employees who work in New York City increased by 15 percent in 2013 to an average of $164,530. (The total bonus pool also rose by 15 percent to $26.7 billion.)

Figure 5

Wall Street Profits



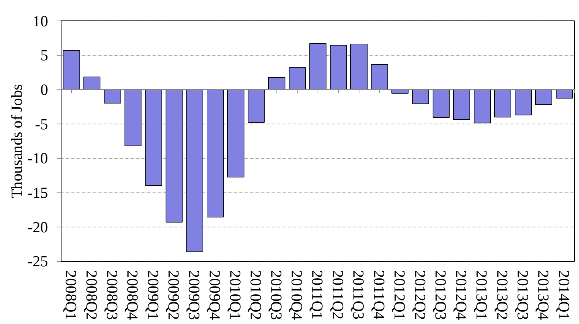
Sources: NYSE Euronext; Securities Industry and Financial Markets Association; NYC Office of Management and Budget

Although Wall Street has been profitable for several years, the securities industry in the City continues to shed jobs as it adapts to new conditions (see Figure 6). After severe losses during the financial crisis, the industry gained 5,900 jobs in 2011, but then lost 6,500 jobs during 2012 and 2013 as it restructured. Employment in 2013 was more than 12 percent lower than in 2007 and the lowest level since 2003. During the first four months of 2014, the securities industry lost another 1,200 jobs (compared to the same period one year earlier). The May Plan assumes modest job growth in the industry during the financial plan period, with an average gain of 1,000 jobs annually.

The City's tourism industry posted another record year in 2013. NYC & Company (the City's tourism agency) estimates that the total number of visitors to New York City increased to 54.3 million (a fourth-consecutive record year), and that visitor spending reached a record of nearly $40 billion. The City expects the number of tourists to break another record in 2014, reaching 55 million.

Figure 6

Changes in Wall Street Employment



Note: Data are not seasonally adjusted. Changes are from the same quarter a year earlier.
Sources: NYS Department of Labor; OSC analysis

New York City's real estate markets also continue to improve. Data from the Department of Finance show that the City's median home value for one-, two- and three-family homes, which fell by almost 20 percent during the recession, has since recovered about one-third of its lost value. Values for condominium and cooperative apartments in Manhattan declined at a slower rate than those for single-family homes, and have since returned to prerecession levels.

While the high-end residential market is strong, the City has a shortage of affordable housing. OSC has reported that, even after the benefit of government subsidies, one-fifth of City households faced a severe rent burden, devoting at least half of their incomes to housing. The Mayor has unveiled a ten-year plan to build and preserve 200,000 units of affordable housing in the City (for more detail, see Section IX).

The City's commercial real estate market is among the strongest in the nation. Sales of large Manhattan office buildings have also rebounded, fueled by international investment and low interest costs. In 2013, the value of office-building sales totaled $11.2 billion, which was 75 percent higher than the value of sales in 2012.

The average asking rent in Manhattan's primary office market has recovered one-third of its recessionary decline, reaching $68.90 per square foot in 2013. The vacancy rate initially fell as the recovery began but then started to rise again, reaching 12.1 percent in 2013, slightly higher than in 2009. The City expects that the completion of the World Trade Center towers will increase the inventory of Manhattan office space, causing the vacancy rate to edge up to 12.8 percent in 2014 while the average asking rent eases slightly. As this new space is absorbed, vacancy rates are expected to fall and rents are expected to increase in 2015.

The economy faces several risks during the financial plan period. Nationally, even though the expansion has been relatively modest, it has now exceeded the average length for all recoveries since the end of World War II. While the City's economy continues to grow steadily, the risk of an economic setback increases with each year.

As long as the expansion continues, the Federal Reserve will continue to unwind its accommodative monetary policy, and many economists (and the City) forecast that both long-term and short-term interest rates will rise in the coming years. If rates rise, the magnitude and timing of the change will affect businesses and consumers throughout the economy, with the most notable effects on the real estate and financial markets. Finally, other factors could have an impact on the national and local economies, including continued weakness of the European economy and geopolitical tensions.

III. Changes Since the June 2013 Plan

Since the beginning of the current fiscal year, the City has recognized $9.6 billion in unplanned resources through FY 2017, mostly from higher revenues ($6 billion), a transfer from the Health Stabilization Fund ($1 billion), and savings in health insurance and debt service (see Figure 7). The resources permitted the City to generate a surplus of $1.6 billion in FY 2014 (which will be used to help balance next year's budget), balance the FY 2015 budget, fund future labor agreements based on the recent agreement with the United Federation of Teachers, rescind planned budget cuts, fund new initiatives and replenish reserves. The May Plan projects out-year budget gaps of $2.6 billion in FY 2016, $1.9 billion in FY 2017 and $3.1 billion in FY 2018, which are larger (but more realistic) than those projected by the City at the start of the fiscal year.

Tax collections are now projected to be higher by $5.1 billion through FY 2017, largely because real estate values and sales activity are increasing faster than had been expected ($2.7 billion). Personal income tax collections are expected to be stronger ($1.8 billion), with most of the benefit coming in FY 2014. The City also now expects to receive $580 million in one-time miscellaneous revenues in FY 2014, mostly from the sale of City-owned buildings and a refund of health insurance premiums.

Health insurance and debt service costs will be lower by $2.6 billion through FY 2017. EmblemHealth, the City's principal insurer, did not seek a premium rate increase for FY 2015 after the former Mayor announced his intention to seek new carriers for the City's health insurance plans for municipal employees. The City projects significant debt service savings because interest rates have been lower than expected, resulting in lower costs for new issuances as well as savings from variable-rate debt and from refinancing outstanding debt.

The City also doubled the general reserve to $600 million annually beginning in FY 2015, and rescinded a planned withdrawal of $1 billion from the Retiree Health Benefits Trust. (The City created the trust to help fund the future cost of post-employment benefits other than pensions, but had used it as a rainy-day fund.)

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

Since January, the City added funding for new initiatives, including programs to prevent and reduce homelessness, improve child protection services, and promote traffic safety (i.e., Vision Zero). The City also added an additional $75 million in FY 2014 for snow removal, and allocated additional funds in subsequent years.

In May, the City reached a labor agreement with the United Federation of Teachers (UFT). The agreement and the pattern it sets for the other municipal unions is expected to increase labor costs by $1.8 billion in FY 2014, $674 million in FY 2015 (before the transfer of $1 billion from the Health Stabilization Fund), $1.2 billion in FY 2016, $890 million in FY 2017 and $2 billion in FY 2018 (for more detail, see Section VI).

Figure 7
Financial Plan Reconciliation–City Funds
May 2014 Plan vs. June 2013 Plan
(in millions)

	Better/(Worse)			
	FY 2014	**FY 2015**	**FY 2016**	**FY 2017**
Surplus/Gaps Per June 2013 Plan	**$ - - -**	**$ (1,965)**	**$ (1,769)**	**$ (1,382)**
Revenue Reestimates				
Personal Income Tax	1,146	161	220	225
Real Estate Transaction Taxes	550	132	174	46
Real Property Tax	401	351	455	576
Other Taxes	383	45	94	12
Audits	151	- - -	- - -	- - -
All Other	580	213	116	(6)
Total	**3,211**	**902**	**1,059**	**853**
Expenditure Reestimates				
Debt Service	535	264	155	136
Health Insurance	91	444	479	517
Judgments and Claims	55	55	55	55
Pension Contributions	47	(25)	84	236
Libraries and Cultural Institutions	- - -	(166)	(166)	(166)
Vision Zero	(15)	(46)	(41)	(41)
Social Services and Health	(57)	(323)	(307)	(300)
Uniformed Agencies	(215)	(280)	(235)	(194)
Labor Reserve	(1,831)	(674)	(1,236)	(890)
Health Stabilization Fund	- - -	1,000	- - -	- - -
Retiree Health Benefits Trust	(1,000)	- - -	- - -	- - -
General Reserve	400	(300)	(300)	(300)
Prior Payables	400	- - -	- - -	- - -
Other Expenditures	(127)	(380)	(346)	(403)
Total	**(1,717)**	**(431)**	**(1,858)**	**(1,350)**
Net Change During FY 2014	**1,494**	**471**	**(799)**	**(497)**
Surplus/(Gap)	**$ 1,494**	**$ (1,494)**	**$ (2,568)**	**$ (1,879)**
Surplus Transfers[6]	(1,494)	1,494	- - -	- - -
Gaps Per May 2014 Plan	**$ - - -**	**$ - - -**	**$ (2,568)**	**$ (1,879)**

Sources: NYC Office of Management and Budget; OSC analysis

[6] The June 2013 Financial Plan projected a surplus of $142 million for FY 2014, which brings the surplus projected for FY 2014 to $1.6 billion.

IV. The Projected Budget Gaps

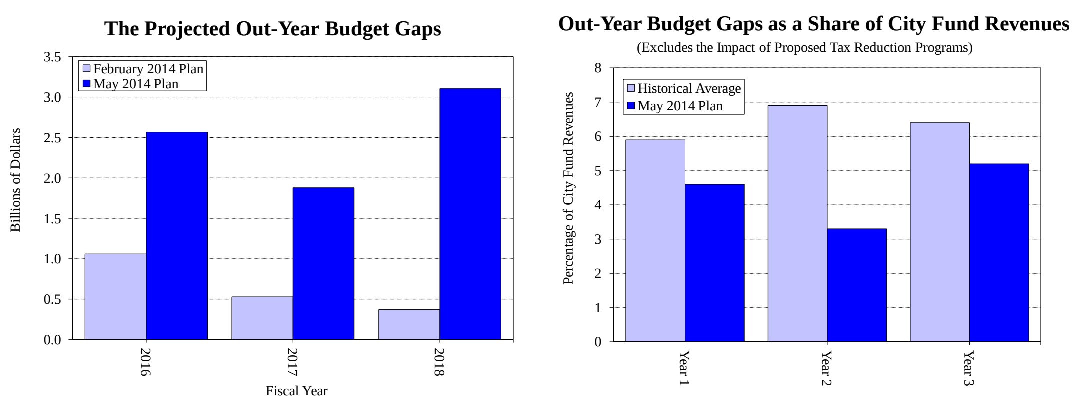
The City projected large out-year budget gaps during the 2008 financial crisis and resulting recession, but the gaps declined quickly as the economic recovery took hold. The dramatic improvement resulted from a number of developments, including continued improvement in the local economy, a drawdown of reserves, low interest rates that permitted the City to refinance outstanding debt at lower cost, expiring labor agreements and the impact of agency cost-reduction initiatives.

The February 2014 Financial Plan projected budget gaps of $1.1 billion in FY 2016, $530 million in FY 2017 and $370 million in FY 2018, but, as we noted in our March 2014 report, these gap estimates were understated because they did not reflect the impact of unfinished labor negotiations. (All of the labor agreements with the municipal unions had expired years earlier, some as long ago as 2008.)

In early May 2014, the City reached a labor agreement with the United Federation of Teachers, which the May Plan assumes will set the wage pattern for agreements with the other municipal unions (for more detail, see Section VI). In addition, the Mayor has proposed a number of new programmatic initiatives.

As a result, the May Plan projects budget gaps of $2.6 billion in FY 2016, $1.9 billion in FY 2017 and $3.1 billion in FY 2018. As shown in Figure 8, these gap estimates are much larger than those projected by the City in February 2014, but are significantly smaller than the historical average over the past 34 years when measured as a percentage of City fund revenues. The City has demonstrated in the past that gaps of this magnitude are manageable, but a significant economic setback during the financial plan period would make closing these gaps more difficult.

Figure 8
The Out-Year Budget Gaps



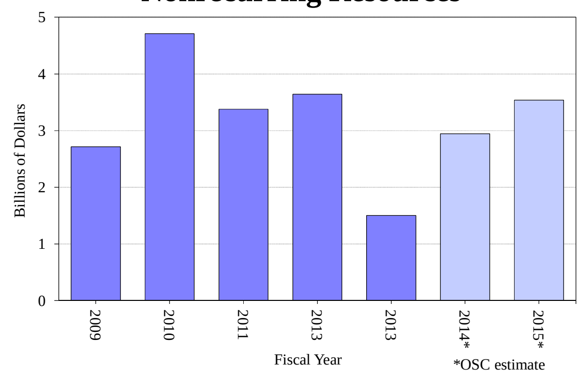
Sources: NYC Office of Management and Budget; OSC analysis

Although the budget gaps for fiscal years 2019 through 2021 could be larger because the cost of the UFT labor agreement (and the wage pattern that it sets for the other unions) is higher in those years, the City has a long lead time to close these gaps. The sooner the City begins the process of identifying and implementing actions that generate recurring resources to close the budget gaps during the financial plan period, the smaller the gaps will be in fiscal years 2019 through 2021.

While the City relied heavily on nonrecurring resources during the recession, its level of reliance dropped significantly (to $1.5 billion) in FY 2013 (see Figure 9). OSC estimates that the budgets for fiscal years 2014 and 2015 include nonrecurring resources of $2.9 billion and $3.5 billion, respectively (see Appendix A).

Figure 9

Nonrecurring Resources



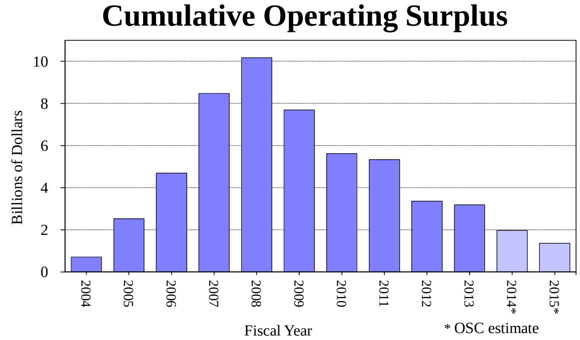
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

During the last economic expansion, the City accumulated surplus resources as revenue growth outpaced spending. The cumulative surplus peaked in FY 2008 at $10.2 billion (see Figure 10). The City began to draw on these resources beginning in FY 2009 to help navigate the recession, and by the end of FY 2013 the City had spent $7 billion of the accumulated surplus.

The adopted budget for FY 2014 had anticipated that the accumulated surplus would be nearly depleted by the end of the fiscal year, leaving the City with little cushion to respond to unanticipated events. Revenue collections, however, were much stronger than the City's initial projections, which allowed the Mayor to increase the City's reserves by rescinding the planned transfer of $1 billion from the Retiree Health Benefits Trust into the operating budget and by doubling the size of the general reserve to $600 million.

Figure 10

Cumulative Operating Surplus



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

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

V. Revenue Trends

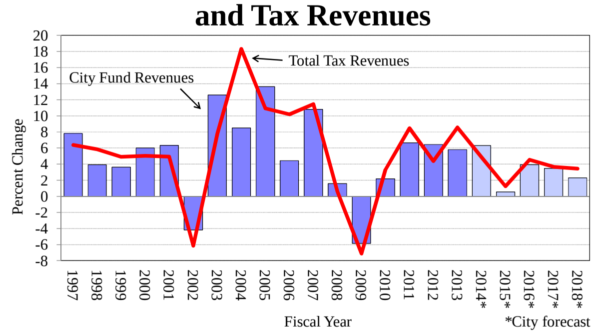
The City has raised its forecast of revenue collections for fiscal years 2014 through 2017 by $6 billion since the beginning of the fiscal year. Most of this additional revenue comes from higher tax collections ($5.1 billion), which reflect stronger job growth, improving real estate market conditions, and a smaller-than-expected falloff in capital gains following a 2013 increase in federal personal income tax rates. The May Plan assumes that City fund revenues will rise by 6.3 percent in FY 2014, comparable to the average annual rate of increase in fiscal years 2011 through 2013.

The May Plan projects that the growth in City fund revenues will slow in FY 2015 to 0.5 percent (see Figure 11). This forecast is largely based on the assumptions of higher interest rates, and weaker job and income growth.

Interest rates may not increase as quickly as the City anticipates, however.[7] In addition, the City's economy remains vibrant, and job and wage growth are likely to be slightly stronger than the City projects. This economic outlook, coupled with year-to-date trends in tax collections, suggests that revenues could be $600 million higher in FY 2015 than the City anticipates, resulting in City fund revenue growth of 1.4 percent for the year.

Figure 11

Annual Changes in City Fund Revenues and Tax Revenues



Note: Adjusted for debt service on TFA and Tobacco Bonds, and the transfer of TSASC revenues.

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

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

[7] Long-term interest rates have stabilized in recent months, and the Federal Reserve has reaffirmed its intentions of holding short-term rates near zero until labor market conditions show further improvement.

Figure 12
City Fund Revenues
(in millions)

	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Taxes						
Real Property Tax	$ 18,751	$ 19,969	$ 20,679	$ 21,714	$ 22,603	$ 23,478
Personal Income Tax	9,168	9,315	9,191	9,617	9,948	10,220
Sales Tax	6,132	6,460	6,666	6,946	7,260	7,556
Business Taxes	5,857	5,907	5,959	6,149	6,312	6,530
Real Estate Transaction Taxes	1,828	2,383	2,226	2,467	2,561	2,638
Other Taxes	2,976	3,051	3,107	3,144	3,204	3,270
Audits	1,009	860	709	709	709	709
Subtotal	**45,721**	**47,945**	**48,537**	**50,746**	**52,597**	**54,401**
Miscellaneous Revenues	4,728	5,645	5,342	5,248	5,237	4,876
Grant Disallowances	(59)	(15)	(15)	(15)	(15)	(15)
Total	**$ 50,390**	**$ 53,575**	**$ 53,864**	**$ 55,979**	**$ 57,819**	**$ 59,262**

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

1. Real Property Tax

The May Plan assumes that collections from the real property tax will rise by 3.6 percent in FY 2015, to $20.7 billion (see Figure 13). This follows an increase of 6.5 percent in FY 2014, when collections were boosted by a number of one-time technical adjustments.[8] Assessed values are forecast to rise by 5.7 percent in FY 2015, the same rate as in FY 2014. These are the strongest growth rates since FY 2010. The final property tax roll for FY 2015, released on May 27, 2014, was consistent with the revenue assumptions in the May Plan.

Much of the growth in FY 2015 can be attributed to commercial properties (market values increased by more than 10 percent) and large residential properties (market values increased by 7.3 percent). For both types of properties, however, increases are required to be phased in over five years, which limits the growth in tax assessments in FY 2015. Property values for one-, two-, and three-family homes increased by almost 5 percent, the largest increase since FY 2008.

Figure 13
Real Property Tax Revenues

Sources: NYC Comptroller; NYC Office of Management and Budget

[8] Including reduced refunds, a restoration of several tax-exempt properties to the tax roll, and higher collections of taxes owed from prior years.

The May Plan assumes that property values will grow at an average annual rate of 4.3 percent during fiscal years 2016 through 2018. This estimate is based on the assumption that interest rates will rise, holding down growth in property values in these years. If long-term interest rates remain near current levels, property values are likely to grow faster than anticipated by the City, which will yield additional tax revenues during those years.

2. Personal Income Tax

Collections from the personal income tax have been much stronger in FY 2014 than the City had anticipated at the beginning of the fiscal year, yielding an additional $1.1 billion. These additional revenues reflect a smaller-than-expected decline in capital gains in 2013, as well as stronger growth in employment and Wall Street bonuses, and payments from the State to correct a distributional shortfall in its processing of City personal income tax returns. The City now projects that personal income tax collections will increase by 1.6 percent to reach $9.3 billion in FY 2014 (see Figure 14).

Figure 14
Personal Income Tax Revenues

Sources: NYC Comptroller; NYC Office of Management and Budget

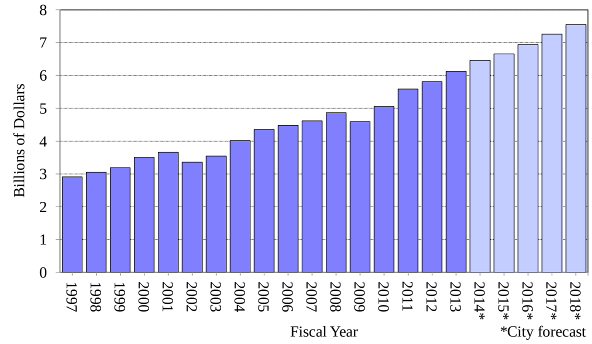
In 2012, tax collections surged when taxpayers accelerated income (primarily from capital gains) into that year from 2013 and subsequent years to avoid an increase in federal personal income tax rates, which became effective in January 2013. The City had previously expected tax payments on this income to decline by 60 percent, but the actual decline was 40 percent. Many other jurisdictions, such as New York State, New Jersey and Illinois, had projected smaller declines and are now experiencing revenue shortfalls.

The May Plan projects that personal income tax collections will decline by 1.3 percent to $9.2 billion in FY 2015, which would be the first decline since FY 2009. The City assumes a decline in withholding (the largest component of the tax), resulting from a slowing in job and wage growth, and a reduction in Wall Street bonuses. The City expects growth in personal income tax collections to resume in FY 2016, and the May Plan forecasts average annual growth of 3.6 percent in fiscal years 2016 through 2018. Based on current trends in the economy and economic forecasts from IHS Global Insight, OSC expects collections from the personal income tax to exceed the City's forecasts by $125 million in FY 2014, $325 million in FY 2015 and about $400 million annually in subsequent years.

3. Sales Tax

Figure 15

Sales Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

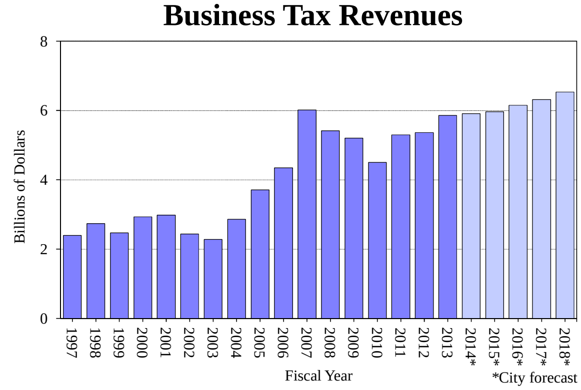
Sales tax collections are forecast to rise by 3.2 percent in FY 2015, to reach $6.7 billion (see Figure 15). This is slower growth than the City anticipates for FY 2014 (5.3 percent), reflecting a projected slowdown in employment and wage growth in 2015. Nevertheless, revenue projections continue to be boosted by the high level of spending from the record number of tourists expected to visit the City.

Growth in collections is expected to rise slightly (to an average annual rate of 4.3 percent) during fiscal years 2016 through 2018, as wage growth rises to 4.5 percent annually and tourism remains strong. Based upon current collection trends, OSC estimates that sales tax receipts could be higher than the City forecasts by $50 million annually in fiscal years 2015 and 2016.

4. Business Taxes

Figure 16

Business Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

The May Plan assumes that collections from the City's business taxes, which are paid by corporations, banking corporations and unincorporated businesses (i.e., partnerships and sole proprietorships), will rise by nearly 1 percent in FY 2015, to $6 billion (see Figure 16). This follows similar revenue growth in FY 2014.

The slow growth in both years reflects continued weakness in payments from financial firms, whose profits have been affected by higher interest rates, a reduction in mortgage activity, and legal settlements related to the financial crisis. Profits at Wall Street firms, for example, declined to $16.7 billion in 2013, and the City expects profits to ease to $14 billion in 2014. Overall, financial firms account for about half of all business tax collections (and securities industry firms make up nearly 40 percent of the financial share). The City expects that payments from nonfinancial firms will grow modestly over the rest of FY 2014 and into FY 2015 now that a backlog of credits from overpayments in prior periods has been exhausted.

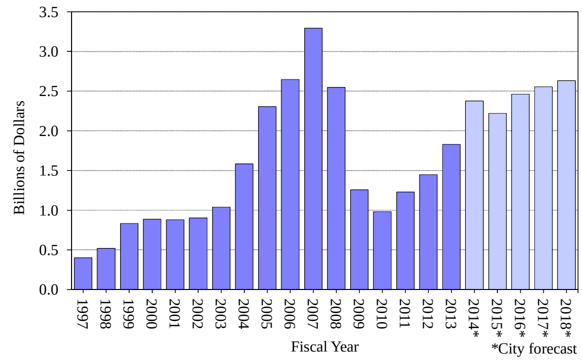
The May Plan projects that the average annual rate of growth for business taxes will rise slightly during fiscal years 2016 through 2018, to 3.1 percent. The City expects that implementation of regulatory reforms, additional legal settlements and rising interest rates will continue to limit increases in profitability for financial firms. Nevertheless, the City expects that continued improvements in the broader economy will allow payments from nonfinancial firms to grow modestly during these years.

5. Real Estate Transaction Taxes

The market for commercial properties in the City, especially for large Manhattan office buildings, has strengthened and is attracting increased interest from international investors. Sales have also been strong for high-end Manhattan residential properties. As a result, collections from the City's two taxes on real estate transactions (the mortgage recording tax and the real property transfer tax) are forecast to rise by 30 percent to reach nearly $2.4 billion by FY 2014 (see Figure 17).

Figure 17

Real Estate Transaction Tax Revenues



Sources: NYC Comptroller; NYC Office of Management and Budget

The May Plan assumes that rising interest rates will significantly reduce transaction activity in FY 2015, resulting in a 6.6 percent decline in collections. The Federal Reserve, however, has renewed its commitment to keep interest rates low until certain economic goals have been met and then to increase them slowly. Thus, OSC believes that collections from real estate transaction taxes are likely to be higher than the City's forecast in FY 2015. The May Plan assumes that, despite higher interest rates, collections will resume growing in FY 2016.

6. Miscellaneous Revenues

Miscellaneous revenues (from sources such as charges for services, licenses, permits, fines, fees and investment income) are projected to total $5.6 billion in FY 2015, including proceeds from the sale of taxi medallions (for more detail, see Section IX). The Mayor recently announced a new regulatory reform initiative to protect small businesses. Changes will affect fines issued by several agencies. For example, to promote fairness and consistency in determining fines against food establishments, the Department of Health and Mental Hygiene will reduce fines for minor violations and may waive other fines in certain instances.

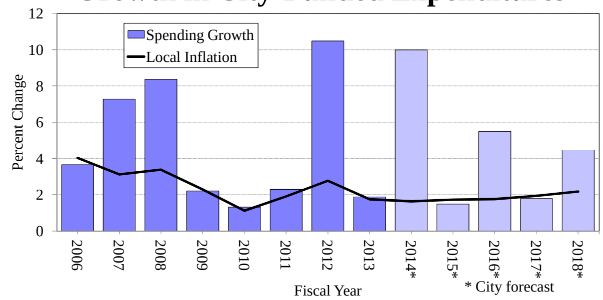
VI. Expenditure Trends

City-funded expenditures are projected to grow by nearly 10 percent in FY 2014 (nearly $5 billion), which is five times faster than the projected inflation rate.[9] This would be the fastest rate of growth in six years except for FY 2012, when the City replaced expiring federal stimulus aid and offset a large cut in State education aid (see Figure 18). The rapid rate of growth reflects the potential cost of new labor agreements, along with continued growth in debt service and fringe benefits.

While spending is projected to grow at about the projected inflation rate during fiscal years 2015 and 2017, costs are projected to grow considerably faster than the projected inflation rate during fiscal years 2016 and 2018. Overall, spending will grow at an average annual rate of 4.6 percent between fiscal years 2013 and 2018, more than twice the projected inflation rate for this period (1.8 percent).

Figure 18

Growth in City-Funded Expenditures



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

Personal service costs (i.e., the cost of employee wages and fringe benefits) will rise by $7.1 billion between fiscal years 2013 and 2018, an increase of 25.4 percent. These estimates reflect the impact of the recent labor agreement between the City and the United Federation of Teachers (UFT), and the May Plan’s assumption that the agreement will set the wage pattern for the other unions (for more detail, see “Collective Bargaining” later in this section). Debt service is projected to increase by nearly $2.2 billion to $7.6 billion in FY 2018, an increase of 39.7 percent.

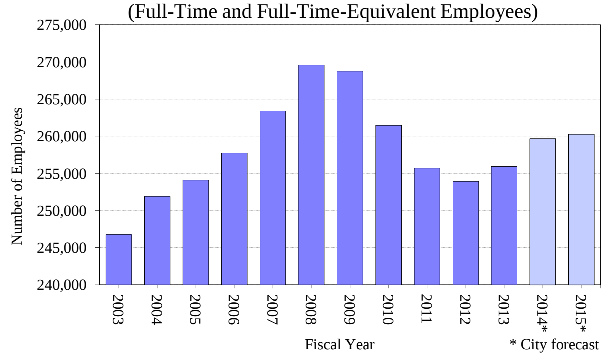
The City-funded workforce grew by 22,800 employees (9.2 percent) between fiscal years 2003 and 2008 (see Figure 19), but staffing levels contracted by 15,666 employees over the next four years as budget cuts were imposed to help weather the Great Recession.

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

Staffing levels resumed growth in FY 2013, increasing by 2,003 employees. The May Plan assumes that City-funded staffing (both full-time and full-time-equivalents) will increase by another 4,300 employees during fiscal years 2014 and 2015 to reach 260,265, which is still below the prerecession peak (see Appendix B).

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

Figure 19
City-Funded Staffing Levels
(Full-Time and Full-Time-Equivalent Employees)



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

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

	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
Personal Service	$ 28,109	$ 31,218	$31,168	$ 32,556	$ 33,181	$ 35,247
Medicaid	6,233	6,272	6,353	6,322	6,322	6,322
Debt Service	5,465	5,565	6,580	7,124	7,366	7,637
Energy	882	936	920	912	922	965
Judgments and Claims	402	523	534	570	606	642
Public Assistance	576	561	600	582	585	585
General Reserve	- - -	50	600	600	600	600
Prior Years' Expenses	(347)	(400)	- - -	- - -	- - -	- - -
Drawdown Retiree Health Benefits Trust	(1,000)	- - -	- - -	- - -	- - -	- - -
Health Stabilization Fund Transfer	- - -	- - -	(1,000)	- - -	- - -	- - -
Other	9,493	10,064	9,844	9,984	10,116	10,369
Total	**$ 49,813**	**$ 54,789**	**$ 55,599**	**$ 58,650**	**$ 59,698**	**$ 62,367**

Sources: NYC Office of Management and Budget; OSC analysis

1. Collective Bargaining

In our March 2014 report, we noted that all of the labor agreements between the City and the municipal unions had expired, some as long ago as 2008. We concluded that the absence of new labor agreements represented the greatest uncertainty facing the City's financial plan. While most of the labor agreements expired in 2010, the City had not reached an agreement with the United Federation of Teachers (UFT) for the 2008-2010 round of collective bargaining. On May 1, 2014, the City and the UFT, which represents the City's teachers and paraprofessionals (37 percent of the City's workforce), announced a nine-year labor agreement, which was subsequently approved by the rank and file on June 3, 2014.

The agreement compensates teachers and other UFT members for two annual wage increases of 4 percent that were provided by the prior mayoral administration to other municipal unions in 2009 and 2010, but not to members of the UFT.[10] In addition, the agreement increases wages by 10 percent over a seven-year period and provides employees with a $1,000 payment upon ratification of the agreement. The City, which has a long history of pattern bargaining, assumes that these terms will set the wage pattern for all municipal unions.[11] However, the Patrolmen's Benevolent Association (which represents the City's police officers) is seeking larger wage increases than those offered by the City, and has begun the process that could lead to binding arbitration.

Under the UFT agreement, the salaries for teachers and other UFT members will increase by 2 percent per year over a four-year period beginning on May 1, 2015 (this represents a restructuring of the two annual wage increases of 4 percent that were provided to other municipal unions). In addition, workers will receive five lump-sum payments over a six-year period to compensate them (without interest) for the time they went without the raises.[12] Employees who retire before July 1, 2014, will receive one large lump-sum payment,[13] while those who retire between July 1, 2014 and October 1, 2020 will receive lump-sum payments on the same schedule as active employees. Employees who otherwise leave City service will be ineligible for any future payments.

The City has set aside resources in its operating budget for FY 2014 ($965 million) to fund the estimated cost of the lump-sum payments to past and future retirees through September 30, 2020. The cost for employees still in service will be funded from the operating budget in the year in which the lump-sum payments are made. The accounting treatment of the UFT agreement[14] in the May Plan is consistent with generally accepted accounting principles (GAAP). State law and the City Charter

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

11 Under the agreement, after an 18-month wage freeze wages will increase by 1 percent retroactive to May 2013, 1 percent in May 2014, 1 percent in May 2015, 1.5 percent in May 2016, 2.5 percent in May 2017 and 3 percent in May 2018.

12 Lump-sum payments will be made on October 1 of 2015, 2017, 2018, 2019 and 2020.

13 A Structured Retiree Claims Settlement Fund will be created in the amount of $180 million to settle all claims by retirees who have retired between November 1, 2009 through June 30 2014. The fund will be distributed based on an agreed-upon formula.

14 A copy of the contract was unavailable because it had not been finalized by the time this report was prepared.

require the City to balance its budget and to prepare its financial plan in accordance with GAAP, except for the application of Statement No. 49 of the Government Accounting Standards Board, which relates to environmental remediation. The City's financial statements will be reviewed by an independent accounting firm at the end of each fiscal year, as required by State law and the City Charter, to determine whether they conform to GAAP.

The City estimates that compensating UFT members and other employees for the 8 percent wage increase for the 2008-2010 round of collective bargaining will cost nearly $4.7 billion during the financial plan period, with an annual cost that grows to $1.2 billion by FY 2021.[15] The City further estimates that a pattern wage increase of 10 percent over seven years for all City employees will cost nearly $8.9 billion during the financial plan period, with an annual cost that grows to $3.8 billion by FY 2021.

These costs (which total $13.6 billion during the financial plan period) will be partially offset by resources previously set aside by the City in its labor reserve ($3.5 billion), and by a total of $4.4 billion in new resources that are expected to become available as the result of an approved agreement between the City and the Municipal Labor Committee (MLC), which represents the City's unions.

The agreement between the City and the MLC is expected to generate cumulative health insurance savings of $3.4 billion through FY 2018, of which $1.3 billion is expected to be recurring.[16] If health care savings exceed $3.4 billion during the four-year period, up to $365 million (the equivalent of a 1 percent wage increase) would be used to provide a one-time lump-sum payment to employees. Any additional savings during the financial plan period would be shared equally between the City and the municipal unions, and after FY 2018 the use of any additional recurring savings above $1.3 billion would be subject to negotiation. The agreement also permits the City to transfer $1 billion in unneeded resources from the Health Stabilization Fund to the operating budget to help fund wage increases.

[15] The City estimates that the lump-sum payments will total $7.1 billion during fiscal years 2014 through 2021, of which $4.2 billion will be included in the budgets for fiscal years 2019 through 2021. Even after all the lump-sum payments are made, the City will incur additional pension contributions of $128 million annually beginning in FY 2023.

[16] 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.

A joint labor-management committee will be formed to identify actions to reduce the cost of health care. A number of different possibilities have already been suggested, including negotiating agreements with the City's health insurance carriers to hold down the growth in health insurance premiums, and conducting audits of health benefits coverage for dependents to reduce the possibility of fraud. The unions will be credited with any savings that result from health insurance premiums growing more slowly than assumed in the City's financial plan.[17] The agreement does not exclude the possibility of higher employee health insurance premiums or higher co-payments, but the City and its unions are focused on reducing the cost to the City, rather than shifting the cost to employees.

The City and the MLC have agreed to hire an independent health care actuary to measure the savings resulting from the agreement. If the City and the MLC are unable to resolve any dispute on their own, the agreement calls for arbitration and a decision within 90 days. The arbitrator has the authority to enforce the terms of the agreement.

The agreement is unprecedented and untested, and this has raised questions about whether the savings will be achieved in the amounts and in the years anticipated in the City's financial plan. The City has agreed to report on the progress of the labor-management committee on a regular basis, which will build confidence that the agreement is generating the anticipated savings.

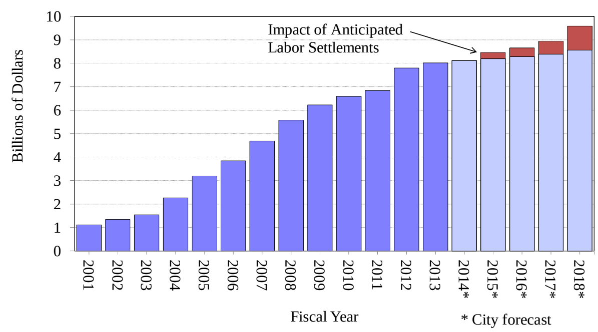
2. Pension Contributions

The May Plan assumes that the recent agreement with the UFT will set a pattern for negotiations with the rest of the municipal workforce. The cost of these agreements, including the impact on pension contributions, has been included in the Labor Reserve. As is customary, the cost will be reflected in the City's estimates of pension contributions when the agreements are finalized. In the meantime, OSC estimates that City pension contributions will rise from \$8.1 billion in FY 2014 to nearly \$9.6 billion in FY 2018 (see Figure 21) when the impact of the new labor agreements have been reflected.

Figure 21

New York City Pension Systems

Annual Contributions



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

17 The May Plan assumes, for example, that health insurance premiums for active employees will grow by 9 percent annually beginning in FY 2016.

These estimates reflect changes in assumptions and methodologies recommended by the City Actuary and approved by the boards of trustees of the City's five pension systems in 2012 and (where necessary) enacted into State law in January 2013. The changes include a reduction in the investment earnings assumption from 8 percent to 7 percent; a different methodology to determine the cost of future pension benefits; a market value restart;[18] and a longer amortization period, which frees up resources during the financial plan period but will result in higher costs over the longer term.

The City has engaged the services of an independent actuarial consultant, as required under the City Charter, to conduct a biennial audit of the pension systems. The audit, which is expected to be released during FY 2015, may recommend additional changes to the actuarial assumptions and methodologies that are used to calculate City pension contributions, which could increase (or decrease) planned City pension contributions.

The estimates also reflect the impact of better-than-expected investment gains during FY 2013, when the City's pension systems earned 12.1 percent on their investments (compared to an expected annual return of 7 percent). As of May 23, 2014, the City's pension systems had earned an estimated 13 percent on their investments.

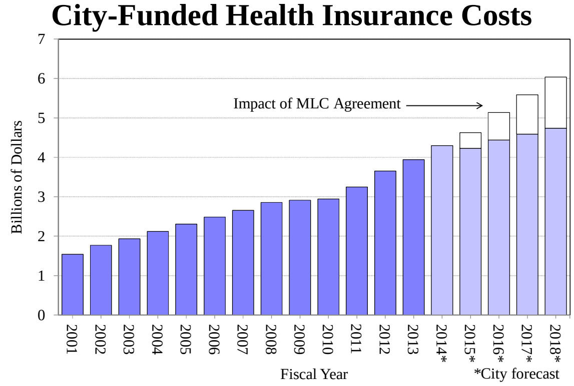
As of June 30, 2011 (the most recent date of pension valuation data reported by the City Actuary), the City's five pension systems had sufficient assets to fund, on average, 61 percent of their accrued liabilities, a smaller percentage than in prior years. The New York City Employees' Retirement System,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

3. Health Insurance

As previously discussed, an agreement with the Municipal Labor Committee is expected to generate $3.4 billion in health insurance savings through FY 2018. If the savings are realized as planned, the growth in health insurance costs would slow from an average annual rate of 9.3 percent to 3.3 percent, but the cost would still reach $4.7 billion by FY 2018 (see Figure 22), 61 percent more than the cost in FY 2010.

Figure 22

City-Funded Health Insurance Costs



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

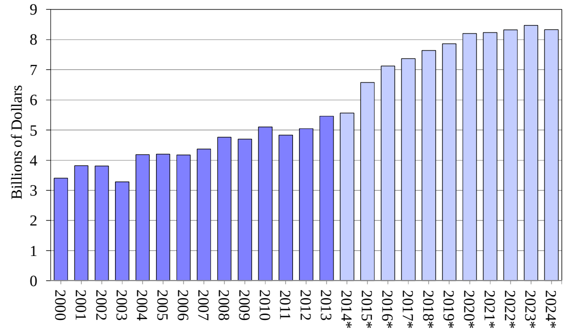
[18] Under a market value restart, the actuarial value of assets is reset to the market value rather than phasing in gains and losses over a six-year period.

4. Debt Service

The City has deferred $3.8 billion in capital commitments that were planned for FY 2014 to better reflect project schedules. At the same time, the City has increased planned capital spending for new mayoral priorities, including increasing affordable housing, reducing school overcrowding, and repairing roads and bridges. As a result, the City-funded capital commitment plan for fiscal years 2014 through 2018 now totals $34.3 billion, or $3.2 billion more than anticipated in February 2014.

Figure 23

City-Funded Debt Service



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

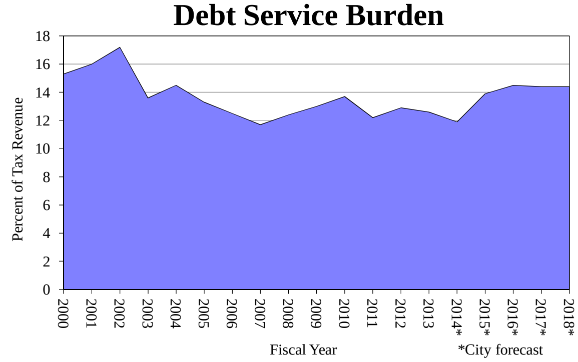
City-funded debt service (adjusted for surplus transfers) will grow from nearly $5.5 billion in FY 2013 to $7.6 billion by FY 2018 (see Figure 23), an increase of 39.7 percent. While the City now projects that debt service will be lower during the financial plan period than forecast in February 2014 (a net reduction of $139 million), it will be higher in subsequent years (by more than $300 million annually by FY 2023) to finance an increase in planned capital commitments.

The City's capital plan has benefited from the current low-interest-rate environment. The City realized savings of more than $200 million in FY 2014 from lower-than-planned interest rates on variable-rate debt, and could realize similar savings in FY 2015 ($150 million) because the City is unlikely to need to borrow to meet its short-term cash flow needs, and interest rates are likely to remain low.

The debt service burden (i.e., debt service as a percent of tax revenues) will rise from 11.9 percent in FY 2014 to 14.4 percent by FY 2018 (see Figure 24). If recent economic trends continue, OSC projects that the debt service burden will remain relatively stable at that level through FY 2024, despite the increase in planned capital commitments.

Figure 24

Debt Service Burden

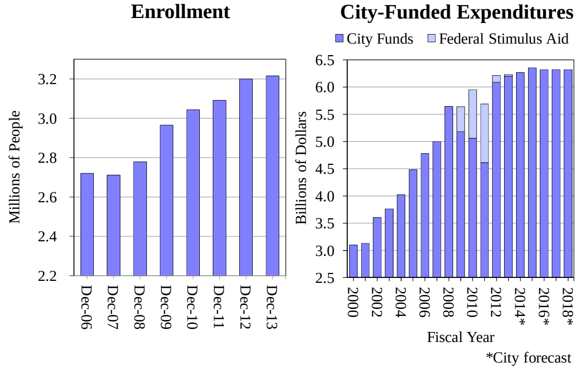


Note: Debt service amounts are adjusted for prepayments and defeasances, and include about $175 million annually in federal and State subsidies.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

5. Medicaid

Between December 2008 and December 2013, enrollment in the Medicaid program rose by 16 percent to reach almost 3.2 million people (see Figure 25), or about one of every three New York City residents. Enrollment over the past year also increased, but at a slower rate than in the five prior years as the economy has slowly improved and unemployment has gradually declined. Enrollment growth is largely attributed to the recent recession, and will continue under the Affordable Care Act, which expands Medicaid eligibility.

Figure 25
Medicaid



Sources: NYS Department of Health; NYC Office of Management and Budget; OSC analysis

Despite the expected growth in enrollment, the City-funded cost of Medicaid will remain relatively flat because of actions taken by the State to provide financial relief to localities. The May Plan assumes that the City's share of the cost of Medicaid will grow slowly in FY 2015 and then level off at $6.3 billion in FY 2016 as the State completes a three-year takeover in the growth in the local share of Medicaid.

In April 2014, the federal government approved New York State's Medicaid waiver application, which allows the State to reinvest about half ($8 billion) of the savings that the federal government will receive from actions the State intends to implement to lower the cost of health care. The State intends to use these resources to improve quality of care and preserve essential safety-net providers across the state.[19] In addition, resources would be available for distressed hospitals in Brooklyn and other parts of the State. The State would offer these hospitals near-term financial support in return for reforms that ensure long-term financial viability.

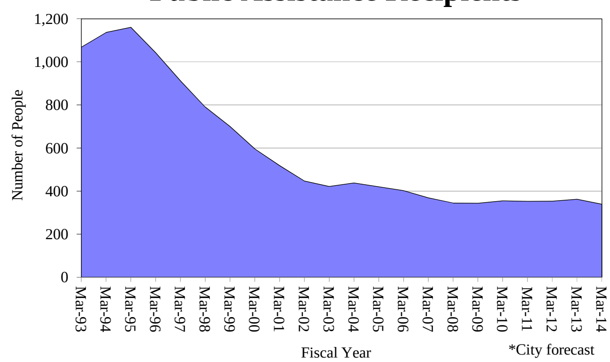
[19] Essential safety-net providers are providers that serve large numbers of Medicaid and uninsured patients.

6. Public Assistance

Despite the recent recession, the public assistance caseload grew by only 5 percent between March 2008 and March 2013, and then declined by 6 percent over the past year to total 339,203 recipients in March 2014 (see Figure 26).[20] The Commissioner of the New York City Human Resources Administration has attributed the small increases in caseload in recent years to policies that have made it difficult for people to receive public assistance. The new administration proposes to make it easier for people to receive benefits (which will likely lead to higher caseloads), and plans to develop training and education programs that could lead to better-paying jobs.

Figure 26

Public Assistance Recipients



Sources: NYC Office of Management and Budget; OSC analysis

The May Plan assumes that City-funded expenditures for public assistance will total $600 million in FY 2015, including $29 million for a new initiative to provide rent relief to public assistance recipients living with HIV/AIDS.

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

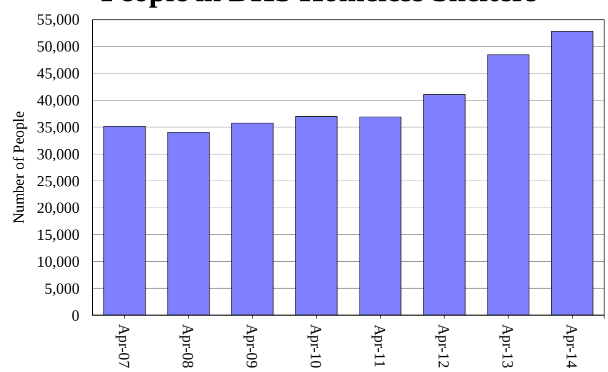
[20] The March 2014 caseload was 821,390 lower than the peak in March 1995, largely as a result of federal welfare reform measures implemented in the late 1990s that enforced work requirements.

7. Homeless Services

A federal assessment found that among the 50 largest cities in the United States, New York City had the largest homeless population (both sheltered and unsheltered) in 2013, which increased by 13 percent from 2012. This was the second-highest rate of increase in a major city behind Los Angeles, which showed a 27 percent increase in its homeless population. Although the number of homeless veterans in New York City declined by 24 percent between 2011 and 2013, the City had the second-largest population of this group among the nation's 50 largest cities (behind Los Angeles).

Figure 27

People in DHS Homeless Shelters



Sources: NYC Department of Homeless Services; OSC analysis

The population of homeless people in shelters managed by New York City's Department of Homeless Services (DHS) reached record-high levels in April 2014, at 52,807 people (see Figure 27), which was 43 percent higher than three years earlier. The growth in this population results in part from the termination of a rent subsidy program for homeless families and individuals by the City in April 2011, following the State's withdrawal of funding. In January 2014, the Mayor established a new policy that guarantees shelter to homeless families (regardless of their eligibility) on the coldest nights of the year. The City estimates the City-funded cost of sheltering homeless people in DHS facilities will be $393 million annually through FY 2018.

Over the past five months, the City has announced a number of initiatives to prevent homelessness and to reduce the number of people in shelters. In FY 2015, the DHS will expand its Homebase prevention program, which provides families and individuals on the brink of homelessness with assistance, to serve 5,000 more families. The DHS will also collaborate with the State to expand the Family Eviction Prevention Supplement program, which provides families at risk of becoming homeless with financial assistance to enable them to remain in their homes.

The City is also working with the State to develop two rental assistance programs. The Working Families Rental Assistance program, a joint City-State pilot, will help working families exit shelters.[21] The May Plan anticipates an implementation date of

[21] The program will target families with children and at least one adult household member who works full-time, and will provide a rent subsidy for three years with the possible option of another two years.

July 1, 2014, with 800 family placements per year over four years at a cost of $40 million to the City. The City also plans to reduce reimbursement rates to certain landlords that operate the City's shelters (those who offer limited social services and whose rents are well above market rates) and to use these savings to fund a new rental assistance program for homeless individuals.

In addition, the New York City Housing Authority will give priority to families in shelters, reinstituting a policy that was terminated in 2005. The City has also aligned itself with the federal government's goal to end homelessness among military veterans by the end of 2015, and plans to meet this goal by enhancing its coordinated efforts among City agencies and the U.S. Department of Veterans Affairs.

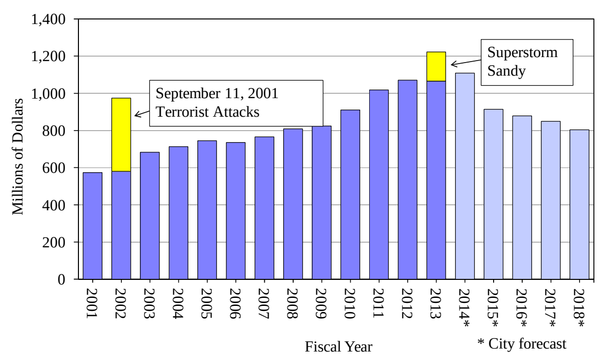
Other City agencies provide shelter targeted to specific needs within New York City's homeless population. The New York City Human Resources Administration shelters more than 2,500 people in facilities for victims of domestic violence, and another 2,000 people in facilities for homeless people with HIV/AIDS. The City's Department of Housing Preservation and Development provides emergency housing to about 2,000 people who have become homeless as a result of extraordinary circumstances, such as fires. Since January 2014, the Department of Youth and Community Development has added funding for an additional 100 shelter beds (for a total of 353 shelter beds) operated by community-based and faith-based organizations for runaway and homeless youths aged 16 to 21.

8. Uniformed Agencies

Overtime costs in the uniformed agencies (i.e., the Police, Fire, Correction and Sanitation departments) grew by 30 percent between fiscal years 2009 and 2012 (see Figure 28), largely as a result of staff shortages in the Fire and Correction departments. Excluding costs associated with Superstorm Sandy, overtime declined slightly in FY 2013.

Figure 28

Overtime Costs in the Uniformed Agencies



Sources: NYC Office of Management and Budget; OSC analysis

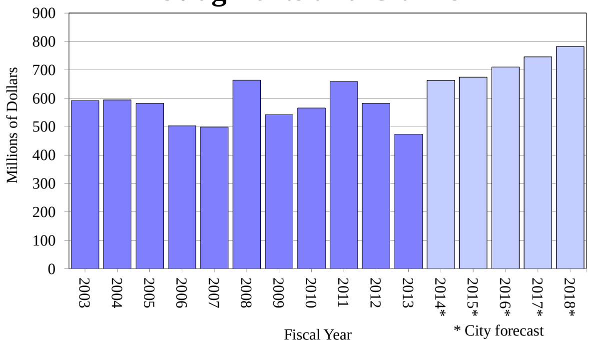
The May Plan assumes overtime will increase by $42 million in FY 2014 to $1.1 billion, and then decline sharply in FY 2015. About half of the decline is attributable to the receipt of federal grants, while the other half results from increased staffing in the Fire and Correction departments, and the assumption of a milder winter. OSC estimates that overtime costs could be higher by $50 million annually beginning in FY 2015.

9. Judgments and Claims

The May Plan assumes that the cost of judgments and claims will grow by $189 million (40 percent) to $663 million in FY 2014 ($523 million excluding costs associated with the Health and Hospitals Corporation), and then increase slowly in subsequent years (see Figure 29). Although such costs through the first nine months of the year are trending well below the City's forecast, a number of extraordinary cases may be settled before the end of the fiscal year.[22] However, OSC estimates that the cost of judgments and claims could be lower by $50 million annually in subsequent years based on current spending patterns.

Figure 29

Judgments and Claims



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

[22] In March 2014, the City reached a settlement in principle in an antidiscrimination case against the Fire Department, which stipulates that the City will pay approximately $98 million for back pay and benefits. In addition, an unspecified amount would cover compensatory damages to claimants who alleged emotional, financial or related harm beyond the loss of pay they would have received from the Fire Department.

VII. Superstorm Sandy Recovery

According to the City's most recent estimates, the effects of Superstorm Sandy could cost about $5.8 billion. Of this amount, $2.1 billion represents storm-related operating expenses (such as emergency repairs, debris removal and overtime), and $3.7 billion represents capital costs for permanent work to repair or replace damaged infrastructure.

As shown in Figure 30, the largest capital need is to restore public hospitals ($1 billion), including more than $700 million in projects that would harden damaged facilities against future storm damage. Other significant capital needs are repairs to parks, beaches and boardwalks ($710 million); roads, bridges and transportation infrastructure ($565 million); schools ($402 million); and public housing ($399 million). Most of the Department of Environmental Protection's estimated expense of $696 million is for the Rapid Repairs program, which provided emergency repairs (such as the restoration of heat, power and hot water) at no cost to private home owners.

Figure 30
Estimated Superstorm Sandy Expenses and Capital Costs
(in millions)

Agency	Expense	Capital	Total
Health and Hospitals Corporation	$ 384	$ 1,027	$ 1,411
Department of Parks and Recreation	105	710	815
Department of Environmental Protection	696	58	754
Department of Transportation	48	565	613
Dept. of Education/School Construction Authority	68	402	470
Police Department	199	22	221
Fire Department	38	168	206
Department of Sanitation	144	10	154
Department of Cultural Affairs	1	128	129
Department of Correction	5	83	88
All Other	261	87	348
Subtotal	**$ 1,949**	**$ 3,260**	**$ 5,209**
New York City Housing Authority	150	399	549
Total Estimated Cost	**$ 2,099**	**$ 3,659**	**$ 5,758**
Estimated NYCHA Insurance Recovery	(135)	(245)	(380)
Net City Cost	**$ 1,964**	**$ 3,415**	**$ 5,378**

Sources: NYC Office of Management and Budget; OSC analysis

The May Plan assumes that all of the costs related to the storm will be funded from non-City sources (i.e., federal funds). Federal law requires a local match of 10 percent of the cost of any claim deemed eligible for reimbursement by the Federal Emergency Management Agency (FEMA). While the May Plan assumes that this cost will be covered with other federal funds, no assurance can be given that the City will be reimbursed for all of its costs, as discussed below.

So far, FEMA has agreed to reimburse the City $1.5 billion (mostly for operating expenses), which is approximately $500 million less than the estimate of storm-related operating expenses not covered by insurance. The reimbursement process for capital projects is proceeding more slowly, but the City will be required to cover about $340 million of the estimated cost of capital repairs even if all claims are deemed eligible for reimbursement by FEMA and insurance. The City is working with FEMA and other federal agencies to maximize reimbursement.

The City has been allocated $4.2 billion in Community Development Block Grant-Disaster Recovery (CDBG-DR) funding, with $805 million of that amount available to fill gaps in FEMA funding. The City, however, has already used $183 million of that amount to cover the cost of storm-related services provided by the Health and Hospitals Corporation, leaving $622 million to fill gaps in FEMA reimbursement. Thus, currently allocated federal funding may not be sufficient to cover all of the costs associated with Superstorm Sandy.[23] In addition, the City could be required to obtain flood insurance for certain properties, but it would be required to purchase only minimal coverage at a cost of about $5 million to $10 million annually.

The City plans to use some CDBG-DR funds to help owners of single-family and multifamily residences (who have not received sufficient recoveries from FEMA and/or private insurance) to repair and rehabilitate their damaged properties. The City has allocated $1.4 billion for this purpose through its Build it Back program, and intends to allocate additional resources in the near future. More than 16,000 property owners are currently registered for the program, but construction has begun on just 36 properties. The Mayor has announced plans to improve the process, and the City Comptroller intends to audit the program. The State has approved legislation that will provide property tax relief for home owners who rebuilt their homes after the storm but now face large property tax increases.

The City is also considering a number of resiliency projects to help protect it from future storms. The City plans to use $579 million in CDBG-DR funding to begin priority coastal protection projects, such as installing floodwalls and raising bulkheads in low-lying neighborhoods. The City has submitted to the State an additional $550 million in proposed resiliency projects, including hardening public housing, hospitals and other City infrastructure. Upon State approval, these projects would be forwarded to FEMA for final consideration. If all of the projects are approved by FEMA, the City will need to fund up to $138 million of the cost.

[23] Additional resources may become available in the future, but other jurisdictions would be eligible to apply.

VIII. Semi-Autonomous Entities

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

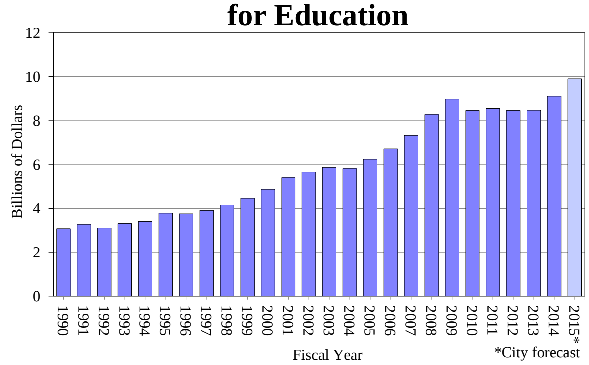
1. Department of Education

The May Plan allocates $25.9 billion to the Department of Education (DOE) in FY 2015, which is $1.3 billion (5 percent) more than the budget for FY 2014.[24] The FY 2015 budget includes the Mayor's initiatives to expand full-day prekindergarten and after-school programs for middle-school students, which are being funded by an increase in State education aid. The proposed budget also includes a number of City-funded initiatives, such as expanding arts instruction and the cost of opening district and charter schools.

In 2007, the State agreed to increase education aid to the City by $3.2 billion over a four-year period as a result of the resolution of the Campaign for Fiscal Equity lawsuit (CFE).[25] The State was unable to fulfill its commitment because of severe budgetary pressures resulting from the Great Recession. Now that the State's finances have improved, State education aid to the City is scheduled to increase by $735 million in FY 2015, the largest increase since FY 2008 (see Figure 31).

Figure 31

State Funding to New York City for Education



Sources: NYC Office of Management and Budget; OSC analysis

In January 2014, the Mayor advocated for the State to increase the personal income tax rate for the City's highest earners so the City could fund an expansion of full-day prekindergarten and after-school programs for middle-school students. Instead, the State increased education aid to the City, and intends to allocate $1.5 billion over five years to support full-day universal prekindergarten programs statewide. The Mayor's prekindergarten initiative will provide high-quality full-day services to 73,250

[24] The DOE budget does not yet reflect the impact of the labor agreement between the City and the United Federation of Teachers, which represents teachers and paraprofessionals (for more detail, see "Collective Bargaining" in Section VI).

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

children by January 2016. In the first phase, the City would provide full-day services to 53,600 children by September 2014.[26] Community-based organizations have submitted proposals to provide 20,000 seats and public elementary schools have submitted applications to provide an additional 9,000 seats, more than needed for the first phase.[27]

At the beginning of FY 2013, the City anticipated $167 million in Medicaid reimbursement for services provided to students with special needs, but it received only $15 million because the department had not overcome all of its problems in preparing adequately documented claims.[28] Although the City reduced its Medicaid revenue forecast to $50 million in FY 2014, so far the DOE has submitted claims totaling less than $13 million. The May Plan assumes that the amount of Medicaid reimbursement will rise to $67 million in FY 2015 and $97 million annually thereafter. Until the DOE demonstrates that it has solved the problems in the reimbursement process, the amounts above last year's level remain at risk.

The City and the United Federation of Teachers have reached a labor agreement covering calendar years 2009 through 2018. The agreement raises starting salaries from $45,530 to $56,709 by May 2018, and raises the top salary to $119,471. The agreement could reduce the number of teachers assigned to the Absent Teacher Reserve, which could generate savings, and teachers could receive bonuses for leadership roles (such as mentoring) and for assignment to certain schools in low-income neighborhoods. Teachers will receive additional time for professional development and parent-teacher interaction, but at the expense of time that had been previously set aside for tutoring students. The City and the teachers' union have also agreed to streamline the teacher evaluation process, which will require State approval. The DOE will be responsible for the implementation and net cost, if any, of these initiatives.

---

26 The Mayor's prekindergarten initiative calls for adding 21,000 full-day seats and enhancing 32,600 existing seats by September 2014. The City currently provides full-day prekindergarten services to about 19,500 children and part-day services to another 39,000 children. Services are provided by a mix of public elementary schools and community-based organizations.

27 For the upcoming school year, the City received a total of 41,603 applications to fill the 21,000 seats available in public elementary schools.

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

2. Health and Hospitals Corporation

The Health and Hospitals Corporation (HHC), the largest municipal hospital system in the country, faces serious financial challenges. The HHC served almost 1.4 million patients in FY 2013, and is the single-largest provider of health care to uninsured City residents (476,000 of its patients were uninsured last year). The HHC relies heavily on Medicaid (which currently provides 74 percent of total patient revenue), and is significantly affected by State and federal government actions that impact Medicaid.

The HHC has struggled for years with an ongoing, significant structural imbalance in its finances. Since FY 2009, the HHC has attempted to address this by instituting cost-saving measures, including a hiring freeze that reduced staff by about 3,700 employees. In spite of these efforts, the HHC has yet to solve the underlying imbalance. The HHC currently expects that its operating revenues will increase by 8 percent from FY 2014 through FY 2018, while operating expenses will grow by 20 percent over the same period.

As recently as FY 2007, the HHC benefited from large Medicaid reimbursements, ending the fiscal year with a cash balance of more than $1 billion (its highest ever). Since then, however, the HHC has drawn on these reserves to balance its budget. As of May 2014, the HHC had enough cash to pay its bills for just 13 days, and is relying on the receipt of two large Medicaid payments before the end of the fiscal year: one from an agreement with the State to accelerate a payment of $450 million that was originally expected in FY 2015, and another that has yet to be approved by the federal government, for $516 million.[29] Even if these payments are received, it is still unlikely the HHC will be able to make an $850 million payment it owes to the City ($390 million of which was due last fiscal year[30]). It is likely that the HHC will need to pursue another financial arrangement with the City as it did last year.

The HHC is counting on the receipt of $400 million annually (for five years, starting in FY 2015) from additional Medicaid funding, but receipt is contingent on a series of actions that have not yet been implemented. In April 2014, the State and federal governments finalized an $8 billion plan to transform the State's health care system, largely by reducing preventable hospitalizations and avoidable emergency room visits. To participate, the HHC will have to submit a plan by December 2014 for the State's approval.

---

[29] Since FY 2007, the HHC has had an average of 36 days of cash on hand at the end of each fiscal year.

[30] The $390 million in payments (for debt service and medical malpractice reimbursement) was delayed until FY 2014 pursuant to an agreement with the City and in response to the HHC's poor cash position at the end of FY 2013.

3. Metropolitan Transportation Authority

The current financial plan for the Metropolitan Transportation Authority (MTA) projects a balanced budget for calendar years 2014 through 2016, and a budget gap of $255 million in 2017. This financial outlook is greatly improved over the MTA's forecasts from only a few years ago, when the Great Recession sharply reduced ridership and tax revenues. Since then ridership has largely recovered, and tax collections continue to improve. When combined with additional cost-cutting initiatives, the MTA has been able to reduce planned fare and toll increases in 2015 and 2017, from 7.5 percent to 4 percent.

The outcome of collective bargaining was one of the largest financial uncertainties facing the MTA. Recently the MTA reached a labor agreement with Local 100 of the Transport Workers Union (TWU), which represents about half of the MTA's workforce. Under the agreement, workers will receive wage increases of 8 percent over five years as well as improved benefits. The cost of the agreement will be partly offset by increased employee contributions for health insurance.

The MTA estimates that the agreement will cost $525 million more than budgeted in its financial plan, but it does not expect the agreement to adversely impact fares and tolls, or service levels. The MTA has indicated that if its other unions agree to follow the wage pattern set by the TWU agreement, it could fund the cost of the agreements with available resources. The MTA and the unions that represent most employees of the Long Island Rail Road, however, have not yet been able to reach an agreement.

Despite progress on labor matters, the MTA still has to address funding for its capital program. The MTA has indicated that the next five-year capital program, which begins in 2015, will total about $24 billion (the same size as its current capital program, excluding costs associated with Superstorm Sandy). The MTA had planned to set aside $3 billion in its operating budget to help fund the capital program, but that amount could be reduced to help fund labor agreements.

Even if the City, the State and the federal government provide funding at traditional levels, the next capital program could have a large funding gap. The Governor has asked the MTA to impanel a Transportation Reinvention Commission to examine the MTA's network and to plan for the next century's transportation needs. The new commission will report its findings to the Governor before the MTA submits its proposed capital program for State approval in September 2014.

4. New York City Housing Authority

The New York City Housing Authority (NYCHA) is a critical component of the City's current supply of affordable housing. As the City's largest landlord, NYCHA manages approximately 179,000 apartments with more than 400,000 residents (including 176,000 families). In total, these units account for more than 8 percent of the rental units citywide. NYCHA also manages the nation's largest Section 8 housing program, which provides rent subsidies for 93,000 private apartments that house 225,000 residents. On average, NYCHA residents pay 30 percent or less of their annual incomes on rent.[31] Currently, more than 247,000 families are on the waiting list for a NYCHA apartment.

Over the years, NYCHA has faced significant fiscal and management challenges that have threatened its ability to provide safe and affordable housing. For example, NYCHA has experienced significant cuts in federal subsidies (which make up 50 percent of its operating budget and 70 percent of its capital budget) and difficulties making timely repairs. Since January 2014, NYCHA has received an additional $123 million from the City for repairs and security enhancements. NYCHA has not revised its four-year financial plan since December 2013, but at that time it projected a budget gap of $191 million in calendar year 2014, and even larger gaps in subsequent years. Although NYCHA has not revised its financial plan since December 2013, it reports that it has reduced its budget deficit for the current fiscal year (which ends on December 31, 2014) to $77 million. NYCHA is considering additional actions to close the remaining budget gap.

[31] According to federal guidelines, a family that pays more than 30 percent of its annual income on housing may have difficulty affording other necessities, such as food and clothing.

IX. Other Issues

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

1. Sale of Taxi Medallions

State law authorizes the City to sell up to 2,000 new taxi medallions for wheelchair-accessible vehicles.[32] The law includes other provisions to improve accessibility for passengers throughout the City by creating a new class of designated livery vehicles, known as “boro taxis” (painted apple green), which may pick up street-hail passengers in areas of the City considered underserved by yellow taxis (such as northern Manhattan and the other boroughs). The City is permitted to issue up to 18,000 of these new boro taxi licenses.

In November 2013, the TLC reached a settlement agreement (currently pending formal court approval) in a federal class action lawsuit filed by a coalition of disabilities rights organizations. As per the agreement, on April 30, 2014, the TLC unanimously passed rules that will raise the number of wheelchair-accessible vehicles to half of the medallion fleet, or 7,500 vehicles, by 2020. To help fund this transition, the rules authorize a new $0.30 surcharge beginning in 2015.[33]

The City auctioned the first 400 taxi medallions in FY 2014, generating $409 million (of which $114 million will be received in FY 2015). The City, however, cannot sell the remaining 1,600 medallions until the Taxi and Limousine Commission (TLC) submits a disabled accessibility plan (DAP) to the State Department of Transportation, and the State approves the plan.

On June 4, 2014, the TLC submitted a draft DAP to the City Council for its review and expects to submit the final DAP to the State by the deadline of June 12, 2014. Within 60 days of submission, the State must approve or reject the DAP.

The May Plan anticipates the receipt of $1.2 billion during fiscal years 2015 through 2017 from the sale of the remaining taxi medallions on the assumption that the DAP will be approved in a timely manner.[34] (OSC estimates that sale proceeds could be $400 million higher based on the strength of medallion sales during FY 2014.) The City has overcome a number of hurdles in its efforts to sell the remaining 1,600 taxi medallions, and the process is nearly complete.

---

[32] When the law was enacted, fewer than 2 percent of the City’s yellow taxis were wheelchair-accessible.

[33] For each surcharge in a yellow taxi, $0.25 will go into a taxicab improvement fund and $0.05 will go to the driver to offset costs of additional training related to accessible vehicles. Similarly, the TLC created a street-hail livery improvement fund, which will be financed by each $0.30 surcharge in a boro taxi.

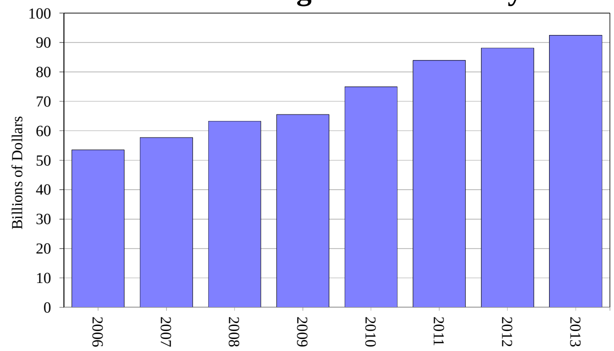
[34] The May Plan anticipates $595 million in FY 2015, $360 million in FY 2016 and $400 million in FY 2017.

2. Other Post-Employment Benefits

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

Figure 32

Outstanding OPEB Liability



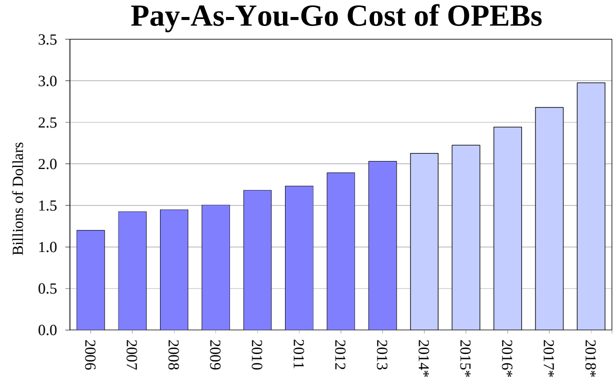
Sources: NYC Actuary; OSC analysis

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

Although the City is required to fund pension costs on an actuarial basis to ensure that current taxpayers pay their fair share of services, the City is not required to fund OPEBs on a similar basis. In FY 2013, the City paid less than one-third of the present value of obligations ($3.8 billion) that is attributed, on an actuarial basis, to services received that fiscal year, deferring nearly $2.6 billion to the future.

Figure 33

Pay-As-You-Go Cost of OPEBs



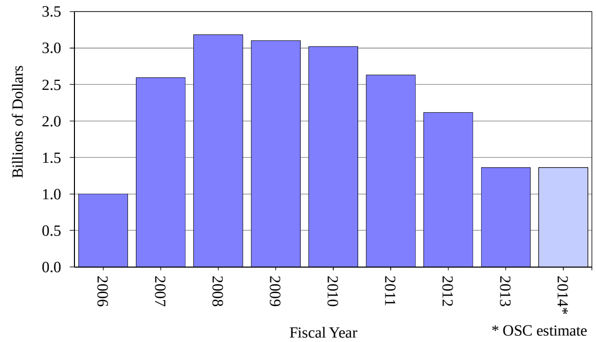
Sources: NYC Actuary; NYC Office of Management and Budget; OSC analysis

The City, like many employers, pays the annual cost of benefits provided to current retirees on a pay-as-you-go (PAYGO) basis. OPEB costs on a PAYGO basis are projected to rise from $2 billion in FY 2013 to nearly $3 billion in FY 2018 (see Figure 33), an increase of nearly 47 percent in five years. The City and the Municipal Labor Committee, which represents the City's municipal workforce, have reached an agreement to create a process for the City to realize $3.4 billion in health insurance savings during the financial plan period, which could slow down the rate of growth (for more detail, see Section VI).

In FY 2006, the City established the Retiree Health Benefits Trust (RHBT), and over two years deposited $2.5 billion of surplus resources into the trust to help fund the future cost of OPEBs. These resources were invested and have earned interest. Although the RHBT was intended to help fund a future liability, in recent years the City instead used it as a rainy-day fund to help balance the budget. The City drew down much of the resources in the RHBT during fiscal years 2009 through 2013 (see Figure 34), leaving future taxpayers to fund the full cost of services provided in those years. The City had planned to transfer $1 billion from the RHBT to help balance the FY 2014 budget, but rescinded the planned transfer in February 2014 because revenues grew much faster than the City anticipated at the beginning of the fiscal year, which leaves a balance of $1.4 billion in the RHBT.

Figure 34

Balance of RHBT Resources



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

3. Impact of the State Budget

The May Plan reflects the impact of the State enacted budget for State Fiscal Year (SFY) 2014-2015, which benefits New York City's budget by $762 million in City Fiscal Year (CFY) 2015, $677 million in CFY 2016, $746 million in CFY 2017 and $796 million in CFY 2018. Nearly all of the aid will come in the form of higher education aid.[35] The City also could benefit from the Smart Schools Bond Act, which, if approved by voters in November 2014, would allocate $2 billion statewide to fund technology investments in schools as well as space for new prekindergarten programs. The City's capital plan anticipates the receipt of $783 million from the bond act.

In January 2014, the Mayor advocated for the State to increase the personal income tax rate for the City's highest earners to fund an expansion in full-day prekindergarten and after-school programs for middle-school students. Instead, the State increased education aid to the City by $735 million in FY 2015, which is the largest increase in education aid in eight years. The State dedicated $300 million of the increase to fund an expansion in prekindergarten (similar to the amount sought by the City), and

[35] The State will also provide rental relief to public assistance recipients living with HIV/AIDS (which requires a $28.9 million matching contribution from the City), and a small increase in transportation aid. In addition, the State eliminated certain resident trust loopholes, which the City anticipates will increase tax revenues by $34 million in CFY 2015, $62 million in CFY 2016 and $45 million in subsequent years.

authorized the use of State education aid to fund an expansion of after-school programs for middle-school students ($145 million).

4. Impact of the Federal Budget

In August 2011, the President and Congress agreed to implement across-the-board spending cuts (known as the sequester) that became effective on March 1, 2013, in an effort to reduce the federal deficit. These cuts reduced funding to the City's budget by a total of $148 million in federal fiscal year (FFY) 2013, which affected City fiscal years 2013 and 2014.[36] In May 2013, the City revised its four-year financial plan to reflect the impact of these cuts on the City's budget, and mitigated most of the effects with City, State and other federal funds. In some cases the City chose not to relieve the impact of federal budget cuts, and some programs, such as Head Start and certain health services (e.g., services for people living with HIV/AIDS, and disease control and immunizations), experienced a loss in funding and reduced services.

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

In December 2013, a two-year budget agreement revised discretionary spending caps, rescinding two-thirds ($22 billion) of the cuts scheduled to take effect in FFY 2014.[37] The agreement maintains federal spending at that level through FFY 2015, but it does not rescind budget cuts planned for subsequent years. The agreement also does not extend unemployment benefits for some 1.3 million people who have been out of work for more than six months (including approximately 73,000 New York City residents), and whose benefits expired on December 31, 2013.

The May Plan does not reflect any additional federal budget cuts because congressional appropriations for FFY 2014 have largely restored funding for discretionary programs. Cuts to discretionary spending in FFY 2015 and subsequent years, however, will be determined by future federal budget negotiations, and could be larger or smaller than those in FFY 2013.

---

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

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

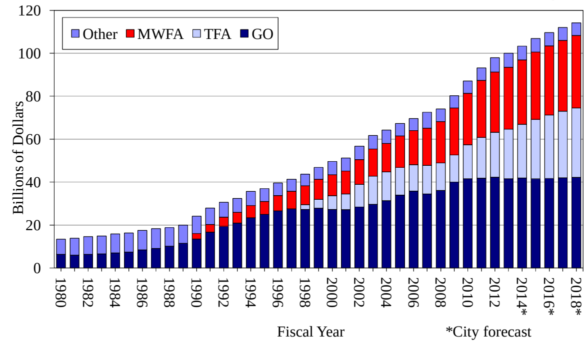
5. Debt Outstanding

The outstanding debt of the City and City-related entities has risen steadily over the past three decades to fund the City's capital program.[38] During the current financial plan period, the City plans to issue $32.6 billion in debt through its general obligation (GO), Transitional Finance Authority (TFA) and Municipal Water Finance Authority credits, which is $1.4 billion more than anticipated in February 2014.

Debt outstanding reached $100 billion at the end of FY 2013, an increase of 56 percent over the past decade (see Figure 35), and is projected to exceed $114 billion by FY 2018. The amount of debt outstanding at the end of FY 2013 was about $12,000 per capita, or $4,000 more than ten years earlier.

Figure 35

City and City-Related Debt Outstanding



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

6. Building Aid Revenue Bonds

The State-funded portion of the Department of Education's capital plan is financed through Building Aid Revenue Bonds (BARBs) issued by the TFA and secured by State building aid. State law currently limits the amount of BARBs that can be outstanding at any time to $9.4 billion. Without an increase in State authorization, OSC estimates that the City will exceed this limit during FY 2017, putting at risk $2.8 billion in State-funded commitments planned for fiscal years 2018 and 2019.

7. Credit Rating

The City-funded portion of New York City's capital program is expected to be financed through GO bonds secured by the City's full faith and credit, and TFA bonds 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 has been able to maintain its ratings through the recession.[39] According to the City Comptroller, GO bonds are at their highest rating in more than 70 years. The City's strong credit ratings

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

[39] Fitch Ratings and Moody's Investors Service 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.

contribute to its ability to access the capital markets to meet its financing needs, and 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).[40] 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.

Moody's recently noted that the labor agreement with the UFT would resolve a long-standing budget risk, but it also noted that the May Plan is "credit negative" because it "shows how personnel costs drive the City's budget and challenge its finances, even in a strong economy."[41] Fitch has commented that the agreement represents a "sizeable but manageable funding need" and would reduce budgetary uncertainty. Standard & Poor's noted that the City's "history of conservative financial projections and ability to close projected budget gaps" would partially mitigate pressure the agreement places on the budget.

8. Housing New York

In response to the lack of affordable housing in New York City, the Mayor has announced Housing New York, a $41.4 billion plan to create and preserve a total of 200,000 units of affordable housing over ten years.[42] The City estimates that the plan will create 194,000 construction jobs and 7,100 permanent jobs.

Funding for the Mayor's plan is expected to come from a mix of City, State, federal and private sources. The City's contribution is expected to total $8.2 billion, including $6.7 billion in capital funds and $1.5 billion in other City funding. Private financing, which makes up the largest funding component, is expected to total $30 billion. Private financing includes the issuance of tax-exempt bonds ($13 billion) on behalf of developers (which lowers the cost of construction), direct investment from private

[40] 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.

[41] Credit negative is not the same as a "negative outlook," which would have signaled a likely reduction in the City's credit rating in the short-to-medium term.

[42] The affordable housing plan is intended to preserve 120,000 units and create another 80,000 units.

entities ($11 billion), the sale of housing tax credits ($5 billion) and City pension fund investments ($1 billion). The State and federal governments are expected to provide the remaining balance of $2.9 billion.

The Mayor's housing plan consists of more than 50 initiatives, some of which are still in the planning phase and will require State and federal approval. Among the key initiatives are a requirement that developers include a percentage of affordable apartments in exchange for zoning changes, and a petition to the State to strengthen and preserve protections for rent-regulated apartments (approximately 47 percent of City apartments are regulated under the rent-stabilization law).[43] Of the 200,000 affordable housing units in the plan, 20 percent are targeted to low-income households. The City is also seeking to reduce the rising homeless population through various efforts that include working with the State to develop two rental subsidy programs for homeless people in shelters.

[43] The State law governing rent stabilization will expire in June 2015.

Appendix A: Nonrecurring Resources

In recent years the City has relied heavily on nonrecurring resources to balance the budget. OSC estimates that the May Plan includes $2.9 billion in nonrecurring resources in FY 2014 and $3.5 billion in FY 2015, as shown in Figure 36 and discussed below.

Figure 36
Nonrecurring Resources
(in millions)

	FY 2014	FY 2015
Net Surplus Transfers	$ 1,202	$ 1,636
Debt Refinancings–Net	554	208
Health Stabilization Fund	- - -	1,000
Prior-Year Payables	400	- - -
Taxi Medallion Sales	295	595
Sale of City-Owned Buildings	256	- - -
Health Insurance Refunds	103	- - -
Verizon Settlement	50	- - -
Uncashed Paychecks	44	- - -
Educational Construction Fund	32	- - -
TFA Redemption	7	99
Total	**$ 2,943**	**$ 3,538**

Sources: NYC Office of Management and Budget; OSC analysis

- Surplus resources accumulated in prior years have been used to help balance the FY 2014 and FY 2015 budgets.
- Historically low interest rates in recent years have permitted the City to refinance outstanding debt, generating savings of $554 million in FY 2014 and $208 million in FY 2015.
- The City plans to transfer $1 billion from the Health Stabilization Fund to help fund the anticipated cost of labor settlements.
- Over the past ten years, the City has realized average annual savings of $514 million from an overestimation of prior years' expenses. The City anticipates $400 million in such savings in FY 2014, but the May Plan does not anticipate any future savings.

- The sale of additional taxi medallions is expected to generate $295 million in FY 2014, $595 million in FY 2015, $360 million in FY 2016 and $400 million in FY 2017, for a total of more than $1.6 billion.
- As part of a plan to consolidate City-owned real estate, the City expects to generate $256 million in FY 2014 from the sale of two buildings in Lower Manhattan.
- The City anticipates a refund of $103 million in health insurance premiums in FY 2014 as a result of the lower-than-expected use of medical services.
- Verizon has agreed to pay the City $50 million in FY 2014 to settle cost overruns resulting from delays to the upgrade of the City's 911 system.
- The City expects $44 million in FY 2014 from paychecks that have not been cashed in more than six years.
- The Educational Construction Fund will transfer $32 million in surplus funds to the Department of Education in FY 2014.
- The City used $196 million in resources generated in FY 2013 to redeem TFA debt due in future years, which lowers debt service by $7 million in FY 2014, $99 million in FY 2015 and $103 million in FY 2016.

Appendix B: Staffing Levels

Between June 2008 and June 2012, the City-funded workforce (full-time and full-time-equivalent employees) declined by 15,666 positions (5.8 percent) to 253,932, reflecting the impact of agency cost-cutting actions in response to the recession. Staffing levels rose, however, by 2,003 positions in FY 2013, and (as discussed below) the City plans to add about 4,300 employees during fiscal years 2014 through 2015 (see Figure 37). This would increase citywide staffing to 260,265 employees by the end of June 2015. Most of the growth is concentrated in the health and welfare agencies, and the Department of Education.

- The Department of Education plans to add 876 pedagogues in FY 2014, and an additional 377 pedagogues in FY 2015 (for a total of 1,253 positions), mostly to staff anticipated enrollment increases in special education programs. (The department plans to add 1,914 employees to staff an expansion of full-day prekindergarten and after-school programs, but these costs will be funded with State education aid.)
- The Administration for Children's Services (ACS) plans to add 508 positions, including additional child protective specialists and supervisors, to improve investigative practices and monitoring of high-risk cases. The increase is expected to reduce the average number of open child-protective cases assigned to ACS caseworkers in the family services unit, from 12 to 8.
- The Police Department plans to increase civilian staffing by 411 positions, including 178 police communication technicians to reduce overtime costs and 147 additional traffic enforcement agents to enforce the Mayor's Vision Zero initiative. The police force will remain at 34,483 officers during the financial plan period, which is 1,290 fewer officers than the peak in FY 2006 before force levels began to decline.
- The Department of Transportation plans to increase staffing by 288 positions primarily to implement aspects of the Mayor's Vision Zero initiative, such as the redesign and construction of roads and traffic intersections, and the installation and maintenance of additional speed cameras.
- The Department of Social Services plans to increase staffing slightly (by 165 positions) to staff a number of mayoral initiatives, but also expects to eliminate the need for more than 1,000 positions once a web-based application process for social services has been implemented.

Figure 37
City-Funded Staffing Levels
(Full-Time and Full-Time-Equivalents)

Additions/(Reductions)

		Actual		City Forecast		Variance		
		June 2013	Mar. 2014	June 2014	June 2015	June 2013 to Mar. 2014	June 2013 to June 2014	June 2014 to June 2015
Public Safety		**80,700**	**81,153**	**80,670**	**80,830**	**453**	**(30)**	**160**
Police	Uniformed	34,708	34,913	34,483	34,483	205	(225)	0
	Civilian	15,598	15,680	15,939	16,009	82	341	70
Fire	Uniformed	10,178	10,437	10,779	10,780	259	601	1
	Civilian	5,293	5,161	5,072	5,150	(132)	(221)	78
Correction	Uniformed	8,970	8,939	8,884	8,889	(31)	(86)	5
	Civilian	1,383	1,393	1,637	1,636	10	254	(1)
District Attorneys & Prosecutors		3,825	3,864	3,137	3,137	39	(688)	0
Probation		730	750	720	725	20	(10)	5
Board of Correction		15	16	19	21	1	4	2
Health & Welfare		**22,430**	**22,160**	**23,420**	**23,828**	**(270)**	**990**	**408**
Social Services		10,103	10,052	10,151	10,268	(51)	48	117
Children's Services		5,957	5,778	6,463	6,465	(179)	506	2
Health & Mental Hygiene		4,224	4,185	4,407	4,594	(39)	183	187
Homeless Services		1,760	1,770	1,983	1,949	10	223	(34)
Other		386	375	416	552	(11)	30	136
Environmental & Infrastructure		**17,614**	**15,634**	**17,793**	**17,975**	**(1,980)**	**179**	**182**
Sanitation	Uniformed	7,020	7,167	7,119	7,239	147	99	120
	Civilian	1,867	1,852	2,092	2,172	(15)	225	80
Transportation		1,938	1,981	2,087	2,226	43	149	139
Parks & Recreation		6,580	4,431	6,273	6,119	(2,149)	(307)	(154)
Other		209	203	222	219	(6)	13	(3)
General Government		**9,254**	**9,371**	**11,609**	**11,457**	**117**	**2,355**	**(152)**
Finance		1,802	1,861	1,977	1,996	59	175	19
Law		1,397	1,407	1,389	1,390	10	(8)	1
Citywide Administrative Services		1,338	1,291	1,506	1,583	(47)	168	77
Taxi & Limousine Commission		514	548	622	683	34	108	61
Investigations		197	210	300	290	13	103	(10)
Board of Elections		669	613	1,866	1,440	(56)	1,197	(426)
IT & Telecommunications		1,007	1,059	1,190	1,266	52	183	76
Other		2,330	2,382	2,759	2,809	52	429	50
Housing		**1,503**	**1,515**	**1,684**	**1,673**	**12**	**181**	**(11)**
Buildings		1,039	1,059	1,179	1,162	20	140	(17)
Housing Preservation		464	456	505	511	(8)	41	6
Department of Education		**113,717**	**115,111**	**114,335**	**114,316**	**1,394**	**618**	**(19)**
	Pedagogues	92,486	93,634	93,362	93,739	1,148	876	377
	Non-Pedagogues	21,231	21,477	20,973	20,577	246	(258)	(396)
City University of New York		**8,399**	**9,770**	**7,768**	**7,828**	**1,371**	**(631)**	**60**
	Pedagogues	5,387	6,597	5,028	5,118	1,210	(359)	90
	Non-Pedagogues	3,012	3,173	2,740	2,710	161	(272)	(30)
Elected Officials		**2,318**	**2,199**	**2,382**	**2,358**	**(119)**	**64**	**(24)**
Total		**255,935**	**256,913**	**259,661**	**260,265**	**978**	**3,726**	**604**

Sources: NYC Office of Management and Budget; OSC analysis