Review of the Financial Plan of the City of New York

Report 2-2019

OFFICE OF THE NEW YORK STATE COMPTROLLER
Thomas P. DiNapoli, State Comptroller
Kenneth B. Bleiwas, Deputy Comptroller

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Message from the Comptroller

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

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

Thomas P. DiNapoli
State Comptroller

Contents

I. Executive Summary

On April 26, 2018, the City of New York released a modification to its financial plan for FY 2018 and a new four-year financial plan ("the April Plan") covering fiscal years 2019 through 2022. The April Plan projects a surplus of nearly $3.7 billion for FY 2018 and a balanced budget for FY 2019 (see Figure 1).

The FY 2018 surplus, which will be used to balance the FY 2019 budget, results mostly from a reduction in unneeded reserves in the current fiscal year, higher-than-planned tax collections and savings from the citywide savings program, partly offset by unplanned agency spending.

As FY 2018 progressed, the City reduced its reserves by $1.9 billion. For example, it reduced the general reserve by nearly $1.2 billion, leaving a balance of $50 million, and it eliminated the capital stabilization reserve ($250 million).

Tax collections exceeded the City's initial forecast by nearly $1.5 billion in FY 2018, driven by higher-than-planned personal income tax collections and an overestimation of the amounts needed to cover property tax refunds, delinquencies and tax abatements. While business tax collections continued to fall short of expectations, the shortfall was offset in FY 2018 by higher audit and other revenue.

Personal income tax collections surged in FY 2018, boosted by an expected near doubling in capital gains, changes in federal law and the strength of the economy. Collections are projected to grow by 9.4 percent (the fastest in three years) and revenue is forecast to rise by nearly $1.1 billion, $817 million more than initially projected.

The citywide savings program is expected to generate $1 billion in each of fiscal years 2018 and 2019 (a cumulative total of nearly $4.7 billion through FY 2022). The program, however, relies heavily on reestimates, funding shifts and debt service savings; only a small share of the savings will come from efficiencies that improve agency operations.

In addition, City agencies identified unplanned spending needs of $1 billion and similar amounts for subsequent years. In FY 2018, more than half of the new needs were concentrated in the Department of Homeless Services and the uniformed agencies.

The City estimates that State actions will adversely impact its financial plan by $745 million in FY 2019 ($531 million in higher operating costs and one-time capital costs of $214 million). The largest impact comes from the State mandate that the City match the State contribution ($418 million) to the Metropolitan Transportation Authority's Subway Action Plan, which is designed to improve subway performance.

The April Plan projects budget gaps of $3.2 billion in FY 2020, $2.9 billion in FY 2021 and $2.3 billion in FY 2022. While the gaps are still relatively small as a share of City fund revenue (averaging 4 percent), they are larger than those projected by the City in February 2018 (by $1 billion in FY 2020, $1.4 billion in FY 2021 and $509 million in FY 2022). While higher agency spending is the main factor behind the growth in the out-year budget gaps, State actions are also a contributing factor.

City-funded spending (after adjusting for surplus transfers) is projected to increase by 6 percent in FY 2018 and by 7.6 percent in FY 2019. After excluding reserves, spending will increase by 5.1 percent in FY 2019. Spending is driven by current labor agreements, higher health insurance premiums, the impact of State actions and rising debt service.

The City's economy is strong and the out-year budget gaps appear manageable under current conditions. However, there are budgetary risks to manage over the next few years, as well as troubling developments at the national level.

The City's gap estimates assume uninterrupted economic growth and do not reflect the potential impact of future federal or State budget cuts. Growing federal deficits may increase pressure to cut entitlement and other federal programs during the financial plan period, which would adversely affect many New York City residents and the City budget.

While the City has set aside resources to fund annual wage increases of 1 percent after the expiration of current labor agreements, the actual cost will be determined through negotiation or arbitration.

Even though the Health and Hospitals Corporation will benefit from a two-year delay in federal budget cuts, it still faces serious long-term financial and structural challenges. In the absence of effective corrective measures, the City could be called upon to increase its financial support during the financial plan period.

The Governor recently issued an executive order calling for the appointment of an independent manager for the New York City Housing Authority (NYCHA). Under the order, the City could be required to provide additional funding for emergency repairs and to fund other costs. The potential impact on the City's operating and capital budgets are not yet known, but could be substantial.

Over the past four years, the City has increased its reserves to historic levels and has replenished the Retirees Health Benefit Trust, which now has a record balance of nearly $4.3 billion. While tax revenues are likely to exceed the City's forecasts (see Figure 2), at least in the near term, the City should increase its reserves given the budget risks on the horizon.

FIGURE 1

New York City Financial Plan

(in millions)

	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
Revenues					
Taxes					
General Property Tax	$ 26,194	$ 27,789	$ 29,295	$ 30,711	$ 31,702
Other Taxes	30,774	31,231	32,333	33,330	34,072
Tax Audit Revenue	1,299	1,056	721	721	721
Subtotal: Taxes	$ 58,267	$ 60,076	$ 62,349	$ 64,762	$ 66,495
Miscellaneous Revenues	7,128	6,789	6,830	6,735	6,714
Unrestricted Intergovernmental Aid	- - -	- - -	- - -	- - -	- - -
Less: Intra-City Revenue	(2,208)	(1,824)	(1,770)	(1,774)	(1,774)
Disallowances Against Categorical Grants	85	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 63,272	$ 65,026	$ 67,394	$ 69,708	$ 71,420
Other Categorical Grants	1,088	879	871	866	861
Inter-Fund Revenues	646	682	641	638	638
Federal Categorical Grants	8,799	7,507	7,127	7,106	7,089
State Categorical Grants	14,865	14,969	15,299	15,760	16,243
Total Revenues	**$ 88,670**	**$ 89,063**	**$ 91,332**	**$ 94,078**	**$ 96,251**
Expenditures					
Personal Service					
Salaries and Wages	$ 27,146	$ 28,717	$ 29,611	$ 30,359	$ 30,060
Pensions	9,632	9,852	9,903	10,162	10,367
Fringe Benefits	9,989	10,733	11,647	12,418	13,098
Subtotal: Personal Service	$ 46,767	$ 49,302	$ 51,161	$ 52,939	$ 53,525
Other Than Personal Service					
Medical Assistance	5,915	5,915	5,915	5,915	5,915
Public Assistance	1,583	1,605	1,617	1,617	1,617
All Other	30,860	29,505	28,864	29,085	29,364
Subtotal: Other Than Personal Service	$ 38,358	$ 37,025	$ 36,396	$ 36,617	$ 36,896
Debt Service	6,231	6,962	7,511	7,903	8,608
FY 2017 Budget Stabilization	(4,180)	- - -	- - -	- - -	- - -
FY 2018 Budget Stabilization	3,652	(3,652)			
Capital Stabilization Reserve	- - -	250	250	250	250
General Reserve	50	1,000	1,000	1,000	1,000
Less: Intra-City Expenses	(2,208)	(1,824)	(1,770)	(1,774)	(1,774)
Total Expenditures	**$ 88,670**	**$ 89,063**	**$ 94,548**	**$ 96,935**	**$ 98,505**
Gap to be Closed	**$ - - -**	**$ - - -**	**$ (3,216)**	**$ (2,857)**	**$ (2,254)**

Source: NYC Office of Management and Budget

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

	Better/(Worse)				
	FY 2018	**FY 2019**	**FY 2020**	**FY 2021**	**FY 2022**
Gaps Per NYC Financial Plan	**$ - - -**	**$ - - -**	**$ (3,216)**	**$ (2,857)**	**$ (2,254)**
Personal Income Tax	525	200	- - -	- - -	- - -
Business Tax	75	- - -	- - -	- - -	- - -
Real Estate Transaction Taxes	30	- - -	- - -	- - -	- - -
Homeless Services	- - -	(33)	(33)	(33)	(33)
Special Education Medicaid Reimbursement	(63)	(63)	(63)	(63)	(63)
Uniformed Agency Overtime	- - -	(125)	(125)	(125)	(125)
Debt Service	- - -	75	22	22	22
Miscellaneous Revenues	- - -	100	100	100	100
OSC Risk Assessment[1]	**567**	**154**	**(99)**	**(99)**	**(99)**
Potential Gaps Per OSC[2,3]	**$ 567**	**$ 154**	**$ (3,315)**	**$ (2,956)**	**$ (2,353)**

[1] Wage increases at the projected inflation rate after the expiration of current labor agreements could increase the City's costs beyond the resources it has set aside for this purpose by $60 million in FY 2018, $173 million in FY 2019, $420 million in FY 2020, $841 million in FY 2021 and $1.4 billion in FY 2022. The actual cost will be determined through negotiation or arbitration and could be more or less than the projected inflation rate.

[2] The April Plan includes a general reserve of $50 million in FY 2018 and $1 billion in each of fiscal years 2019 through 2022. In addition, the Capital Stabilization Reserve has a balance of $250 million in each of fiscal years 2019 through 2022.These resources could mitigate budget risks or, if not needed, could be used to help close the projected budget gaps.

[3] The Retiree Health Benefits Trust, which the City has used in the past as a rainy-day fund, has a balance of nearly $4.3 billion (net of any prepayments).

II. Changes Since the Beginning of the Fiscal Year

The City has made a number of changes to its revenue and expenditure forecasts since the budget was adopted in June 2017. As a result of these changes, the City now projects a surplus of nearly $3.7 billion in FY 2018, which will be transferred to FY 2019 to balance that year's budget. The surplus results mostly from a reduction in unneeded reserves, higher-than-planned tax collections and savings from the citywide savings program, partly offset by unplanned agency spending (see Figure 3).

As the year has progressed, the City has reduced its reserves in the current fiscal year by $1.9 billion. For example, the City reduced the general reserve by nearly $1.2 billion in FY 2018, leaving a balance of $50 million, and eliminated the capital stabilization reserve ($250 million). In addition, the City realized savings of $400 million because it traditionally overestimates accruals for prior years' expenses.

Tax collections are projected to exceed the City's initial forecast by nearly $1.5 billion, driven by higher-than-planned personal income tax collections ($817 million). The unexpected windfall resulted from solid job gains and wage growth, a large increase in Wall Street bonuses, strong capital gains realizations and changes in federal law.

In addition, the City overestimated the amount needed to cover property tax delinquencies, refunds and tax abatements ($469 million). Business tax collections continued to fall short of the City's expectations ($524 million), but the shortfall was more than offset by unplanned revenue from tax audits and other revenue.

The citywide savings program is expected to generate more than $1 billion in each of fiscal years 2018 and 2019, and nearly $4.7 billion through FY 2022. Most of the savings will come from reestimates, funding shifts and debt service. Only a small portion will come from actions that improve agency operations.

Since the beginning of the fiscal year, City agencies have identified new spending needs of $1 billion in FY 2018 and slightly larger amounts in subsequent years. In FY 2018, more than half of the needs are concentrated in the Department of Homeless Services ($380 million) and the uniformed agencies ($181 million). Other agencies with significant needs include the Department of Education, Small Business Services, and the Department of Information Technology and Telecommunications.

The April Plan projects budget gaps of $3.2 billion in FY 2020, $2.9 billion in FY 2021 and $2.3 billion in FY 2022. While the gaps are still relatively small as a share of City fund revenue (averaging 4 percent), they are larger than those projected by the City as recently as February 2018 (by $1 billion in FY 2020, $1.4 billion in FY 2021 and $509 million in FY 2022).

While higher agency spending is the main factor behind the growth in the projected budget gaps, State actions were a contributing factor. The enacted State budget for State fiscal year (SFY) 2018-19 includes actions that create new unfunded mandates or shift costs from the State to the City. In total, the City estimates that State actions will increase its operating costs by $531 million in FY 2019 and by about half of that amount in subsequent years (see Section III, "Federal and State Issues," for a detailed discussion).

The City also eliminated from its financial plan any expectation of proceeds from the sale of taxi medallions. The City had previously anticipated $929 million during fiscal years 2019 through 2022 from the sale, but the market for new medallions has deteriorated with the introduction of ride-share services such as Uber and Lyft.

FIGURE 3
Financial Plan Reconciliation—City Funds
April 2018 Plan vs. June 2017 Plan
(in millions)

	Better/(Worse)			
	FY 2018	FY 2019	FY 2020	FY 2021
Projected Gaps Per June 2017 Plan	**$ - - -**	**$ (3,473)**	**$ (2,807)**	**$ (2,330)**
Revenue Reestimate				
Personal Income Tax	817	305	345	224
General Property Tax	469	288	432	728
Business Taxes	(524)	(360)	(397)	(507)
Tax Audits	449	335	- - -	- - -
All Other Taxes	256	(51)	(169)	(173)
Subtotal: Taxes	**1,467**	**517**	**211**	**272**
Proceeds of Taxi Medallion Sales	- - -	(107)	(257)	(367)
All Other	223	131	179	210
Total	**1,690**	**541**	**133**	**115**
Citywide Savings Program				
Agency Actions	709	898	538	569
Debt Service	325	195	279	356
Total	**1,034**	**1,093**	**817**	**925**
Reserves				
General Reserve	1,150	- - -	- - -	- - -
Prior-Years' Expenses	400	- - -	- - -	- - -
Capital Stabilization Reserve	250	- - -	- - -	- - -
Reserve for Disallowances of Federal and State Aid	100	- - -	- - -	- - -
Collective Bargaining	40	75	75	75
Pension Reserve	- - -	(100)	(100)	(400)
Total	**1,940**	**(25)**	**(25)**	**(325)**
New Agency Needs				
Homeless Services	(380)	(313)	(311)	(310)
Uniformed Agencies	(181)	(105)	(101)	(100)
Department of Education	(138)	(207)	(241)	(254)
Small Business Services	(50)	(81)	(33)	(24)
Department of Information Technology & Telecom.	(35)	(55)	(89)	(129)
Environmental Protection	(28)	(69)	(68)	(65)
Department of Transportation	(15)	(77)	(47)	(40)
All Other	(178)	(274)	(166)	(147)
Total	**(1,005)**	**(1,181)**	**(1,056)**	**(1,069)**
Pension Contributions (excludes Audit Reserve)	(60)	119	139	243
All Other	52	(195)	(122)	(120)
State Actions	**1**	**(531)**	**(295)**	**(296)**
Net Change During FY 2018	**3,652**	**(179)**	**(409)**	**(527)**
Surplus/(Gap)	**$ 3,652**	**$ (3,652)**	**$ (3,216)**	**$ (2,857)**
Surplus Transfer	(3,652)	3,652	- - -	- - -
Projected Gaps Per April 2018 Plan	**$ - - -**	**$ - - -**	**$ (3,216)**	**$ (2,857)**

Sources: NYC Office of Management and Budget; OSC analysis

III. Federal and State Issues

As discussed below, changes in federal and State policies can have important implications for New York City's budget and its residents.

1. Changes in Federal Tax Policy

In December 2017, Congress approved revisions in the federal tax code that reduce corporate and personal income taxes by a net of nearly $1.5 trillion over 10 years (according to the Congressional Budget Office), cap the deductibility of state and local taxes at $10,000 and reduce the size of mortgages for which interest can be deducted.

Despite lower tax rates, some taxpayers in New York City will pay higher federal taxes beginning in 2018 because of the cap on the deductibility of state and local taxes. To mitigate this impact, the State will permit itself, New York City, and other school districts and counties to establish charitable gift trusts and accounts.[4] Taxpayers who make donations will receive a tax credit against their State personal income or local property taxes, and could claim a charitable deduction against their federal tax liability.

The City has not yet determined whether it will create charitable accounts, or if it did, what limitations it would impose on the amount or percentage of such property tax credits. While the Internal Revenue Service (IRS) has not yet issued a formal opinion on such charitable accounts, it has cast doubt on whether such contributions will be treated as charitable deductions for federal income tax purposes. An adverse interpretation by the IRS will likely be challenged in the courts.

Congress also eliminated the ability of municipal issuers to refund debt on a tax-exempt basis more than 90 days in advance of the call date. In the past, the City has realized savings of about $100 million annually from advance refundings. In addition, lower federal tax rates may reduce the attractiveness of housing tax credits, which the City relies on for its housing program.

2. Federal Budget

In February 2018, Congress approved a two-year budget agreement that increases the cap on military spending by $165 billion and raises the cap on nondefense spending by $131 billion. It also includes $89 billion for disaster relief in California, Florida, Puerto Rico and Texas, and suspends the debt limit for one year. Congress also agreed to extend funding for the Children's Health Insurance Program for 10 years.

As a result of the changes in federal tax policy and increased federal spending, the federal budget deficit could reach nearly $1 trillion in federal fiscal year (FFY) 2019, and even higher amounts in subsequent years. The combination of economic stimulus and growing budget deficits could increase interest rates, which will make it more expensive to service the federal debt and more difficult to stimulate the economy in the event of a recession. Rising federal deficits could also increase the risk of cuts to entitlement and other federal programs.

After signing the budget agreement, the President called on Congress to pare back planned spending under the bipartisan budget agreement. In addition, the President's budget proposal for FFY 2019 focused heavily on cuts to social safety net programs and nondefense discretionary spending. While no action has been taken on either proposal, pressure to cut federal spending may mount after the midterm elections in November 2018.

Most recently, the President has stated that he may veto legislation to fund government operations beyond September 30, 2018, if Congress excludes funding to extend the U.S.-Mexico border wall. A veto could result in a federal government shutdown, reducing or disrupting government services.

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4 The law also decouples the State tax code from the federal tax code, where necessary, to avoid more than $1 billion in State tax increases that would have resulted from the recent revisions in the federal tax code.

3. State Actions

On March 30, 2018, the State enacted a budget for the fiscal year beginning on April 1, 2018 (i.e., SFY 2018-19). The State increased education aid to the City by more than 3 percent, similar to the statewide increase. Although education aid will rise by $334 million in FY 2019, the increase is $140 million less than anticipated by the City in its financial plan.

The State took other actions that impose new mandates on the City or shift financial responsibility from the State to the City. In addition, the April Plan reflects the impact of State actions that were approved in prior years, but not previously reflected in the City's financial plan. In total, the City estimates that State actions had an adverse impact on its financial plan of $745 million in FY 2019 (see Figure 4). The City estimates that its operating costs will increase by $531 million in FY 2019 (and by about $300 million annually thereafter), and that it will incur one-time capital costs of $214 million in FY 2019.

In FY 2019, the largest impact comes from a requirement that the City match the State's $418 million contribution to the Metropolitan Transportation Authority's Subway Action Plan. It is expected that the City will contribute $254 million toward the operating cost and $164 million to the capital cost of the program in FY 2019. The State budget also requires the City to match the State's $50 million capital contribution to the Hudson River Park.

Although the State reauthorized the Close to Home program (which allows juvenile offenders to remain in their communities) for five years, it shifted financial responsibility for the program from the State to the City. The City estimates that this action will increase its costs by $31 million annually beginning in FY 2019.

On April 2, 2018, the Governor issued an executive order calling for the appointment of an independent manager for the New York City Housing Authority (NYCHA) in response to concerns that it has failed to adequately inspect and maintain its properties. Under the order, the City will be required to pay for the cost of the independent manager and State health inspections, and could be required to provide additional capital funding for emergency repairs.

The potential impacts on the City's operating and capital budgets are not yet known, but could be substantial since NYCHA has unfunded capital needs that exceed $20 billion. The federal government also could impose financial penalties on NYCHA for failing to comply with federal lead-paint laws and require additional City funding.

Figure 4

Financial Plan Impact of State Actions in FY 2019

(in millions) Better/(Worse)

	Operating Cost	Capital Cost	Total Impact
Subway Action Plan	$ (254)	$ (164)	$ (418)
Education Aid	(140)	- - -	(140)
Raise the Age	(108)	- - -	(108)
Close to Home	(31)	- - -	(31)
MTA Bus Company	3	- - -	3
Hudson River Park	- - -	(50)	(50)
NYCHA	TBD	TBD	TBD
Total	**$ (531)**	**$ (214)**	**$ (745)**

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

Last year, the State raised the age of criminal responsibility for most crimes from 16 years to 17 years, effective on October 1, 2018, and to 18 years, effective on October 1, 2019. Under the law, the City will be required to contribute to the cost of implementation unless the State waives the local share (which would be based on proof of financial hardship).

As recently as April 3, 2018, the City had estimated that this law would increase its costs by $200 million annually, but the April Plan (which was released 23 days later) assumes the City's costs will increase by $108 million in FY 2019, growing to $131 million in FY 2020. Although the State budget includes a dedicated appropriation of $100 million for State and local costs associated with this initiative, as well as other possible sources of funding, it remains to be seen whether the City will receive any of those funds.

The State also enacted legislation last year that requires school districts to fund increased tuition costs at charter schools beginning in FY 2019. The City had estimated that this requirement would increase its costs by $101 million in FY 2019, growing to $633 million in FY 2022 if not offset by changes in State education aid to the City.

The City no longer believes that this requirement will increase its costs in FY 2019 because it did not reflect an increase in State funding for this purpose that was approved last year, and also because it overestimated the growth in charter school enrollment in FY 2018. The City also has lowered its estimate of the potential impact in future years ($119 million in FY 2020, growing to $478 million in FY 2022). These potential liabilities have not been reflected in the April Plan.

In addition, the City had not previously reflected in FY 2019 the impact ($150 million) of legislation enacted in 2016 that allows the State to reap the benefits of refinancing outstanding debt of the Sales Tax Asset Receivable Corporation.[5] However, the City realized the benefit of the refinancing in prior years. Thus, this State action had no net impact on the City's finances over the long term.

[5] For a detailed discussion of the Sales Tax Asset Receivable Corporation, see the Office of the State Comptroller's report 1-2017, *Review of the Financial Plan of the City of New York*, May 2016.

IV. Revenue Trends

The April Plan assumes revenues, including federal and State categorical aid, will total $89.1 billion in FY 2019. Of this amount, nearly three-quarters ($65 billion) will come from locally generated revenues (i.e., City funds), primarily tax collections. City fund revenues are projected to increase by 2.8 percent in FY 2019 after increasing by 4.9 percent in FY 2018.

After growth slowed for two consecutive years (see Figure 5), tax collections are forecast by the City to increase by 6.6 percent in FY 2018. The increase is driven by a surge in personal income tax collections (9.4 percent).

The City now expects personal income tax collections to increase by nearly $1.1 billion in FY 2018, $817 million more than anticipated at the beginning of the fiscal year. The unanticipated revenue results from changes in federal law, a large increase in Wall Street bonuses and a near doubling in capital gains.

The April Plan reasonably assumes that the factors that contributed to the surge in personal income tax collections in FY 2018 will not recur. In fact, the FY 2018 surge may come partly at the expense of future revenue.

The City expects tax collections to increase by 3.1 percent in FY 2019 and similar rates in subsequent years. The forecast assumes continued solid job and wage growth.

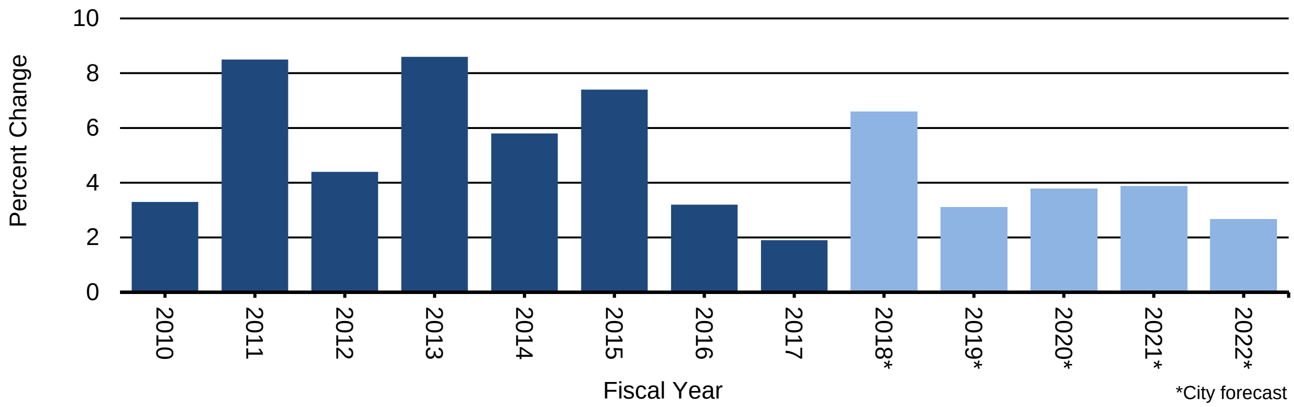
New York City's economy is strong and continues to post solid job gains. It added 715,000 jobs between 2009 and 2017, the largest and longest job expansion in the post–World War II period. After adding 81,000 jobs in 2017, employment reached 4.4 million, 615,000 more than the prerecession peak.

With record job gains, the unemployment rate has declined from a recessionary peak of 10.1 percent in January 2010 to 4.2 percent in March 2018, the lowest level in 42 years. The City is on pace for continued job gains in 2018, although growth is expected to slow for the fourth consecutive year as the labor market tightens.

Based on current trends, the Office of the State Comptroller (OSC) estimates that tax collections could exceed the City's forecast by $630 million in FY 2018 driven by the personal income tax. Although most of the benefit in FY 2018 is expected to be nonrecurring, personal income tax collections could still be $200 million higher in FY 2019.

FIGURE 5

Annual Change in Tax Revenues



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

FIGURE 6

Trends in City Fund Revenues

(in millions)

	FY 2018	FY 2019	Annual Growth	FY 2020	FY 2021	FY 2022	Average Three-Year Growth Rate
General Property Tax	$ 26,194	$ 27,789	6.1%	$ 29,295	$ 30,711	$ 31,702	4.5%
Personal Income Tax	12,658	12,378	-2.2%	12,969	13,390	13,722	3.5%
Sales Tax	7,399	7,762	4.9%	8,167	8,491	8,779	4.2%
Business Taxes	5,503	5,864	6.6%	5,978	6,108	6,094	1.3%
Real Estate Transaction Taxes	2,392	2,397	0.2%	2,359	2,437	2,511	1.6%
Other Taxes	2,822	2,830	0.3%	2,860	2,904	2,966	1.6%
Tax Audits	1,299	1,056	-18.7%	721	721	721	-11.9%
Subtotal: Taxes	**58,267**	**60,076**	**3.1%**	**62,349**	**64,762**	**66,495**	**3.4%**
Miscellaneous Revenues	4,920	4,965	0.9%	5,060	4,961	4,940	-0.2%
Grant Disallowances	85	(15)	NA	(15)	(15)	(15)	0.0%
Total	**63,272**	**65,026**	2.8%	**67,394**	**69,708**	**71,420**	**3.2%**

Sources: NYC Office of Management and Budget; OSC analysis

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

1. General Property Tax

Property tax revenues are projected to increase by 6.1 percent in FY 2019, reaching $27.8 billion, reflecting continued growth in property values. The April Plan assumes property values will increase by 7 percent based on the preliminary tax roll, which was released in January 2018. The final tax roll was released on May 25, 2018, which could result in a change in the City’s forecasts.

In FY 2018, property tax revenues exceeded the City’s forecast by $469 million because the City overestimated the amount needed for delinquencies, refunds and tax abatements. In FY 2019, the City has set aside $1.8 billion for this purpose, $292 million more than needed in FY 2018. It is likely that these additional resources will not be needed in FY 2019 and will be reallocated as the year progresses.

The April Plan assumes that collections will slow during the remainder of the financial plan period. Part of the slowdown reflects the expectation that rising interest rates will hold down the growth in property values. In addition, the new federal tax code limits the deductibility of property taxes and reduces the size of new mortgages for which interest can be deducted. These factors could also dampen the growth in home values.

On April 24, 2017, Tax Equity Now New York (a coalition of advocates, property owners and tenants) filed suit against the State and City challenging the current real property tax system in New York City, alleging that it violates the State and federal constitutions and the Fair Housing Act. In addition, the lawsuit alleges that the valuation methodology mandated by the State Real Property Law results in a disparity and inequality in the amount of taxes paid by Black and Hispanic property owners and renters. Oral arguments on a motion to dismiss the case are scheduled for June 13, 2018.

2. Personal Income Tax

Personal income tax collections surged in FY 2018, growing by an estimated 9.4 percent (the fastest rate of growth in three years).[6] As a result, collections increased by nearly $1.1 billion in FY 2018, $817 million more than projected by the City at the beginning of the fiscal year. While the strength of the City's economy contributed to the growth, other factors were responsible for most of the increase.

Estimated payments (i.e., quarterly payments made on nonwage income) are projected to increase by 28 percent in FY 2018, exceeding the City's initial forecast by $667 million. According to the City, growth was driven by nonwage income (e.g., pass-through business income, interest and dividends) and a near-doubling of capital gains, driven in part by the strength in the financial markets.

Withholding (i.e., the amount of tax taken from employees' paychecks) is expected to increase by 7.5 percent, the fastest growth since FY 2007, reflecting a large increase in securities industry bonuses, and solid job and wage growth. Some of the growth in bonuses may have resulted from an acceleration of deferred compensation for top executives since it was still a deductible expense in 2017. OSC estimated that securities industry bonuses increased by 17 percent in 2017, the largest increase in four years.

A 2008 federal law requires the repatriation of deferred compensation held overseas. The law offered taxpayers 10 years to repatriate income (and to pay taxes on such income) with a deadline of December 31, 2017. Most of this income was held by hedge fund managers. The repatriation of overseas income contributed to the growth of both withholding and estimated tax payments.

State distribution payments were $196 million higher than anticipated by the City in FY 2018.[7] OSC believes such payments could exceed the City's revised forecast by $100 million in FY 2018 and at least $50 million in FY 2019.

Withholding and estimated payments for December 2017 were $1.3 billion higher than during the same period one year earlier. Many observers thought taxpayers prepaid their taxes when such payments were still fully deductible.[8] However, it is now clear that the surge resulted not just from prepayments, but also from higher-than-expected tax liabilities. Collections also exceeded the City's forecast for April 2018, which could result in $350 million in unanticipated revenue in FY 2018.

The April Plan also assumed that refunds would be 10 percent higher in FY 2018 than last year, but refunds are up by less than 4 percent through April 30, 2018. As a result, the City is likely to realize an additional $75 million.

The April Plan assumes that personal income tax collections will return to trend in FY 2019. Although the City continues to forecast solid job and wage growth, securities industry bonuses are expected to decline in 2018 (by 1.1 percent) while capital gains are projected to fall sharply (by one-third). However, collections could exceed the City's forecast for FY 2019 by at least $150 million based on stronger job growth. The City assumes job growth will slow to 60,000 in 2018, but it is on pace to add 72,000 jobs.

Much of the unanticipated revenue in FY 2018 results from changes in taxpayer behavior, which is difficult to forecast. Some of the revenue could have come at the expense of future years. For example, some taxpayers may have applied their overpayments to next year's tax liabilities rather than receive a refund.

6 All personal income tax growth rates are adjusted for changes in the administration of the New York State School Tax Relief Program (STAR).

7 The State administers the City's personal income tax. The State remits to the City an estimate of its share each month. The State subsequently reviews the results and makes adjustments as necessary.

8 Under the revised federal tax law, the deductibility of state and local taxes is limited to $10,000 beginning in 2018.

3. Sales Tax

Sales tax collections are forecast to increase by 5.4 percent in FY 2018, the strongest growth in four years. The gain reflects higher wages, high consumer confidence, strong holiday sales and a record number of tourists. In addition, the City received a large payment from the State as part of a settlement with a single taxpayer.

The April Plan assumes that collections will increase by 4.9 percent in FY 2019 to reach $7.8 billion.[9] The City expects consumer spending to remain strong, supported by job growth and rising wages. NYC & Company (the City's tourism agency) forecasts that the number of visitors to New York City will rise to 65.1 million in 2018, exceeding the record 62.8 million reached in 2017.

4. Business Taxes

New York City business taxes consist of two taxes: the business corporation tax and the unincorporated business tax. The business corporation tax was created in April 2015 through State legislation that combined the City's banking and general corporation taxes. The change was intended to be revenue-neutral, but since implementation, collections have declined and fallen short of expectations.

Pretax profits for the broker-dealer operations of New York Stock Exchange member firms rose by 42 percent in 2017. Profits totaled $24.5 billion, the highest level since 2010, driven by higher revenues. Despite job gains in recent years, the securities industry in New York City is still 6 percent smaller than before the financial crisis.

The federal Tax Cuts and Jobs Act provided an incentive to corporations to repatriate overseas income. However, such income is not taxable under State and City law.

Business corporation tax collections have fallen short of the City's expectation at the beginning of the fiscal year (by $592 million), despite strong securities industry profits. The April Plan assumes that collections will decline by 4.3 percent to $3.3 billion in FY 2018 (the third consecutive year of lower collections), but collections were very strong in April 2018. While collections are still likely to decline in FY 2018, the shortfall will likely be smaller (by $75 million).

In FY 2019, the City is again expecting a rebound in business corporation tax collections. The April Plan assumes that collections will rise by 8.9 percent to reach $3.6 billion, as a result of strong Wall Street profitability and lower levels of overpayments. Even with such an increase, collections would still be $389 million lower than forecast in June 2017.

Collections from the unincorporated business tax have been affected by some of the same factors impacting the personal income tax. Receipts surged in December 2017 as many taxpayers accelerated payments from 2018 in response to the new federal tax law, and collections have remained strong through April 2018. As a result, collections are expected to increase by 10 percent in FY 2018. The April Plan assumes unincorporated business tax collections will return to their trend in FY 2019, rising by 3 percent to reach $2.3 billion.

[9] The April Plan now reflects a $150 million reduction in collections as the State recoups savings that accrued to the City from refinancing bonds of the Sales Tax Asset Receivable Corporation.

5. Real Estate Transaction Taxes

Although property values continue to rise, real estate transaction activity has weakened over the past two years. More recently, there has been some sign of improvement, particularly for commercial transactions. In FY 2018, the City benefited from Google's purchase of Chelsea Market for $2.4 billion. Nonetheless, the April Plan assumes that collections from the mortgage recording and real property taxes will decline by 5.6 percent in FY 2018, but collections could be $30 million higher based on current trends.

The City expects commercial transaction activity will continue to improve in FY 2019, aided by favorable investment provisions in the new federal tax law. Rising interest rates, however, are expected to dampen mortgage activity. Overall, collections from the real estate transaction taxes are expected to edge up by 0.2 percent in FY 2019, to $2.4 billion.

6. Miscellaneous Revenues

Miscellaneous revenues exceeded the City's forecast at the beginning of the fiscal year by $223 million in FY 2018, and the City has raised its forecast for subsequent years as well. Based on historical trends, the City is likely to realize additional revenues from this source. OSC anticipates that the City will realize an additional $100 million annually from this source beginning in FY 2019.

V. Expenditure Trends

The Mayor's executive budget for FY 2019 totals nearly $89.1 billion, including programs funded with federal and State categorical grants. The portion funded with locally generated revenue (i.e., City funds) totals $65 billion.

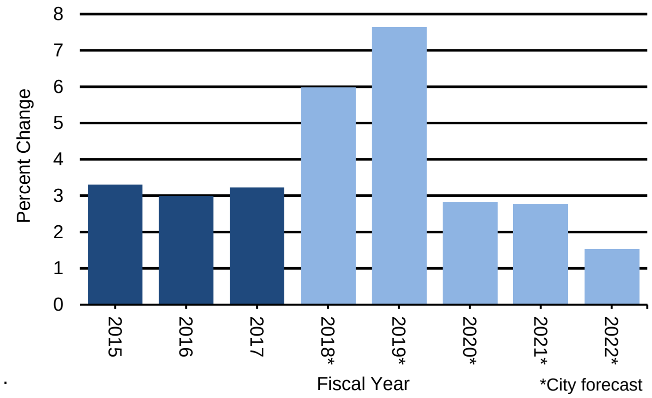
City-funded spending (after adjusting for surplus transfers that can mask expenditure trends) is projected to increase by 6 percent in FY 2018, twice the average of the three prior years (see Figure 7). Spending is projected to grow by 7.6 percent in FY 2019. Even after excluding reserves and taking into account potential savings from prior years' expenses, spending would increase by 5.1 percent (still more than three times faster than the projected inflation rate). Spending is driven by current labor agreements, higher health insurance premiums, the impact of State actions and rising debt service.

The pace of spending is projected to slow over the balance of the financial plan period, from 2.8 percent in FY 2020 to 1.5 percent in FY 2022. While health insurance and debt service costs are expected to grow rapidly, the April Plan assumes salary and wage costs will grow slowly and decline after 2021, when the last of the lump-sum payments under the current collective bargaining agreement will be made.

The April Plan assumes annual wage increases of 1 percent after the expiration of current contracts, but the actual cost will be determined by negotiation or arbitration. While overtime costs in the uniformed agencies are likely to exceed the City's forecasts, debt service will likely be lower based on the City's conservative interest rate assumptions and optimistic capital commitment schedule.

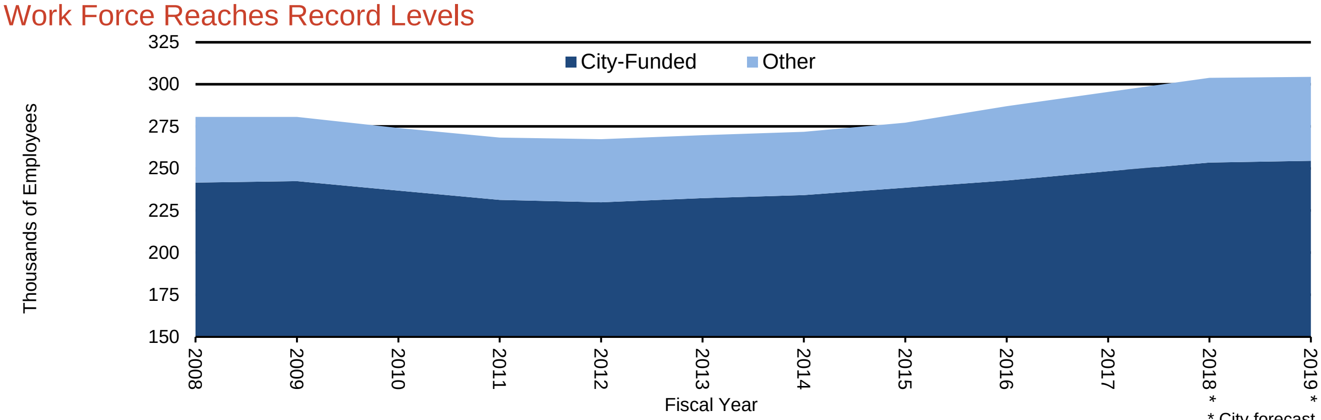
Since FY 2012, the City's full-time work force (including positions funded by federal and State categorical grants) has increased by more than 28,000 employees (10.5 percent) to reach 295,455 in June 2017, the highest level since the 1975 fiscal crisis (including 248,349 City-funded employees; see Figure 8). As of March 31, 2018, the City has added 2,532 employees, and plans to add another 6,461 by June 30, 2019.

FIGURE 7
Growth in City-Funded Expenditures



Sources: NYC Office of Management and Budget; OSC analysis

FIGURE 8
Work Force Reaches Record Levels



Sources: NYC Office of Management and Budget; OSC analysis

FIGURE 9
Trends in City-Funded Spending
(in millions)

	FY 2018	FY 2019	Annual Growth	FY 2020	FY 2021	FY 2022	Average Three-Year Growth Rate
Salaries and Wages	$ 18,388	$ 20,071	9.2%	$ 20,973	$ 21,466	$ 20,729	1.1%
Pension Contributions	9,488	9,707	2.3%	9,759	10,017	10,223	1.7%
Debt Service	5,968	6,705	12.3%	7,259	7,659	8,367	7.7%
Medicaid	5,813	5,813	0.0%	5,813	5,813	5,813	0.0%
Health Insurance	4,717	5,305	12.5%	5,838	6,445	6,996	9.7%
Other Fringe Benefits	2,807	2,969	5.8%	3,259	3,410	3,538	6.0%
Energy	784	785	0.1%	800	824	843	2.4%
Judgments and Claims	572	557	-2.6%	572	587	602	2.6%
Public Assistance	713	713	0.0%	719	719	719	0.3%
Other	14,900	14,803	-0.7%	14,368	14,375	14,594	-0.5%
Subtotal	**66,150**	**67,428**	**5.1%**	**69,360**	**71,315**	**72,424**	**2.4%**
Prior Years' Expenses	(400)	- - -	NA	- - -	- - -	- - -	NA
General Reserve	50	1,000	NA	1,000	1,000	1,000	NA
Capital Stabilization Reserve	- - -	250	NA	250	250	250	NA
Total	**$ 63,800**	**$ 68,678**	**7.6%**	**$ 70,610**	**$ 72,565**	**$ 73,674**	**2.4%**

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

The April Plan is based on the trends shown in Figure 9 and discussed below.

1. Collective Bargaining

As of March 31, 2018, the labor agreements covering nearly half of the municipal work force had expired. The April Plan includes resources to fund annual wage increases of 1 percent after the expiration of these agreements, but the actual cost will be determined through negotiation or arbitration, and could be higher (or lower) than assumed in the April Plan. Wage increases at the projected inflation rate, for example, would increase costs by $60 million in FY 2018, $173 million in FY 2019, $420 million in FY 2020, $841 million in FY 2021 and $1.4 billion in FY 2022.

In March 2018, the Patrolmen's Benevolent Association (which represents the City's police officers) filed a petition with the New York State Public Employment Relations Board requesting the appointment of a three-member panel for arbitration. According to State law, arbitration awards for disputes between the City and police officers are binding on both parties.

2. Health Insurance

The City and the Municipal Labor Committee (MLC) reached an agreement in May 2014 to generate health insurance savings for the City's budget to help fund wage increases for municipal employees. Under the agreement, the City and the unions agreed to generate a cumulative total of $3.4 billion during fiscal years 2015 through 2018, and $1.3 billion in recurring savings beginning in FY 2019.

In March 2018, the Commissioner of Labor Relations reported that the City will meet or exceed the FY 2018 target and will likely exceed the $3.4 billion four-year target. Despite savings of $1.3 billion, the City-funded cost of health insurance will reach $7 billion by FY 2022 (see Figure 10), $2.7 billion (63 percent) more than before the agreement took effect in FY 2014.

More than three-quarters of the $3.4 billion in cumulative savings has come from lower-than-planned increases in health insurance premiums and other administrative actions. Cost-containment initiatives are expected to account for one-fifth of the savings ($693 million), mostly from higher co-payments.

The City is seeking additional health insurance savings to help fund wage increases in the next round of collective bargaining. Since the April Plan assumes that the growth in health insurance premiums for active employees will slow from 7 percent in FY 2019 to 5.5 percent in FY 2022, the potential for savings may be reduced.

The Health Stabilization Fund (HSF) was established in 1986 pursuant to collective bargaining. Under the agreement, the City pays $35 million annually into the HSF, and contributes additional amounts for each fiscal year in which the rate approved for the Health Insurance Plan for Greater New York exceeds the rates for Group Health Incorporated and Blue Cross Blue Shield.

Under prior agreements between the City and the MLC, significant resources have been freed up by drawing down the balance in the HSF. In May 2014, the City and the MLC agreed to transfer $1 billion from the HSF to help fund wage increases, reducing the balance to less than $800 million. Since then, the HSF has grown to $1.6 billion.

3. Pension Contributions

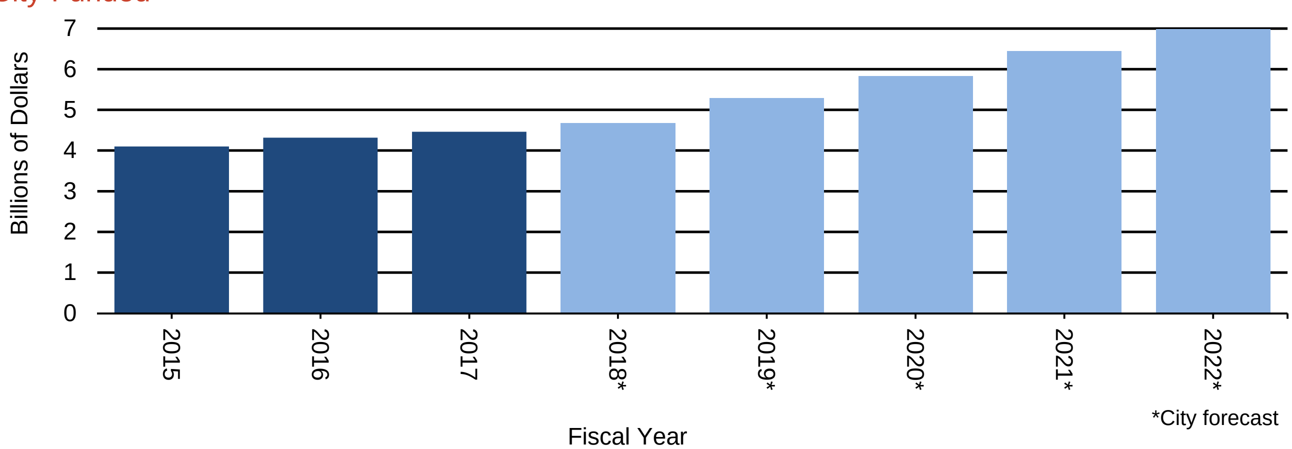
As shown in Figure 11, the April Plan assumes that pension contributions will rise slowly during the financial plan period, from nearly $9.3 billion in FY 2017 to $10.2 billion in FY 2022 (averaging 14.6 percent of City fund revenues over the same period).

The pension funds have earned, on average, 7.9 percent on their investments during fiscal years 2012 through 2017, compared to the expected annual gain of 7 percent. Investment earnings totaled about 11 percent through

FIGURE 10

Health Insurance Costs Continue to Grow

City-Funded



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

January 31, 2018, but the market has fallen since then and has become more volatile. The pension funds have earned about 9 percent as of May 30, 2018.

In the four years since the City adopted new more transparent financial reporting standards for pension liabilities in FY 2014, the financial condition of the City's five actuarial pension systems has improved. In the aggregate, the pension systems had enough assets to fund (on a market-value basis) 71 percent of their accrued pension liabilities as of the end of FY 2017 (see Figure 12). During this period, the unfunded net liability for all five systems declined by $3.6 billion to $56.3 billion.

After rising rapidly between fiscal years 2003 and 2012, the growth in City-funded pension contributions slowed during the next two years. The slower rate of growth reflected the impact of changes in assumptions and methodologies used to calculate City pension contributions, better-than-expected investment earnings, and savings from lower-cost pension plans for employees hired after March 31, 2012.

The April Plan includes reserves ($100 million in each of fiscal years 2019 and 2020, rising to $400 million beginning in FY 2021) to fund potential changes in the actuarial assumptions and methodologies used to calculate employer pension contributions.

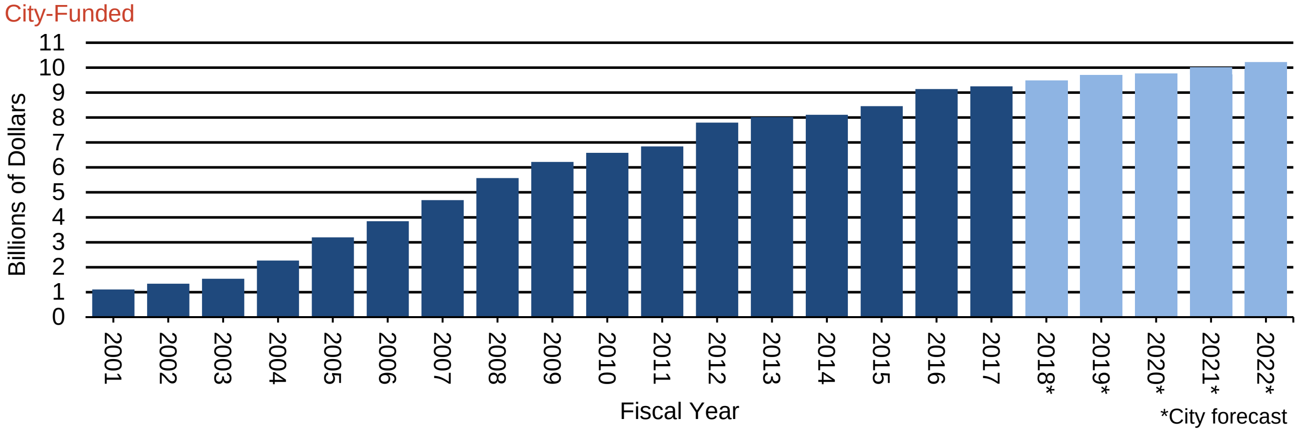
Potential changes may follow recommendations issued by an independent actuarial consultant, who recently completed a charter-mandated biennial audit of the pension systems and is expected to issue final recommendations by July 2019. Based on the preliminary findings, the consultant may recommend changes to reflect recent trends such as higher overtime and lower mortality rates for active employees, and to reduce long-term inflation and investment earnings assumptions.

FIGURE 12
Funded Status of the NYC Retirement Systems
(As of June 30, 2017)

Pension System	Funded Status
Board of Education Retirement System	81%
New York City Employees' Retirement System	75%
Police Pension Fund	75%
Teachers' Retirement System	68%
Fire Pension Fund	61%
All Systems	**71%**

Sources: NYC Retirement Systems; NYC Comptroller; OSC analysis

FIGURE 11
Pension Contributions
City-Funded



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

4. Debt Service

City-funded debt service increased at an average annual rate of only 2.7 percent during fiscal years 2014 through 2018 because of historically low interest rates, which reduced the cost of new issuances and created opportunities to refinance outstanding debt. The City has realized savings of $325 million in FY 2018 and an average of $578 million in the three prior years.

The April Plan assumes that debt service will increase more than three times as fast during the financial plan period to reach $8.4 billion by FY 2022 (an increase of $2.4 billion; see Figure 13). As discussed below, debt service could grow more slowly for a number of reasons, but the opportunities for savings may be reduced compared to recent years.

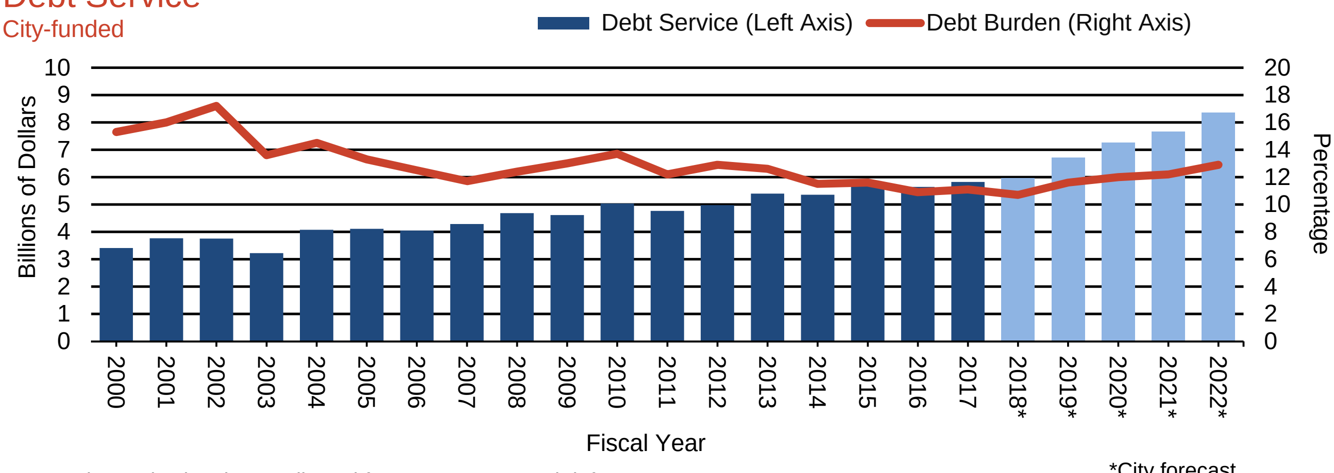
Municipalities are no longer permitted under federal law to refinance outstanding bonds on a tax-exempt basis more than 90 days in advance of their call date. In recent years the City has realized annual savings of about $100 million from this practice. While the City's interest rate assumptions remain conservative, the Federal Reserve is increasing short-term interest rates, and the combination of low unemployment and rising inflation could push up long-term rates.

Despite these developments, the City could still realize debt service savings of $50 million in FY 2019 because interest rates are likely to remain below the City's assumptions. In addition, the City has historically fallen short of its capital commitment targets, creating the potential for additional savings. The City could also realize savings when the Dormitory Authority refinances bonds issued on behalf of the Health and Hospitals Corporation (estimated at $91 million over four years).

Debt service as a share of tax revenue (i.e., the debt burden) has fallen from 12.6 percent in FY 2013 to 10.7 percent in FY 2018. The April Plan assumes that the debt burden will rise to 12.9 percent by FY 2022, but this estimate is also based on conservative assumptions for revenue, interest rates and capital commitments.

Although debt service would account for a larger share of tax revenue, the share would remain below 15 percent under current conditions, a level that is considered high. To prevent debt service from rising too quickly as a share of tax revenues in the event of a rapid rise in interest rates or a sharp decline in tax revenue, the City established a capital stabilization reserve in FY 2016. The reserve is valued at $250 million annually during fiscal years 2019 through 2022.

FIGURE 13
Debt Service
City-funded



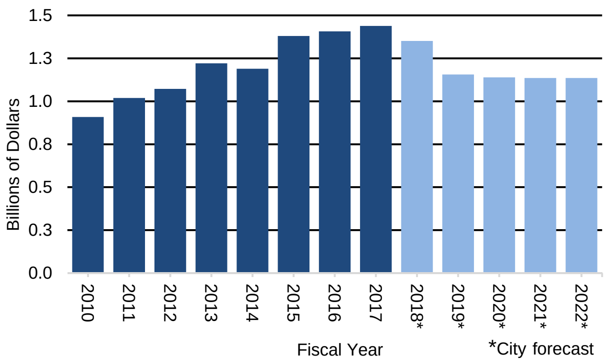
Note: Debt service has been adjusted for prepayments and defeasances.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSC analysis

5. Uniformed Overtime

Overtime costs in the four uniformed agencies reached $1.4 billion in FY 2017, setting a new record. While overtime exceeded the City's initial estimate by $351 million, these unplanned costs were mostly offset by hiring delays and by savings in other personal services costs.

FIGURE 14

Uniformed Agency Overtime



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

The April Plan assumes overtime will decline from last year's level to $1.3 billion in FY 2018 (see Figure 14). While overtime will likely exceed the City's forecast, the unplanned cost could be offset by savings in other personal services costs or by the receipt of unplanned federal and State categorical grants.

The April Plan assumes overtime will decline by $195 million in FY 2019 and essentially remain at that level. While offsetting savings may materialize during the course of the fiscal year, it is premature to identify such savings. Thus, overtime could exceed planned levels by at least $125 million annually beginning in FY 2019.

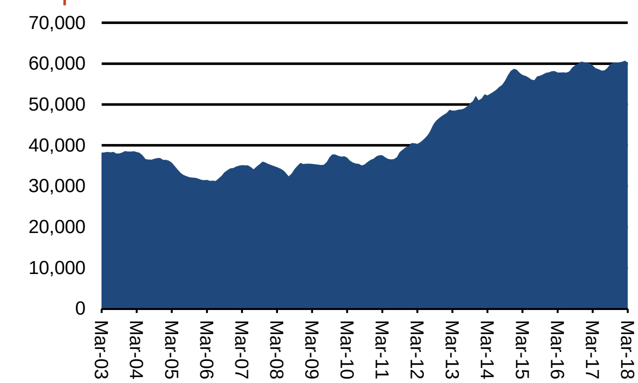
6. Homeless Services

The number of homeless people residing in shelters operated by the Department of Homeless Services (DHS) remains at historic levels despite City efforts to prevent homelessness and to create permanent housing. In March 2018, the caseload totaled 60,289 (see Figure 15), a slight decline since the peak reached in February 2018 (60,713).

After experiencing a decline in FY 2017, the average number of individuals in families in the City shelter system has increased slightly through March 2018. In addition, families are staying in shelters an average of 25 days longer compared to the same time period last year.

FIGURE 15

People in Homeless Shelters



Source: NYC Department of Homeless Services

The number of single adults in shelters has grown by an average of more than 1,000 people annually in fiscal years 2014 through 2017. The number of single adults in shelters continues to increase, and has already grown by 1,315 with three months remaining in the fiscal year. The April Plan, however, assumes that the cost for housing single adults will decline in FY 2019, which seems unlikely given current trends.

The Mayor reports that the City is only slightly behind schedule in building new shelters to accommodate the growing shelter population, and has been phasing out the use of cluster-site apartments to shelter people. The result is that the City has had to rely on placing people in more costly hotels as a bridge until the new shelters are available. The City reports that it spends $32 million each month on hotels to shelter the homeless. The Commissioner of Social Services has indicated that phasing out the use of hotels may take up to seven years.

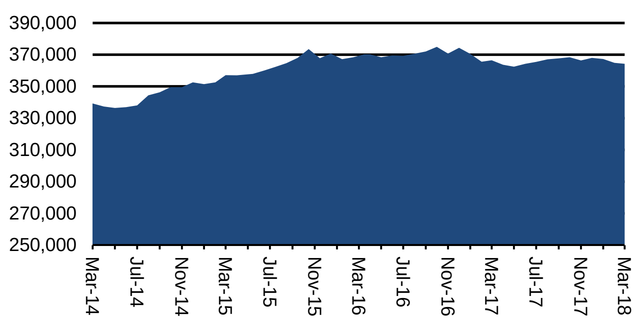
Since the beginning of the fiscal year, the City has increased funding for shelters by $336 million in FY 2018 and $309 million annually through FY 2022. Three-quarters of the additional funding is allocated for single adults in the shelter system. The cost of providing homeless services is projected to total $2.1 billion in FY 2019, double what it cost five years earlier. The City-funded cost is projected to total $1.2 billion.

7. Public Assistance

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

FIGURE 16

NYC Public Assistance Caseload



Source: NYC Human Resources Administration

The public assistance caseload has averaged 367,200 during most of FY 2018, consistent with the City's forecast, but it averaged 364,500 during February and March 2018 (see Figure 16). It remains to be seen whether the caseload will continue at this lower level or return to its higher level. The City-funded cost of public assistance is expected to total $714 million in FY 2019 and increase slightly to $719 million beginning in FY 2020.

8. Medical Assistance

Medicaid provides health insurance to low-income children and adults, and is the largest payer of long-term care. It also provides subsidies to health care providers (such as the Health and Hospitals Corporation) that serve large numbers of low-income patients and uninsured patients.

The Medicaid caseload grew steadily after the recession and accelerated after January 1, 2014, when Medicaid eligibility expanded under the federal Affordable Care Act (ACA). Enrollment reached almost 3.7 million people in December 2015, an increase of 16 percent (more than 510,000 people) since December 2013.

In January 2016, the Medicaid caseload fell (by 134,000) as the State transferred certain immigrants who were ineligible for federal Medicaid to the State-funded Essential Plan. Since then, the Medicaid caseload has gradually declined to less than 3.5 million as of September 30, 2017.

The April Plan assumes that the City-funded share of Medicaid will total $5.8 billion in FY 2018 (9 percent of City fund revenues) and will remain at that level because the State has assumed financial responsibility for the growth in the local share. These estimates assume there will be no changes in federal and State policies.

VI. Semi-Autonomous Entities

1. Department of Education

New York City has the largest public school system in the nation, operating more than 1,800 schools and serving more than 1.1 million students. The April Plan allocates $32.2 billion to the Department of Education in FY 2019 to cover the cost of educating students (see Figure 17). Since FY 2000, the City share has grown 10 percentage points to 57 percent, while the State share has fallen from 43 percent to an average of 37 percent since FY 2010.

In FY 2019, the City intends to contribute $18.3 billion (including the cost of debt service and employee benefits), while the State contribution is expected to total $11.9 billion. The federal government is expected to contribute $2 billion (6 percent). Since FY 2014, the department has increased staffing by more than 11,000 (including more than 9,700 pedagogues), and it plans to add more than 1,000 pedagogues by June 30, 2019.

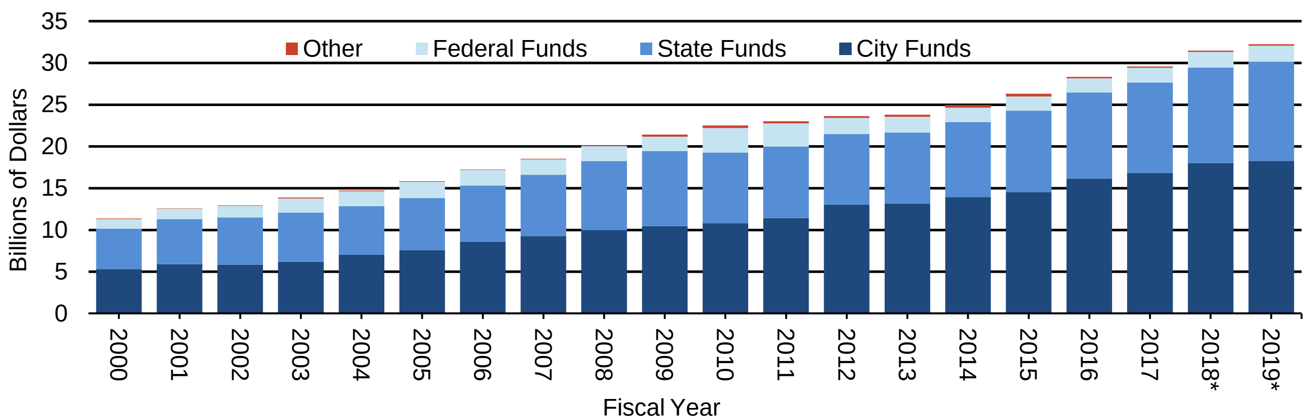
The education budget includes funding for new policy initiatives and for the expansion and support of existing programs. For example, the FY 2019 budget allocates additional resources for Fair Student Funding, an initiative that was begun in the 2007-2008 school year. The initiative is designed to improve equity across the school system by taking into account certain needs, such as special education and English-language learners.

The budget also includes resources to expand 3-K for All. Other initiatives include additional funding for universal literacy, air conditioning in classrooms and students living in homeless shelters. According to the State Education Department, there were 38,000 homeless schoolchildren in the City's shelters during the 2016-17 school year.

Each year, the Department of Education submits Medicaid reimbursement claims for eligible services provided to special education students. However, the department has historically had difficulty substantiating such claims to the federal government. Although the department is making several improvements to improve the process, it continues to fall short of target.

The April Plan anticipates $97 million annually in Medicaid reimbursement beginning in FY 2018. Last year, the department received $34 million, and as of May 23, 2018, the department had submitted claims for only $22 million in FY 2018. Until the department demonstrates the ability to increase claims above last year's amount, the receipt of $63 million annually remains at risk.

FIGURE 17
Education Funding by Source



Sources: NYC Office of Management and Budget; OSC analysis

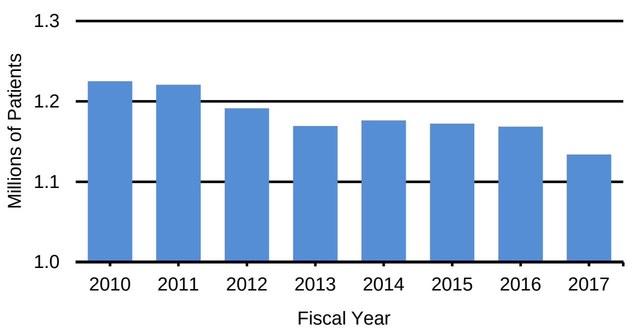
*City forecast

2. Health and Hospitals Corporation

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

As shown in Figure 18, the number of patients served by the Corporation (both inpatient and outpatient) has declined by 91,000 patients (7 percent) between fiscal years 2010 and 2017. While the health care industry is moving toward outpatient settings, the Corporation experienced a decline of nearly 6 percent in outpatient visits in FY 2017 and a decline of 3 percent during the first seven months of FY 2018.[10]

FIGURE 18
Patients Served at the Health and Hospitals Corporation



Sources: NYC Mayor's Management Report

In recent years, the Corporation has increasingly relied on the City for financial assistance to fulfill its obligations. In FY 2018, the City is expected to provide $1.8 billion in financial support, representing nearly 30 percent of the Corporation's total revenues.

Cuts to federal supplemental Medicaid payments have been delayed for two years as a result of a bipartisan congressional budget agreement. Consequently, the Corporation will receive unanticipated resources of $224 million in FY 2018, $402 million in FY 2019 and $78 million in FY 2020. However, the cuts could be larger than previously planned beginning in FY 2021.

Enrollment in MetroPlus (the Corporation's own health insurance provider) has begun to increase, reaching almost 520,000 members in March 2018. Nevertheless, more than half of MetroPlus members receive medical services from providers other than those in the Corporation. In March 2018, MetroPlus served nearly 11,500 New York City government and other public employees, more than twice as many as two years earlier.

As part of its efforts to improve its financial condition, the Corporation has reduced staffing by a net of 4,955 full-time-equivalents since November 2015. The reduction has resulted in shortages at some facilities.

In January 2018, a new president took control of the Corporation. On May 24, 2018, the City released a revised cash-based financial plan for the Corporation.[11] The financial plan projects a year-end cash balance of $670 million in FY 2018, but growing deficits in the absence of corrective measures.[12] While the City has released a corrective action plan, there can be no assurance that the initiatives will generate the anticipated revenues or savings.

The City and the Corporation need to act quickly to take advantage of the temporary financial relief provided by the delay in federal Medicaid cuts. If they fail to take corrective measures, the City could be called upon to further increase its financial support.

[10] Primary care visits, a subset of outpatient care, declined by 8 percent in FY 2017.

[11] The City has not released an accrual financial plan for the Corporation since October 2016.

[12] The projected year-end cash balance for FY 2018 assumes the Corporation will fulfill its obligations to the City for FY 2018 and reimburse the City for $588 million in expenses incurred by the City on the Corporation's behalf as far back as FY 2015.

3. Metropolitan Transportation Authority

In July 2017, the MTA proposed an $836 million Subway Action Plan (SAP) to address the deterioration in the City's subways. The MTA suggested that the State and City split the cost, but an agreement could not be reached.

In November 2017, OSC concluded in a report that if new funding sources were not identified, the MTA might have to raise fares and tolls faster than planned to improve the subways. The report also raised concerns that the MTA still had not explained how the recurring cost of the SAP would be funded so the system would not fall back into disrepair.

On March 30, 2018, the State enacted a budget for SFY 2018-19. The State budget requires the State and the City to split the cost of the SAP in 2018. The State also imposed congestion surcharges (effective January 1, 2019) on all taxi trips, for-hire transportation trips and pooled for-hire trips that originate in or enter Manhattan south of 96th Street.

According to the MTA, the State estimates that the congestion surcharges will provide the MTA with $435 million annually. Under the law, $362 million will be used for the exclusive purpose of funding the SAP in 2019 (and about $300 million in subsequent years), while $50 million annually will be used to support outer-borough projects that improve connectivity to Manhattan as well as to reduce tolls on MTA bridges and tunnels. The remainder could be used by the MTA to support the operating or capital budgets.

The MTA's latest financial plan, released in February 2018, projects positive year-end cash balances through calendar year 2019, but budget gaps that grow from $403 million in 2020 to $602 million in 2021. The gap estimates already assume fare and toll increases of 4 percent in 2019 and in 2021.

The MTA's financial plan sets aside resources to fund annual wage increases of 2 percent after the expiration of current contracts.[13] The terms of the next round of collective bargaining will be determined through negotiation or arbitration, and the actual cost could be higher (or lower) than assumed by the MTA.

In May 2016, after a 17-month delay, the State approved a new five-year capital program for the MTA for the 2015-2019 period. The State initially agreed to commit $8.3 billion to the MTA's capital program, but it has since increased its commitment to $8.6 billion.

So far, the State has identified $1.3 billion in resources.[14] It intends to provide the remaining $7.3 billion after the MTA has effectively exhausted all other MTA sources of capital funding, but no later than SFY 2025-26 or the completion of the capital program. The City will contribute $2.7 billion and has already allocated $821 million, including $164 million for the SAP.[15]

The MTA partly depends on the federal government to help fund its capital improvements. The President's proposed budget, if enacted, would eliminate funding for new projects under the New Starts program. The MTA anticipates funding from this program to cover about $2 billion of the $6 billion estimated cost of the next phase of the Second Avenue Subway.

In March 2018, the Long Island Rail Road (LIRR) released a plan to improve on-time performance. According to a recent report from the State Comptroller, last year the LIRR had its worst on-time performance in 18 years, and 2018 began with mixed results. The report found that Amtrak

[13] The current contract with the Transport Workers Union, the MTA's largest union, will expire in May 2019.

[14] The $1.3 billion includes $989 million from bond proceeds and $315 million from financial settlement funds.

[15] The City has indicated that it will provide proportional matches concurrently with additional State funds.

was responsible for more than half of the increase in the delays experienced by the LIRR, but the LIRR itself was responsible for more than twice as many delays as Amtrak.[16]

In April 2018, the MTA announced that it would develop a comprehensive plan to restructure New York City's public bus system as part of an effort to provide immediate and long-term improvements. Bus ridership has been in decline for years as riders abandon buses for alternative transportation options.

On May 23, 2018, the president of New York City Transit (NYCT) presented to the MTA board a 10-year comprehensive plan to improve subway and bus operations, and to modernize the system. For example, the plan calls for accelerating the installation of computerized signals in the subway system. The MTA has not publicly stated the cost of the 10-year plan, but it is expected to be substantial. The costs of the first five years of the plan are expected to be included in the MTA's 2020-2024 capital program, which will be released next year.

4. New York City Housing Authority

The New York City Housing Authority (NYCHA) is an important component of the City's supply of affordable housing. NYCHA manages approximately 176,000 apartments that house nearly 400,000 residents, which amounts to 8 percent of the City's rental apartments. As of March 2017, more than 257,500 families were waiting for apartments to become available.

Federal funds make up 60 percent ($2 billion) of NYCHA's operating budget and 89 percent of the portion not funded with rent proceeds. NYCHA's capital budget also relies heavily on federal funding. As a result of shortfalls in federal funding, coupled with other fiscal and management challenges, the City's public housing properties have fallen into disrepair.

In 2011, NYCHA estimated that its total capital needs over the next five years totaled $17 billion. Although NYCHA was scheduled to release an updated assessment in 2016, it still has not done so. The Mayor has indicated, however, that NYCHA's capital needs now exceed $20 billion.

On April 2, 2018, the Governor issued an executive order that declared a State disaster emergency at all NYCHA developments in the City. The order directs the Mayor, the City Council, and the president of the NYCHA Citywide Council of Presidents (CCOP) tenant group to appoint an independent emergency manager within 60 days.

The manager, in cooperation with the Mayor, the City Council and the CCOP, will assess conditions and develop a prioritized list of repairs and remediation projects at NYCHA properties. Under the order, the City will be required to pay for the cost of the independent manager and State health inspections.

The independent manager, in collaboration with State and local agencies and authorities as may be appropriate, will develop a comprehensive emergency remediation plan for the use of $550 million in emergency State resources and any unspent State and City funds, as well as future City funding.[17] The City could be required to provide additional capital funding beyond the amounts already planned.

The City has committed to provide $1.6 billion in operating support to NYCHA between fiscal years 2014 and 2022. This includes $20 million in fiscal years 2019 and 2020 (proposed in the April Plan) to help NYCHA close out 50,000 open work orders. The City has also increased capital support to NYCHA.[18]

[16] Office of the State Comptroller, Report 12-2018, *Long Island Rail Road: On-Time Performance by the Numbers*, March 2018.

[17] The manager will select, in consultation with the City Comptroller, an independent contractor to perform the repairs.

[18] The City has made $1.5 billion in capital commitments to NYCHA during the financial plan period and expects to commit another $682 million from fiscal years 2023 through 2027.

The federal government has conducted a two-year investigation of NYCHA, which included investigating whether NYCHA was in compliance with federal lead-paint laws. A settlement is expected shortly that could impose financial penalties on the City and could require additional City funding.

The U.S. Department of Housing and Urban Development recently proposed legislation that would require public housing authorities to raise the rent for non-elderly and non-disabled households to 35 percent of gross income. Currently, most tenants are charged 30 percent of gross incomes, adjusted for the number of children and disabled people in the household. NYCHA estimates that the rise will increase the monthly rent in non-elderly and non-disabled households by up to $240 (an average increase of $175 per month). The average NYCHA household earns $24,000 a year.

Contact

Office of the New York State Comptroller
110 State Street
Albany, New York 12236

(518) 474-4015

www.osc.state.ny.us

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

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