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The Coming Storm City can't afford to put off looming budget crisis

By Doug Turetsky

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When Republican delegates from around the country arrive here later this month, they will find a city seemingly on the rebound: much to the delight of their host, Mayor Michael Bloomberg. But consider it calm before the storm.

Less than two years ago, amid mounting job losses and aftershocks from September 11, New York faced a budget gap of more than \$6 billion and warnings of a fiscal implosion. But this past June the city passed a budget for the new fiscal year with relative ease—it even includes a tax rebate for property owners.

Despite the recent upturn in the local economy and forecast of improving revenue growth, the city's fiscal condition remains precarious—and the mayor and the City Council will have to deal with it sooner rather than later. The reason is basic: City spending is rising at a faster pace than the revenues. From fiscal year 2004 (the year that ended on June 30) through fiscal year 2006, we estimate that city tax revenues will grow by \$1.7 billion. But over that same period, spending is expected to increase by nearly \$4 billion. This imbalance results in a budget gap of more than \$3 billion in the fiscal year that begins in just 11 months. And the city, by statute, must balance its budget.

Closing that gap won't be easy because spending is not growing equally throughout the budget. In fact, spending on basic city programs and services will grow much more slowly than total city spending. For example, the more than \$6 billion that the city currently spends on police, fire, correction, and sanitation together will grow by just \$13 million from 2004 through 2006, according to our projections. That figure is based on the assumption that the police and fire unions agree to the same pattern of wage hikes as other municipal unions have accepted. But, of course, that could change.

The conundrum facing the city is that nondiscretionary or uncontrollable costs are driving the overall increase. They include Medicaid, debt service, the settlement of lawsuits against the city; and pensions, health care, and other fringe benefits for city employees. These expenditures could grow by \$3 billion, from \$14.2 billion in 2004 to \$17.2 billion in 2006.

The mushrooming Medicaid bill offers a good example of the problem we face. The city's share of Medicaid spending will grow from \$4.2 billion in 2004 to an estimated \$4.9 billion in 2006. Mandates from Albany and Washington determine who is covered and for what services. The city could stop actively seeking to enroll more New Yorkers on Medicaid as a means of controlling future costs, but that could be self-defeating. The city is home to roughly 2 million people with no health insurance, and their health needs could be even more expensive to meet in the public hospitals. Last year the city's public

hospitals provided \$400 million in unreimbursed health care, a big reason the hospitals' own budgets are on shaky ground. The city is providing them with a \$200 million subsidy this year and \$150 million next year.

One way the visiting Republican delegates could help the city after they go back home is by urging the Bush administration to change the way the federal government determines how much of the Medicaid bill it will cover. Under the current formula, New York State gets the lowest possible federal share. Last year, to provide some assistance to cash-strapped states, the federal government provided a one-time increase in the share it covers. This change saved the city more than \$230 million.

But it will take a lot more than that to bridge the city's looming budget chasm. Sometime soon after the conventioners pack up and leave town, the City will have to make some tough choices. It is very unlikely that either the state or the federal government, both also facing very steep deficits, will bail the city out. The city borrowed substantially to fill its budget gap in the wake of 9/11. That type of practice led the city to the brink of bankruptcy in the 1970s and the imposition of Albany's fiscal controls. So, borrowing to close the gap is essentially off the table.

So that leaves spending cuts and tax hikes which couldn't come at a worst time, considering that Mayor Bloomberg will be up for re-election next fall. The longer he and the City Council take to address the coming fiscal storm, the deeper and steeper these actions may need to be.