

**Testimony of the New York City Independent Budget Office
To the New York City Council Finance Committee
On the Fiscal Year 2002 Preliminary Budget and Financial Plan**

March 5, 2001

Good afternoon Chairman Berman and members of the committee. My name is Ronnie Lowenstein, director of the city's Independent Budget Office. The City Charter gives IBO a critical role in the budget process, including responsibility for providing a comprehensive revenue projection and helping all New Yorkers better understand and discuss the Mayor's budget proposals. As part of our effort to increase public information about the budget, IBO will be releasing some key sections of its Charter-mandated analysis of the Mayor's preliminary budget in conjunction with the Council's hearings.

Today I will present IBO's reestimate of the Mayor's revenue and expenditure projections for the 2002 Preliminary Budget and Financial Plan through 2005. While IBO anticipates the city will end the current fiscal year with a large surplus, much as it has over the last five years, we do not believe this will continue. I am not suggesting a recession looms, but a slowdown in the rate of the city's growth does lie ahead. This means that future gaps will be much harder to close since the city will no longer have significant surpluses available to roll into the years ahead.

IBO projects that even with a \$2.3 billion surplus in the current year, under the Mayor's 2002 budget proposal the city faces a \$1.03 billion gap. The gaps grow exponentially in future years, from \$3.3 billion in 2003 to \$4.5 billion in 2004 and 2005.

Accompanying copies of my testimony are tables that detail our revenue and expenditure estimates. I will summarize some key points.

IBO estimates that between the current year and 2005 revenues will grow at a modest 1.2 percent on an average annual basis. Much of the increase is driven by the property tax, which IBO expects to grow at a 5.4% average annual rate. This growth is due largely to the fact that the rise in property values that occurred during the latter half of the 1990s is only now being reflected in property tax bills.

Economically sensitive taxes such as income and sales taxes are projected to grow at less than half the average pace of the property tax. IBO also projects that several significant revenue sources anticipated for 2002 will not materialize. These include \$345 million in back rent for the airports, \$250 million from the sale of OTB and \$350 million in state and federal actions.

Looking at expenditures under the Mayor's plan, IBO anticipates that the city's average annual rate of spending from 2001 through 2005 will grow 3.7 percent—or more than three times the rate of revenue growth. This rate of spending growth does not include restoration of proposed cuts to libraries, youth and senior programs, cultural activities, legal services and other Council initiatives.

One of the key factors driving our projected expenditure increases is the cost of labor contract settlements. Assuming that labor negotiations result in a wage increase matching the rate of inflation, IBO projects a substantial shortfall in the budget plan's labor reserve. This shortfall amounts to \$270 million in 2003, \$541 million in 2004, and \$860 million in 2005. I would add that for each percentage point above inflation, contract settlements will cost an additional \$140 million per year. This amount compounds, so a settlement 1 percent above inflation will cost another \$700 million in 2005; likewise, a settlement 2 percent above inflation would cost nearly \$1.5 billion in 2005.

IBO also expects spending to increase significantly on education. We project Board of Education spending to grow by \$1.9 billion between this fiscal year and 2005—an annual average rate of 3.9 percent. It is worth noting, however, that this growth rate is less than the nearly 10 percent annual increase from 1997-2000.

Another large spending increase will result from a rise in debt service. Spending on debt service will increase by more than \$1.7 billion between this year and 2005—an average annual change of 11.5%. Rising debt service will consume nearly 19 cents of every tax dollar by 2004.

I would be pleased to answer any questions you have today about IBO's revenue and expenditure projections. And we look forward to continuing to work with you in the weeks and months ahead.

IBO Expenditure Estimates Under the Mayor's Proposals

Dollars in millions

	2001	2002	2003	2004	2005	Average Change
Health / Social Services:						
Social Services	\$5,693	\$5,611	\$5,640	\$5,849	\$6,041	1.5%
Admin. for Children Services	2,335	2,297	2,332	2,345	2,349	0.1%
Health	1,980	1,973	1,991	2,009	2,028	0.6%
Homeless	484	487	502	504	505	1.1%
All Other	523	428	424	424	425	-5.1%
Subtotal	11,015	10,796	10,889	11,131	11,348	0.7%
Education:						
Board of Education	11,606	12,175	12,656	13,103	13,507	3.9%
CUNY	395	389	393	397	401	0.4%
Subtotal	12,001	12,564	13,049	13,500	13,908	3.8%
Uniformed Services:						
Police	3,404	3,422	3,563	3,706	3,806	2.8%
Fire	1,107	1,140	1,171	1,207	1,239	2.9%
Correction	861	911	963	985	1,006	4.0%
Sanitation	941	1,011	1,053	1,072	1,096	3.9%
Subtotal	6,313	6,484	6,750	6,970	7,147	3.2%
Debt Service	3,142	2,238	4,093	4,672	4,853	11.5%
All Other	8,188	9,004	9,274	9,705	9,841	4.7%
Total Expenditures as Estimated by IBO	\$40,659	\$41,086	\$44,055	\$45,978	\$47,097	3.7%

SOURCE: IBO.

NOTES: Expenditures are not adjusted for prepayments. If adjusted for prepayments, spending would grow at a 3.2 percent average annual rate from 2001 through 2005, and debt service would grow at an average annual rate of 5.6 percent. Excludes intra-city expenditures.

Details of Pricing Differences Between IBO and the Administration

Items that Affect the Gap

Dollars in millions

	2001	2002	2003	2004	2005
Gaps as Estimated by the Mayor	\$-	\$-	\$(2,423)	\$(2,466)	\$(2,307)
IBO Pricing Differences:					
Revenues:					
Taxes:					
Property	(14)	(4)	24	52	89
Personal Income	185	186	96	17	(56)
General Sales	(27)	31	47	28	30
Business Income	43	(1)	(36)	(26)	(70)
Real-Estate Related	27	51	6	(46)	(89)
	214	263	137	25	(96)
Tax Reduction Program	-	(11)	(16)	46	(8)
STaR Reimbursement	-	(4)	34	(20)	44
Miscellaneous Revenues:					
Airport Rent	-	(345)	(200)	(135)	(65)
Asset Sales	-	(250)	250	-	-
Total Revenues	214	(347)	205	(84)	(125)
Expenditures:					
Public Assistance	(65)	(83)	(69)	(70)	(70)
Medicaid	(114)	(111)	(117)	(121)	(207)
Education (excluding labor adjustment)	(136)	(147)	(285)	(414)	(474)
Education Reserve (shift to BOE)	43	5	21	21	21
Interim Waste Export Contracts	15	11	11	8	4
State & Federal Actions not Expected	-	(350)	(350)	(350)	(350)
Labor Costs Exceeding Reserve	-	-	(270)	(541)	(860)
Campaign Finance Board	-	(50)	-	(30)	-
Sports Facilities	90	104	95	(289)	-
Overtime	(23)	(83)	(146)	(146)	(146)
Total Expenditures	(190)	(704)	(1,110)	(1,932)	(2,082)
Additional Debt Service Prepayment	(24)	24	-	-	-
Total Pricing Differences	-	(1,027)	(905)	(2,016)	(2,207)
IBO Surplus/(Gap) Estimate	\$-	\$(1,027)	\$(3,328)	\$(4,482)	\$(4,514)

SOURCE: IBO.

NOTES: Negative pricing differences (in parentheses) widen the gap estimated by the Mayor.
Positive pricing differences narrow the gaps.

IBO Revenue Estimates Under the Mayor's Proposals

Dollars in millions

	2001	2002	2003	2004	2005	Average Change
Tax Revenues:						
Property Tax	\$8,078	\$8,586	\$9,044	\$9,503	\$9,962	5.4%
Personal Income tax (includes TFA)	5,810	5,536	5,765	6,044	6,333	2.2%
General Sales tax	3,572	3,614	3,764	3,895	3,960	2.6%
General Corporation Tax	1,707	1,519	1,555	1,632	1,730	0.3%
Unincorporated Business Tax	828	767	798	843	872	1.3%
Banking Corporation Tax	428	378	393	396	414	-0.8%
Real-Estate Related Taxes	1,121	1,167	1,225	1,264	1,310	4.0%
Other Taxes (with Audits)	1,388	1,484	1,443	1,448	1,447	1.0%
Total Taxes Before Reductions	22,932	23,051	23,987	25,025	26,028	3.2%
Tax Reduction Program	-	(400)	(721)	(955)	(1,241)	n/a
Total Taxes After Reductions	22,932	22,651	23,266	24,070	24,787	2.0%
STaR Reimbursement	504	666	765	735	821	13.0%
Miscellaneous Revenues	3,360	2,953	2,852	2,571	2,608	-6.1%
State / Federal Categorical Aid	12,555	12,478	12,648	12,931	13,189	1.2%
All Other Revenues	1,308	1,311	1,196	1,189	1,178	-2.6%
Total Revenues as Estimated by IBO	\$40,659	\$40,059	\$40,727	\$41,496	\$42,583	1.2%

SOURCE: IBO.

NOTES: Miscellaneous revenues are net of intra-city revenues. All other revenues include unrestricted government aid, anticipated aid, other categorical grants, inter-fund revenue, and disallowances. A portion of the commercial rent tax reduction proposed in the preliminary budget has already been enacted and is therefore reflected in our baseline forecast.