NEW YORK CITY
INDEPENDENT BUDGET OFFICE

Analysis of the Mayor's Preliminary Budget for 2000

IBO's Reestimate of the Mayor's Preliminary Budget for 2000 and Financial Plan through 2003

March 1999

Preface

March 23, 1999

As required by section 246 of the New York City Charter, the Independent Budget Office (IBO) completed this analysis of the Mayor's preliminary budget for 2000. It provides a follow-up to *New York City's Fiscal Outlook*, issued by IBO in January 1999. That report included a forecast of city finances under the assumption that existing spending policies and tax laws are allowed to run their course. IBO's *Fiscal Outlook* projections serve as the starting point for our consideration of the Mayor's budget.

In this report, we have identified a number of policy initiatives contained in the budget that are of public interest or are expected to have a fiscal impact that is different than estimated by the Administration. Chapter 1 provides an overview of IBO's repricing of the Mayor's budget for 2000 and financial plan through 2003. Chapter 2 provides our reestimate of the preliminary budget revenue forecast along with a discussion and repricing of the Mayor's tax reduction initiatives. Chapter 3 contains an analysis of preliminary budget spending proposals, highlighting major changes from existing law and those areas where significant pricing differences with the Mayor's projections occur.

This report was completed under the supervision of Ronnie Lowenstein who leads our Economic Analysis Division and Frank Posillico who heads our Budget Projections Unit. Christine Lidbury served as project manager for the report, while Mark Schreiner coordinated final production. A list of IBO contributors and their respective areas of responsibility follows at the end of the report.

Douglas A. Criscitello
Director

Notes

- The Mayor's preliminary budget for 2000 is generally referred to as the "preliminary budget" or simply "budget," while the financial plan through 2003 is referred to as the "financial plan."
- Unless otherwise noted, all references to years in both text and figures denote New York City fiscal years (July 1st to June 30th).
- Numbers in the text and figures in this report may not add to totals because of rounding.

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Chapter 1

Overview

In a recent report by the Independent Budget Office (IBO), *New York City's Fiscal Outlook*, we found that the city's budget outlook is brightening although dark clouds remain. The good news results from a growing local economy that has generated large budget surpluses in each of the past three years. Nevertheless, challenges remain to the long-run fiscal health of the city—including the need to balance revenue and spending growth rates, finance substantial capital improvements, and control the expansion of debt service costs.

In constructing the baseline estimates contained in our January *Fiscal Outlook* report, we assumed existing spending policies and tax laws are allowed to run their course over the next few years. This report, alternatively, provides IBO's analysis and repricing of the Mayor's preliminary budget for 2000 and financial plan through 2003 by dropping that assumption and allowing spending and tax policies to change (consistent with the Mayor's plan) over the next few years.

Figure 1-1.
Mayor's Financial Plan Results in Budget Balance through 2000, But Large Gaps Thereafter

Dollars in millions

	1999	2000	2001	2002	2003	Average Change
Total Revenues	36,242	36,339	36,422	37,517	38,528	1.5%
Expenditures:						
Before 1999/2000 Prepayments	34,487	37,764	39,107	40,407	41,472	4.7%
1999 Budget Stabilization Acct.	1,579	(1,579)	---	---	---	
2000 Budget Stabilization Acct.	---	345	(345)	---	---	
Additional Surplus (IBO est.)	176	(176)	---	---	---	
Total Adjustments	1,755	(1,410)	(345)	---	---	
Total Spending	36,242	36,354	38,762	40,407	41,472	3.4%
IBO Gap Estimate	**---**	**(15)**	**(2,340)**	**(2,890)**	**(2,944)**	

SOURCE: Independent Budget Office.
NOTE: Excludes intra-city revenues and expenditures.

As shown in Figure 1-1, IBO projects that the city's fiscal fortunes during 1999 and 2000 would remain strong if the Mayor's financial plan were adopted. Although the figure reports a balanced budget for the current year, in fact, we expect a surplus of nearly $1.8 billion to occur. Because the city is forbidden by state law from carrying excess funds over from one fiscal year to the next, we have assumed (as does the Mayor's budget) that all current year surplus funds will be used to prepay 2000 debt service. The resulting reduction in 2000 expenses contributes to a budget essentially in balance for the upcoming fiscal year.

A gap of $15 million is projected for 2000 because we assume adoption of a proposal to replenish a reserve fund (known as the "budget stabilization account") with $345 million generated from the sale of the New York Coliseum. If we assumed no new funds were provided for the stabilization account, a surplus of $330 million would be forecast for the upcoming fiscal year.

Beyond 2000, we project gaps in the range of $2 billion to $3 billion annually. Our gap projections are higher than the Mayor's forecast by $0.9 billion in 2001, $1.3 billion in 2002, and $1.8 billion in 2003. While the precise reasons for these differing estimates are detailed below, they result more generally from varying policy, economic, and technical assumptions that IBO has used to reprice the Mayor's proposals.

As we have pointed out in the past, such large out-year gaps could portend the need to cut services or raise taxes in the years ahead, particularly in the event of an economic downturn. It is important to note that the Mayor's financial plan through 2003 assumes continued growth in the local economy. In the event of an economic downturn, however, spending needs would increase—particularly for social programs—at a time when revenues would be decreasing, thereby making future budget gaps even larger. If this were to occur, the city would face an unenviable choice between increasing taxes in a slow economy or reducing spending when it is needed most.

Absent an economic downturn, if history is any guide these out-year gap projections will become smaller as a result of changes to the Mayor's financial plan as each new fiscal year approaches. Traditionally, those changes have included incremental service reductions, tax increases, and the use of non-recurring revenues to pay for ongoing expenses. The negative consequences of such last minute budgetary changes, however, highlight the need for the city to plan strategically for its financial future. While the preliminary budget contains a plan to balance annual budgets beyond 2000, details are very sketchy. A more detailed systematic, long-term plan to close projected gaps would help eliminate budget-year balancing scrambles and further improve the city's bond rating.

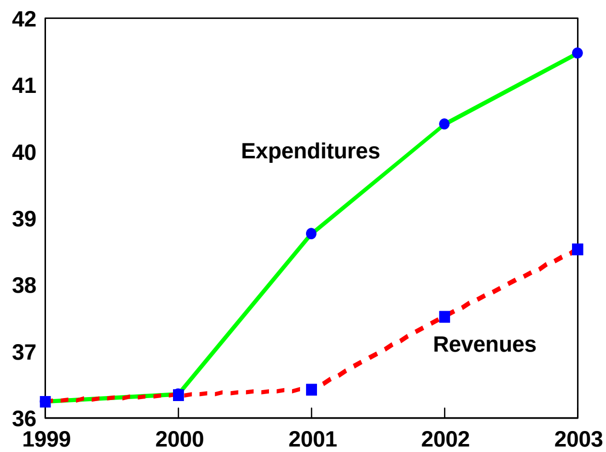
IBO's pricing of the preliminary budget suggests the Mayor's policies would substantially increase the size of the gaps projected to occur under existing laws and policies. Compared with IBO's baseline estimates of revenues and spending, our repricing of the Mayor's budget yields substantially higher gaps—ranging from $0.4 billion to $0.7 billion annually. (See Appendix A for IBO's forecast of gaps under the Mayor's plan along with our baseline gap estimates.)

Budget Summary

The preliminary budget reflects an improving local economy bolstered by the continuing profitability of Wall Street securities firms. Such prosperity has allowed the Mayor to propose relatively modest total spending reductions and a reduction in certain taxes paid by New Yorkers. IBO projects that both city-funded and overall spending for 2000 would rise if the Mayor's budget were adopted in its entirety. The budget would result in expenditures of about $36.4 billion in 2000, including $25.3 billion in city-funded spending—a

Figure 1-2.
Spending Growth Would Outpace Revenues under the Mayor's Plan…

Billions of dollars



SOURCE: Independent Budget Office.

5.8 percent increase over 1999 when debt service prepayments are excluded.

Under the Mayor's plan, spending would grow at an average annual rate of 4.7 percent (excluding debt service prepayments) while revenues would grow more slowly—averaging 1.5 percent each year. As shown in Figures 1-2 and 1-3, this imbalance results in large gaps beyond 2000.

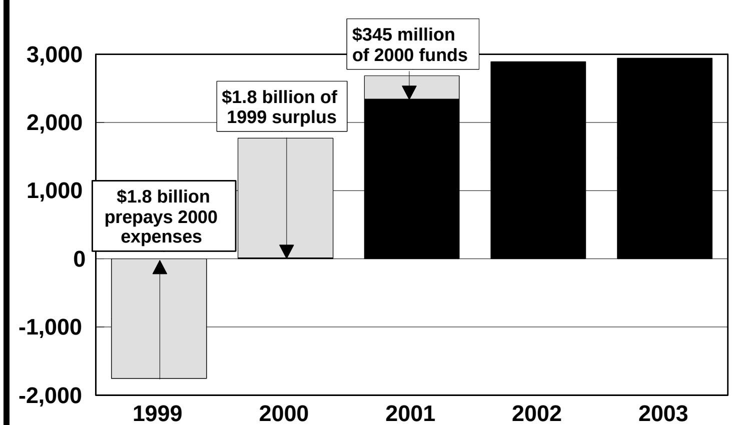
A key feature of the financial plan is the proposed utilization of the large surplus (IBO's projection is $1.8 billion) in the current year. As noted above, all surplus funds must be fully spent each year. The city can, however, effectively carry over some of these funds by providing new appropriations to the budget stabilization account. The Mayor's plan to replenish the account in 2000 with an appropriation of $345 million from the sale of the Coliseum would be earmarked to help balance the budget in 2001.

The Mayor proposes to continue a tax reduction program started in 1994. Specific items in this year's program include the elimination of the sales tax on clothing, extension of a soon-to-expire property tax abatement for owners of coops and condominiums, and additional commercial rent tax reductions. The fiscal prudence of cutting taxes depends on anticipated spending requirements, the specific taxes under consideration and their impact on the local economy, and on the sustainability of recently strong revenue growth. The larger budgetary question is whether the city will ultimately be able to afford the proposed tax reduction program. Nevertheless, strategic tax reductions can have a productive impact on the local economy by encouraging development and investment.

In the short term, the prepayment of next year's expenses along with other factors such as an increase in forecast revenue growth next year would more than eliminate what had been a projected budget gap for 2000 of more than $2 billion at the beginning of fiscal year 1999.

Figure 1-3.
…Leading to Large Out-Year Budget Gaps

Budget gaps in millions of dollars



SOURCE: Independent Budget Office.

Figure 1-4.
IBO's Repricing of the Mayor's Financial Plan

Dollars in millions

	1999	2000	2001	2002	2003
Revenues:					
Taxes	21,037	20,239	20,366	20,804	21,791
Miscellaneous Revenues	2,582	3,289	2,714	2,818	2,714
State/Federal Categorical Aid	11,176	11,089	11,278	11,520	11,612
Other Revenues	1,447	1,722	2,064	2,375	2,411
Total Revenues	36,242	36,339	36,422	37,517	38,528
Expenditures:					
City Funded	25,066	25,265	27,484	28,887	29,860
State/Federal Categorical Aid	11,176	11,089	11,278	11,520	11,612
Total Expenditures	36,242	36,354	38,762	40,407	41,472
IBO Gap Estimate	**---**	**(15)**	**(2,340)**	**(2,890)**	**(2,944)**

SOURCE: Independent Budget Office.

NOTE: Excludes intra-city revenues and expenditures.

IBO Reestimates

Figures 1-4 and 1-5 summarize significant differences between IBO's reestimated projections and the projections contained in the Mayor's preliminary budget. It must be emphasized that differing estimates of city revenues and city-funded spending have a direct impact on projected gaps, while varying estimates of state and federal aid have no net budgetary impact because any additional aid is exactly offset by an identical amount of spending.

City Funds

As shown in Figure 1-5, IBO projects larger gaps than those included in the Mayor's budget documents over the 2000-2003 period even though we forecast higher tax revenues. Much of the difference in revenues results from IBO's view that personal and business income taxes will be significantly higher than estimated by the Mayor. These additional tax revenues, however, will be largely offset by our more conservative projections of property taxes and miscellaneous revenues. Most of the difference in spending estimates can be found in our higher projections for base pay and overtime costs for city employees, anticipated state and federal actions, garbage exportation costs resulting from closure of the Fresh Kills landfill, and higher public assistance and education costs.

Taxes. IBO's forecast of city tax revenues is higher than the estimates contained in the Mayor's budget for each year of the financial plan. Most of the difference between the two revenue estimates is attributable to IBO's more optimistic economic forecast. As shown in Figure 1-5, we project higher tax revenues over the near term, with $526 million of additional revenue in 2000 and $390 million in 2001. Moreover, our estimates exceed those of the Administration by about $350 million each year thereafter through 2003. In all years, IBO's estimates of the Mayor's tax reduction program are similar to those projected in the budget. As a technical adjustment, we have included in our projections personal income tax revenues—no longer shown in the budget by the Administration—that have been dedicated to pay debt service costs of the Transitional Finance Authority. See chapter 2 for our tax revenue presentation.

Figure 1-5.
Details of Pricing Differences between the Administration and IBO

Dollars in millions

	1999	2000	2001	2002	2003
Gap As Estimated by Mayor	**---**	**---**	**(1,441)**	**(1,640)**	**(1,167)**
IBO Reestimates:					
Revenues:					
Taxes:					
Property Tax	16	33	(59)	(176)	(281)
Personal Income Tax (excluding TFA)	77	168	157	151	139
General Sales Tax	8	(51)	(19)	37	54
Business Income Taxes	179	357	289	284	326
Real Estate Related Taxes	22	19	22	54	110
Tax Revenue Reestimates	302	526	390	350	348
Tax Reduction Program	---	(16)	(6)	(7)	(13)
STaR Reimbursement	---	(9)	(5)	34	11
Dedicated PIT (TFA)	144	284	446	548	577
Anticipated State/Federal Actions	---	(65)	(65)	(65)	(65)
Miscellaneous Revenues:					
Airport Rent	---	---	(330)	(150)	(120)
Asset Sales	---	(30)	---	---	---
Total Revenue Reestimates	446	690	430	710	738
Expenditures:					
Public Assistance	5	29	16	(5)	(44)
Medicaid	(56)	(75)	(80)	(85)	(90)
Education	(5)	18	(48)	(7)	(59)
Fresh Kills Closure	---	---	---	(161)	(161)
Overtime	(70)	(113)	(113)	(113)	(113)
Labor Costs	---	(36)	(235)	(614)	(1,040)
Anticipated State/Federal Actions	---	(420)	(423)	(427)	(431)
TFA Debt Service	(144)	(284)	(446)	(548)	(577)
Prepayment Adjustment	(176)	176	---	---	---
Total Expenditure Reestimates	(446)	(705)	(1,329)	(1,960)	(2,515)
Total Reestimates	---	(15)	(899)	(1,250)	(1,777)
Gap As Estimated by IBO	**---**	**(15)**	**(2,340)**	**(2,890)**	**(2,944)**

SOURCE: Independent Budget Office.

NOTES: Negative reestimates (in parentheses) widen the gaps estimated by the Mayor. Positive reestimates narrow the gaps. Excludes intra-city revenues and expenditures.

Spending. Although we forecast more tax revenues than does the Mayor for each year of the financial plan, our higher spending estimates more than offset those additional collections. As illustrated in Figure 1-5, we project higher spending for each year of the financial plan. Our estimates exceed those of the Administration by $705 million in 2000, increasing steadily to $2.5 billion in 2003. See chapter 3 for a discussion of our spending reestimates.

Chapter 2

Revenue Estimates

Overview

In the current fiscal year, IBO estimates that city revenues from all sources will total $36.2 billion, a healthy 3.8 percent increase from 1998. For 2000 and 2001, however, IBO forecasts only minimal revenue growth, averaging 0.3 percent per year. In the following two years, we expect growth to pick up and average 2.9 percent annually, with total revenues reaching $38.5 billion by 2003. The forecast reflects IBO's projected changes in the growth of baseline tax and other revenues—assuming the continuation of current tax policies—plus our estimates of the impact of the proposed tax reduction program.

This chapter presents details of IBO's revenue forecast. The first section summarizes the economic outlook behind our forecast. The second section, which comprises the majority of the chapter, focuses on tax revenues. It begins with a review of IBO's baseline forecast and provides a close look at the three major components of the Mayor's tax reduction program: extension of coop and condo property tax abatements, phased-in reductions in the commercial rent tax, and complete elimination of the retail sales tax on clothing. The chapter concludes with a discussion of our forecasts of state and federal categorical aid and revenues other than taxes.

Economic Outlook

After a strong 1998, IBO forecasts a slowdown in economic growth in calendar years 1999 and 2000 and a moderate pick-up starting in 2001.[1] The preliminary budget also forecasts a slowdown this year, but is somewhat more pessimistic in that it does not anticipate any economic acceleration in the out-years of the plan. (IBO's economic forecast is contrasted with the Administration's in Appendix B of this report.)

National forecast. The IBO national forecast predicts a 1 percentage point decline in the rates of growth of both the real gross domestic product (GDP) and nationwide payroll employment in 1999 and then even slower growth in 2000. OMB's forecast also anticipates slowing growth; both forecasts call for a 2.0 percent increase in GDP in 2000 and an increase in payroll employment just above 1 percent in that year. After 2000, however, the forecasts differ considerably. IBO expects output and employment growth to rebound in 2001 (to 3.1 percent and 1.7 percent, respectively), and anticipates accelerating inflation and rising interest rates (as measured by the 30-year Treasury Bond). On the other hand, the preliminary budget forecasts milder increases in inflation and interest rates, and no pick-up in output or employment.

[1] All economic data in this section are presented on a calendar year basis.

City forecast. For the city's economy, IBO again forecasts a one percentage point decline in the rates of growth of two leading indicators in 1999, city personal income and city payroll employment. OMB's forecast also anticipates slowing growth in 1999. Starting in 2000, the IBO economic forecast for New York City is considerably more optimistic. IBO projects that personal income growth will accelerate in the second half of 2000 and subsequently return to its growth rate prior to the 1999 slowdown. In contrast, OMB expects a more gradual pick-up in personal income growth beginning in 2001. Moreover, OMB does not expect growth in city payroll employment to exceed 1 percent in any year of the forecast period after 1999. Finally, both IBO and OMB forecast gradually rising local inflation and gradually rising Manhattan office rents over the forecast period.

Tax Revenues

With the local economy continuing to expand, New York City's tax revenues have continued to grow and by the end of fiscal year 1999 will total $21.2 billion, including $144 million in personal income tax (PIT) revenues that are dedicated to the Transitional Finance Authority (TFA).[2] The 1999 rate of growth of tax revenues—3.9 percent—is not expected to be matched in the near future. Slower economic growth in the near-term, expiration of the 12.5 percent PIT surcharge, less robust Wall Street profits, already enacted tax cuts, and new tax reduction initiatives will all contribute to a 3.1 percent *decline* in tax revenues in 2000. Growth resumes at an average annual rate of 3 percent in the later years of the forecast, and projected city tax revenues reach $22.4 billion in 2003.

IBO's forecast of baseline tax revenues—revenues excluding proposed tax reductions—is summarized below. This is followed by detailed descriptions of the three major components of the Mayor's tax reduction program.

Baseline Revenue Forecast

- Following a 1.4 percent decline in 2000, IBO forecasts a resumption of baseline tax revenue growth at a modest but increasing rate.

- IBO's total baseline tax forecast exceeds OMB's by more than $300 million a year through 2003, with the greatest difference—$526 million—in 2000. IBO's stronger forecast of personal and business income taxes account for most of the difference.

Even without incorporating the effects of the proposed tax reduction program, only modest revenue growth is forecast. Baseline revenues, which are projected to reach $21.2 billion in 1999, will decline by 1.4 percent to $20.9 billion in 2000 due to slower economic growth on both the national and local levels starting in calendar year 1999 (see Figure 2-1). Collections of personal income, sales, and real estate-related taxes in 2000 are expected to decline by at least 1 percent.

In 2001, IBO forecasts significant reductions in the general corporation and banking corporation taxes—the former reduction a delayed response to slower economic growth. In spite of weakness in business tax collections, however, overall revenue growth of baseline tax revenues resumes in 2001 in response to the improved local economy after calendar year 1999. Baseline tax revenues expand at an average annual rate of 3.2 percent during the out-years of the forecast. The projected annual growth of the unincorporated business and real-estate related taxes in the out-years (8.2 and 5.5 percent on

[2] In order to present a clearer picture of revenue growth, references to tax revenues in the text of this chapter will include the portion of personal income tax (PIT) revenues dedicated to the Transitional Finance Authority. In the tables, however, TFA-dedicated revenues are reported on a separate line, below the sum of tax revenues, in order to present figures that are comparable to those of the preliminary budget. See IBO's May 1998 report, *Analysis of the Mayor's Executive Budget for 1999*, for a critical discussion of the Administration's decision to remove TFA-dedicated revenues and TFA debt service payments from the city budget.

Figure 2-1.
IBO Revenue Estimates Under the Mayor's Proposals

Dollars in millions

	1999	2000	2001	2002	2003
Tax Revenues:					
Property Tax	7,543	7,876	8,127	8,392	8,766
Personal Income Tax (excluding TFA)	5,105	4,481	4,371	4,324	4,556
General Sales Tax	3,228	3,184	3,250	3,383	3,513
General Corporation Tax	1,526	1,525	1,462	1,525	1,555
Unincorporated Business Tax	608	630	675	729	785
Banking Corporation Tax	430	450	431	411	481
Real Estate Related Taxes	1,142	1,019	1,036	1,096	1,187
Other Taxes (with Audits)	1,455	1,428	1,430	1,412	1,434
Total Taxes Before Reductions	21,037	20,593	20,782	21,272	22,277
Tax Reduction Program	---	(354)	(416)	(468)	(486)
Total Taxes After Reductions	21,037	20,239	20,366	20,804	21,791
STaR Reimbursement	117	306	503	714	721
Dedicated Personal Income Tax (TFA)	144	284	446	548	577
Miscellaneous Revenues	2,582	3,289	2,714	2,818	2,714
State / Federal Categorical Aid	11,176	11,089	11,278	11,520	11,612
All Other Revenues	1,186	1,132	1,115	1,113	1,113
Total Revenues as Estimated by IBO	36,242	36,339	36,422	37,517	38,528

SOURCE: Independent Budget Office.

NOTES: Miscellaneous revenues are net of intra-city revenues. All other revenues include unrestricted government aid, anticipated aid, other categorical grants, inter-fund revenues, and disallowances. Personal income tax revenues dedicated to the Transitional Finance Authority (TFA) are not included in the financial plan.

average) is especially strong, while growth of the general corporation tax (0.7 percent on average) is particularly weak.

IBO's baseline tax forecast exceeds that presented in the preliminary budget throughout the forecast period. Most of the difference between our forecast and the Administration's comes from IBO's higher estimates of personal and business income taxes. Underlying IBO's income tax forecasts are projections of both faster local income and employment growth and a higher though still conservative forecast of profits in the securities industry.[3]

For specific taxes in some years, IBO's forecast of revenues is lower than the Administration's. Our sales tax forecast is somewhat below OMB's in 2000 and 2001, in part because of our higher

[3] In contrast to OMB's expectation that securities industry profits will average $5 billion annually, IBO projects profits averaging between $8 billion and $9 billion a year over the next five years—a significant decline from the nearly $11 billion annual average over the last three calendar years.

estimate of the first-year cost of exempting purchases of clothing items costing under $110 from taxation. Our property tax forecast is on average 2 percent less than the preliminary budget forecast, largely because IBO does not assume as strong an appreciation in assessed values in class 2 (apartment buildings) and especially class 4 (commercial and industrial properties).

Tax Reduction Program

The Mayor's tax reduction program focuses on three initiatives that have been proposed in the past and reserves funding for additional tax cuts currently being developed. The budget calls for extension of coop and condo property tax abatements, phased-in reductions in the commercial rent tax, and complete elimination of the retail sales tax on clothing. The Administration has appointed a task force charged with making specific proposals by the end of March for an additional $100 million in tax cuts.

Assuming that the task force recommends tax cuts totaling the full $100 million a year, IBO estimates that the tax reduction program would cost $354 million in 2000 and grow to $486 million by 2003. The remainder of this section reprices and discusses each of the three proposals.

Coop/Condo Abatement

- Extending the abatement—which was intended as a stopgap measure pending more comprehensive reform—for four more years would cost the city $171 million in 2000 and $205 million by 2003.

- Abatement does a poor job of targeting benefits to apartment owners being taxed at the highest rates.

The preliminary budget tax program calls for extending the existing coop/condo property tax abatement, which expires at end of this fiscal year. Designed to reduce the disparity in tax burdens between owners of cooperative and condominium apartments and owners of one-, two-, and three-family homes, the abatement will cost the city $159 million in 1999. IBO estimates that if the abatement were extended at the 1999 level, the cost would grow to $171 million in 2000 and $205 million by 2003. These estimates, which are somewhat higher than those given in the financial plan, take into account IBO's forecast of assessment growth for these properties and a gradual increase in the number of qualifying properties. The cost of the abatement in 2003 accounts for 42 percent of total tax program costs for that year, and equals 2.3 percent of baseline property tax revenues.

Background. The city's property tax system has four tax classes, with assessment procedures and tax rates differing for each class. Most coop and condo apartment buildings in the city are assigned to tax class 2 for property tax purposes, while one-, two-, and three-family homes are designated as tax class 1. The city's average effective tax rate (property tax as a percentage of market value) for class 1 houses is 0.74. In contrast, average effective tax rates for most coops and condos are 1.18 and 1.44, respectively, both significantly higher than the class 1 rate.[4]

Advocates for coop and condo owners have long contended that the city should treat all homeowners equally, regardless of whether they live in apartment buildings or houses. In 1996, legislation was enacted to create a temporary three-year abatement to narrow the gap in effective rates. For 1999, the abatement reduces taxes on qualifying apartments by 17.5 percent.[5] The abatement was instituted as a stopgap measure to provide some relief while the

[4] The effective tax rates for coops and condos are based on "true market value" rather than the official city market value, which is artificially lowered under section 581 of the real property tax law. See IBO, *The Coop/Condo Abatement and Residential Property Tax Reform in New York City,* December 1998.

[5] For apartments in buildings with average assessed values of $15,000 or less per apartment, the percentage is 25 percent. Only apartments that have been sold by the sponsor or developer qualify. Also, buildings enjoying J-51 or 421-a benefits are excluded.

Figure 2-2.
IBO's Reestimate of the Mayor's Revenue Forecast

Dollars in millions

	1999	2000	2001	2002	2003
Total Revenues as Estimated by the Mayor	35,604	35,464	35,591	36,163	37,039
IBO Reestimates:					
Tax Revenues					
Property Tax	16	33	(59)	(176)	(281)
Personal Income Tax (excluding TFA)	77	168	157	151	139
General Sales Tax	8	(51)	(19)	37	54
General Corporation Tax	100	216	208	224	190
Unincorporated Business Tax	16	44	53	64	87
Banking Corporation Tax	63	97	28	(4)	49
Real Estate Related Taxes	22	19	22	54	110
Tax Reduction Program	---	(16)	(6)	(7)	(13)
STaR Reimbursement	---	(9)	(5)	34	11
Miscellaneous Revenues:					
Airport Rent	---	---	(330)	(150)	(120)
Asset Sales	---	(30)	---	---	---
State / Federal Categorical Aid	192	185	401	644	751
All Other Revenues	---	(65)	(65)	(65)	(65)
Inclusion in the Budget:					
Dedicated Personal Income Tax (TFA)	144	284	446	548	577
Total Revenues as Estimated by IBO	36,242	36,339	36,422	37,517	38,528

SOURCE: Independent Budget Office.

NOTES: Miscellaneous revenues are net of intra-city revenues. All other revenues include unrestricted government aid, anticipated aid, other categorical grants, inter-fund revenues, and disallowances. Personal income tax revenues dedicated to the Transitional Finance Authority (TFA) are not included in the Mayor's financial plan.

city developed a long-term solution to eliminate the difference in tax burdens faced by apartment owners and class 1 homeowners. The law included a requirement that the city deliver such a plan by December 1996. Now, more than three years past the deadline and with no long-term solution forthcoming, the Mayor proposes to extend the abatement at the current level for four more years.

Abatement shortcomings. Extending the current abatement for four years may have consequences that are undesirable from the perspective of sound tax policy. First, there are serious problems with the abatement itself that would not be addressed by simply extending it in its present form. IBO's December 1998 study found that the abatement does a poor job of targeting benefits to the buildings with the greatest need.

Effective tax rates on coops and condos—and hence the gap between class 1 tax burdens and the burdens on apartment owners—vary greatly across the city. These differences stem from distortions in the assessment process that can not be equalized by an abatement that reduces tax bills by the same percentage for all owners. The areas of the city receiving the largest reductions in the class 1 gap (the difference between the effective rate for coops and condos and the class 1 effective rate) are those with the smallest gaps to begin with, and therefore the least need for relief.

Second, the current abatement is inefficient, with $29 million (19 percent) of the benefits going to apartment owners who either already had tax burdens below the class 1 level *before* the abatement, or who needed only a portion of their abatement to reach the class 1 level. This inefficiency could be mitigated by reducing or eliminating the abatement for some apartments based on such criteria as value or location. However, the Mayor's tax program does not propose any changes.

Finally, extending the abatement for four years postpones the promised reform that would give all apartment owners the full benefits of class 1 treatment. Although there are important implementation issues to be resolved, the outlines of a long-term solution are clear. Coops and condos would be assessed and taxed using sales-based market values subject to the same protections enjoyed by class 1 property owners. Such reform would eliminate the differences in effective rates among apartment owners, and all coops and condos with tax burdens above the class 1 level would have their taxes brought down to that level. Those with burdens already below the class 1 level would likely be held harmless from the reform. The largest reduction in tax burdens—in percentage terms—would be concentrated in the areas of the city which now have the largest class 1 gaps. In IBO's December 1998 study, we estimated that it would cost $270 million in 1999 to completely eliminate the gap, $114 million more than the cost of the abatement this year.

Other considerations. When evaluating proposed tax reductions targeted at resolving a particular inequity in a tax, it is appropriate to consider whether other inequities in the tax result in greater hardship and therefore should have a greater call on the revenues being "expended." In the case of the city's property tax, the disparity in burdens between apartment owners and house owners is much smaller than the gap in burdens between rental apartment buildings and owner-occupied apartment buildings.

The effective rate on rental buildings is 3.7, or more than three times as large as the rate on coops and more than double the rate on condos. Given that a portion of the landlord's property tax is passed along as part of the rent, some portion of this higher effective tax rate is borne by tenants—many of whom are unaware that they pay any property tax. If a significant share of the tax is passed through, it is likely that tenants—who are generally less well off than owners of coops and condos—are paying a higher proportion of their income in property taxes than apartment owners. This suggests that the revenue reductions directed towards apartment owners under the coop/condo abatement program might create greater equity between all occupants of residential property if they were directed at lowering the effective tax rate on rental properties instead.

Commercial Rent Tax Cut

- The Mayor's plan for a new round of CRT reductions would lower the effective tax rate by 26 percent.
- The proposal would leave remaining CRT revenue on-budget rather than specifically dedicated to stadium construction (as proposed by the Mayor in the past).

Figure 2-3.
IBO's Reestimate of the Mayor's Tax Reduction Program

Dollars in millions

	1999	2000	2001	2002	2003
IBO Estimate of the Tax Reduction Program					
CRT Reduction to 3 Percent ETR Plus Lost Audits	---	(22)	(44)	(82)	(84)
Extension of Coop/Condo Property Tax Relief	---	(171)	(181)	(192)	(205)
Sales Tax: Exemption on Clothing over $110	---	(61)	(91)	(94)	(97)
Initiatives of Tax Reform Task Force	---	(100)	(100)	(100)	(100)
Total	---	(354)	(416)	(468)	(486)
Mayor's Estimate of the Tax Reduction Program					
CRT Reduction to 3 Percent ETR Plus Lost Audits	---	(21)	(48)	(89)	(91)
Extension of Coop/Condo Property Tax Relief	---	(166)	(173)	(180)	(187)
Sales Tax: Exemption on Clothing over $110	---	(51)	(89)	(92)	(95)
Initiatives of Tax Reform Task Force	---	(100)	(100)	(100)	(100)
Total	---	(338)	(410)	(461)	(473)
Difference	---	(16)	(6)	(7)	(13)

SOURCE: Independent Budget Office; Mayor's Preliminary Budget for 2000.

The Mayor's preliminary budget tax program calls for a reduction in the commercial rent tax (CRT) beginning in 2000. When fully phased in for 2002, the effective tax rate would be 26 percent lower than its current level. The cost to the city would be $22 million in 2000 and would grow to $84 million in 2003.

The CRT is paid by commercial tenants based on the amount of rent they pay to their landlords. Tax liability is determined by a single flat rate applied to the base rent. A sliding-scale credit (which phases out as taxable rent increases) helps to moderate what would otherwise be a steep rise in the marginal tax paid on rents just over the zero-liability threshold.

Although the CRT tax burden has been lowered several times since its peak in 1977, in the last four years the city has made much more dramatic changes, significantly reducing both the number of firms subject to the tax and the liability of the remaining taxpayers.[6] Since September 1995, only leases in buildings south of 96th Street in Manhattan are subject to the tax, and since June 1997, only tenants with base rents above $100,000 have any tax liability.

For tenants still subject to the tax, the most important change has been a reduction in the effective tax rate, which has fallen from 6 percent to 3.9 percent. The cumulative value in 1999 of the cuts enacted since 1995 is $364 million. These reductions account for the precipitous fall in CRT revenues (excluding audits) from $629 million in 1994 to $351 million in 1999; without the cuts, CRT revenue would be $715 million this year.

These enacted changes have greatly reduced the number of CRT taxpayers while increasing the share

[6] See Independent Budget Office, *Analysis of The Mayor's Preliminary Budget*, March 1998, pp. 13-14 for a fuller discussion of recent changes in the CRT and the CRT's place in the city's tax structure.

of large firms still paying the tax. Nevertheless, tenants with relatively modest rents still account for the majority of remaining taxpayers. Based on rent distributions supplied by the Department of Finance, IBO estimates that over 75 percent of the remaining taxpayers have annual rents of $500,000 or less, paying an average rent of $200,000. Unfortunately, information about the type of firms and the space rented is not available. (For illustrative purposes, however, consider that $200,000 in rent would pay for roughly 8,000 square feet of office space at $25 per square foot, or 2,700 square feet of retail space at $75 per foot.)

Proposed change. The preliminary budget calls for reducing the effective tax rate on the CRT to 3.4 percent in December 1999 and then to 3.0 percent in June 2001. The effective rate would be lowered by discounting the amount of base rent subject to tax. The estimated costs of these reductions are $22 million in 2000, $45 million in 2001, and $84 million in 2003.[7] The CRT owed by a firm paying $200,000 a year in rent would fall from $7,800 in 1999 to $6,000 in 2002. Although reducing the effective rate benefits all taxpayers, the dollar value is concentrated at the higher end, with over 60 percent of the benefit flowing to taxpayers with annual rents of $1 million or more.

CRT and stadiums: the missing link. In his budget presentation, the Mayor indicates that a portion of the remaining CRT revenues "will be used to fund the New York City Sports Facility Corporation," although there is no mechanism to formally dedicate the revenues towards the new stadium-building entity.

The CRT has been linked to the Mayor's attempts to finance the city's share of the cost of building new professional sports facilities since the 1999 executive budget was released last spring. At that time, the Mayor scaled back an earlier proposal to gradually phase out the CRT between 2000 and 2002, replacing it with the same proposal to reduce the effective rate to 3 percent included in this year's preliminary budget. In last year's executive budget, the money saved by not moving towards full elimination of the CRT would have been taken off-budget and dedicated to a new Sports Facility Corporation. If last year's proposal had been enacted, a clear link between the CRT and stadium financing would have been established.

This year's plan differs significantly in that the CRT revenues remaining after the proposed tax cut are simply part of the general fund. The amount budgeted for the Sports Facility Corporation would be appropriations from the same general fund. The only link between the CRT and stadium building is that the decision to retain the tax allows for increased spending without adding to the budget gap.

Clothing Sales Tax Exemption

- IBO anticipates substantial deferments of clothing purchases prior to the December 1, 1999 start date of the city's approved and proposed permanent clothing tax exemptions; consequently, IBO's cost estimates for both exemptions are higher than the preliminary budget's cost estimates for 2000.

- While all sales taxes on clothing priced under $110 will be eliminated on December 1st, it is unlikely that the state would join the city in cutting taxes on clothing priced $110 or higher.

- Increased economic activity from clothing tax cuts will yield modest increases in other city tax revenues.

- Without the additional economic stimulus provided by a state clothing tax cut, secondary city revenue gains would offset less than 10 percent of the direct city costs of the proposed $110-and-over clothing tax cut.

[7] In order to be consistent with OMB's presentation, these estimated costs include reductions in audit revenues attributable to the proposals. Note that all other tax program costs are estimated without accounting for their impact on audit revenues.

Starting December 1, 1999, apparel items priced under $110 will be fully exempt from city and state sales taxes and surcharges. The cost of the city sales tax exemption is now included in the baseline forecast of total city sales tax revenues. This includes an additional cost for reimbursing the Metropolitan Transit Authority for half of its losses from exempting city clothing sales from the 0.25 percent Metropolitan Commuter Transportation District (MCTD) surcharge.[8]

The Mayor's 2000 tax program carries over from last year a proposal to eliminate the city tax on clothing and footwear priced at $110 or more. This additional clothing tax cut would take effect on December 1st of this year.

There has not been much enthusiasm for additional clothing tax cuts outside New York City, where localities have fewer alternatives to sales taxes and perceive less of an economic disadvantage from taxing apparel. If the city does gain state approval for an additional clothing exemption, it may be without actual state participation in the cut. This would mean that if the proposed additional exemption were enacted, shoppers in New York City would pay no sales taxes on items priced under $110 and a 4 percent state tax and 0.25 percent MCTD surcharge (but no city sales tax) on items costing $110 or more.

Direct costs. IBO's $164 million cost estimate for the approved under-$110 clothing tax cut in 2000 is $30 million larger than the amount baselined in the preliminary budget. Similarly, our first-year estimate for the proposed additional clothing tax cut, $61 million, runs $10 million above the Administration's estimate.

These differences largely stem from the fact that IBO anticipates substantial shifting of apparel sales that would normally occur in the weeks leading up to the December 1st start date of both the enacted and proposed clothing tax cuts. We expect that consumers will postpone their purchases to take maximum advantage of the exemptions.[9]

Apart from this one-time effect, IBO's clothing tax cut impact estimates are only slightly higher than OMB's throughout the financial plan period.

Secondary impacts. While the city's projections of tax program costs do not incorporate secondary revenue gains from impacts on economic growth, the potential for significant secondary gains has been an important part of arguments for clothing tax cuts.

IBO addressed the issue of secondary clothing tax cut impacts in a fiscal brief issued in June 1997, *Would Clothing Sales Tax Cuts Pay for Themselves?* In that report, IBO's estimate of a clothing tax cut's total impact on city apparel sales (including the recapture of sales currently shifted to New Jersey) was not far below the estimate produced by the city's Economic Development Corporation (EDC). However, we found that these additional sales translated into less overall growth in city economic output and jobs, and hence into smaller offsetting increases in other city tax revenues. EDC concluded that growth in other city revenues would make up for fully 40 percent of the direct cost of a clothing sales tax cut. For a comparable scenario (clothing taxes reduced to zero), IBO estimates secondary city revenue gains would offset no more than 15 percent of the direct city costs of the clothing tax cut.[10]

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[8] The MCTD reimbursement cost will be billed on a quarterly basis by the State Comptroller, with city payments deposited in the Mass Transportation Operating Assistance Fund. Any amounts not paid will be deducted from subsequent transfers to the city of sales taxes collected for it by the state. Thus making payments would add the reimbursement cost to the expense side of the city budget, while forgoing payments would subtract the cost from the revenue side.

[9] A study of the January 1997 one-week clothing tax exemption by the State Office of Tax Policy (*The Temporary Clothing Exemption: Analysis of the Effects of the Exemption on Clothing Sales in New York State*, November, 1997) provides evidence that the timing of clothing purchases is sensitive to changes in sales tax rates.

[10] It should be noted that in obtaining these results we hold the level of government outlays (and the positive economic impact of those outlays) constant while the level of taxes (and the negative economic impact of taxes) falls.

Figure 2-4.
Estimated Direct and Secondary Revenue Impacts of Clothing Tax Cuts

Dollars in million

	1999	2000	2001	2002	2003
Direct City Cost of Tax Cuts					
Items under $110 (baselined)[1]	---	(164)	(240)	(249)	(258)
All other clothing and footwear (proposed)	---	(61)	(91)	(94)	(97)
Total direct city tax cut costs	---	(225)	(331)	(342)	(356)
Secondary City Revenue Impacts					
Items under $110 (baselined)					
Impact of city clothing tax cut	---	7	11	13	15
Impact of state/MCTD clothing tax cut	---	8	12	14	16
Total secondary city revenue impact	---	15	23	27	31
All other clothing and footwear (proposed)					
Impact of city clothing tax cut	---	3	5	6	7
Impact of state/MCTD clothing tax cut	---	0	0	0	0
Total secondary city revenue impact	---	3	5	6	7
Net City Cost of Clothing Tax Cuts					
Items under $110 (baselined)	---	(149)	(218)	(222)	(227)
All other clothing and footwear (proposed)	---	(58)	(86)	(88)	(91)
Total net city tax cut costs	---	(206)	(304)	(310)	(318)
Memo: Total Impact on Private Jobs[2]					
Items under $110 (baselined)	---	*4,800*	*7,090*	*7,160*	*7,250*
All other clothing and footwear (proposed)	---	*1,010*	*1,520*	*1,540*	*1,560*
Total private sector jobs impact	---	*5,810*	*8,610*	*8,700*	*8,810*

SOURCE: Independent Budget Office.

NOTES: (1) Includes city costs of reimbursing MTA for related MCTD surcharge losses ($5 million in 2000, $7 million in 2001, and $8 million annually in 2002 and 2003). (2) Impact on jobs includes impact of state/MCTD tax cuts where applicable.

The main reason for the differences with EDC is that IBO recognizes that for every dollar of apparel sold at retail in New York City, typically no more than 53 cents covers work performed or output ("value added") produced in the city itself. The rest pays for value produced outside New York City—where, in most cases, the articles of clothing and footwear sold here are manufactured. That does not mean that new sales generated by a clothing tax cut have a weak overall impact on jobs and other tax revenues—just that the city itself captures only a little more than half of that overall impact, sharing the rest with other localities.

In the taxes-reduced-to-zero scenario, which applies to the enacted under-$110 clothing exemption, city clothing sales are being stimulated by both city *and* state sales tax cuts. When only city sales taxes are eliminated—the more likely scenario for the $110-and-over clothing proposal—the smaller economic stimulus generates secondary city revenue gains covering less than 9 percent of the primary city costs of the cut.[11]

Taking all this into account, IBO estimates that the direct costs of the proposed additional city clothing tax exemption would be offset by annual secondary revenue increases rising from $3 million to $7 million over the financial plan period. (When the property tax revenue impacts of the full exemption are completely phased in, secondary revenue increases would rise to about $10 million per year.[12]) At the same time, secondary city revenue increases associated with the enacted under-$110 clothing exemption are estimated to rise from about $15 million in 2000 to $31 million in 2003. (When all secondary tax impacts are phased in, secondary revenue increases will reach $46 million.) As Figure 2-4 shows, more than half of the secondary city revenue gains associated with the enacted under-$110 clothing exemption will be due to the stimulus of the accompanying state tax exemption.

Other Revenues

IBO projects that revenue from sources other than taxes will total $4.4 billion in 2000, about $95 million lower than is projected in the budget. Moreover, IBO projects that the city will realize less revenue from these sources beyond 2000 than is estimated in the budget (lower by $395 million in 2001, $215 million in 2002, and $185 million in 2003).

Other revenues include funds from unrestricted intergovernmental aid, private grants, inter-fund capital transfers, state and federal revenue sharing, and miscellaneous revenues from recurring and non-recurring sources. Based on our review of all other revenues, the following items should be noted:

Airport rent. IBO estimates that airport rental income would be $15 million in 2000 and $35 million each year thereafter. Our estimates diverge from those contained in the budget beginning in 2001, and are lower by $330 million in that year, $150 million in 2002, and $120 million in 2003. Airport rent consists of two factors: prior-year rental income and anticipated current-year rent receipts. The collection of airport back rent has been under arbitration for some time and there is little evidence to suggest that this issue will be resolved in the city's favor. Accordingly, IBO's revenue forecast entirely excludes contested rental income from past years.

Tobacco settlement payments. The budget anticipates the city receiving $1.2 billion in payments from the nation's tobacco companies from 2000 through 2003. The tobacco companies have agreed to reimburse states and cities $246 billion over the next 25 years for health care expenditures they incurred due to smoking-related illnesses. New York State has been slated to receive $25 billion to be shared as follows: 51 percent for the state, 27 percent for New York City, and 22 percent for the 57 counties outside the city.

It is unclear, however, how much money the city will actually receive from the settlement—particularly in the near term. First, the President's budget for 2000 asserts that the federal government is entitled to recoup roughly half of the proposed settlement. Second, New York City is seeking 36 percent of the New York State total through its appeal of a State Supreme Court decision that approved a state plan to provide the city with a 27 percent share. Third, the settlement must be ratified (requiring at least 80 percent of the states accounting for 80 percent of the population to accept the settlement). Fourth, the magnitude of tobacco

[11] In this case, the primary costs do not include an MCTD surcharge reimbursement, and the secondary city revenue boost reflects the city's gain of a tax advantage over the surrounding New York counties, leading to some capture of $110-and-over clothing sales from these counties (as well as from New Jersey and Connecticut). All this somewhat mitigates the absence of the economic stimulus from a state clothing tax cut.

[12] Because of the long lags between changes in output and changes in property tax revenues, the full secondary revenue impact of clothing tax cuts introduced in 2000 would not be felt until about 2007.

settlement payments in the out-years depends on the level of future tobacco sales.

The Mayor proposes three uses for the tobacco payments: 1) spending $15 million per year for public health programs; 2) securitizing the payments by selling $2.5 billion in tax-exempt bonds; and 3) using the remainder for general fiscal relief. The budget indicates that because the proposed bonds would be issued by the city's new Tobacco Settlement Asset Securitization Corporation and backed by the tobacco companies, they would not count towards the city's debt limit. The $2.5 billion in capital would help the city fulfill its previously announced strategy of contributing $6.1 billion over five years for school construction and modernization.

Although details of Mayor Giuliani's tobacco bond plan remain sketchy, some budget process concerns exist. The charter clearly stipulates that the City Council is to be a partner with the Mayor on budgetary matters. If the tobacco proceeds are securitized and deposited up front in the city's treasury as a lump sum, the City Council's flexibility in deciding what to do with the settlement money would be substantially impaired. For example, proposals by the Council to use the annual payments as they are received over the next 25 years would not be possible if a large portion of the revenue stream were sold to generate immediate cash.

State and federal revenue sharing. The budget proposes an incremental increase in state revenue sharing of $15 million and a federal initiative of $50 million in 2000 and each year thereafter. Because neither initiative is currently under consideration, IBO projects that no additional revenue sharing funds will be received from either the state or the federal governments.

The state initiative would represent an increase of roughly 4.5 percent in state revenue sharing for New York City. The initiative would require state legislation, but the enactment of such a bill appears unlikely. Similarly, the Mayor has proposed that the federal government provide revenue sharing aid to the nation's 75 largest cities to help meet obligations taken on by cities since the Federal General Revenue Sharing program was eliminated in 1986. At this time, there is little evidence that the federal government is actively considering this initiative.

Non-recurring revenues. The budget projects $542 million in non-recurring revenue for 2000. IBO accepts the city's projected revenues for the largest of those sources: the sale of the New York Coliseum ($345 million); a technical adjustment in federal foster care funding ($47 million) resulting from settlement of a lawsuit; and the sale of mortgages ($75 million) held by the city through the Department of Housing and Development and the Department of Citywide Administrative Services. (See page 44 for a more detailed discussion of the Coliseum sale, including plans to use a portion of the revenue to pay for the proposed LaGuardia Rail Link project.)

In contrast, IBO diverges from the budget's projection of revenues generated from asset sales in 2000. We estimate $45 million would be raised from this source rather than $75 million projected in the budget. Asset sales include the sale of long-term leasehold interests, real property held by the United Nations Development Corporation, and various development sites under the jurisdiction of the Economic Development Corporation. IBO's lower estimate reflects the uncertainties involved in selling as yet unspecified assets—identifying and marketing sites, finding buyers, processing transactions—raising the risk that much of the revenue would not be realized within the budget year.

Categorical Grants

Categorical grants received from the state or federal government to fund specific expenditures account for approximately 30 percent of all funds spent by the city each year. IBO projects that state and federal categorical grants will total $6.8 billion and $4.2 billion, respectively, in 2000. For some types of categorical aid, such as education and welfare, IBO has developed forecasts based on programmatic changes and caseload projections that affect the level of aid received from the state and federal governments. IBO's forecast of categorical aid in other parts of the budget is based on a methodology that takes the grant level in the current year, adjusts for historical trends, and applies growth factors on an agency-by-agency basis.

IBO's forecast of state categorical grants is $119 million lower than the estimate contained in the budget for 2000, but then exceeds the Mayor's projections by $51 million in 2001 growing to $447 million in 2003. The major reason for the difference is IBO's decision to exclude $280 million annually in state aid anticipated by the administration.[13] The difference is partly offset by IBO's significantly higher forecast of state aid for education.

IBO's forecast of federal categorical grants is $304 million higher than the estimate contained in the budget for 2000, and remains higher through 2003. Although IBO's forecast excludes $140 million of anticipated federal aid that we believe is unlikely to occur, our estimates of education, health, childcare, and housing aid—which together account for nearly 60 percent of all federal grants—are significantly greater than the budget estimate.

[13] The major portion of anticipated state and federal aid is related to proposed changes in Medicaid expenditure policy. Discussion of the proposals is provided in chapter 3.

Chapter 3

Expenditure Estimates

Overview

- While the Mayor's plan would result in almost no overall change in spending levels from 1999 to 2000, expenditure growth—particularly for city-funded spending—would accelerate beyond 2000.

- City-funded spending does, however, grow significantly from 1999 to 2000 (by 5.8 percent) when debt service prepayments are excluded from the calculations.

- The policies contained in the Mayor's budget would result in substantially more spending than estimated by the Administration.

- Growth in spending varies in different parts of the budget: spending on education, debt service and police are growing while health and social service spending is fairly stable.

- Although the Mayor's plan assumes a number of changes in state and federal policy that would help the city's fiscal condition, these changes are unlikely to be enacted.

IBO estimates that under the policies proposed in the preliminary budget, total expenditures would barely change in the near future—from $36.2 billion this year to $36.4 billion next year. Beyond 2000, overall spending growth picks up and by 2003, city spending reaches $41.5 billion. The projected average annual rate of growth from 1999 to 2003 is 3.4 percent. Figure 3-1 shows IBO's projections of city spending by major area from 1999 to 2003.[14]

Most of the spending contained in the budget is funded with revenues generated from the collection of city taxes and other revenues from sources such as licenses and fees. (Such spending is known as "city funded.") City-funded spending under the Mayor's plan would rise from $25.1 billion in 1999 to $29.9 billion in 2003, an average annual rate of 4.8 percent. As discussed in chapter 1, this growth rate exceeds the rate of growth of city-generated revenues, resulting in significant budget gaps in the out-years of the financial plan (see Figure 1-4).

As shown in Figure 3-2, IBO's spending forecast exceeds the estimates contained in the Mayor's budget for each year of the financial plan. In this chapter, we explain the reasons for differences in our spending estimates. Generally, those differences occur due to varying economic, technical, and legislative assumptions. For instance,

[14] Agency expenditures have been adjusted to reflect an allocation of the labor reserve as well as expected increases in labor costs.

Figure 3-1.
IBO Expenditure Estimates Under the Mayor's Proposals

Dollars in millions

	1999	2000	2001	2002	2003
Health / Social Services:					
Social Services	5,369	5,176	5,250	5,394	5,515
Children Services	2,085	2,088	2,096	2,123	2,139
Health	1,646	1,679	1,691	1,712	1,736
Homeless	405	410	411	414	418
All Other	465	449	448	452	457
Subtotal	9,970	9,802	9,896	10,095	10,265
Education:					
Board of Education	9,601	9,944	10,353	10,836	11,207
CUNY	412	407	410	415	420
Subtotal	10,013	10,351	10,763	11,251	11,627
Uniformed Services:					
Police	2,825	2,994	3,088	3,159	3,285
Fire	1,031	1,075	1,097	1,128	1,162
Correction	849	911	949	962	990
Sanitation	759	819	857	1,073	1,093
Subtotal	5,464	5,799	5,991	6,322	6,530
Debt Service	3,189	2,092	3,660	4,234	4,418
All Other Spending	7,606	8,310	8,452	8,505	8,632
Total Expenditures as Estimated by IBO	36,242	36,354	38,762	40,407	41,472

SOURCE: Independent Budget Office.
NOTE: Excludes intra-city expenditures.

we have assumed higher overtime costs for city employees (a technical reestimate) and have assumed that certain state and federal actions would not occur over the next year (a legislative reestimate).

In addition to presenting IBO's spending estimates, this chapter discusses the budgetary implications of a number of programmatic initiatives presented in the preliminary budget and is organized around broad spending areas. First, discussions of spending estimates and initiatives in the areas of health/social services, education, and uniformed services are presented. Next, spending in a variety of other broad program areas, such as housing and cultural affairs, is discussed, followed by a section on debt service costs. The chapter concludes with a presentation of several miscellaneous spending issues, including labor costs and stadium financing.

Figure 3-2.
IBO's Reestimate of the Mayor's Expenditure Proposals

Dollar in millions

	1999	2000	2001	2002	2003
Total Expenditures as Estimated by the Mayor	35,604	35,464	37,032	37,803	38,206
IBO Reestimates:					
City Funded:					
Public Assistance	(5)	(29)	(16)	5	44
Medicaid	56	75	80	85	90
Education	5	(18)	48	7	59
Fresh Kills Closure	---	---	---	161	161
Overtime	70	113	113	113	113
Labor Costs	---	36	235	614	1,040
Anticipated State & Federal Actions	---	420	423	427	431
TFA Debt Service	144	284	446	548	577
Prepayment Adjustment	176	(176)	---	---	---
City Funded	446	705	1,329	1,960	2,515
State Funded	13	(119)	51	301	447
Federal Funded	179	304	350	343	304
Total Expenditures as Estimated by IBO	36,242	36,354	38,762	40,407	41,472

SOURCE: Independent Budget Office.
NOTE: Excludes intra-city expenditures.

Health/Social Services

Expenditures in the health and social services areas—public assistance, health, children's services, and others—account for roughly one-quarter of all city spending. IBO projects that by 2003 health and social services spending would total $10.3 billion under the Mayor's financial plan, $0.3 billion higher than its current level.

This section begins with overviews of public assistance and Medicaid, including IBO's forecasts and how they differ from the Administration's. The discussion of public assistance includes a close look at the potential costs of pursuing a policy of universal work requirements, while the Medicaid discussion also reports on the Mayor's proposed changes in state and federal Medicaid policy. The section closes with an examination of three human services spending cuts proposed in the Mayor's preliminary budget—cuts affecting anti-eviction legal services, children's services, and youth services.

Public Assistance

- IBO's caseload projections significantly diverge from the Mayor's in 2002 and 2003, when we expect that the five-year limit on federal assistance will cause thousands of individuals to lose eligibility for Family Assistance.

- IBO expects city expenditures for public assistance to exceed the Mayor's projections by $5 million in 2002 and $44 million in 2003.

Recent public assistance caseload data show a continuation of the four-year downward trend in the number of individuals receiving assistance. The budget assumes that city welfare policy changes combined with favorable economic conditions will continue to generate caseload declines through 2001 and limit decreases thereafter.

Mayor's projections. The budget projects that the number of persons on Family Assistance (FA) will decrease from 579,000 in December 1998 to 562,000 in June 1999, 530,000 in June 2000, and 502,000 in June 2001 and the remaining years of the financial plan. Similarly, the number of Safety Net Assistance (SNA) recipients is projected to decrease from 137,000 in December 1998 to 132,000 in June 1999, 125,000 in June 2000, and 122,000 in June 2001 and thereafter.

Based on the expected caseload reductions, the Mayor projects that total expenditures for public assistance grants will decrease from $1.6 billion in 1999 to $1.5 billion in 2000, and $1.4 billion in 2001 and later years.

IBO projections. Our caseload projections for the Family Assistance and Safety Net Assistance programs as compared with the budget can be seen in Figure 3-3 and Figure 3-4. For Family Assistance we project a faster caseload decline than the Mayor in the near term. This rapid decrease will be driven largely by the continued conversion of all income maintenance centers to job centers over the next several months, a process that has been temporarily delayed by litigation. The new job centers are being created to implement the Mayor's policy of front-end diversion, employing new job search requirements and other mechanisms designed to greatly reduce the number of individuals who end up on the welfare rolls. We expect this emphasis on front-end diversion to contribute to the decline in FA recipients to 500,000 by June 2000. Beyond 2000, IBO expects the downward trend to moderate as the new policies result in a FA caseload that is smaller but increasingly needy and difficult to place in private employment. By June 2001, we expect the FA caseload to reach 497,000, a projection similar to the Mayor's.

However, our projections begin to significantly diverge from the Mayor's in January 2002, when we project that the five-year limit on federal assistance will cause 54,000 individuals to lose eligibility for Family Assistance, even if the state exempts the maximum number of households based on hardship. By January 2003, we project that the number of individuals losing FA eligibility because of the five-year rule will total 123,000. As a result we expect the FA caseload for 2002 and 2003 to dip well below the Mayor's projections, which do not take this provision of federal welfare law into account.

Our SNA caseload projections follow a similar course through 2000, with the extension of job centers and front-end diversion contributing to the reduction in the number of individuals receiving assistance to 126,000 in June 1999 and 117,000 in June 2000—somewhat lower than the Mayor's projections. By 2001 we expect the decline to end and a modest rise in caseloads to begin due to the movement onto Safety Net Assistance of newer immigrant families who are ineligible for FA under federal law. As with Family Assistance, our SNA projections begin to diverge widely from the Mayor's in 2002 due to our incorporation of the impact of the five-year limit on federal assistance, which we expect to shift thousands of individuals from FA to SNA. As a result we expect the SNA caseload to greatly exceed the Mayor's projections for 2002 and 2003.

Welfare Reform: Universal Work Program

On July 20, 1998, the Mayor announced a new policy designed to dramatically alter the welfare system in New York City by instituting front-end diversion measures to reduce the number of new cases and requiring virtually all adults receiving assistance to engage in work activities. A September 1998 IBO study, *Welfare Reform Revisited: Implementation in New York City*, indicates that full implementation of the Mayor's plan could result in additional costs of more than $500 million annually by 2000. Significantly, the budget includes no new funds to implement this plan.

The basic outline of the new welfare plan includes:

- a universal work requirement with exemptions only for the severely disabled;
- heightened emphasis on job search and placement in unsubsidized employment;
- conversion of income maintenance centers to job centers to underscore this new employment effort; and
- expansion of the Work Experience Program to cover all recipients who cannot immediately find a job.

Under the announced plan, the program is to be fully phased in by calendar year 2000. At that point, all family heads receiving assistance will be required to participate in a full-time, 35 hour work week—usually including 20 hours of actual work and 15 hours of training or other activities—leading to the earliest possible full-time private employment.

IBO's analysis indicates that even with significant additional caseload reductions, the net new cost to the city of fully implementing the Mayor's plan would reach more than $500 million annually by 2000. These costs arise from the need to administer work activities for about 150,000 additional adult recipients and to provide subsidized child care for their children.

The lack of new funding in the budget for this initiative could indicate that city officials have chosen to put greater emphasis on one aspect of the program—front-end diversion—than on a costly expansion of work programs for those already on the welfare rolls. The front-end diversion policy is focused within the new job centers, which are meant to be the initial point of contact for those interested in accessing the welfare system.

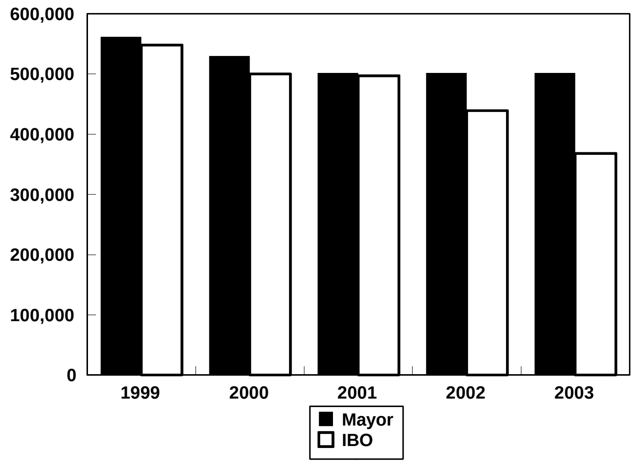
The process of transforming income maintenance centers into job centers began in the summer of 1998. As of January 1999, 13 of the 31 welfare offices had been converted. The conversion of the remaining centers has been temporarily delayed by court order, but it is expected to be completed over the next several months. Results from the earliest job centers suggest that the front-end diversion techniques used there—such as mandatory job search while applications for assistance are being processed—have significantly reduced the number of new public assistance cases.

The rapid expansion of front-end diversion has not been accompanied by an increase in the number of current adult recipients engaged in work programs, however. According to the Mayor's Management Report, from June 1998 to October 1998 the number of Family Assistance (FA) cases engaged in some form of work activity decreased from 53,000 to 46,000, while the number of working Safety Net Assistance (SNA) recipients declined from 17,000 to 16,000.

If the city follows through on its plan to engage virtually all adult recipients in work activities, it will need to commit significant new resources for work program administration and child care. One potential source of new funds is New York State's growing surplus of federal Temporary Assistance to Needy Families (TANF) funds. Due to declining caseloads and unspent funds from previous years, the TANF surplus for the next state fiscal year is projected to reach more than $1.4 billion. The Governor's executive budget proposes to use some of this surplus to expand statewide child care spending by $111 million. Recent history suggests that the city could expect to receive about half of these new child care funds. Even if these new TANF funds become available, however, full implementation of the Mayor's universal work plan would still require a major infusion of city funds.

Figure 3-3.
Declining Family Assistance Caseloads…

Number of FA recipients

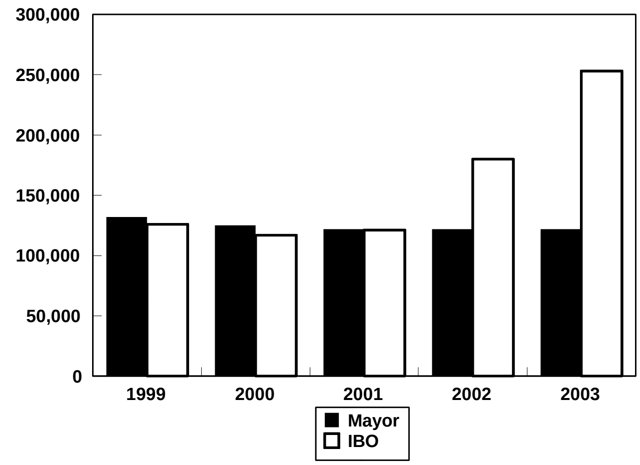


SOURCE: Independent Budget Office.

NOTE: Prior to 1998, Family Assistance was known as Aid to Families with Dependent Children.

Figure 3-4.
…But Rising Safety Net Assistance Needs

Number of SNA recipients



SOURCE: Independent Budget Office.

NOTE: Prior to 1998, Safety Net Assistance was known as Home Relief.

IBO projects that both total and city expenditures for public assistance grants will run somewhat below the Mayor's projections through 2001. However, we expect the impact of the five-year limit on federal assistance to cause city expenditures to exceed the Mayor's projections by $5 million in 2002 and $44 million in 2003. This results from the movement of recipients from FA (city shares 25 percent of costs) to the non-federally funded SNA program (city share is 50 percent of costs).

Medicaid

- IBO's forecast of Medicaid spending at the Human Resources Administration (HRA) exceeds the preliminary budget estimate by $76 million in 2000.
- Proposed changes in federal and state policy that would reduce city Medicaid spending are unlikely to be approved.
- A disagreement between the state and federal governments over a patient's right to fair hearings prolongs the delay of Medicaid managed care.

Despite delays in implementing Medicaid managed care, the budget anticipates considerable savings in Medicaid expenditures. Nevertheless, the city's share of Medicaid spending is likely to exceed the amounts forecast. The budget assumes changes in state and federal policies that would translate into savings for the city, but such initiatives have not been successful in the past and are unlikely to be enacted for 2000.

Mayor's projections. The budget projects that city Medicaid expenditures at the Human Resources Administration will increase by 1.7 percent in 2000 to $2.3 billion, with an average annual increase of 4.1 percent from 2001 through 2003. These estimates do not reflect savings that would occur if the federal and state governments adopted policy changes proposed in the budget (see below for a discussion of these initiatives).

IBO's projections. We project that Medicaid expenditures at HRA will exceed the levels forecast in the budget (see Figure 3-5). Based on historical trends, IBO projects that growth in Medicaid costs will outpace those reflected in the budget, especially for 1999 and 2000. For example, the budget anticipates that spending for outpatient care will reach $202 million in 1999 and will grow 3.5 percent in 2000 because of the delay in managed care implementation. In contrast, IBO expects outpatient care will cost $227 in million in 1999 and rise 5.0 percent in 2000 if current spending patterns continue. Similarly, IBO projects that spending on skilled nursing facilities, home nursing, prescription drugs, and personal care will increase more rapidly in the near term than the budget forecasts.

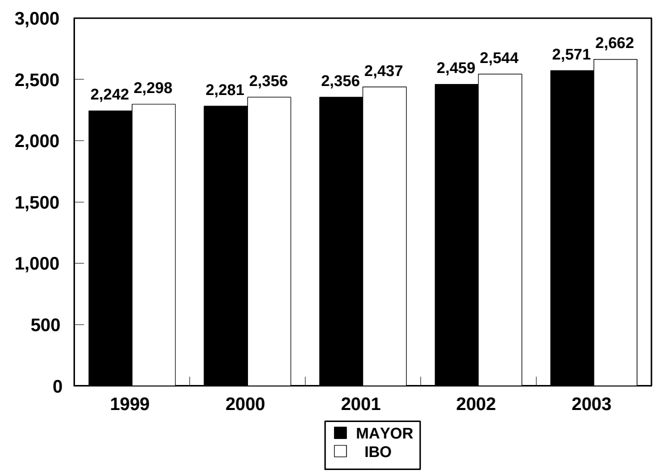
Thus, IBO estimates that overall Medicaid expenditures will rise by 2.5 percent in 2000 to $2.4 billion, and then increase by an average of 4.1 percent annually from 2001 through 2003. While this average growth rate is identical to the rate in the budget, our projections build off a higher base in 1999 and 2000. Accordingly, anticipated spending will surpass the Mayor's estimate by $76 million in 2000, $81 million in 2001, $86 million in 2002, and $90 million in 2003.

State and federal policy. The budget proposes that the federal Medicaid matching rate increase from its current rate of 50 percent to 52.5 percent, a change that would save the city $140 million in 2000. Currently, the matching rate for each state is based on per capita income without adjusting for other indicators such as the incidence of poverty. If a broader measure were used, New York State would receive a higher match. While the current method of determining the matching rate may be unfavorable to New York State, no legislation has been introduced in Congress to alter the current formula. Therefore, the city is unlikely to achieve these savings, at least in the near term.

If state cost containment measures are enacted, the city would save $200 million. These actions include freezing reimbursement rates for hospitals and nursing homes at 1998 levels, fighting pharmaceutical fraud, monitoring transportation expenses, and curbing Medicaid utilization for substance abusers. Although the Mayor proposes working closely with the Governor to pursue these initiatives, it will be difficult to obtain legislative approval in Albany.

Figure 3-5.
HRA's Medicaid Costs Exceed Preliminary Budget Estimates

Dollars in millions



SOURCE: Independent Budget Office.

Another obstacle in the city's efforts to contain Medicaid expenditures is the continued postponement of Medicaid managed care. This July will mark the second anniversary of the Health Care Financing Administration's (HCFA) preliminary approval of New York State's Medicaid waiver, yet there is still no mandatory enrollment of Medicaid recipients into managed care programs. Negotiations between the state and the federal government have reached an impasse over patients' rights to fair hearings. HCFA is reluctant to grant final approval to the state's plan unless it guarantees a patient's right to a fair hearing should the plan deny medical care.

Early intervention services. The New York City Department of Mental Health is proposing to have the Child Health Plus program fund early intervention services for children whose family income falls between 133 percent and 222 percent of the federal poverty level. Early intervention is an interagency program that provides support services for children with developmental delays who are under the age of 3. Currently, early intervention services are funded by a combination of federal, state, and city dollars. Under the proposal, the portion of early intervention services shifted to Child Health Plus would be entirely state and federally funded, resulting in city savings of $10 million annually. However, the transfer is still being negotiated and approval is uncertain.

Anti-Eviction Legal Services

- The Mayor's budget proposes to cut $5 million in city funds for anti-eviction and SRO legal services, resulting in an additional loss of $9 million in state and federal aid.

- These cuts would make it more difficult for the city's poor to secure legal representation when faced with eviction.

The budget proposes to eliminate the Human Resource Administration's (HRA) legal services contracts with non-profit organizations that provide anti-eviction legal services to the poor. The cut would result in savings of nearly $3 million for the city annually. The city would, however, lose nearly $9 million in state and federal matching funds. The HRA program provides legal services for about 10,000 cases annually.

The budget also proposes to eliminate $2 million in anti-eviction legal services programs run by the Department of Housing Preservation and Development (HPD). Unlike the newly proposed cuts in HRA's legal services programs, in recent years the Mayor has routinely proposed cuts to the HPD programs that have been subsequently restored by the City Council.

According to the Administration, the anti-eviction legal services contracts duplicate other HRA programs and contracts. The city's other anti-eviction services, however, seek either to prevent eviction by providing financial assistance to meet rent costs or deal with the after-effects of eviction by preventing homelessness. Where proactive interventions fail and tenants face eviction, there are no service alternatives that provide legal representation in housing court. HRA is developing a plan, which has not yet been revealed, for improving its ability to prevent evictions.

The city's Jiggets program (which remains funded in the budget), provides help to meet rent costs through increased housing grants for qualified families. In his testimony at the preliminary budget hearings, the HRA Commissioner contended that legal service providers spend most of their time completing Jiggets' applications and are less frequently called upon to represent clients in housing court. He also emphasized that HRA already contracts with community-based organizations to assist clients with those applications. Unlike these other services, however, attorneys are required to stay evictions until the Jiggets application and aid determination processes are complete.

Moreover, other HRA and HPD programs do not provide anti-eviction legal services. Homeless Diversion Teams (HDTs) find individuals places to live once they are evicted, but do not work to prevent eviction. The Eviction Prevention Units, non-profit organizations contracted to operate from the city's welfare centers, provide support services and referrals, but not legal representation. Other types of legal services that exist for financially needy populations are not housing-related services and therefore may not necessarily take on cases that anti-eviction legal services providers currently handle.

Children's Services

- The Mayor's budget proposes to cut $18.1 million in city, state, and federal funds from homemaking services.

The budget proposes a 66 percent cut to the Administration for Children's Services' preventive homemaking services program. Homemaking services are funded by a combination of city, state, and federal dollars. Under the proposal, the city would eliminate $4.6 million in city, $5.3 million in state, and $8.2 million in federal funds. The program provides homemaking services to families involved with the child welfare system that need assistance due to a family member's disability. According to the Mayor's Management Report, there were 1,341 homemaking cases in 1998.

The budget proposes to reallocate the $5.3 million in state funds cut from the homemaking program, along with other funds, to increase the city's contracted foster care budget. The Mayor is proposing that the state provide an additional $18.1 million in new funds through the Family and Children's Services Block Grant (FCSBG)—the main source of state child welfare funds—in order to restore full funding to the homemaking program. Under the Mayor's plan, however, if the state does not provide the additional $18.1 million, the city will not step in to restore the 66 percent cut, leaving the homemaking program to operate at the reduced budget level.

There is no evidence at this time to suggest the state will provide the additional funds. Since the creation of the FCSBG in 1995, the city has seen significantly fewer child welfare dollars than would have been available under previous formula grant sources. As a result, there are already a host of child welfare programs competing for scarce dollars. In addition, the Governor has already proposed a 3 percent, or $15 million, statewide increase to the FCSBG for 2000. The city's share of the increase is expected to be $9.4 million and according to the state, the funds are already targeted for compliance with fire regulations and cost of living increases for agency personnel.

Funding for two other prevention programs was also eliminated—$5.8 million for Beacon schools and $500,000 for a specialized program targeting youth.

Youth Services

- The Mayor's budget proposes to eliminate the city's contribution to the Youth Development and Delinquency Program, thereby cutting the overall YDDP budget nearly in half.
- Removal of all city funds from the After Three program, financed with a matching grant from George Soros, would leave the future of the program in question.

The budget calls for a cut of $19.7 million in city funds for youth services, primarily made up of $8.5 million from the Youth Development and Delinquency Program (YDDP), $5.6 million from councilmember and borough president discretionary funds, and $5 million from an after school program known as After Three. The reduction, which represents 17 percent of the Department of Youth and Community Development budget, is the largest proposed since the 1996 budget season. Aside from the cuts, the budget also adds funds to extend the Citizenship NYC program.

The reduction in the YDDP budget would eliminate all city funds from the program, cutting it nearly in half. The city is not required to match state funds and, under the proposal, $10.5 million in state funds would remain in the budget. YDDP is the primary funding source for youth services; the city holds contracts with 330 community based organizations citywide to provide youth programming. Current YDDP contracts will end June 30, 1999.

The budget proposes to eliminate $2.6 million traditionally provided to the City Council to use on youth programs in each councilmember's district. Numerous youth programs run by community-based organizations receive small sums to sustain themselves through this funding mechanism. Similarly, borough presidents receive discretionary monies for use according to individual borough needs. Borough presidents are slated to lose a total of $3 million in discretionary funds, or 11 percent of their collective budgets.

The proposed $5 million cut to After Three would eliminate all city funding for the program starting in 2000. In the current school year, the program's first year, city funds were combined with $6 million from other public and private sources to match $10 million donated by financier George Soros for after school programs in 25 schools. Soros has indicated he is willing to give an additional $12 million to expand to 100 schools for next year. In June 1998, Soros initially proposed to support after school programming by offering up to $25 million annually for five years, provided each dollar was matched 3-to-1 with public and private funds. It is not clear what would happen to the program or Soros' support if the city does not fund its portion.

The proposed addition of $3.7 million would fully fund the Citizenship NYC program, which began in July 1997, for another year. The program assists immigrants in becoming American citizens. It is expected to serve about 13,000 people, or about 14 percent of the city's 94,000 immigrants who are likely to be eligible for citizenship.

Education

Education comprises roughly 28 percent of city spending—a projected $11.6 billion by 2003. About 96 percent of education spending is attributable to the Board of Education, with the remainder allocated to the City University of New York (CUNY).

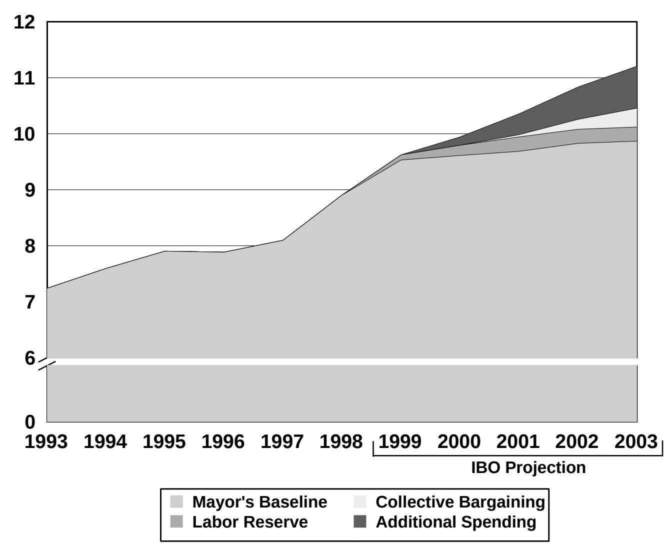
This section begins with an overview of the Board of Education (BOE) budget, highlighting several factors contributing to spending growth. The focus then turns to the Governor's budget and its impact on state education aid for the city, followed by a discussion of the recently enacted Charter Schools legislation. The section continues with an analysis of the Board's $11.2 billion capital plan for 2000-2004. The last item pertains to CUNY, particularly the budget of the university's six community colleges.

Board of Education

- Board of Education spending has grown rapidly during the last two years as thousands more teachers have been hired.
- The Mayor proposes to extend the city's commitment to Project Read, Project ARTS, and summer camps.

Figure 3-6.
Board of Education Spending Continues to Rise

Dollars in billions



SOURCES: IBO; Mayor's Preliminary Budget for 2000; Comprehensive Annual Financial Reports of the Comptroller, 1993-1998.

NOTE: Total expenditures do not include intra-city sales.

- IBO's forecast of education spending exceeds the estimates contained in the preliminary budget due to differences in projected expenditures for city and state initiatives, above and beyond differences in accounting for collective bargaining agreements.

Budget overview. IBO estimates that under the Mayor's preliminary budget, Board of Education (BOE) spending will be $9.9 billion in 2000, an increase of $340 million over the estimated 1999 level. Spending will grow at an average annual rate of 3.9 percent during the financial plan period, reaching $11.2 billion in 2003.

By comparison, the Mayor projects total spending of $9.6 billion in 2000 and $9.9 billion in 2003 (see Figure 3-6). Some of the variation between IBO's projections and the preliminary budget stems from differences in accounting for collective bargaining agreements.[15] The remaining gap between the two forecasts, about $150 million for 2000 and $753 million for 2003, is attributable to differing assumptions about costs of baseline spending and new initiatives, and differing enrollment and headcount projections. To forecast education spending, IBO employs an econometric model incorporating the historical relationship between actual expenditures and enrollment and staff levels.

Recent growth in spending. In the last two years, BOE spending has grown at an annual rate of 8.9 percent (see Figure 3-7). This expansion follows a period of several years during which BOE spending barely kept pace with inflation. Growth in spending has been due in part to the cumulative impact of enrollment growth coupled with improved teacher recruitment efforts to fill vacancies. Another important factor propelling spending has been state and local pressure to improve student performance, which has led the Board to devote more resources to instruction, especially for early childhood and arts programs. As a result, pedagogical staff has increased from 80,900 to 88,800 during the last two school years (see Figure 3-8). IBO projects that under the Mayor's budget, pedagogical headcount will continue to rise but at a more moderate rate, approaching 93,000 employees by 2003.

Enrollment growth has slowed. Preliminary data from the current school year indicates that overall enrollment has leveled off. Total enrollment increased steadily from 1990 to 1997, adding roughly 20,000 students per year. Since 1997, however, enrollment has increased by only about 5,000 pupils (not counting 13,600 4-year-olds entering the system for universal prekindergarten).

Figure 3-7.
Average Annual Change in BOE Spending

	Nominal	Real
1993-1997 (actual)	2.8%	0.3%
1997-1999 (IBO projection)	8.9%	7.6%
1999-2003 (IBO projection)	3.9%	1.8%

SOURCE: Independent Budget Office.

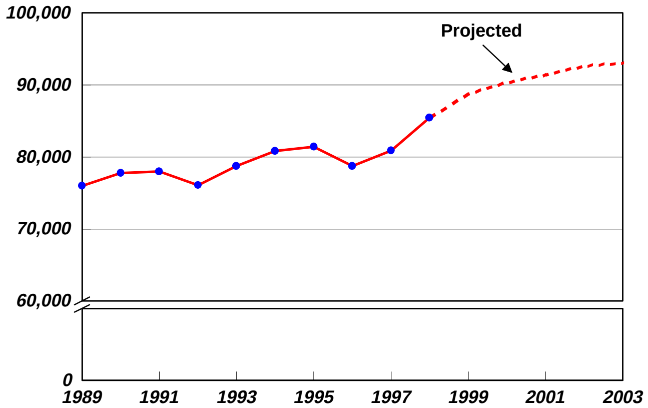
The Board expects general education enrollment to increase by less than 3,000 students per year (0.2 percent) through 2003, while full-time special education enrollment is anticipated to increase more rapidly, adding more than 1,000 pupils (1.2 percent) per year.[16] This projected growth in special education may be overstated because the Board faces mounting pressure from the federal and state governments to place students in the least restrictive environment and may lose intergovernmental aid if it fails to limit special education referrals. BOE spent an average of $22,600 per full-time special

[15] IBO's spending projections include the money needed to fund the Board's current collective bargaining agreements. In contrast, the preliminary budget accounts for these funds in its labor reserve. Moreover, we assume that the next round of contracts, which will take effect in January 2001, will increase salaries at the rate of inflation. The preliminary budget includes no provision for raises after the current contracts expire.

[16] Census data, published in March, reveals higher than anticipated NYC population growth in 1998, suggesting the potential for a resumption of more rapid increases in school enrollment.

Figure 3-8.
Number of Teachers Increasing

Number of pedagogical employees



SOURCES: IBO; Comprehensive Annual Financial Reports of the Comptroller, 1989-1998.

NOTES: Includes teachers, principals, assistant principals, guidance counselors, psychologists, social workers, school secretaries and others. Excludes universal prekindergarten teachers.

education pupil in 1998, more than triple the $6,700 per pupil spent on general education.

Funding of high profile initiatives. The Mayor's budget presentation highlighted several ongoing programs to enrich the curriculum, strengthen standards, and extend instructional schedules. The proposed budget would expand or extend the Board's commitment to several of these initiatives including Project Read, Project ARTS, and Break-Aways. The Mayor also highlighted several programs, including Project Smart Schools, expanded summer sessions, and Post-5 night schools, which have been added to the budget in recent years and whose funding will continue at planned levels.

Project Read, an intensive literacy program serving young, academically at-risk students, had been funded a single year at a time. The Mayor's budget proposes to make the program ongoing, by extending the current funding of $125 million to each year in the financial plan. Since 1998, Project Read has offered three types of literacy training for students in grades 1-3. Roughly 80,000 pupils receive six hours of after-school lessons per week, while 50,000 students receive intensive instruction in small groups during the regular school day. In addition, students and parents in over 400 schools participate in family literacy workshops.

Project ARTS, phased in over three years, is restoring visual arts, dance, music, and theater instruction throughout the school system. Conducted in partnership with the city's cultural institutions, the program received $25 million in 1998 and $50 million in 1999. The budget proposes to increase annual funding to $75 million beginning in 2000.

The preliminary budget provides $10.4 million for Break-Aways summer camps, a fourfold increase over the $2.4 million provided last year to a pilot program. The program engages students in grades 4 to 8 in academic and recreational activities in outdoor settings. The program began in summer 1998 with 1,500 students attending residential and day camps and will expand to 4,000 campers in 1999 and to as many as 10,000 by 2001.

Established in 1998, Project Smart Schools has been equipping classrooms in grades 6-8 with computers. With capital spending of $150 million nearly completed, the Mayor's proposed budget includes $22 million in expense budget funds for professional development and technical support in 2000. These operating funds for 2000 were added to the financial plan last year.

The Board has been devoting increasing resources to summer instruction. The number of K-8 participants jumped from 30,000 in summer 1996 to 105,000 in summer 1998, with a total cost of $65 million. The K-8 programs focus on literacy and meet for a minimum of 25 days for at least five hours per day. Summer high school has also expanded as standard subjects and vocational training together attract more than one out of every three students in grades 9-12. The Board's concentration on summer instruction will intensify in 1999 as participation becomes mandatory for an estimated 52,000 students in grades 3,6, and 8 who do not meet standards for promotion. Although the Mayor's budget includes $25 million for ending social promotion that was added last year, no additional funds have been allocated to handle the record number of students expected in class this July and August.

The Board has also expanded its options for older students by opening young adult centers offering evening courses in each of the five boroughs. These high schools offer diploma programs for students who have already completed five years in other high schools. The preliminary budget includes $9 million for the post-5 night schools in 2000, money first budgeted in the financial plan last year.

Funding of state initiatives. The Board is currently participating in the first year of a state initiative to make prekindergarten classes available to all 4-year-olds by 2002. The program is scheduled to expand rapidly, serving 29,000 students in the next year and as many as 97,000 by 2002. Sufficient state funding to accomplish that goal, however, is uncertain. (See section on Governor's education proposals below and IBO's *Fiscal Outlook* report.) IBO's projections assume a state aid commitment of $2,000 per aidable prekindergarten pupil and a BOE commitment of $8 million per year—the minimum resources available under current policy.

Beginning in 2000, BOE plans to participate in a new state program that provides money to reduce class sizes to an average of 20 students in kindergarten through grade 3 over a three-year period. In New York City, average class sizes for those grades currently range from 24 to 26 students. In accordance with BOE planning, IBO's projections assume that the Board will implement class size reduction in 75 percent of city schools by 2002. As with universal prekindergarten, the Governor's executive budget proposals cast doubt on the availability of sufficient funding for class size reduction.

Expense budget surplus. As of February, the Board has identified $116 million in surplus 1999 funds that it intends to roll into 2000. Based on recent history and IBO's budget projections, that figure will likely grow by the end of the fiscal year. The Board ended 1998 with an expense budget surplus of $301 million, of which $300 million was rolled into 1999. The roll consisted of two components: 1) $259 million in city funds and unrestricted state aid; and 2) $41 million in restricted state aid and federal funds. Potential strategic uses of this year's surplus include replacing terminated state grants, funding pay-as-you-go capital projects, and supporting the Chancellor's budget request.

Chancellor's budget request. The Chancellor's budget request, which was released after the preliminary budget but in time to influence the executive budget, follows many of the themes discussed above. The Chancellor has asked for $718 million in additional expense budget funding above resources already identified. For example, the Chancellor requests increased funding to help students achieve higher standards, such as $19 million in city funds to develop a long-term strategy to improve middle school student performance and $35 million in city and state funds to help high school students fulfill tougher Regents graduation requirements. The Chancellor also proposes $20 million in city and private funds for Fit for Life, a proposed program that would increase student participation in physical education and sports. The Chancellor's budget asks the state to maintain programmatic grants for universal prekindergarten, class size reduction, and minor maintenance, and to restore teacher support aid. Finally, the Chancellor requests $169 million from both the city and state to fund local needs identified by 36 superintendents and 778 schools.

Governor's Proposals for BOE

- The Governor proposes retreating from prior commitments on universal prekindergarten, class size reduction, and minor maintenance aid.
- A proposed replacement block grant would leave the city with $63 million less than expected for the three programs in 2000.

After two years of significant increases in state aid, the trend may be reversed in 2000. In his executive budget, the Governor proposes substituting an Educational Improvement Block Grant for what had previously been dedicated funding for three programs—universal prekindergarten, early class size reduction, and minor maintenance aid. Although the block grant would allow the city greater flexibility in spending these funds, the $77 million the city would receive in 2000 under the Governor's proposal is $63 million less than the $140 million that had been expected for these programs. (See Figure 3-9.)

Under a multi-year spending agreement enacted in 1997, the state promised grants to localities for the prekindergarten and class size reduction programs. The education agreement was reached in the same year that the state committed to property tax relief under the School Tax Relief (STaR) program and the two were generally seen as a package deal.

The universal prekindergarten program—scheduled to be phased in over four years beginning with the 1998/99 school year—is intended to make publicly funded prekindergarten available to all 4-year-olds. Nearly 14,000 city students are participating in the current year, and the number is expected to grow to as many as 97,000 by 2002. Under the 1997 agreement, the city is slated to receive $58 million from the state for the program in 2000 and $194 million by 2002. Even without the Governor's proposal, the state funding for the prekindergarten initiative for 2000 to 2002 is not sufficient to allow the city to maintain this year's total per student spending, as the number of students grows to meet the state's participation targets. In IBO's *Fiscal Outlook* report, we estimated that the Board would need to spend an additional $49 million in 2000 and $165 million in 2002, if it wanted to maintain the same level of resources put in place for this school year.

Figure 3-9.
Impact of State Education Improvement Block Grant on NYC

Dollars in millions

	State Fiscal Year 1999-2000	2000-2001
Expected State Aid to NYC Prior to Block Grant		
Universal Prekindergarten ($2,000/pupil)	58	128
Class Size Reduction (estimated)	49	91
Minor Maintenance (statutory amount)	33	53
Subtotal of Individual Grants	140	272
Educational Improvement Block Grant (proposed)	77	unknown
Estimated Impact of Block Grant on NYC	-63	unknown
Unfunded Universal Pre-K (add'l $1,700/pupil)	-49	-109
Estimated NYC Shortfall	-112	unknown

SOURCE: Independent Budget Office.

Under the class size initiative component of the 1997 agreement, state funds are provided to school districts to cover the operating costs (primarily teachers' salaries) associated with reducing average class sizes in kindergarten through third grade to 20 students. The program is to be phased in over three years beginning with the 1999/2000 school year. Given the city's unusually large class sizes, however, the Board is aiming to reach the target in about 75 percent of its schools by 2002. Based upon the 1997 agreement, BOE expects to receive $49 million in state aid for class size reduction in 2000 and $146 million by 2002.

Including the $33 million expected under the minor maintenance grant, the funds expected by the city under these three programs total $140 million in 2000—$63 million more than would be available in the $77 million block grant. Although the Governor's budget provides no information on the size of the block grant beyond 2000, the loss to the city would likely be even greater over time because the city had expected receipts for the three programs to almost double from 2000 to 2001 and to grow further in 2002. In addition, if the Governor's proposal is adopted, federal funds intended to supplement class size reduction efforts may be jeopardized.

Finally, the Governor proposes to eliminate $66 million in annual categorical aid currently provided to the city ($30 million in reading aid and $36 million for improving pupil performance aid) and replace it with $58.4 million for a new early grade literacy program (EAGLE). If adopted, the change would take effect for the 1999/2000 school year.

Charter Schools

- New York State law permits creation of 100 new charter schools plus an unlimited number of conversions of existing schools that will be exempt from some regulations and oversight.
- The Board of Education is developing plans for charter schools in New York City.
- Charter schools may add to the fiscal stress already faced by the city's public schools.

New York State charter school law. Enacted in December 1998, the new law outlines a process by which 100 charter schools can be created statewide and an unlimited number of existing public schools can be converted to charter status. The hope is that charter schools, which are public schools free from many of the rules of the central bureaucracy, will raise student achievement through innovative teaching and expanded opportunities and choices. Advocates of charter schools maintain that even students who remain in regular public schools will benefit as charter schools compete with regular schools for both students and the budget dollars associated with them. Some educators and public school advocates are concerned, however, that charter schools pose a significant threat to public school budgets and yield achievement gains that are only illusory.

New and conversion charter schools. Parents, teachers, administrators, businesses, and community groups may apply to State University of New York (SUNY), the Board of Regents, or a local school board (the Schools Chancellor in New York City) for approval to create up to 100 new charter schools, statewide. Once an application is approved, the Board of Regents is authorized to issue the actual charter, 50 of which are to be recommended by SUNY. Charters are authorized for up to five years and may be renewed in five-year increments.

While private schools are explicitly prohibited from becoming charter schools, existing public schools can convert to charter status and are not included in the 100-school limit. In order for a school to convert, the parents of a majority of the students enrolled in that school must vote in favor of conversion and an application must be submitted for approval. In the case of New York City, only the Chancellor can approve a conversion.

Implementation. While charter schools are free from some regulations, they are not completely autonomous. All charter schools, including those with a special focus, must meet state student performance standards. None are allowed to apply selective admission criteria or charge tuition. While public per pupil funding from the city and state will be a major source of operating funds, charter schools will be free to solicit private money to supplement the public grants; other than per pupil funding, charter schools can use any financing source to construct or lease facilities. Finally, the charter school legislation largely preserves the union presence in the schools. For example, large new charter schools (more than 250 students) and all conversion charter schools will be subject to existing labor contracts. Many details remain to be worked out as the city goes forward with charter school implementation, ranging from how attendance will be reported to how (if at all) Title I funds will be collected in the first year.

Charter school proposals for New York City. The Chancellor has proposed several ways for the city to get involved in charter schooling. His initiatives include converting a number of existing schools to charter status, establishing model districts (where schools would be given increased autonomy but retain BOE status) and creating several new, industry-specific charter schools (in music, business, automotive technology, and animation arts). Some of the conversions may be completed as early as September 1999. The first new charter schools are scheduled to open in September 2000.

Budgetary implications. The Mayor has proposed spending $2.5 million per year on charter schools in 1999 and 2000, most of which would go to support local efforts to start charter schools. The budgetary impact will grow much larger if charter schools are successful in attracting students away from BOE schools. Total BOE resources would be reduced, as funding follows students to charter schools. With reduced resources, it may be harder for the Board to compete with charter schools by improving the quality of education it offers. In addition, if those drawn to charter schools are disproportionately students with greater ability or motivation, the average cost associated with improving academic achievement in BOE schools, both to make them competitive and to meet new state standards, will rise. Until we know how successful charter schools are at attracting BOE students, and the type of students attracted, it is unclear how significant the fiscal impact of charter schools will be. However, there is the potential for significant fiscal stress if, as pressure mounts to raise public school achievement, budgetary resources are being lost to the charter schools.

BOE Capital Plan for 2000-2004

- The proposed five-year capital plan calls for $11.2 billion to repair and build school facilities. The plan relies on various funding sources, some of which are uncertain.
- Innovative proposals to leverage tobacco settlement proceeds and state aid could provide some of the financing.
- The Board's capital plan, while unprecedented in its scope and expense, will not completely solve the problem of overcrowding or restore all buildings to a state of good repair.

Overview. In November 1998, the Board of Education released the preliminary version of its capital plan for 2000 to 2004. After soliciting comments in a round of public hearings, the Board is revising the plan and expects to complete its work in late March, at which time the plan will be sent to the Mayor and the City Council for final approval. The plan, now expected to cost $11.2 billion, would increase capacity by at least 75,600 seats (including 44,900 in 64 new schools) and fund a wide variety of rehabilitation and repair projects for hundreds of existing schools.[17]

The capital needs of the city's public schools are daunting, as the system has been struggling to absorb enrollment increases (over 140,000 students since 1990) in facilities that are often outdated—the majority of buildings were constructed before 1950—and in a poor state of repair. In recent years, several new factors have exacerbated the Board's facilities problems, including court orders

[17] The new capacity figures are based on a November plan that will be amended as a result of the comment and review process. The Board has indicated that the final plan will include additional construction in Community School Districts 21, 27, and 31.

compelling the Board to fix hazardous conditions, state initiatives to expand pre-kindergarten classes and reduce class sizes in early grades, and new Regents requirements for additional science labs. Given the extent of the problems, the Board's plan—despite being far more expensive and ambitious than previous ones—will still not solve the problem of overcrowding in all parts of the city, nor will it restore all buildings to a state of good repair.

Significant questions have been raised about components of the capital plan, including the priority given to new construction, BOE's ability to actually manage such a vast effort, and the criteria used in selecting projects. A crucial budgetary issue is the viability of proposals for financing the plan. While some of the proposed funding sources are fairly secure, others are more speculative. If major pieces of the funding puzzle fall through, as was the case with the previous capital plan, the Board and the Mayor would need to identify alternative funds or pursue a less ambitious capital agenda.

City contribution. City capital contributions, at $6.1 billion, are the biggest funding source in the plan. Even though the Mayor's 10-year capital strategy assumes that level of spending can be provided, the city may be hard-pressed to deliver, due in part to limits on the amount of outstanding city debt imposed under the state constitution. (See page 47 for more on the debt limit). In addition, both the Mayor and City Council Speaker want to use tobacco settlement payments to finance a portion of the city's $6.1 billion contribution. The Mayor has proposed issuing bonds backed by the settlement proceeds that would be exempt from the debt limit, while the Speaker has proposed using the settlement to fund pay-as-you-go capital spending. (See page 17 for more discussion of tobacco settlement payments).

State building aid. The plan also calls for raising $2.6 billion by selling bonds backed by anticipated state building aid funds. Building aid is credited as BOE revenue, so securitizing a portion of the aid that the Board receives for approved construction projects would create a hole of $185 million per year in the operating budget. The Board plans to use expected increases in building aid to fill that gap. Building aid is projected to grow because of changes in the formulas that benefit the city. In addition, BOE will receive more building aid because the formulas are driven by the amount of capital spending undertaken by a school district. Therefore, as the city spends more under the capital plan, it can expect to receive more building aid. The Board projects that enough enhanced aid would be generated by the third year of the plan to cover the $185 million needed for anticipated annual debt service on these bonds.

This proposal to leverage the benefits of more capital spending raises several concerns. First, using anticipated building aid that is already included in the Board's baseline budget to service new bonds means that those funds would not be available for capital investments in later decades, although the Board is assuming that enough new aid would result from the leveraging to offset the loss. Second, the building aid formula can be counted on to provide the new revenue needed to cover the debt service only if the formula is not changed in the future. Given that the state makes annual changes to school aid formulas, with the primary focus on the total amount of aid rather than on individual types of aid, this assumption may not hold. Third, the amount of aid that can be leveraged will depend on how much of its $6.1 billion commitment to the capital plan the city ultimately funds. Because $6.1 billion is an ambitious figure, especially in light of the city's continuing problems with its debt limit, there is reason for concern. Finally, proceeding with this proposal would require the enactment of state legislation and approval by the City Comptroller.

Expense budget savings. A third funding source outlined in the plan is $750 million in operating budget savings ($150 million per year for five years). Some of these savings—a total of $195 million—would be required to fill the operating budget gap in the first two years of the plan created by capitalizing building aid. The remaining $555 million would be used for pay-as-you-go capital. Although the Board's recent history of recurring surpluses may offer some grounds for such optimism, it is risky to build a capital plan on savings that depend on future expense budget efficiencies or surpluses. Recognizing this risk, the plan states that the pay-as-you-go projects could be postponed if unanticipated budget gaps occur during the five-year period.

Other funding sources. The remaining funds identified in the plan are from federal and state sources; many are risky because they would require significant policy changes in Albany and Washington. The funds least likely to materialize include $400 million in payment of prior-year state aid claims (funding for which has not been appropriated by the state), $300 million in savings from repeal of the Wicks Law, and $160 million in federal Qualified Zone Academy Bonds.[18]

The plan counts on $70 million in state funds, earmarked under the Clean Water/Clean Air Bond Act of 1996, for conversion of coal-fired boilers in schools. Those funds, in contrast, are considered secure.

Preventative maintenance. The proposed capital plan includes a strategy to devote greater resources to preventative maintenance in school facilities. The City Comptroller estimates that the Board spends only one-tenth of the maintenance dollars that would be spent under private industry standards.[19] Maintenance has historically been underfunded; it is generally considered low priority during the budget process because spending in most other educational policy areas is prescribed by federal and state regulations.

According to the Board, $122 million in the 1999 expense budget has been allocated to preventative maintenance, including $33 million in minor maintenance aid from the state. The Board's strategy would boost maintenance spending in the expense budget to $274 million by 2004—a large improvement over the status quo, albeit much less than would be required to keep education facilities in a state of good repair. Fulfilling this strategy may be difficult, however, because it depends on additional building aid growth above the amount needed to finance capital expenditures.

The budget does not include additional funds for school maintenance, perhaps because the Board's capital proposal has not been finalized. Moreover, the Governor has proposed folding the minor maintenance aid into a block grant at a considerably lower level, a move that would likely impede the Board's facilities strategy (details of the Governor's budget are provided in a separate section). Other than asking the state to restore minor maintenance aid, the Chancellor has omitted maintenance funding initiatives from his budget request.

CUNY Community Colleges

- CUNY increasingly relies on tuition revenue because the city subsidy has shrunk to 23 percent of the community college budget.
- Despite increased need for financial aid, the Mayor and the Governor seek to reduce student scholarships and grants.

Budget overview. IBO estimates that the Mayor's proposed budget for the City University of New York (CUNY) would result in total spending of $407 million in 2000, a reduction of $5 million from the estimated 1999 level, and then rise at an annual average rate of 1.1 percent from 2000 to 2003. The budget would provide $331 million for

[18] The $400 million in prior-year claims were approved by the State Education Department but not booked by the Board or City Comptroller as receivables because of the backlog of other prior year claims. Therefore, if appropriated, the $400 million would be available for pay-as-you-go capital spending in the city. The $400 million is separate from the set of prior-year receivables which had been booked by the city but which are now being written off by the City Comptroller after they remain unpaid for ten years.

[19] New York City Comptroller, *Dilemma in the Millennium: Capital Needs of the World's Capital City*, August 1998, p. VIII-6.

CUNY's community colleges, not counting pension contributions. In addition, $67 million in state and city funds would be allocated to the senior colleges, and $9 million to public schools for the gifted sponsored by Hunter College.

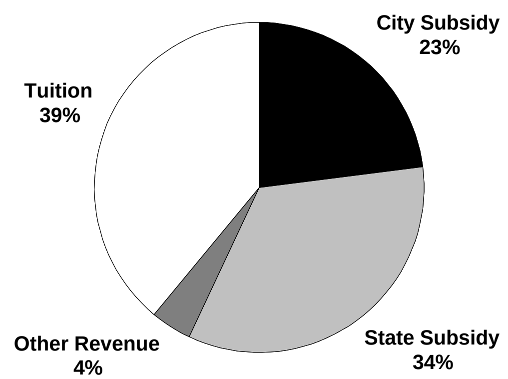
The slow projected growth, below the inflation rate, is partially attributable to the city's decision not to fund collective bargaining settlements for the community colleges. Although the CUNY budget does not provide funds for increased labor costs, the university still must pay salary and wage increases already negotiated with its unionized employees. In response to this budget constraint, the CUNY administration has testified before the City Council that it would reduce instructional and other services.

Reforms. New York City currently subsidizes 23 percent of the budget for the six CUNY community colleges (see Figure 3-10).[20] The city share has fallen from 43 percent in 1989, leading to an increased reliance on tuition and therefore an increased need for student financial aid. Nevertheless, both the Mayor and the Governor in their budget proposals seek reductions in financial aid grants. The Mayor would eliminate a $7 million merit scholarship program presently benefiting 4,000 CUNY students who graduated from high school with at least a "B" average.

Meanwhile, the Governor's executive budget proposes reducing the maximum Tuition Assistance Program (TAP) award from the present 90 percent of tuition to 75 percent and restricting TAP eligibility to only those students taking 15 or more credits per semester. Eligibility for associate's degree students would be capped at four semesters instead of the current six semesters. The Governor would create a new tuition rebate, payable upon graduation, to students completing an associate's degree within two years or a bachelor's degree within four.

Figure 3-10.
Tuition Exceeds State or City Subsidy

1999 CUNY Community College Budget



SOURCE: Independent Budget Office.

NOTES: City subsidy includes pension contributions. Other revenue includes private grants, adult and continuing education fees, rental income, and sundries.

While these TAP changes would affect students across the state, they would hit CUNY students, many of whom are older and poorer than traditional college students, especially hard. More than two-fifths of CUNY undergraduates come from households with incomes under $20,000, a majority work full or part time, and many are single parents. Thus, it is not surprising that less than 5 percent of CUNY associate degree candidates attempt enough credits to make it possible to graduate within two years. CUNY estimates that TAP awards to its students would decline from $129 million to $30 million under the Governor's proposals.

IBO will continue to monitor several ongoing policy developments that may soon have an impact on the CUNY budget. The CUNY Board of Trustees voted in January to prohibit students requiring remedial instruction from matriculating in bachelor's degree programs at senior colleges, a

[20] CUNY advocates often contend that the city is betraying its obligation to subsidize one-third of costs based on an expectation that the city, state, and tuition fund equal shares. The state education law for full opportunity institutions such as CUNY, however, permits the city to pay less than one-third provided that it maintains its nominal dollar contribution from the previous year.

move that is expected to decrease total CUNY enrollment and therefore reduce tuition revenue. Implementation may be delayed because the State Education Commissioner has indicated that under the law, CUNY cannot implement its plan until the policy is approved by the Board of Regents.

Another policy change with significant fiscal impacts is the Mayor's proposal to develop a voucher program that would allow students to use public funds to enroll in remedial courses at private institutions. Although the Mayor's budget presentation highlighted this initiative, the details have not yet been publicized. Finally, the Mayor's Advisory Task Force on CUNY will issue its recommendations this Spring, following a year-long study. The task force has been auditing the university's use of city funds and examining options for privatizing remedial studies, among other duties.

Uniformed Services

About 15 percent of city spending funds uniformed services activities, such as police, corrections, fire, and sanitation. In the following section, we take a closer look at the budget of two uniformed services departments—Police and Sanitation. For the New York City Police Department (NYPD) we consider the Mayor's plan to accelerate the hiring of additional police officers, and for Sanitation we examine the adequacy of the city's budgeting for waste disposal given the planned closure of the Fresh Kills landfill.

Police

- The preliminary budget includes a proposal to hire almost 1,600 new police officers six months earlier than previously planned, bringing police staffing levels to an all-time high.
- While the city's build-up in the size of the police force since 1990 has been accompanied by a very dramatic drop in crime, inter-city data reviewed by IBO raise questions as to the precise relationship between police staffing and crime reduction.
- A recent study by the City Comptroller reports the city could save several million dollars each year by converting 1,200 positions held by police officers to civilian jobs.

Acceleration of police recruit class. The budget includes $32 million in city funds for the purpose of accelerating by six months the hiring of 1,589 NYPD recruits, previously scheduled for the first day of fiscal year 2001. Hiring the new officers would elevate police staffing in the city to an all-time high of 40,915 by January 1, 2000.

How many officers are needed? As reported in *New York City's Fiscal Outlook,* issued by IBO in January, police staffing in New York City has increased by over 20 percent since 1990, with the city now having about 54 police officers per 10,000 citizens—a per capita level of staffing significantly greater than the average ratio of 28 police officers per 10,000 residents in other large U.S. cities. Meanwhile, New York City has enjoyed a dramatic 50 percent decline in serious crime, a drop larger in both absolute and percentage terms than in any other major city.

While it is reasonable to assume that the increase in our police force's size has played a significant role in the city's declining crime rate, our survey of comparable data from across the country indicates that the precise relationship between police staffing and crime levels is not well established. That is, although many other American cities have also opted to increase police staffing, it is noteworthy that some cities have enjoyed significant declines in crime with no increases or even *decreases* in per capita police staffing. For example, San Diego was one of a few major American cities (besides New York) to enjoy a drop in its crime rate of more than 40 percent between 1990 and 1997, but that city accomplished its crime reduction with virtually no increase in per capita police staffing.

Meanwhile, the rate of serious crime fell by 40 percent and 25 percent in Dallas and Denver, respectively, although per capita police staffing in both of those cities actually declined by 3 percent.

As impressive as New York City's drop in crime has been, these trends have led IBO to consider whether significant productivity differences exist between police agencies in major American cities. For example, cities such as San Diego and San Jose (both among the nation's 20 most populous cities) have crime rates nearly as low or lower than New York City, yet on average police officers in the former two cities make significantly more arrests per year than do their New York City counterparts. More precisely, police officers in San Diego and San Jose made 28 and 30 arrests in 1996, as compared with 17 arrests per officer in New York City.

Civilianization. The City Comptroller recently released a report indicating that the city could realize about $36 million in annual cost savings by staffing 1,257 positions currently occupied by police officers with less costly civilian personnel.[21] Although the Comptroller's recommendations would result in a decrease in the department's total uniformed headcount, the number of police personnel directly engaged in law enforcement activities would not be diminished.

The NYPD responded that the report's projected cost savings were overstated, in part due to inclusion of an unspecified number of positions that the NYPD contends should remain staffed by uniformed personnel. Also of significance was NYPD's response that any diminution in overall uniformed headcount within the NYPD would violate conditions attached to federal Crime Bill funding currently received by the agency.

Spending forecast. Based on our estimates, adoption of the budget would result in NYPD spending just under $3.0 billion in 2000, about $104 million more than estimated in the budget. Our higher estimate is in large part attributable to projected overtime expenditures above those funded in the budget. From 1999 through 2003, we project NYPD spending will increase by an annual average rate of 3.8 percent, with salary increases the most significant factor associated with the rise in spending.

Sanitation

- The city has not budgeted realistically for waste export costs that would result from closing the Fresh Kills landfill in 2002.
- Political concerns in other states may hamper New York's plans for waste export, potentially increasing costs.

The Fresh Kills landfill is scheduled to close on December 31, 2001, after which the city will need to export or recycle all of its solid waste. The Department of Sanitation has planned for its closure by evaluating proposals for export from waste disposal firms and returning to weekly collection of recycling. Without any other landfills in the five boroughs, we estimate the city would need to export roughly 3.3 million tons of refuse costing about $70 per ton, or $230 million annually in 2002 and 2003. However, the city has not budgeted a realistic amount for waste export—only $72 million in 2002 and nothing in 2003. The reason for such understated costs appears to stem from the fact that the city is currently negotiating with waste disposal firms on final exportation prices and does not want to reveal the amount it is willing to pay. Moreover, there are political issues that may affect the final cost of exporting refuse.

Waste export is a sensitive political issue, especially with the states that may be receiving the waste. Prospective exporters of trash have proposed siting waste transfer facilities in New Jersey. Both Governor Whitman and leaders of the towns where the facilities would be located have denounced the

[21] *Opportunities for Savings Through Civilianization in the New York City Police Department,* Office of the Comptroller, February 1, 1999.

plan as being environmentally detrimental. In Virginia—a likely destination of New York's waste—Governor Gilmore has stated, "I believe the Commonwealth has a right—and I would say a duty—to ban the use of barges for the transportation of garbage on Virginia's waterways." However, the Supreme Court has ruled that sending garbage across state lines is interstate commerce, which can only be regulated by Congress.

While states may not be able to outlaw refuse coming into the state, they may be able to make transporting it more difficult. For example, Virginia may be able to regulate barge traffic on its rivers, or as several states have done, step up enforcement of current regulations on hauling waste over the road. Such measures would make waste export more expensive.

Other Spending Areas

About one-fifth of city spending—about $8.6 billion by 2003—concerns a variety of other city agencies. In this section, we review a number of the major initiatives proposed in the budget affecting those agencies.

First, we discuss both budget cuts and a spending initiative involving the Department of Housing Preservation and Development. We then consider budget reductions proposed for public libraries and cultural institutions. The proposed rail link to LaGuardia Airport and how it is likely to reduce spending on other public transportation projects is then discussed. Finally, the section ends with a short description of a Department of Parks program that is highlighted in the preliminary budget but is not a new initiative at all—the city's tree planting service.

Housing

- The budget would reduce the number of housing inspectors—funding for which was sharply increased in the 1999 budget—and cut $6.5 million for several other housing-related initiatives in the 1999 budget.

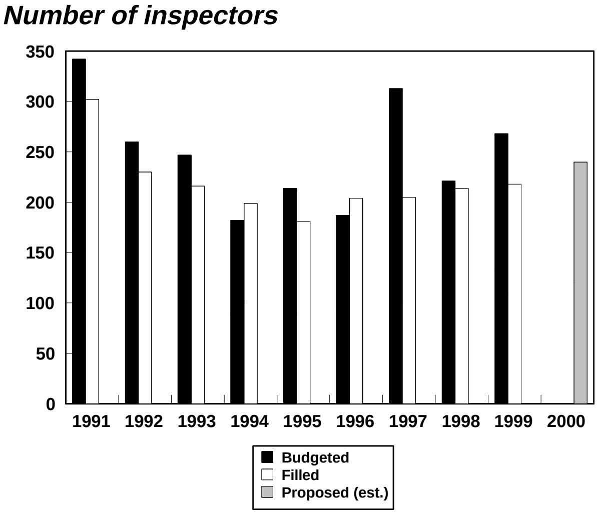
- The budget adds $2 million per year in new city funds for court-ordered lead-paint abatement under Local Law 1. IBO estimates that the costs could substantially exceed the budgeted amount.

The budget proposes to reduce or eliminate funding for several City Council initiatives included in the adopted 1999 budget. Most notably it reduces funding for enhanced housing code enforcement, for which the Council had added $2 million for 1999. The new funds were designated for an additional 78 housing inspectors, thereby increasing the authorized headcount to 268. Funding was later reduced to $1.3 million, more than half of which was allocated for other than personal services; as a result, the number of inspectors actually on staff in January 1999 was only 215. As shown in Figure 3-11, the Mayor proposes to lower the authorized headcount to 240 inspectors for 2000. The savings associated with this proposal, combined with other reductions in code enforcement personnel (through attrition), would result in annual savings of $2.7 million compared to the 1999 adopted budget.

The budget also proposes to eliminate $2 million for HPD anti-eviction and SRO legal services (see page 27 for a full discussion), as well as $1.8 million for various other Council-backed programs, including Community Consultants and landlord training. In recent years the Mayor has routinely proposed cutting these programs, only to have them restored by the Council.

The budget also includes $2 million per year in new city funds for implementation of Local Law 1, which requires elimination of lead-based paint in any pre-1960 dwelling unit in which a child under the age of 7 resides. Although this law has been on the books since 1982, the city has regularly been cited for lax enforcement. A recent court order directed HPD and the Department of Health to write regulations implementing the law under a strict

Figure 3-11.
Fewer Housing Inspectors Planned



SOURCE: Independent Budget Office.

interpretation. Implementation is stayed until April 30, 1999, however, to provide the Council time to draft alternative legislation. One such alternative, known as Intro. 205, would require a lower level of lead hazard reduction, but for a potentially larger universe of dwelling units, and with higher future enforcement standards. In the absence of alternative legislation, the costs to the city of implementing Local Law 1 could exceed, perhaps substantially, the $2 million budgeted.

Public Libraries

- The Mayor's budget proposes large reductions in the operating budgets of the city's three public library systems.

- Library officials believe the savings can only be absorbed through major reductions in library hours, and significant reductions in book purchasing and special programs.

The budget includes reductions of nearly 18 percent, $37.8 million, in city funds from the budgets of the New York, Queens, and Brooklyn library systems for 2000. In 1999, a $15 million reduction in library spending proposed by the Mayor was subsequently restored by the Council, and $7.1 million in new spending for the Connecting Libraries and Schools Program (CLASP) was added. With city funds accounting for approximately 84 percent of total funding for libraries, the proposed reduction would require cutbacks in areas such as staffing, hours of operation, materials (including books and CDs), and special program services.

The budget proposes half the cut be taken from the materials budget, with the other half offset by funds raised from private sources, matched on an equal basis with city funds through the Private Partnership Incentive Program.

It is debatable whether the libraries would be able to attract sufficient funds from the private sector for this purpose. Over the past five years, private funds have accounted, on average, for only 5 percent of total funding for public libraries. In general, raising funds from private sources for unrestricted operating support has proved difficult for these institutions, with donors preferring to give money for targeted programs that expand and enrich offerings.

While the budget directs that the cuts not result in service decreases, analyses by Brooklyn and Queens library officials suggest that cutbacks in staffing levels and hours/days of service would also be required to meet the reduction. In the Queens Library System, for example, just under 9 percent ($5 million) of the city funds in their operating budget are used for materials. Assuming that the library cannot offset the cuts by raising funds from private sources, the proposed reduction would likely cut service to four days a week in most branches; only the Main Library and the new Flushing branch would continue daily operations. The materials budget would decline by $900,000 (18 percent of city-funded levels) and special programs such as Adult Literacy would also be scaled back.

Cultural Affairs: Operating

- The budget proposes a reduction of nearly 13 percent in its operating subsidies to large cultural institutions and a reduction of 65 percent in funding for smaller arts groups in 2000.

- Starting in 2001, the budget would not provide city funding to cultural institutions and programs unless at least 50 percent of all operating funds are from private sources. Such a restriction would likely have the greatest effect on smaller arts groups, potentially less able to meet the private funding threshold.

The budget proposes to reduce the Department of Cultural Affairs' (DCA) budget by 18 percent, or $17.9 million, for 2000. The reduction includes $10.6 million less for the cultural institutions group (CIGs) and $7.3 million less for program services. The CIGs are the larger cultural institutions, such as the Metropolitan Museum of Art and the Brooklyn Academy of Music, that are housed in city-owned facilities and receive subsidies from the city for basic operating and energy costs. These subsidies supplement funds raised from private sources. Program services support smaller arts groups.

Preliminary budget reductions of a similar level have been proposed for the CIGs in recent years, with funding restored and even enhanced during the budget negotiation process with the City Council. However, the proposed reduction for program services—the smaller arts programs—is higher than in previous years (65 percent in 2000 versus 40 percent in 1999 and 35 percent in 1998).

The budget also provides for two programs designed to elicit greater private funding for the operations of arts organizations. The Cultural Challenge, now in its sixth year, distributes a portion of DCA funding on a competitive basis matched with funds raised from private sources. For 2000, $5 million would be cut from the budgets for cultural institutions and program service—5.6 percent and 2.2 percent, respectively—and reallocated to the Challenge. In addition, the budget proposes restricting city funding (grants and subsidies) for 2000 to only those institutions and programs that raise at least 25 percent of their funding from private sources. In 2001, the threshold increases to 50 percent of funding.

Cultural Affairs: Capital Projects

- Proposed city capital commitments for cultural institutions for the period 2000 to 2009 have decreased by about half compared to the level of funding provided during the 1990s.

- Major proposed capital commitments include $65 million for the Museum of Modern Art, $25 million for the Metropolitan Museum of Art, and $18 million for Jazz at Lincoln Center.

The city has historically provided support for capital expansion and improvement projects for selected cultural institutions, particularly those housed in city-owned buildings. The preliminary capital strategy proposes $184 million in city capital commitments for cultural institutions from 2000 to 2003—slightly less than 1 percent of the proposed $21.6 billion in city capital commitments for the period. Over the longer term, the preliminary capital strategy for 2000 to 2009 includes $245 million in city capital commitments for cultural institutions. This amount is about 51 percent of the level of funding provided during the 10-year period from 1989 through 1998.

Thirty-four of the city's cultural institutions enjoy a special status with the city as members of its cultural institutions group (CIGs). Traditionally, most capital funding by the city for cultural institutions has been used for the CIGs. Among current proposals, however, one of the largest capital projects would provide $65 million for the Museum of Modern Art—a private cultural institution not linked to the CIGs. Highlights of the larger proposed capital projects for cultural institutions are provided below.

Museum of Modern Art. The city proposes to contribute $65 million as part of the museum's $650 million capital campaign for expansion and renovation. The proposed city capital funds would be provided over a three-year period—$15 million in capital commitments are provided in 1999, with $20 million proposed for 2000 and $30 million for 2001. The project includes a new building dedicated to education and research, with more classroom space for school children, as well as renovation of the sculpture garden, expansion of stores and restaurants, new gallery space, and a state-of-the-art storage and study facility.

Metropolitan Museum of Art. The Mayor proposes a $25 million capital commitment, $5 million per year over five years (2000-2004). That funding would be part of a $250 million capital renovation and expansion program to make improvements to infrastructure and visitor amenities, and carry out restoration and renovation activities. A centerpiece of the capital program is the restoration and improvement of the Great Hall. According to museum officials, the remaining 90 percent of the funds for the capital program would be raised from private sources.

Other. Capital funding has also been proposed for the Museum of Jewish Heritage to contribute to the building of a new wing, and Jazz at Lincoln Center to construct a new performance and education facility. As with the other cultural capital projects, they would be funded by a combination of public and private funding sources.

LaGuardia Rail Link

The Mayor's budget includes a proposal to build a rail link to LaGuardia Airport.

- Three-fourths of the project's $1.2 billion cost would be funded from the city's capital budget.
- The Mayor's proposal would reallocate planned city contributions to various MTA capital projects. Unless new funding sources are found, the rail link would consume most of the city money planned between 2000 and 2004 for subway expansion projects and the rehabilitation of existing infrastructure.

The LaGuardia rail link project would be funded with $100 million each from the Port Authority, New York State, and the federal government, along with $945 million in city capital funding. City contributions would include $600 million from the capital budget with the remainder provided pursuant to an agreement under discussion with the MTA to give the city $345 million in one-time general fund revenues from the sale of the New York Coliseum. While the proposed link to LaGuardia clearly has merits, in the coming months there will need to be public debate as to whether it would be the best use of scarce capital funds.

The proposal has been under development for some time. In July 1998, the MTA, the Port Authority, Mayor Giuliani, Governor Pataki, and Queens Borough President Shulman signed a memorandum of agreement regarding improved access to LaGuardia. The agreement led to a public meeting in August at which the MTA and the Port Authority presented four alternative routes for the Queens portion of the rail link. The public also suggested alternatives.

Under the budget proposal, the LaGuardia link would provide a no-transfer ride to the airport from Manhattan. The train would begin at City Hall, travel express along the N line to the Ditmars Boulevard station in Astoria, and then continue either under Ditmars or along an elevated route above 31st Street and 19th Avenue. The project would involve constructing between 1.5 and 2 miles of new rail line, a terminal station at the airport, and possibly one or more additional stations in Queens.

There is general agreement that better public transportation access to LaGuardia is needed.

According to the Port Authority, 93 percent of LaGuardia's 80,000 daily passengers use private automobiles, taxis, or limousines to reach the airport. The main public transportation alternatives from Manhattan are the M60 bus that runs along 125th Street and a limited amount of ferry service from the East Side.

The LaGuardia proposal represents a major financial commitment for New York City and the MTA. (In contrast, the Port Authority's proposed rail link to Kennedy Airport would be financed entirely through passenger facility charges—a three-dollar tax on departing air passengers.) The $600 million direct city contribution for the rail link, however, does not represent additional public transportation spending. Instead, funds already planned for MTA capital spending over the 2000 to 2004 period would be diverted to the LaGuardia project. Accordingly, building the rail link would reduce the likelihood of carrying out other subway expansion projects, such as the Second Avenue subway from 125th Street to 63rd Street currently under study by the MTA, or the more ambitious Metrolink project of the Regional Plan Association. Funding the LaGuardia project would also mean slower progress toward New York City Transit's goal of bringing the entire subway system to a state of good repair.

Parks: Tree Planting

The budget proposes $35 million in capital spending, $7 million per year over five years, for planting trees along city streets. This is not a new proposal, but rather a continuation of recent funding levels. The program is highlighted in the budget to build greater public awareness for the city's free tree planting service. The proposed funding level would allow for the purchase of 12,000 to 15,000 trees per year. Trees are distributed to residents by the Department of Parks and Recreation on a first-come, first-served basis (requests are channeled through community boards). New trees are also used for fill-in and replacement of existing trees along city streets. According to the Department of Parks web site, the wait for residents requesting trees is one to two years. The Mayor's 10-year preliminary capital strategy extends annual funding of $7 million through 2009.

Debt Service

By 2003, debt service payments will total $4.4 billion—approaching 20 percent of city tax revenues—once TFA debt is taken into account. This section explores the relationship between the city's high debt service burden to the city's bond rating and the state constitutional debt limit. It also touches upon the proposal to issue bonds backed by the proceeds of the tobacco settlement.

- Debt service payments have risen sharply in recent years and are expected to continue to rise over the forecast period.

- The city's high level of debt increases the interest rates the city must pay to borrow, and its rising debt service costs compete with operating needs.

- The constitutional debt limit and the exhaustion of authorized borrowing by the TFA is expected to seriously constrain the city's ability to issue bonds over the next two years.

- To avoid being constrained by these limits, the Mayor proposes to use tobacco bonds backed by revenue from the recent court settlement to finance capital expenditures from 2000 to 2003.

The city borrows money by issuing bonds to pay for capital spending on schools, bridges, and other kinds of public infrastructure. Debt service is the scheduled repayment of the borrowed funds plus interest.

The city's debt service payments pay for three types of city debt: General Obligation (GO), Municipal Assistance Corporation (MAC), and

Transitional Finance Authority (TFA). GO debt is backed by the broad taxing powers of the city and accounts for the vast majority of debt service, averaging close to three-fourths of the total from 1990-1999. GO indebtedness is subject to a New York State constitutional debt limit. MAC debt, backed by dedicated sales tax revenues, was used to meet borrowing needs when the city's access to capital markets was cut off as a result of the 1970s fiscal crisis. MAC no longer issues any new debt and has refunded as much of its portfolio as possible. By 2008, MAC bondholders will be repaid and the Corporation will sunset.

The TFA was created in calendar year 1997 in response to an impending exhaustion of GO borrowing authority. It issues debt backed by a dedicated stream of personal income tax revenues. TFA has issued nearly $3.1 billion of its $7.5 billion statutory debt limit since its inception and will account for an increasing share of future debt service costs. Beginning last year, the city moved TFA debt service (and the personal income tax revenues that fund it) off-budget. Such treatment provides an incomplete picture of the allocation of public resources and makes it difficult to evaluate changes in the city's debt burden. Accordingly, IBO will continue to include TFA debt in its analysis of debt service.

Spending forecast. IBO forecasts debt service payments of $3.2 billion in 1999, $2.1 billion in 2000, $3.7 billion in 2001, $4.2 billion in 2002, and $4.4 billion in 2003. These funding levels differ from those forecast in the preliminary budget because they reflect TFA debt service and a somewhat larger estimate of the 1999 surplus. IBO assumes that the $1.8 billion surplus we forecast for 1999 will be used to prepay debt service scheduled for 2000 during the current fiscal year. Prepayment of debt service is a well-established mechanism for transferring surplus funds from one budget year to the next. Because these prepayments distort the trends in scheduled debt service payments, however, we have reversed their impact in the analysis below.

Debt service has increased sharply in the 1990s. After adjusting for prepayments and inflation, debt service on GO, MAC, and TFA debt is projected to rise 42 percent from 1991 to 2000. The rise is expected to continue beyond 2000, with a real increase in adjusted debt service of 16 percent between 2000 and 2003. The large upswing is primarily the result of increased new borrowing.

The city's past practice of refunding bonds created an additional source of upward pressure on debt service payments. A number of financings dating from the late 1980s and early 1990s were structured so as to reduce debt service in the near term and increase payments scheduled for the more distant future. Refundings saved an average of $170 million per year from 1986 to 1995, but increased debt service payments by an average of $210 million annually from 1996 to 2003.

Significantly, tax collections (especially property taxes) have failed to keep pace with the rapid increase in borrowing, contributing to a rising ratio of debt service to tax revenues—from 11.1 percent in 1990 to a projected 16.9 percent in 2000 and 19.3 percent in 2003 (see Figure 3-12).

High debt service costs constrain other forms of spending. From 1993 and 2003, real debt service is projected to climb at an average rate of 3.0 percent and non-debt service spending at a rate of 0.8 percent per year.

Figure 3-12.
Debt Service Continues to Rise

Debt Service as a Percent of Tax Revenue
GO, TFA, and MAC Combined

SOURCE: Independent Budget Office.

NOTE: Excludes prepayments.

High debt burdens yield lower credit ratings from bond rating agencies, which in turn increase the cost of borrowing. Although the city's credit rating was upgraded by both Standard & Poor's (S&P) and Moody's rating services in calendar year 1998, its ratings remain below other major cities, such as Chicago, Boston, and Los Angeles. According to S&P, "a higher rating is precluded by extraordinarily high debt levels, significant ongoing capital needs, and the city's persistent inability to translate robust surpluses into more lasting budget relief."

Fitch IBCA recently upgraded the city's general obligation debt, citing the strong broad-based performance of the economy, a surging real estate market, strong management of the city's finances, and a declining tax burden. Nevertheless, Fitch expressed concern about the city's high level of debt.

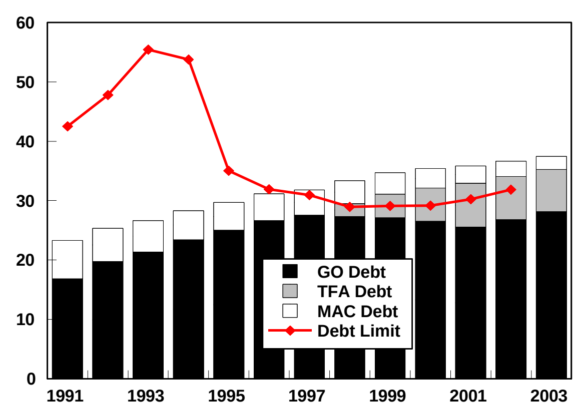
Debt limit. As noted above, the state constitution imposes a limit on the GO indebtedness of all municipalities in New York State. Figure 3-13 shows the debt limit superimposed over the amount of GO debt the city has outstanding. TFA and MAC debt, which do not count toward the debt limit, are also shown since all three are obligations of the city.

The debt limit is equal to 10 percent of the value of all taxable real estate in the city, calculated as an average over the five preceding years. The methodology used to generate the estimates of market value is seriously flawed. It relies, in part, on projecting market values using very old market data. This methodology can produce very inaccurate estimates of market values. Also, as Figure 3-13 shows, the methodology has produced a particularly volatile debt limit, first rising sharply and then plummeting in the first half of the 1990s.

Figure 3-13 shows that without the TFA, capital commitments would have had to be reduced starting in 1998. Even with the additional TFA borrowing capacity, however, the constitutional debt limit will constrain borrowing in the near future. With a strong need for infrastructure improvements in the city, the debt limit represents an obstacle to maintaining New York as a world class city.

Figure 3-13.
Overall Debt Level, 1991 – 2003

Dollars in billions



SOURCE: IBO; Comprehensive Annual Financial Reports of the Comptroller, 1991-1998; Comptroller's Office.

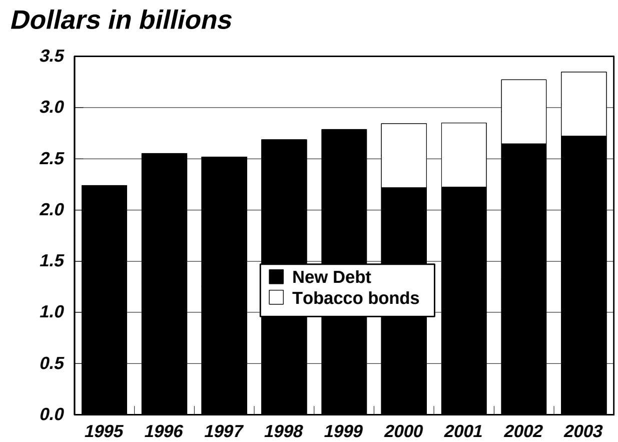
NOTE: GO debt based on actual levels through 1998 and forecast through 2003.

Complicating matters further, as indicated above, growing debt service costs remain a serious budgetary concern. Figure 3-13 shows that despite the debt limit, no decline in the city's overall level of debt has occurred or is expected to occur in the near future.

The preliminary budget warns that the city expects to exhaust its capacity to incur general obligation debt in 2000. A possible temporary solution to the debt limit problem has arrived in the form of the recently negotiated settlement between states and cities and the nation's four largest tobacco companies. The Mayor has proposed to securitize part of the stream of revenues expected from the settlement, potentially generating $2.5 billion in capital funds from tobacco bonds from 2000 to 2003. A more detailed discussion of the tobacco settlement is provided on page 17 of this report.

Assessing the city's overall debt outlook, it appears the tobacco bonds would enable a more ambitious capital agenda, as well as slow the growth of the city's debt burden. Figure 3-14 shows new debt issued from 1995 to 2003. In the four-year period of the projected tobacco bond sales (2000-2003), the financial plan calls for capital expenditures of $12.3 billion—about $9.8 billion in other GO and TFA debt and $2.5 billion in tobacco bonds. Compared to the $10 billion of new debt proceeds borrowed in the previous four-year period (1995 through 1998), capital expenditures will increase by 12 percent, adjusting for inflation, while issuance of new GO and TFA debt will decline by 11 percent.

Figure 3-14.
Proceeds from Bond Sales, 1995 – 2003



SOURCE: IBO; Comprehensive Annual Financial Reports of the Comptroller, 1995-1998; Mayor's Preliminary Budget for 2000.

NOTE: New debt is new GO or TFA debt, not to be used for refinancing.

Other Spending Issues

This section examines several miscellaneous areas affecting the city budget: labor costs, tort reform, and stadium financing. Our analysis indicates that the preliminary budget underestimates likely labor costs and monetary judgements against the city. Moreover, a clear plan is not laid out to spend a proposed $882 million to build new sports stadiums.

City Labor Costs

- The financial plan does not budget for salary increases beyond the current round of collective bargaining agreements that expire in 2000 and 2001.
- IBO forecasts overtime spending in 1999 to be $539 million or 10 percent greater than the all-time high of $490 million reached in 1994.

Collective bargaining agreements. About 98 percent of the city's workforce have labor contracts that end in 2000 and 2001. Those five-year contracts are the result of settlements and arbitration awards and provide for a wage freeze in the first two years and salary increases over the last three years. The total cumulative net increase (salary and benefits less any givebacks) over the life of the contracts is roughly 13 percent.

Labor reserve. The labor reserve funds the costs associated with collective bargaining agreements for city employees. For the current round of collective bargaining agreements, IBO projects that the labor reserve will be $505 million in 2000, increase at an average annual rate of 2.8 percent, and reach $548 million in 2003.

Since the city has not provided funding in the labor reserve for wage increases beyond the current settlements, we assume that wages will increase at the projected rate of inflation after the current contracts end. The only exception to this assumption is wage increases at the Board of Education, which are estimated using an econometric model that takes into account historical spending, enrollment and staffing trends, and economic variables. IBO projects that salary increases for the city's total workforce will require an additional $36 million in 2000. This amount grows to $235 million in 2001, $614 million in 2002, and $1 billion in 2003. The Board of Education accounts for $332 million of the additional funds required in 2003.

Overtime. Overtime costs are affected by many factors, including collective bargaining agreements, management initiatives, planned events, and emergencies. IBO forecasts that overtime spending will be $539 million in 1999. This level of spending would be $166 million greater than the amount included in the adopted budget and $49 million greater than the all-time high of $490 million reached in 1994. Over 75 percent of the increased overtime costs in 1999 are due to additional spending in the uniformed agencies. This increase is due mainly to the city's expanded anti-drug initiatives (which in turn have resulted in increased arrests), higher prison populations, increased anti-terrorism measures, and other emergencies and unplanned events.

IBO projects that these trends will continue to boost city overtime spending. We forecast that overtime spending will reach $532 million in 2000, exceeding the preliminary budget estimate by $113 million. For 2001-2003, we assume the city will spend $500 million annually on overtime—nearly 30 percent more than is budgeted.

Tort Reform

In order to control the rapidly rising costs of personal injury claims against the city, the Mayor has proposed that the state government enact a number of tort-reform measures that would generate an estimated $70 million in city savings. The Administration projects that the city will pay out $371 million in personal injury cases in 1999. Moreover, costs are expected to grow more than 5 percent annually over the financial plan period, reaching $451 million in 2003. The city's proposals would limit awards for pain and suffering and other non-economic loss to $250,000, and would require plaintiffs to prove they incurred medical expenses of at least $5,000 in order to recover damages for non-economic loss. Because these proposals have been submitted to the state legislature in the past without success, we do not assume that the city will achieve its proposed tort reform savings.

Stadium Financing

- Operating funding for the Department of Business Services increases substantially in 2000 due to a $96 million appropriation for proposed spending on city-owned sports facilities.

- Appropriations for construction of major league facilities total $882 million over the 2000-2003 period.

- The city is proposing to spend $86 million in capital budget funds to build two new minor league stadiums.

The Mayor's plan would set aside almost $1 billion in operating and capital budget funds for construction of publicly owned sports facilities.

Projects being discussed include a major league sports complex in Manhattan, a new Flushing Meadows stadium for the Mets, a new or rehabilitated Yankee Stadium, and minor league baseball stadiums in Brooklyn and Staten Island.

The city's contributions to major league facilities are to be funded on a pay-as-you-go basis with general operating budget appropriations. The financial plan earmarks $96 million in 2000, $194 million in 2001, $289 million in 2002, and $303 million in 2003 (a total of $882 million) for these projects. Previously, these funds had been placed off-budget along with the dedicated commercial rent tax revenues that were originally supposed to finance them. They are now housed within the Sports Facilities Corporation (SFC) unit of appropriation under the Department of Business Services (DBS), and presumably now will cover the SFC's own operating expenses as well.[22]

Despite the size of the city appropriation for major league stadium construction, a great deal of uncertainty surrounds such basic issues as which projects will be funded, how much they will cost, what share of total costs will be borne by taxpayers, what kinds of collateral infrastructure investments they will require, and how much of an economic payoff they will produce.[23]

Funding for the new minor league stadiums, $57.0 million for the Brooklyn project and $28.9 million for the Staten Island project, would be provided through the capital budget. This funding covers the entire projected cost of both construction projects. It comes on top of $11.2 million being spent in this year's general operating budget to retrofit an existing facility in Staten Island for temporary use and for cleanup and waterfront repair at the site of the planned new stadium.

[22] Last year, the city proposed to fund the then-off budget SFC with an annually renewable $2 million contract with DBS; this funding was separate from the dedicated CRT revenues that the corporation was supposed to channel into stadium construction.

[23] While the Administration is anticipating a substantial economic payoff, most research on the subject suggests that sports stadiums are generally not great engines of local economic development. See IBO's fiscal brief, *Double Play*: *The Economics and Financing of Stadiums for the Yankees and Mets,* April 1998.

Appendix A

Gap Sheets

IBO's Reestimate of the Mayor's Budget (In millions of dollars)

	1999	2000	2001	2002	2003
Revenue:					
Taxes:					
Property	7,543	7,876	8,127	8,392	8,766
Personal Income (excluding TFA)	5,105	4,481	4,371	4,324	4,556
General Sales	3,228	3,184	3,250	3,383	3,513
Business Income	2,564	2,605	2,568	2,665	2,821
Real-estate Related	1,142	1,019	1,036	1,096	1,187
Other Taxes (with Audits)	1,455	1,428	1,430	1,412	1,434
Total Taxes	21,037	20,593	20,782	21,272	22,277
Tax Reduction Program	-	(354)	(416)	(468)	(486)
STaR Reimbursement	117	306	503	714	721
Miscellaneous Revenues (net of intra-city revenue)	2,582	3,289	2,714	2,818	2,714
All Other Revenue:					
Unrestricted Intergovernmental Aid	606	565	564	564	564
Anticipated Revenue	-	-	-	-	-
Other Categorical Grants	325	301	286	284	284
Inter-Fund Revenues	270	281	280	280	280
Disallowances	(15)	(15)	(15)	(15)	(15)
Total Other Revenue	1,186	1,132	1,115	1,113	1,113
Total City Funds	24,922	24,966	24,698	25,449	26,339
Dedicated Personal Income Tax (TFA)	144	284	446	548	577
Categorical Grants:					
State	6,770	6,844	7,061	7,350	7,503
Federal	4,406	4,245	4,217	4,170	4,109
Total Revenue	36,242	36,339	36,422	37,517	38,528
Expenditures:					
City Funded (net of intra-city sales)	24,922	24,981	27,038	28,339	29,283
TFA Debt Service	144	284	446	548	577
Categorical Grants:					
State	6,770	6,844	7,061	7,350	7,503
Federal	4,406	4,245	4,217	4,170	4,109
Total Expenditures	36,242	36,354	38,762	40,407	41,472
Surplus / (Gap)	**-**	**(15)**	**(2,340)**	**(2,890)**	**(2,944)**

SOURCE: Independent Budget Office.

Current Services Projections (In millions of dollars)

	1999	2000	2001	2002	2003
Revenue:					
Taxes:					
Property	7,543	7,876	8,127	8,392	8,766
Personal Income (excluding TFA)	5,105	4,481	4,371	4,324	4,556
General Sales	3,228	3,184	3,250	3,383	3,513
Business Income	2,564	2,605	2,568	2,665	2,821
Real-estate Related	1,142	1,019	1,036	1,096	1,187
Other Taxes (with Audits)	1,455	1,428	1,430	1,412	1,434
Total Taxes	21,037	20,593	20,782	21,272	22,277
Tax Reduction Program	-	-	-	-	-
STaR Reimbursement	117	306	503	714	721
Miscellaneous Revenues (net of intra-city revenue)	2,582	3,289	2,714	2,818	2,714
All Other Revenue:					
Unrestricted Intergovernmental Aid	606	565	564	564	564
Anticipated Revenue	-	-	-	-	-
Other Categorical Grants	325	301	286	284	284
Inter-Fund Revenues	270	281	280	280	280
Disallowances	(15)	(15)	(15)	(15)	(15)
Total Other Revenue	1,186	1,132	1,115	1,113	1,113
Total City Funds	24,922	25,320	25,114	25,917	26,825
Dedicated Personal Income Tax (TFA)	144	284	446	548	577
Categorical Grants:					
State	6,770	6,882	7,125	7,440	7,640
Federal	4,406	4,283	4,300	4,294	4,308
Total Revenue	36,242	36,769	36,985	38,199	39,350
Expenditures:					
City Funded (net of intra-city sales)	24,922	24,952	26,866	28,112	29,078
TFA Debt Service	144	284	446	548	577
Categorical Grants:					
State	6,770	6,882	7,125	7,440	7,640
Federal	4,406	4,283	4,300	4,294	4,308
Total Expenditures	36,242	36,401	38,737	40,394	41,603
Surplus / (Gap)	**-**	**368**	**(1,752)**	**(2,195)**	**(2,253)**

SOURCE: Independent Budget Office.

Appendix
B

Economic Forecasts: IBO and OMB

	Calendar Year					
	1998	1999	2000	2001	2002	2003
United States						
Real GDP						
IBO	3.9	2.5	2.0	3.1	2.6	2.4
OMB	3.8	2.7	2.0	2.0	1.9	2.1
Payroll Employment						
IBO	2.6	1.4	1.1	1.7	1.4	1.4
OMB	2.5	1.5	1.2	1.1	0.8	1.0
Unemployment Rate						
IBO	4.5	4.8	5.1	5.0	5.2	5.3
OMB	4.5	4.5	4.6	4.9	5.3	5.5
Consumer Price Index						
IBO	1.6	2.1	2.5	2.7	2.9	2.9
OMB	1.6	2.2	2.3	2.4	2.7	2.7
30-Year Treasury Bond Rate (%)						
IBO	5.6	5.2	5.9	6.7	6.5	6.0
OMB	5.6	5.0	5.1	5.2	5.4	5.4
New York City						
Personal Income						
IBO	5.5	4.5	4.9	5.5	5.7	5.3
OMB	4.7	3.9	3.3	3.6	3.9	4.1
Payroll Employment						
IBO	2.3	1.3	1.0	1.2	1.0	1.0
OMB	2.3	1.6	0.6	0.8	0.5	0.5
Unemployment Rate						
IBO	8.0	8.5	8.7	8.3	8.5	8.6
OMB						
Consumer Price Index						
IBO	1.6	1.6	1.8	2.2	2.5	2.5
OMB	1.6	2.3	2.4	2.5	2.8	2.8
Manhattan Office Rents ($/sq.ft)						
IBO	42.71	45.30	45.87	46.69	47.76	48.83
OMB	41.24	44.52	46.44	48.92	50.88	51.97

SOURCE: Independent Budget Office.

NOTES: Actual values for 1997 are denoted by bold type. With the exception of bond rates and office rents, all figures reflect year-over-year percentage increases. The local consumer price index covers the New York/Northern New Jersey region.

Appendix C

Major Contributors to the Revenue and Expenditure Projections

Revenue Projections

David Belkin	Sales Taxes	(212) 442-8698
Frank Posillico	State and Federal Aid	442-0222
George Sweeting	Property Taxes	442-8642
Luan Lubuele	Econometric Modeling/Education Finance	442-8696
Michael Jacobs	Personal Income Taxes/Business Taxes	442-0597
Ronnie Lowenstein	Economic Analysis	442-0225
Stephen Mark	Business Taxes/Debt Service	442-8640

Spending Projections

Alan Treffeisen	Transportation	(212) 442-8614
Bernard O'Brien	Police/Corrections	442-8656
Christine Lidbury	Culturals/Parks	442-8612
Joyce Sun	Economic Development/Debt Service	442-8620
Kevin Koshar	Libraries	442-0227
Lisa Melamed	Education	442-8618
Mark Schreiner	Sanitation/Finance	676-1364
Martha Prinz	Education	442-8616
Michelle Billies	Health and Social Services	676-9247
Paul Lopatto	Public Assistance	442-8613
Preston Niblack	Housing	442-0220
Rebecca Hernandez	Health and Social Services	442-8619
Richard Greene	Overtime/Labor Reserve	442-8611
Robert Weiner	Education	442-0332
Sofía Quintero	Medicaid	676-9248

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