

WILLIAM C. THOMPSON, JR.  
NEW YORK CITY COMPTROLLER

TESTIMONY BEFORE THE FINANCE COMMITTEE  
NEW YORK CITY COUNCIL  
CITY HALL  
MONDAY  
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12:30 PM

Speaker Miller, Committee Chair Weprin, honorable members of the Finance Committee, good afternoon.

A year ago at this time, I appeared before you to report the City confronted a 3.76 billion dollar budget deficit for Fiscal Year 2006. Today, I can report to you that the 49.7 billion dollar Executive Budget for Fiscal Year 2006 appears on course towards balance. As in previous years, the task of balancing the budget has been an act of great collaboration. The Mayor and the entire City Council have earned our thanks for their work together, and the people of the City of New York deserve special credit.

The Executive Budget, however, is not without risk. My office has identified 665 million dollars in quantifiable risks. The largest risk lies in the likely cost of retroactive collective bargaining agreements with the teachers' and the uniformed employees' unions. The pattern set by other settled contracts includes wage increases that are offset by productivity savings. The administration has maintained that similar provisions would apply to the outstanding contracts. Unfortunately, the inability to reach labor agreements in a timely fashion makes it far more difficult for the City to achieve its goal of funding raises through offsetting productivity, since productivity cannot be created retroactively. The reserves to cover the expense of new labor contracts the administration has set aside are currently inadequate. My office estimates the additional cost of funding the retroactive wage increases will be 455 million dollars in Fiscal Year 2006.

Overtime costs and the introduction of a new State social services block grant account for the remaining risks. The City has been unable to limit overtime costs to budgeted targets, making this a chronic management problem for City agencies, especially the Police Department.

My office projects that the City has underestimated overtime costs in the upcoming fiscal year by 175 million dollars. Finally, the State has enacted a social services block grant that will require service reductions unless the City replaces 35 million dollars in funding.

My office projects, however, that higher tax revenue may be available to offset some of the risks I just enumerated. For example, although it would benefit City residents and our economy, the City is unlikely this year to attain its goal of

reinstating the sales tax exemption on clothing and foot-wear items costing up to 110 dollars. Therefore, the 230 million dollars the Executive Budget treats as lost sales tax revenue is likely to be available to offset risk in Fiscal Year 2006. My office expects other tax collections to be 255 million dollars higher than expected for economic reasons. This 485 million in higher-than-expected tax revenues should reduce the City's net risk to a manageable 180 million dollars.

The City faces additional uncertainties which are yet to be resolved – and therefore more difficult to quantify -- and may affect expenses in Fiscal Year 2006 and beyond. First, the pending collective bargaining agreements with teachers and uniformed personnel I mentioned earlier could result in wage increases in excess of the pattern set with the DC 37 civilian contract. Every additional percentage point wage increase will cost the City 145 million dollars annually.

Second, the City's Chief Actuary has recommended a number of adjustments that would affect the City's pension obligations. These recommended adjustments taken as a whole would reduce the City's projected costs by \$764 million in FY 2006. However, the Executive Budget includes costs of \$325 million to reflect only some of the actuarial recommendations. Additionally, the Boards of the five pension systems must approve the Actuary's recommendations, some of which require State legislation.

Third, the financial condition of the Health and Hospitals Corporation (HHC) continues to be a cause for concern. In recent years, the City has prepaid its subsidy a year early as a stop-gap measure to keep HHC's year-end cash balances at a respectable level.

However, a more viable way of addressing this problem is to recognize the need for an adequate level of support from the outset. Given recent subsidy levels, an adequate level of support could necessitate an infusion of at least 200 million dollars in Fiscal Year 2006.

I would now like to discuss what I regard as my biggest concern regarding the Fiscal Year 2006 budget. To achieve balance in the upcoming year, the City is repeating a pattern it has increasingly followed in recent years: relying on a surplus in the current fiscal year to prepay the next year's expenses.

In the Fiscal Year 2006 Executive Budget, the Administration is using an unprecedented 3.3 billion dollar surplus, in the form of a Budget Stabilization Account, in the current fiscal year to prepay Fiscal Year 2006 expenses. The surplus is the result of real estate transaction tax and personal income tax revenues exceeding projections for FY 2005 by 2.1 billion dollars.

The robust revenue growth the City experienced in the current fiscal year is not expected to continue in the out-years of the Financial Plan. In Fiscal Year

2007, the City will likely face a projected 4.473 billion budget deficit. In Fiscal Year 2008, the deficit will likely decrease to 4.236 billion dollars, and in Fiscal Year 2009, the deficit is projected to be 3.703 billion dollars.

The City's heavy reliance on non-recurring revenues to balance the budget is unsustainable over the long term and fails to address the City's central budget challenge: the fact that year after year, the City's expenses dwarf its revenues. Until the causes of this structural imbalance are addressed, the City will continue to face budget deficits on an annual basis.

This approach also leaves the City little margin for error in the event of another economic downturn. My office's forecast for the New York City economy in the near future is slow, continued growth. In 2005, we project Gross City Product to grow 3.3 percent, and in 2006 2.9 percent. While my office is not currently projecting a downturn, there are no guarantees one will not occur.

In order to achieve long-term fiscal stability, we must reduce our reliance on both non-recurring resources and year-to-year surpluses. To help us do so, the City should work to establish a Rainy Day Fund that would require some portion of budget surpluses to be deposited in an account accessible only under specified circumstances. The City Council has also proposed a Rainy Day Fund and I look forward to working with you on this. As you know, the City Charter would have to be altered. Additionally, the State Financial Emergency Act would have to be amended, requiring the assistance of our colleagues in Albany.

A Rainy Day Fund would serve the dual purpose of cushioning services during downturns and creating incentives for better fiscal management in good years. With a Rainy Day Fund, the City would set aside some percentage of excess revenues each year, to be held in a separate account to be used only in moments of fiscal stress. This account can be funded over a period of years and then used to stabilize City services in a downturn.

In this regard, New York would join many other local governments and it would be a vast improvement over the City's current "Budget Stabilization Account" because the Rainy Day Fund could be used only when the economy falters. If the City did not have easy access to this rolled-over surplus, it would be forced into adopting a budget that more accurately reflects our current financial status. For this reason and others, creating a permanent Rainy Day fund would do much more to ensure stability in the City's finances.

Thank you.