The Comptroller's Comments on The Adopted Budget for Fiscal Year 2006 and The Financial Plan for Fiscal Years 2006-2009

The City of New York
Office of the Comptroller
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I. Executive Summary

The City of New York passed a balanced budget for FY 2006 with expenses of $50.2 billion. It also submitted a four-year Financial Plan to the New York State Financial Control Board showing large budget gaps of $4.5 billion in FY 2007, $4.5 billion in FY 2008, and $3.9 billion in FY 2009. Moreover, the FY 2006 budget is balanced only because the City has used an unprecedented FY 2005 surplus of $3.5 billion to prepay FY 2006 expenses. The gaps emerge because a significant portion of FY 2005 revenues is not expected to recur. One-time revenues, including back airport rent and MAC debt service reimbursement, provided $1.5 billion in FY 2005 miscellaneous revenue, while unexpected strength in the housing market and economy produced greater-than-projected tax revenues of $3.7 billion. With surcharges for the personal income and sales taxes expiring, the City's revenue base shrinks markedly.

Our findings suggest that the City could face significant risks in FY 2006, but these may be offset through additional revenues.

Risks to the Budget

Readily quantifiable risks to the budget include overtime expense, retroactive costs related to labor settlements, and impacts of the State's Flex Fund for Family Services. The City chronically underestimates its overtime expenses, especially in the uniformed agencies. These costs have proved difficult to manage and have historically been underfunded in the Adopted Budget. Overtime expenses will likely exceed the City's estimates by $181 million in FY 2006, and by $75 million in succeeding years. The City faces a risk of at least $30 million for retroactive payments when an agreement is reached with the teacher's union. This amount would follow the pattern set by DC 37, although the ultimate agreement is likely to be more generous (see below). Finally, a change in State policy resulting in the creation of the Flex Fund for Family Services has created a small risk of $10 million throughout the outyears of the plan.

Two issues with significant fiscal implications remain unsettled and are uncertain with respect to timing and magnitude. The first is the resolution of the remaining labor settlements. Costs in excess of current reserves for a teachers' settlement similar to the PBA pattern, rather than the DC 37 pattern, would reach $980 million in FY 2006 for retroactive payments and $120 million for annual wages. Furthermore, the next round of collective bargaining is funded by the City at half the projected rate of inflation. While it is prudent to set aside reserves for future labor settlements, this level of funding will require that new collective bargaining agreements contain substantial productivity savings.

The second issue is the resolution of the Campaign for Fiscal Equity lawsuit. This matter is unlikely to have an impact in FY 2006, but looms over the FY 2007 budget and beyond. The court order, which is under appeal, would require a phased-in goal of $5.6 billion in additional education spending each year. It is unknown whether this amount will stand under appeal or how much, if any, will be the City's liability.

Potential for Additional Resources

The Comptroller's review of the budget finds that there are potential resources that may offset the FY 2006 risks. Our analysis concludes that the City will very likely again collect significantly more tax revenues in the current fiscal year than projected. A more optimistic outlook in the near term, stronger tax revenues derived from housing sales than the City is projecting, and adjustments to the FY 2006 forecast that account for the high level of actual tax collections in FY 2005 should result in higher revenues of $1.1 billion in FY 2006.

The City could also attain significant resources from other developments in FY 2006. The City Actuary has made recommendations regarding changes to actuarial assumptions and methods governing the calculation of the City's pension costs which, if adopted by the boards of the various pensions, would result in savings of over $855 million in FY 2006 and $528 million in FY 2007. These changes would, however, lead to additional expense in the outyears. Further, the additional near-term resources will have little impact on the City's longer-term fiscal imbalance.

Aligning Expenses and Revenues

The City's program to eliminate the gap is very small relative to the task: only $253 million in new gap-closing initiatives has been included in the FY 2006 Adopted Budget. While the reliance on one-time resources and prior year-surpluses could result in near-term budget relief, these actions do not generate recurring benefits over the longer term. To achieve long-term fiscal stability, the City must take actions that would also narrow budget gaps in future years. Accordingly, the financial plan would have been more structurally sound if a higher level of recurring savings were included in the City's gap closing program.

The failure to make progress in closing the structural budget gap and the absence of any excess reserves to address contingencies puts the City at risk over the course of the financial plan. The magnitude of the outyear gaps poses significant fiscal challenge to the City that, if coupled with a recession or other event that places further stress on the budget, will require additional service cuts, tax increases, or both.

The Financial Emergency Act (FEA) was created in the 1970s to ensure that such occurrences would not lead the City to bankruptcy. Initially set to expire in 2008, recent changes in State law have extended the FEA, a development that the City has sought to reverse. The FEA has been beneficial in helping the City maintain sound fiscal management. Rather than seeking the reversal of the FEA extension, the City should look to develop an alternative FEA procedure to preserve the benefits of the current system and allow the creation of a Rainy Day Fund. Such a fund would provide a transparent and predictable mechanism for setting aside reserves in case of contingencies, thus stabilizing services and taxes in a volatile fiscal environment.

Table 1. FYs 2006-2009 Financial Plan

($ in millions)

	FY 2006	FY 2007	FY 2008	FY 2009	Changes FY 2006 – FY 2009 Dollar	Changes FY 2006 – FY 2009 Percent
Revenues						
Taxes:						
General Property Tax	$12,609	$13,295	$14,229	$14,884	$3,237	27.8%
Other Taxes	$17,434	$17,352	$17,518	$18,472	($641)	(3.4%)
Tax Audit Revenues	$512	$509	$509	$509	($16)	(3.1%)
Tax Reduction Program	($221)	($233)	($92)	($141)	($141)	N/A
Miscellaneous Revenues	$4,826	$4,486	$4,506	$4,528	($1,901)	(29.6%)
Unrestricted Intergovernmental Aid	$562	$562	$562	$562	$0	0.0%
Anticipated State & Federal Actions	$50	$0	$0	$0	$0	0.0%
Less: Intra-City Revenues	($1,289)	($1,271)	($1,270)	($1,271)	$48	(3.6%)
Disallowances Against Categorical Grants	($15)	($15)	($15)	($15)	$0	0.0%
Subtotal: City Funds	$34,468	$34,685	$35,947	$37,528	$585	1.6%
Other Categorical Grants	$927	$923	$928	$934	$32	3.5%
Inter-Fund Revenues	$364	$355	$344	$343	($6)	(1.7%)
Total City & Inter-Fund Revenues	$35,759	$35,963	$37,219	$38,805	$611	1.6%
Federal Categorical Grants	$5,109	$4,860	$4,850	$4,850	($2,071)	(29.9%)
State Categorical Grants	$9,320	$9,372	$9,432	$9,475	$444	4.9%
Total Revenues	$50,188	$50,195	$51,501	$53,130	($1,016)	(1.9%)
Expenditures						
Personal Service						
Salaries and Wages	$18,151	$18,260	$18,437	$18,651	$287	1.6%
Pensions	$4,735	$5,086	$4,979	$4,851	$1,479	43.9%
Fringe Benefits	$5,549	$5,804	$6,145	$6,467	$1,279	24.7%
Subtotal-PS	$28,435	$29,150	$29,561	$29,969	$3,045	11.3%
Other Than Personal Service						
Medical Assistance	$5,024	$5,172	$5,319	$5,458	$541	11.0%
Public Assistance	$2,516	$2,504	$2,504	$2,504	($102)	(3.9%)
Pay-As-You-Go Capital	$200	$200	$200	$200	$0	0.0%
All Other	$14,246	$13,769	$13,886	$14,066	($943)	(6.3%)
Subtotal-OTPS	$21,986	$21,645	$21,909	$22,228	($504)	(2.2%)
Debt Service						
Principal	$1,433	$1,726	$1,730	$1,750	$241	16.0%
Interest & Offsets	$1,904	$2,390	$2,758	$3,091	$1,334	75.9%
Total	$3,337	$4,116	$4,488	$4,841	$1,575	48.2%
Prepayment	($3,528)	($193)	$0	$0	$1,923	(100.0%)
NYCTFA						
Principal	$341	$369	$414	$432	$51	13.4%
Interest & Offsets	$606	$586	$569	$556	$40	7.7%
Total	$947	$955	$983	$988	$91	10.1%
General Reserve	$300	$300	$300	$300	$260	650.0%
Subtotal	$51,477	$55,973	$57,241	$58,326	$442	681.3%
Less: Intra-City Expenses	($1,289)	($1,271)	($1,270)	($1,271)	$48	(3.6%)
Total Expenditures	$50,188	$54,702	$55,971	$57,055	$2,910	5.4%
Gap To Be Closed	**$0**	**($4,507)**	**($4,470)**	**($3,925)**	**($3,925)**	

NOTE: Tax revenues include STAR and PIT revenue retained for NYCTFA debt service. Expenditures include NYCTFA debt service.

Table 2. Plan to Plan Changes, Adopted Budget FY 2006 vs. Executive FY 2006

($ in millions)

	FY 2006	FY 2007	FY 2008	FY 2009
Revenues				
Taxes:				
General Property Tax	$130	$79	$53	$34
Other Taxes	$226	$0	$0	$0
Tax Audit Revenues	$0	$0	$0	$0
Tax Reduction Program	$14	($56)	($75)	($103)
Miscellaneous Revenues	$61	$24	$21	$22
Unrestricted Intergovernmental Aid	$0	$0	$0	$0
Anticipated State & Federal Actions	$0	$0	$0	$0
Less: Intra-City Revenues	($40)	($22)	($21)	($22)
Disallowances Against Categorical Grants	$0	$0	$0	$0
Subtotal: City Funds	$391	$25	($22)	($69)
Other Categorical Grants	$4	($4)	($4)	($4)
Inter-Fund Revenues	$0	$0	$1	$0
Total City & Inter-Fund Revenues	$395	$21	($25)	($73)
Federal Categorical Grants	$28	$2	$2	$3
State Categorical Grants	$41	$11	$11	$11
Total Revenues	$464	$34	($12)	($59)
Expenditures				
Personal Service				
Salaries and Wages	$380	$242	$191	$133
Pensions	($27)	$68	$68	$68
Fringe Benefits	($3)	($7)	($9)	($10)
Subtotal-PS	$350	$303	$250	$191
Other Than Personal Service				
Medical Assistance	$0	$0	$0	$0
Public Assistance	$108	$151	$151	$151
Pay-As-You-Go Capital	$0	$0	$0	$0
All Other	$344	($116)	($119)	($118)
Subtotal-OTPS	$452	$35	$32	$33
Debt Service				
Principal	$6	$6	$19	$20
Interest & Offsets	($47)	($61)	($58)	($59)
Total	($41)	($55)	($39)	($39)
Prepayment	($257)	($193)	$0	$0
NYCTFA				
Principal	$0	$0	$0	$0
Interest & Offsets	$0	$0	$0	$0
Total	$0	$0	$0	$0
General Reserve	$0	$0	$0	$0
Subtotal	$504	$90	$243	$185
Less: Intra-City Expenses	($40)	($22)	($21)	($22)
Total Expenditures	$464	$68	$222	$163
Gap To Be Closed	**$0**	**($34)**	**($234)**	**($222)**

NOTE: Tax revenues include STAR and PIT revenue retained for NYCTFA debt service. Expenditures include NYCTFA debt service.

Table 3. FYs 2006-2009 Risks and Offsets

($ in millions)

	FY 2006	FY 2007	FY 2008	FY 2009
City Stated Gap	**$0**	**($4,507)**	**($4,470)**	**($3,925)**
Tax Revenue Assumptions				
Property Tax	$10	$10	$40	$100
Personal Income Tax	200	325	190	(125)
Business Taxes	240	125	140	(45)
Sales Tax	60	(25)	(45)	(170)
Real-Estate-Related Taxes	600	140	40	0
Subtotal	**$1,110**	**$575**	**$365**	**($240)**
Expenditure Projections				
Overtime	($181)	($75)	($75)	($75)
Labor	($30)	$0	$0	$0
Flex Fund for Family Services	(0)	(10)	(10)	(10)
Subtotal	**($211)**	**($85)**	**($85)**	**($85)**
Total Risk/Offsets	**$899**	**$490**	**$280**	**($325)**
Restated Gap	**$899**	**($4,017)**	**($4,190)**	**($4,250)**

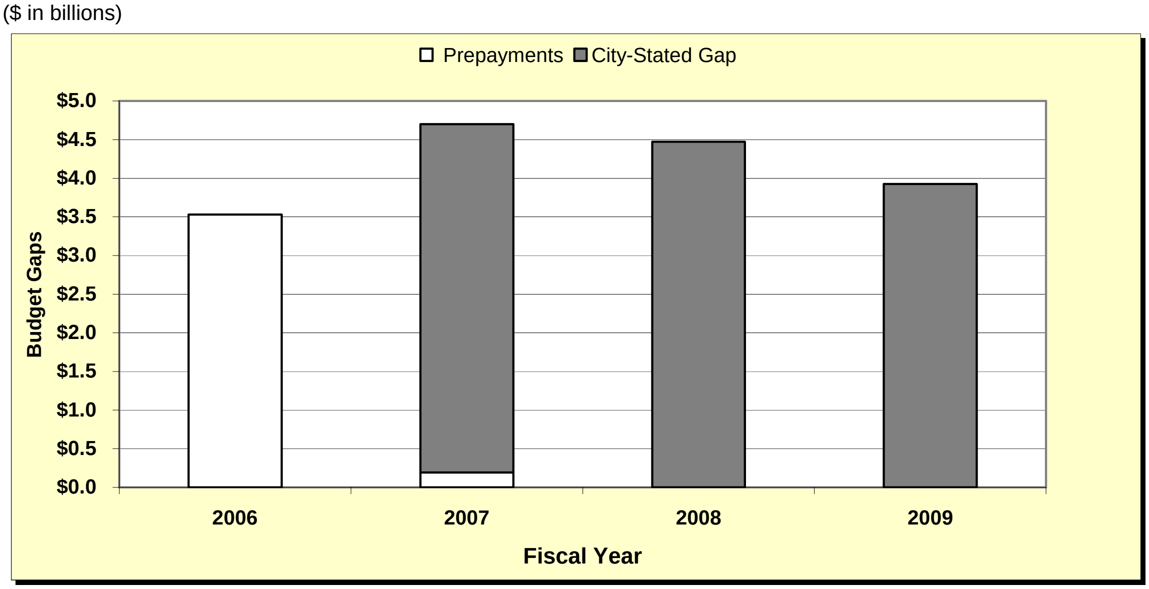
II. The Outyear Gaps

The City's FYs 2006-2009 Financial Plan shows that while the City has adopted a balanced budget of $50.2 billion for FY 2006, multi-billion dollar gaps loom in the outyears of the Financial Plan. The persistence of outyear gaps reflects the underlying imbalance between revenue and expenditure growth as well as the use of significant non-recurring resources to balance the FY 2006 budget, almost all of which consists of the prepayment of $3.5 billion of FY 2006 expenditures from the FY 2005 surplus. [1]

As Chart 1 below shows, without the benefit of the prepayments, FY 2006 expenditures exceed revenues by $3.5 billion. The gap widens to $4.5 billion in FY 2007 as expenditure growth is expected to outpace revenue growth. In the latter half of the financial plan period, the gaps narrow modestly when revenue growth is projected to exceed expenditure growth. However, because of the disparity between spending and revenue levels in the first half of the Financial Plan, the gaps remain significant at $4.5 billion in FY 2008 and $3.9 billion in FY 2009.

***Chart 1.* Multi-Billion-Dollar Gaps Persist in the Outyears of the Financial Plan**

($ in billions)



SOURCE: NYC Office of Management and Budget and NYC Office of the Comptroller

[1] In addition to the $3.5 billion prepayments, the City is transferring $193 million of FY 2005 pay-as-you-go capital as a grant to the New York City Transitional Authority (NYCTFA). The grant will enable the NYCTFA to reduce FY 2007 NYCTFA debt service by a like amount.

The FY 2006 prepayments are funded with an unprecedented FY 2005 surplus of $3.5 billion.[2] The surplus resulted from an unexpected surge in revenues fueled by the continued strength in the economy and a robust real estate market that exceeded expectations. Personal income tax (PIT), sales, and business tax revenues for FY 2005 are now projected to total $2.2 billion more than FY 2005 Adopted Budget projections. Real-estate-related tax revenues, driven by refinancing and real-estate transaction activities, have been revised upward by $1.3 billion. Consequently, the expected FY 2005 surplus has grown to $3.5 billion from the $220 million projected in June 2004.

In addition to the prepayments, the City's FY 2006 Adopted Budget includes $708 million of initiatives to help close the FY 2006 budget gap.[3] Of these, only $253 million are new FY 2006 gap closing initiatives, placing the total value of FY 2006 gap-closing actions among the least of the last ten years. The remaining $454 million in relief derive from gap-closing actions initiated in FY 2005 and earlier. If the City had developed a more aggressive gap-closing program with recurring benefits, not only would it have narrowed the outyear gaps, but part of the surplus could then have been reserved for future budget relief.

A. RISKS AND OFFSETS TO THE FYS 2006-2009 FINANCIAL PLAN

The Comptroller's Office projects higher revenues of $1.1 billion in FY 2006, $575 million in FY 2007, and $365 million in FY 2008 than the Adopted Budget, as shown in Table 3 on page 3. The higher revenues more than offset additional spending identified by the Comptroller's Office, totaling $211 million in FY 2006 and $85 million in each of FYs 2007 and 2008. As a result, the Comptroller's Office projects additional resources of $899 million in FY 2006, $490 million in FY 2007, and $280 million in FY 2008 that will generate a surplus of $929 million in FY 2006 and narrow the FY 2007 gap to $4.0 billion and the FY 2008 gap to $4.2 billion, not counting any benefit that the FY 2006 surplus might confer to the FY 2007 budget.

As discussed in "The Comptroller's Forecast of Tax Revenues" beginning on page 16, the Comptroller's revenue offsets and risks to the City's forecast stem from a different economic outlook.

The expenditure risks to the budget stem primarily from the City's under-budgeting of overtime expenditure. As discussed in "Overtime" beginning on page 25, the Comptroller's Office estimates that FY 2006 overtime expenditure may be

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[2] The estimated $3.5 billion FY 2005 surplus is the projected excess revenues over expenditures after prepayments of certain FY 2005 expenditures in FY 2004. The City prepaid $1.9 billion of FY 2005 expenditures in FY 2004. Without the benefit of this prepayment, projected FY 2005 expenditure would be $1.9 billion higher and the surplus generated from FY 2005 operations would be $1.6 billion.

[3] Includes gap-closing initiatives from the Preliminary FY 2006 Budget, the FY 2006 Executive Budget, and the FY 2006 Adopted Budget.

$181 million higher than the City's projection, with the outyears being $75 million more than the City's forecast. Also, the City has not taken into account the full impact of the new Flex Fund for Family Services which could require additional City funding of $10 million per year in FYs 2007 to 2009.

Because the outcome of current labor negotiations is uncertain as to timing and magnitude, risks associated with potential settlements are not categorized in Table 3. While the City has increased its labor reserve to fund wage increases for all uniformed employees patterned after the Public Employment Relations Board's (PERB) decision on the Patrolmen's Benevolent Association's (PBA) contract, it continues to fund the unsettled teachers' contract based on the DC 37 agreement. Past settlement patterns and the PERB decision suggest that the teachers' contract will likely exceed the terms of the DC 37 agreement. Every percentage point increase over the DC 37 contract awarded to the teachers, whose contract expired on May 31, 2003, would cost the City an additional $95 million in back pay and $80 million a year going forward. Furthermore, the retroactive cost of the second increase of 2.0 percent on the 25th month of the DC 37 contract would total $30 million. Also, if the teachers' contract were to be settled along the terms of the PBA contract, it would cost the City $980 million in retroactive payments in FY 2006 beyond what has been put in the reserve, plus $120 million in additional FY 2006 wages.[4]

[4] This analysis assumes that going forward the City will be able to achieve productivity savings equivalent to the PBA contract, thereby resulting in a differential of 1.5 percent between the UFT and the DC 37 contract.

III. The State of the Economy

A. THE U.S. ECONOMY

Recent Highlights

The U.S. economy continues to expand, but at a slower pace than in 2004 and with continued weakness in job gains. Real gross domestic product (GDP) grew at an annualized rate of 3.8 percent in the first quarter of 2005, after averaging 4.4 percent for the entire year 2004. But after three years of economic recovery, private-sector job growth from the previous peak of December 2000 to June 2005 was only 0.1 percent, despite 5.7 percent growth in population during the period.

Key recent developments include:

- The Federal Open Market Committee has steadily raised the federal funds rate to 3.25 percent in July, closer to the long-term rate. The Fed's Chairman told Congress in July that the "measured pace" of increases in the rate will continue.

- Disagreements within the European Union have weakened the euro relative to the dollar.

- On July 21 the People's Bank of China (PBoC) announced a 2.1 percent revaluation of the yuan (renminbi) against the dollar and at the same time announced that it would in the future stop pegging the yuan exclusively to the dollar and would peg it against a basket of unspecified currencies. The yuan will now be allowed to fluctuate up to 0.3 percent per day.

- Recent demand for long-term debt has been high, keeping long-term interest rates lower than expected.

- Crude oil prices passed the $60-per-barrel mark in June, almost $20 above the average of $43.3 per barrel six months earlier.

Forecasts

U.S. economic growth is likely to be slower in 2005 and 2006 than in 2004, but the Blue Chip forecasters project a low probability of a full-blown recession. Developments relating to the U.S. trade deficit, oil prices, and interest rates will be key in determining how quickly GDP growth decelerates. Important factors include the following:

- *Higher short-term rates* usually put upward pressure on long-term rates, but long-term yields have not increased as expected. One reason for low long-term rates is a relatively weak outlook for company dividends and stock prices, as evidenced by the fact that stock-market indexes have failed to rally much in 2005. If short-term interest rates eventually exceed long-term rates (an "inverted yield curve"), it is a leading indicator of recession.

- *A stronger dollar relative to the euro* raises the relative prices of the U.S. goods above goods produced abroad and therefore makes U.S. goods less competitive in international markets. The consequent tendency is for U.S. exports to fall and imports to rise, increasing the U.S. trade deficit and creating a drag on GDP growth.

- *The yuan revaluation* is small to start with and by itself is not expected to reduce the U.S. trade deficit substantially. But as other Asian countries diversify their reserves and other adjustments occur, the impact could be larger over time.

- *The PBoC's new policy implies higher U.S. Treasury rates*. Maintaining the dollar peg had required the PBoC to purchase hundreds of millions of dollars of U.S. Treasuries. Now the PBoC will not depend as much on dollar-denominated reserves, which implies upward pressure on Treasury interest rates. The extent of the pressure depends in part on the speed with which the PBoC implements further revaluation of the yuan, as it has made clear it intends to do.

- *Some projections show crude oil prices exceeding $100 per barrel* in 2006. Governments can deal with the threatened rise in oil prices by letting the market adjust or by reducing the impact of higher oil prices with some form of price subsidy. Either way, it means significant economic costs to consumers or economic efficiency, or both, and a problematic outlook for real GDP.

Table 4 shows the forecasts of real GDP and payroll jobs by the Comptroller and the City, for 2005 to 2009:

- The Comptroller expects a gradual slowing of GDP growth over the Plan period, but expects little change in the 1.3 percent growth rate of jobs.

- The City forecasts a sharp decline in GDP growth in 2006, to 3.0 percent from 3.7 percent. The City expects a steady decline in the rate of growth of jobs through 2008, with a negligible recovery in 2009.

Table 4. Forecasts of Real GDP and Payroll Jobs, Percent Change, 2005-2009

Forecasts by	Forecasts of	2005	2006	2007	2008	2009
Comptroller	GDP	3.5	3.4	3.0	2.8	2.6
	Payroll Jobs	1.4	1.3	1.3	1.3	1.3
City	GDP	3.7	3.0	3.0	3.1	3.2
	Payroll Jobs	1.7	1.2	0.9	0.7	0.8

SOURCE: Comptroller=Forecast by the NYC Comptroller's Office. Mayor=Forecast by the NYC Office of Management and Budget.

B. THE NEW YORK CITY ECONOMY

Recent Highlights

In the first quarter of 2005, NYC's gross product grew 4.0 percent, slightly faster than GDP growth of 3.8 percent. During the first half of 2005, NYC payroll jobs grew at an annualized rate of 1.7 percent, slightly above the 1.6 percent rate of the nation. However, the City's inflation and unemployment rates were both disappointing relative to the nation's – the City's inflation rate averaged 3.7 percent, higher than the nation's 3.0 percent. The City's unemployment rate averaged 5.7 percent in the first half 2005, exceeding the nation's 5.2 percent.

In the first half of 2005, the City added 31,600 jobs in the private sector, and lost 1,200 jobs in the public sector, and experienced a net gain of 30,400 jobs. The sectors showing the largest job gains included education and health services, which added 10,400 jobs; professional and business services, which added 9,000 jobs; leisure and hospitality, which added 6,000 jobs; and the high-paying financial-activities sector, which added 5,000 jobs.

In line with the higher level of jobs, the rate of vacant commercial space in Manhattan (according to Cushman & Wakefield) declined to 10.4 percent in the first quarter of 2005, an improvement but substantially higher than the 5.9 percent average vacancy rate for the two years (1999-2000) leading up to the last recession. Similarly, the hotel occupancy rate (according to PKF) has risen to an average of 83.4 percent during the first five months of 2005, an increase over the 79.2 percent average during the first five months of 2004. The decline in the value of the dollar has attracted more tourists to the City, which has increased demand for hotel rooms.

Forecasts

The outlook for the City is similar to that for the nation. Local leading indicators are positive:

- *The help-wanted advertising index* averaged 19.2 in the first five months of 2005, 11.6 percent more than the 17.2 in the first five months of 2004.

- *The National Association of Purchasing Managers-NYC index* was 19.8 percent higher in the first six months of 2005 than it was in the first six months of 2004.

- *The number of building permits authorized* increased 6.8 percent in the first half of 2005 compared with the first half of 2004.

However, national developments focus attention on the impact on the City of inflation and higher interest rates:

- The City's inflation rate has been above the national average since 2001. If U.S. prices rise, and the City's inflation remains higher than the nation's, a widening disparity in costs could make the City less competitive relative to other cities.

- Diversification away from the dollar threatens Wall Street profits by reducing the relative attractiveness of equity investments and raising the cost of capital. Higher interest rates also dampen consumer spending – the largest component of gross product – by diverting a larger share of spending to debt service, raising the cost of many goods, and lowering consumers' net worth by reducing the price of housing.

Table 5 shows the Comptroller's forecast of real gross city product (GCP) and payroll jobs for 2005 to 2009. The City's forecasts are shown in the lower part of the table. Both the Mayor and the Comptroller expect the City's economy to improve in 2005 compared with 2004. However, the Comptroller is projecting a gradual slowing of growth over the Plan period, while the City expects a sharper decline in growth in 2006 and 2007, followed by recovery.

The key difference between the two forecasts is that:

- The Comptroller's Office believes long-term interest rates will rise gradually, reducing GCP growth steadily over the plan period. The Comptroller's forecast is for long-term interest rates (10-year Treasuries) to average 4.3 percent through 2005, which implies rates higher than 4.3 percent in the fourth quarter of 2005.

- The City forecasts rapid near-term increases in long-term interest rates that induce a downturn on Wall Street in calendar year 2006, sharply slowing overall growth in the City's economy.

Table 5. Forecasts of NYC GCP and Payroll Jobs, Percent Change, 2005-2009

Forecast by	Forecast of	2005	2006	2007	2008	2009
Comptroller	GCP	3.3	2.9	2.7	2.4	2.4
	Payroll Jobs	30.0	28.0	26.0	25.0	28.0
City	GCP	2.6	1.7	0.6	3.9	4.0
	Payroll Jobs	39.9	37.8	24.8	26.4	31.4

SOURCE: Comptroller=Forecast by the NYC Comptroller's Office. Mayor=Forecast by the Mayor (Office of Management and Budget) in the Executive Budget.
Note: Payroll Job changes are in thousands and GCP changes are in percent.

IV. The FYs 2006-2009 Financial Plan

The FYs 2006-2009 Financial Plan projects that revenues will decline by 1.9 percent over the financial plan period, from $54.1 billion in FY 2005 to $53.1 billion in FY 2009.[5] Over the same period, expenditures are projected to grow by 5.4 percent, from $54.1 billion to $57.1 billion.[6] However, spending growth rates in the Financial Plan are distorted by prepayments. After adjusting for the effect of prepayments, the expenditure growth over the financial plan period increases to 8.6 percent. The disparity in growth rates and the underlying gap before prepayments lead to outyear gaps of $4.5 billion in FY 2007 and FY 2008, and $3.9 billion in FY 2009.

In the latter part of the financial plan period, revenue growth is projected to outpace that of expenditures. After falling by 7.3 percent in FY 2006 due to the expiration of the temporary tax increase, revenues are projected to hold steady in FY 2007 and then show increasing strength in FY 2008 and FY 2009. Expenditures are expected to slow down in the outyears with growth of 2.6 percent in FY 2007, followed by growth of 2.0 percent in FY 2008, and 1.9 percent in FY 2009.

A. REVENUE OUTLOOK

The overall decline in revenues projected by the City over the next four fiscal years is driven by the loss of non-recurring miscellaneous revenues and a fall-off in real estate transactions. Approximately $1.5 billion of non-recurring FY 2005 revenues include $744 million in back rents from the Port Authority of New York and New Jersey and $631 million for the reimbursement of MAC debt service. With no commensurate revenue sources in FY 2006 and beyond, projected miscellaneous revenues will drop 30.8 percent in FY 2006 and remain stable in the outyears. In contrast, tax revenues are projected by the City to grow 7.8 percent over the financial plan period. The property tax, which accounts for more than 40 percent of tax revenues, will be the main engine of growth. Property tax revenues are projected to grow 27.8 percent over the financial plan period as strong appreciation in property values in recent years will be reflected in increased assessed values. Property tax revenues are discussed in greater detail in "Property Tax Revenues," beginning on page 15. Real-estate-related tax revenues, which escalated in recent years due to refinancing and transaction activities, are projected in the plan to decline 50 percent as these activities are expected to plummet in response to rising interest rates.

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[5] Revenues include that portion of PIT revenues earmarked for NYCTFA debt service.

[6] Expenditures include NYCTFA debt service.

Table 6. Projected Revenue Growth, FYs 2006-2009

(Percent)

	FY 2006	FY 2007	FY 2008	FY 2009	FY 06-09	Average Annual Growth
Property Tax	8.3	5.4	7.0	4.6	27.8	6.3
PIT	(7.7)	(2.0)	3.1	7.0	(0.2)	(0.0)
Real-Estate-Related	(37.6)	(17.9)	(3.6)	1.2	(50.0)	(15.9)
Other Non-Property Tax	(4.8)	3.0	1.5	4.2	3.7	0.9
Subtotal Tax Revenues	(3.0)	1.9	4.0	4.9	7.8	1.9
Miscellaneous Revenue	(30.8)	(9.1)	0.7	0.6	(36.3)	(10.6)
Others	3.2	(1.0)	(0.5)	0.4	2.1	0.5
IGA	0.0	0.0	0.0	0.0	0.0	0.0
Anticipated State & Federal Aid	0.0	(100.0)	0.0	0.0	0.0	0.0
Federal Categorical Grant	(26.2)	(4.9)	(0.2)	0.0	(29.9)	(8.5)
State Categorical Grant	3.2	0.6	0.6	0.5	4.9	1.2
Subtotal Non-Tax Revenues	(13.1)	(2.9)	0.3	0.4	(15.1)	(4.0)
Total Revenues	(7.3)	0.0	2.6	3.2	(1.9)	(0.5)

SOURCE: NYC Office of Management and Budget and NYC Office of the Comptroller
NOTE: PIT includes that portion of PIT revenues earmarked for NYCTFA

Tax Revenues

In the FY 2006 Adopted Budget and Financial Plan, the City forecasts tax revenues at $30.3 billion in FY 2006, $30.9 billion in FY 2007, $32.2 billion in FY 2008, and $33.7 billion in FY 2009. Non-property tax revenue projections decline in FYs 2006-2007 reflecting the City's anticipation of slower growth in the local economy, and the expiration of temporary tax rate increases. Starting in FY 2008, the City expects non-property tax revenues to improve in response to an expected rebound in the local economy. Throughout the plan period, property tax revenue growth rises because of higher property values. Higher property tax revenue more than offsets the anticipated decrease in the economically sensitive non-property tax revenues.

The Comptroller's forecasts of non-property tax revenues are higher than the City's through FY 2008 and slightly lower in FY 2009, reflecting differences in the anticipated impact of tax policy changes and economic assumptions for the local economy. The risks and offsets noted by the Comptroller are compared with the City's assumptions in Table 7, on page 13.[7]

City Estimates of Growth in Tax Revenues

The City expects that property tax revenues will be the main driver of tax-revenue growth, increasing by $3.2 billion, or 6.3 percent annually, during the plan period. This

[7] Revenues include that portion of PIT revenues earmarked for NYCTFA debt service.

growth offsets a 1.0 percent annual decline in non-property tax revenues. (See Table 7 for details of the City revenue forecast.)

Table 7. Changes in NYC Tax Revenues, City Forecast, FYs 2006-2009

($ in millions)

	Forecast Annual Change in Revenues				Change	Average Annual
	FY 2006	**FY 2007**	**FY 2008**	**FY 2009**	**FYs 2006-09**	**Growth (%)**
Property	$962	$686	$934	$654	$3,236	6.3%
Non-Property	(1,912)	(96)	307	906	(795)	(1.0)
PIT	(548)	(131)	200	466	(13)	(0.05)
Business	(186)	189	32	210	245	1.6
Sales	(222)	143	114	237	272	1.5
Real-Estate-Related	(876)	(260)	(43)	14	(1,165)	(15.9)
All Other	(80)	(37)	4	(21)	(134)	(1.6)
Total Change	**($950)**	**$590**	**$1,241**	**$1,560**	**$2,441**	**1.9%**

SOURCE: NYC Office of Management and Budget.
NOTE: The revenue changes include the impact of both economic conditions and tax policy changes.

Overall, property, business, and sales tax revenues show the most rapid growth. PIT revenues are projected to decline over the financial plan period because the temporary tax rate increase expires and because economic growth in the near term is expected to be slow. The City forecasts that real-estate-related tax revenues will plunge $1.2 billion, or 16 percent annually, based on its expectation of higher long term interest rates. Sales tax revenues are projected to increase in the outyears in response to anticipated increases in wages.

Tax revenues are projected to decline $952 million in FY 2006. Most of the decline is from a projected drop of $876 million in real-estate-related tax revenues. The City expects this to be partially offset by higher property tax revenues in FY 2006.

Business tax revenues are expected to drop 5.1 percent in FY 2006 and rise in the outyears. The City expects New York Stock Exchange member-firm profits to increase in calendar year 2005 to $14.4 billion, then decline slightly to $14 billion in 2006 and more sharply to $10 billion in 2007. The slide in Wall Street profits in 2006 and 2007 leads to little growth in business taxes in FY 2008.

Tax reduction initiatives account for nearly $830 million of forgone revenues in FY 2006, growing to $888 million in FY 2009, including:

- *Expiration of two temporary tax rate increases worth $353 million in FY 2006.* These include**:** (1) ending the temporary PIT rate increase worth $236 million in FY 2006, and (2) expiration of the temporary sales tax rate increase of 0.125 percent, worth $117 million in FY 2006.

- *A $400 property tax rebate worth $256 million annually in FY 2006 and FY 2007.* The rebate is scheduled for owners of one-, two-, and three-family homes, and cooperative and condominium owners.

- *Acceleration of the reinstatement of the exemption from local sales tax on clothing and footwear purchases under $110, worth $184 million in FY 2006 and $166 million in FY 2007.* This has been approved by the State Legislature to take effect on September 1, 2005.

- *Other small tax relief provisions worth $36.7 million, growing to $141 million in FY 2009***.** The largest program is tax relief for the rehabilitation of certain rental housing stock. Other provisions include a phase-out of taxation of out-of-City small-business transactions (by aligning the City's unincorporated business tax with the City's general corporation tax and with national business income tax methods), an increase in the income threshold for the Senior Citizen Rent Increase Exemption, and several tax incentives for Lower Manhattan economic development.

City's Anticipated PIT Recovery

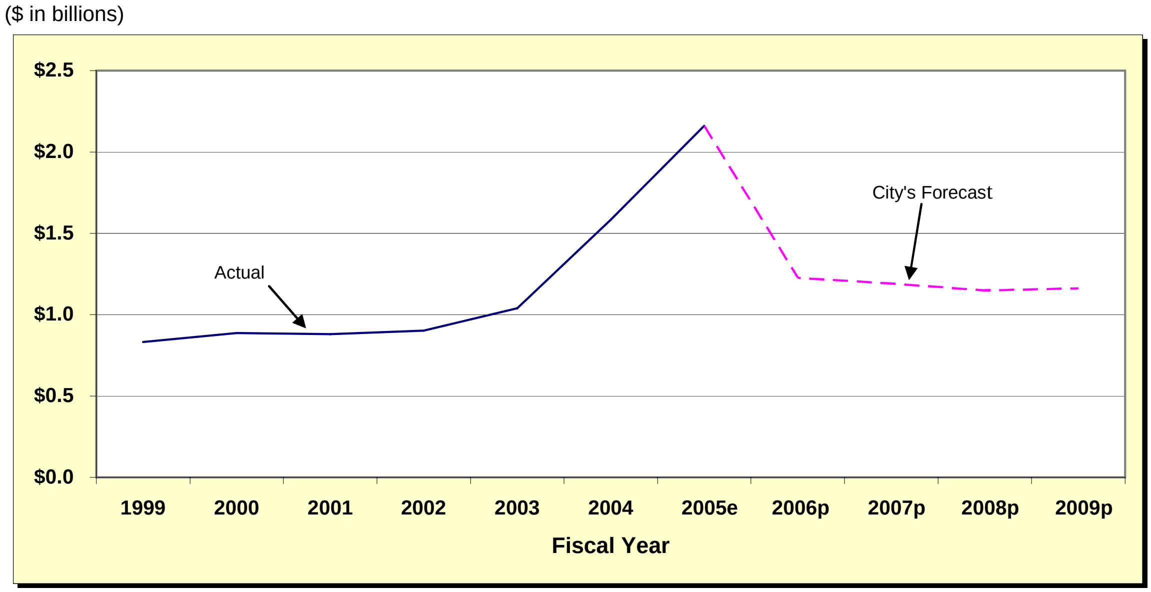
The City forecasts that PIT revenues, including revenues earmarked for NYCTFA debt service, will decline by 7.7 percent in FY 2006 and 2.0 percent in FY 2007. This decline reflects the City's anticipation of a slowdown in economic growth, as well as the expiration of the temporary PIT rate increases. For FY 2008, the City projects an increase of $200 million (3.1 percent) and for FY 2009 an increase of $466 million (7.0 percent).

Effective January 1, 2003, the City imposed a temporary PIT increase through a revised rate schedule. The higher tax rates were 4.25 percent for single filers with income over $100,000 and joint filers with incomes over $150,000, and 4.45 percent for all filers with incomes above $500,000 in 2003. The temporary increase is phased out by dropping the first additional rate to 4.175 percent in 2004 and to 4.05 percent in 2005. In FY 2005, the temporary PIT rate increase generated $538 million. In FY 2006, with the scheduled expiration of the increase on December 31, 2005, the revised rate schedule is projected to generate $308 million.

City Forecast for Real-Estate-Related Taxes

The persistence of low mortgage interest rates has spurred housing transactions and refinancing activities in recent years. Real-estate-transaction tax revenues consequently increased 52.4 percent in FY 2004 and 47 percent in FY 2005. The City expects long-term interest rates to rise, reducing real-estate-related tax revenues (from the real-property transfer tax and the mortgage recording tax), from $2.3 billion in FY 2005 to $1.5 billion in FY 2006, a drop of $876 million. After the decline in FY 2006, the City expects the level of real-estate-related taxes to revert to the long-term trend, with a decline of 17.9 percent in FY 2007, a decline of 3.6 percent in FY 2008, and growth of 1.2 percent in FY 2009. The City's forecast for real-estate-related taxes is based in part on Mortgage Bankers Association data showing that third-quarter 2004 mortgage refinancings were 74 percent below peak levels in 2003.

Chart 2. **Real-Estate-Related Tax Revenues, Actual and Forecast, FYs 1999-2009**



SOURCE: NYC Comptroller's Office, based on data from NYC Office of Management and Budget. Data are actual through FY 2004.

City's Expectations for Property Tax Revenues

For FY 2006, the City forecasts property tax revenue of $12.5 billion, an increase of $962 million, or 8.3 percent, over FY 2005. Property tax revenues account for 27 percent of the total increase in projected revenues in FY 2006. For the plan period, property tax revenues are projected to increase at an average annual rate of 6.3 percent. This favorable outlook is attributable to a sustained appreciation in market values in recent years that are associated with multi-family residential (Class 2) and commercial (Class 4) properties, which together account for more than three-quarters of the City's aggregate billable assessed value.[8.]

Property tax revenues are generally less variable than non-property revenues because of legal restrictions and adjustments on property assessment growth and decline. Assessment increases are limited for all one-, two-, and three-family residential properties and small condominiums (Class 1) and for Class 2 properties with fewer than 11 units. In addition, a five-year phase-in of assessment changes applies to all other Class 2 properties and all Class 4 properties, redistributing assessment increases and decreases into billable assessments over a five-year horizon at 20 percent each year. Increases in value not yet phased into billable assessed value are referred to as the "pipeline." This distributive mechanism serves to attenuate the impact of assessment

[8] Properties are not assessed at full market value but a proportion of market value for tax purposes. Billable assessed value is the assessed value on which tax liability is based.

changes, stabilizing the revenue stream while protecting property owners from large swings in property taxes.

Since FY 2002, market values of real estate properties have, on average, exhibited double-digit percentage growth. Consequently, the existing pipeline has increased substantially, enough to cushion a decline in market values should a slowdown in the housing market occur in FY 2006 or later. Even if long-term mortgage rates rise, property tax revenues will probably remain stable throughout the financial plan period.

Market values and actual and billable assessed values for all classes of properties are published by the New York City Department of Finance in the final assessment roll. Because of differences in assessment ratios, legal restrictions on assessment changes and different tax rates for different classes, larger increases in market values do not necessarily translate into larger increases in billable assessed values. For FY 2006, in the aggregate, the market value for Class 1 shows the greatest increase, 14.7 percent, but Class 1 actual assessed values increased by only 4.9 percent because of legal restrictions. (See Table 8.)

Table 8. NYC Property Valuation Growth, Year-Over-Year , FY 2005 to FY 2006

Type of Valuation	Class 1	Class 2	Class 3	Class 4	Total
Market Value	14.7%	13.6%	13.5%	12.7%	**13.9%**
Actual Assessed Value	4.9%	11.9%	13.5%	11.4%	**11.0%**
Billable Assessed Value	4.9%	7.0%	13.5%	7.5%	**7.5%**

SOURCE: NYC Comptroller's Office, based on data from NYC Department of Finance. Classes are based on the nature of the property.

The other three classes have larger relative increases in assessed value. Growth in assessed values in both Class 2 and 4 exceeded 11 percent, the highest rates since FY 1991. These increases provide sizeable contributions to the pipeline until FY 2010 and provide a buffer for the property tax base.

Comptroller's Forecast of Tax Revenues

The Comptroller's forecast of tax revenues for FY 2006 is higher than the City's by approximately $1.1 billion, or more than 3.0 percent of projected tax revenue in the Adopted Budget.

The Comptroller's forecasts of PIT, business, and sales tax revenues for FYs 2006-2009 reflect projections of the local economy that are slightly more positive than the City's in FYs 2006-2007 and are more negative than the City's in FYs 2008-2009. The Comptroller forecasts that tax revenues over the plan period will be cumulatively $1.8 billion higher than the City estimates (about $2 billion over the first three years, with an offset in the fourth year). The Comptroller's tax revenue forecast for FY 2006 reflects the Comptroller's anticipation of an additional $600 million in real-estate related tax revenues, and higher PIT, business, and sales tax revenues. (See Table 9.)

Table 9. Comptroller's Risks and Offsets to the City's Tax Revenues, FYs 2006-2009

($ in millions)

Tax	FY 2006	FY 2007	FY 2008	FY 2009
Property	($10)	$10	$40	$100
PIT	200	325	190	(125)
Business	240	125	140	(45)
Sales	60	(25)	(45)	(170)
Real Estate-Related	600	140	40	0
Total	**$1,090**	**$575**	**$365**	**$(240)**

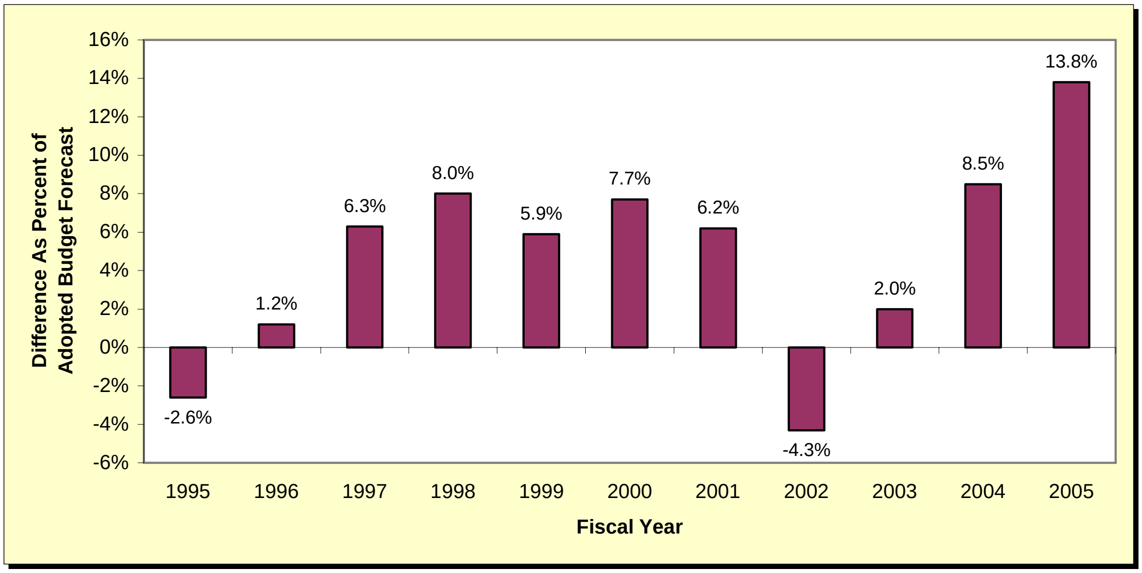
SOURCE: NYC Comptroller's Office, based on data from NYC Office of Management and Budget. A positive number indicates the Comptroller's forecast is higher than the City's.

Because of expected upward pressure on long-term interest rates, the Comptroller, like the City, expects a softening in the real estate markets, and therefore a decline in the volume of transactions. However, the Comptroller does not expect long term rates to rise as fast as the City anticipates and mortgage origination activity in late 2004 and the first half of 2005 has shown continued strength. The Comptroller's forecast of real-estate-related tax revenues in FY 2006 is therefore $600 million above the City's. In the outyears, the Comptroller's forecasts are higher than the City's but the gap narrows.

By the time of budget adoption, year-end FY 2005 collections of PIT, business, and sales taxes were $381 million greater than had been anticipated by the City at the time of the FY 2006 Executive Budget forecast. However, the Adopted Budget projections for FY 2006 were not adjusted to reflect the momentum revealed by actual tax collections. The Comptroller's Office expects that these tax revenues will increase in FY 2006, consistent with the economic outlook.

From FY 1995 to FY 2005, actual tax revenues have exceeded the City's adopted budget forecasts by an average of 4.0 percent. In nine years during that period, taxes have been underestimated at the time of budget adoption by an average of approximately $1.5 billion per year, or 6.9 percent of the forecast. (See Chart 3.)

Chart 3. **Actual Tax Revenues minus Adopted Budget Forecasts As a Percentage of the Adopted Budget Forecast**



SOURCE: Actual tax revenues from the *Comprehensive Annual Financial Reports of the Comptroller.* Forecasts from OMB, *Adopted Budgets*.

NOTE: Underestimates are actual tax revenues less forecast. Percentages are underestimates divided by the forecast.

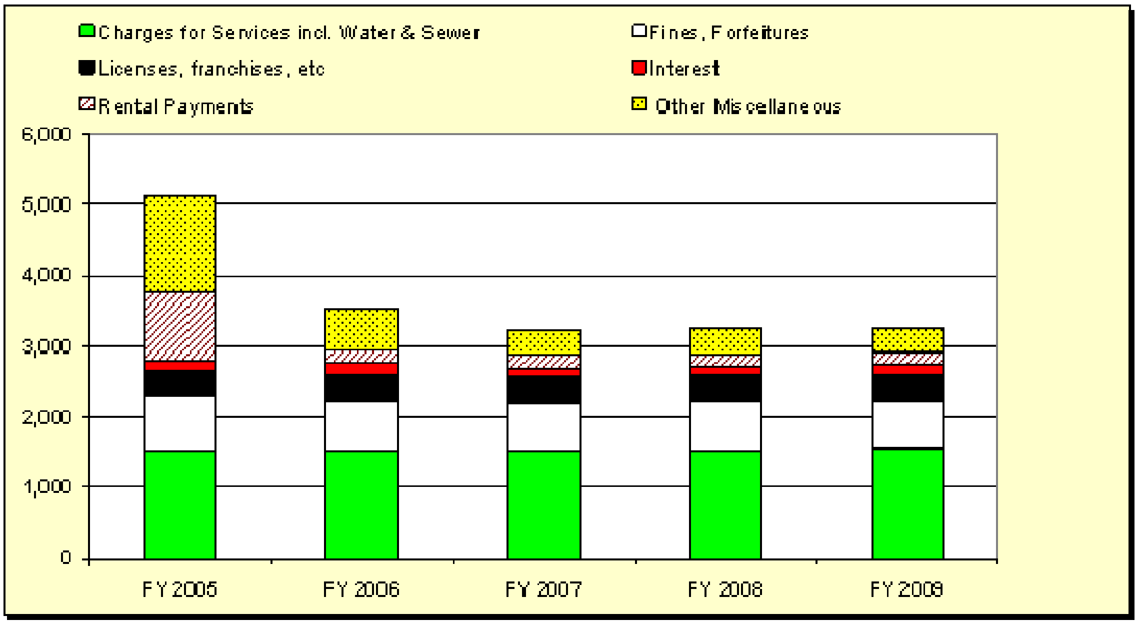
The only two years since 1994 with overestimates of tax revenues were: (1) FY 1995, which included an unexpected hike in interest rates to 5.5 percent (from 3.0 percent earlier in 1994), a substantial appreciation in the value of the dollar, the devaluation of the Mexican peso in December 1994 and a subsequent global financial crisis; (2) FY 2002, which included the shock of 9/11.

Miscellaneous Revenues

Miscellaneous revenues are locally-raised non-tax revenues, including fees charged for licenses, franchises and permits, charges for municipal services, fines, rental income, interest income, and water and sewer revenues. As Chart 4 shows, in the FY 2006 Adopted Budget and Financial Plan the City forecasts that miscellaneous revenues will decline nearly 31 percent to $3.5 billion in FY 2006, from more than $5 billion in FY 2005 (exclusive of private grants and intra-City revenues). This decrease in large part reflects the loss of certain non-recurring resources available in FY 2005 such as the State reimbursement for FY 2004 MAC debt service, airport rental arrears, and asset sales. As these funds will not be available in the outyears, the City expects miscellaneous income to drop sharply in the current fiscal year and remain flat throughout the plan period.

Chart 4. **Miscellaneous Revenues, City Forecast, FYs 2005-2009**

($ in millions)



SOURCE: NYC Comptroller's Office, based on data from NYC Office of Management and Budget.

Federal and State Aid

The City has established baseline assumptions for Federal and State aid totaling $14.43 billion in the FY 2006 Adopted Budget, constituting about 29 percent of its overall revenue estimates. The projections represent a decline of about $523 million from the FY 2005 forecast, net of FEMA insurance proceeds. The decrease is mainly attributable to more conservative assumptions regarding Federal support for education, welfare, and emergency response initiatives. The projections in the outyears average about $14.28 billion each year and reflect only marginal changes from the April Plan assumptions. Outside of moderate growth in education aid stemming mainly from rising State reimbursement for pupil transportation, the June Plan contains relatively stable projections for most aid categories from FY 2007 to FY 2009.

Over the term of the Financial Plan, the City could face risks of $10 million annually in the outyears stemming from the creation of the Flex Fund for Family Services. The flex fund, which was approved as part of State budget adoption, would consolidate funding for certain welfare programs while reducing overall State support for these services. The projected risks are substantially lower than the City's initial estimates, which pegged the potential cost at $121 million annually. The City indicates that it would identify options to further minimize the impact of this block grant.

Among developments that could have a major impact on the City's State aid assumptions in the outyears is the ongoing Campaign for Fiscal Equity (CFE) litigation. The case, which is currently under appeal, has been scheduled to be heard by the State

Appellate Court in October 2005. The State filed an appeal in May 2005 challenging a final order by State Justice Leland DeGrasse that would substantially increase funding for the City's education budget. The Court order established a phase-in schedule under which education support would increase by an increment of $1.41 billion each year. By the end of the four-year phase-in period, education funding would increase by about $5.63 billion going forward. The final outcome of the CFE case could have a significant impact on expected education aid beginning in FY 2007.

B. EXPENDITURE ANALYSIS

Spending on debt service and non-discretionary spending on pension, health insurance, Medicaid, and judgments and claims (J&C) account for $17.4 billion of projected FY 2006 spending. These areas are expected to grow the fastest over the financial plan period. As Table 10 shows, total spending in these areas is projected to increase 32.3 percent while spending in the remaining areas is projected to decline 1.3 percent.

Of these spending categories, pension contributions, health insurance cost, and debt service, which together account for $11.8 billion of FY 2006 expenditures are projected to grow at a combined growth rate of 43 percent. Most of this growth is projected for the first two years of the Financial Plan, when spending is expected to increase by 32 percent. Pension contributions, which show the most rapid expected growth overall, are projected to decline in FY 2008 and FY 2009, as shown in Table 10. This reversal in pension contribution cost reflects the recognition of actuarial investment gains and losses. Fiscal years 2006 and 2007 are the final years of the cumulative phase-in of actuarial investment losses in FY 2001 and FY 2002 and the beginning years of the phase-in of actuarial investment gains in FY 2003, FY 2004, and FY 2005.[9] At that point, pension contributions are expected to decline as the recognition of investment losses from prior years remains flat while recognition of gains continues to be phased-in.

The growth in debt service is driven mainly by new general obligation debt of $18.3 billion over the course of the financial plan period. After rising 18.3 percent in FY 2007, growth in debt service is expected to moderate to 7.9 percent in FY 2008 and 6.7 percent in FY 2009. The spike in debt service spending in FY 2007 reflects the scheduled amortization of principal of existing debt, which is anticipated to increase $320 million.[10]

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[9] Recognition of actuarial investment returns above or below the actuarial investment return assumption of 8.0 percent is currently phased in, cumulatively, over a five-year period beginning at 10 percent in year one, 25 percent in year two, 45 percent in year three, 70 percent in year four, and 100 percent in year five. Pension contributions are reduced or increased by the recognition of actuarial investment gains or losses.

[10] Includes both G.O. and NYCTFA debt service.

Table 10. Projected Expenditure Growth, FYs 2006-2009

	FY 2006	FY 2007	FY 2008	FY 2009	FY 06-09	Average Annual Growth
Pension	42.2%	7.6%	(2.2%)	(2.6%)	45.7%	9.9%
Health Insurance	11.3%	8.7%	9.5%	8.3%	43.5%	9.4%
Medicaid	2.2%	3.0%	2.8%	2.6%	11.0%	2.6%
Debt Service	2.9%	18.3%	7.9%	6.7%	40.3%	8.8%
J & C	5.3%	7.6%	6.7%	7.7%	30.3%	6.8%
Subtotal	**12.3%**	**9.0%**	**4.1%**	**3.6%**	**32.3%**	**7.2%**
Fringe Benefits	2.5%	0.1%	1.6%	1.4%	5.7%	1.4%
Salaries and Wages	(1.2%)	0.6%	1.0%	1.2%	1.6%	0.4%
Public Assistance	(3.4%)	(0.5%)	0.0%	0.0%	(3.9%)	(1.0%)
Other OTPS	(5.1%)	(2.4%)	0.6%	0.9%	(5.9%)	(1.5%)
Subtotal	**(2.5%)**	**(0.6%)**	**0.8%**	**1.0%**	**(1.3%)**	**(0.3%)**
Total	**1.9%**	**2.6%**	**2.0%**	**1.9%**	**8.6%**	**2.1%**

SOURCE: NYC Office of Management and Budget and NYC Office of the Comptroller.
NOTE: Includes NYCTFA debt service.

Spending growth on health insurance is projected to average 9.4 percent in each of the four years of the Financial Plan. The growth in health insurance cost reflects both anticipated rate increases and changes in headcount. The City assumes rate increases of 8.75 percent in FY 2006 and 8.0 percent in each of FY 2007 through FY 2009.

Pensions

The FY 2006 Adopted Budget projects that the City's pension expenditures will increase in FY 2006 and FY 2007 and then level off, as shown in Table 11 below. However, these projections will likely be revised later this fiscal year when changes in actuarial assumptions and methods are expected to be adopted.

Table 11. FY 2006 Adopted Budget Projections of the City's Pension Expenditures

($ in millions)

	FY 2005 Actual*	FY 2006	FY 2007	FY 2008	FY 2009
Five Actuarial Systems	$ 3,284	$ 4,639	$ 4,987	$ 4,875	$ 4,745
Other Systems	88	96	99	104	106
TOTAL	$ 3,372	$ 4,735	$ 5,086	$ 4,979	$ 4,851

* Preliminary Estimate

In April and May, 2005 the Chief Actuary of the City's pension systems issued recommendations for changes in actuarial assumptions and methods to each of the Boards of the five pension funds. The changes, some of which require State enabling legislation, can be classified into four categories. [11]

1. Updating of actuarial assumptions, based mostly on the findings of the experience study conducted by the independent actuarial auditor, Gabriel, Roeder, Smith & Company.

2. Fully recognizing all actuarial liabilities created by the Cost of Living Allowances (COLA) benefits enacted by Chapter 125 of the Laws of 2000 that are being phased-in over 10 years in accordance with Chapter 278 of the Laws of 2002.

3. Introducing a one-year lag methodology for the computations of employer pension contributions.

4. Changing to a new asset valuation method that phases in "unexpected" investment returns over a six-year period.[12]

These recommendations, which were originally expected to be implemented in time to compute employer contributions for FY 2005, have not yet been approved by any of the pension boards. As a result, FY 2005 employer contributions were based on existing assumptions and methods. If the Chief Actuary's recommendations for changes are modified, resubmitted to each Board of Trustees in late summer or fall, and approved, it is likely that they will be implemented effective FY 2006. Should the recommendations be approved in their entirety, the City's contributions to the five actuarial pension funds will be lower than the Adopted Budget projections by approximately $855 million in FY 2006, $528 million in FY 2007, and $11 million in FY 2008, but higher by $175 million in FY 2009.

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[11] For a more detailed discussion of the Chief Actuary's recommendations, see "Pensions" in *The Comptroller's Comments on The Preliminary Budget for Fiscal Year 2006 and The Financial Plan for FYs 2006-2009*.

[12] The Chief Actuary defines Unexpected Investment Returns as investment returns above or below the long-term Actuarial Investment Return Assumption (AIRA), which is currently 8.0 percent. The City's current actuarial asset valuation method recognizes Unexpected Investment Returns over a five-year period, cumulatively 10 percent in year one, 25 percent in year two, 45 percent in year three, 70 percent in year four and 100 percent in year five. If implemented, the new six-year actuarial asset valuation method, plus the one-year lag, would effectively recognize Unexpected Investment Returns over a seven-year period, cumulatively zero percent in year one, 15 percent in year two, 30 percent in year three, 45 percent in year four, 60 percent in year five, 80 percent in year six, and 100 percent in year seven.

Table 12. Comparison of Comptroller's Projections of Pension Contributions to the Five Actuarial Pension Funds with the City's Estimates

($ in millions)

	FY 2006	FY 2007	FY 2008	FY 2009
Chief Actuary's FY 2005 Projection[a]	$ 3,721	$ 4,396	$ 4,801	$ 4,857
Add: WTC Vicinity Legislation[b]	63	63	63	63
Comptroller's Office Estimate	**$ 3,784**	**$ 4,459**	**$ 4,864**	**$ 4,920**
FY 2006 Adopted Budget Projections	**$ 4,639**	**$ 4,987**	**$ 4,875**	**$ 4,745**
Contribution Decrease/(Increase)	**$ 855**	**$ 528**	**$ 11**	**($175)**

[a] Adjusted for Investment and Administrative Expenses for FY 2006
[b] Estimated by the Office of Management & Budget
Note: The annual pension contribution increase of about $32 million for Police as a result of the recent PBA arbitration ruling, and the potential annual contribution increase of about another $68 million if similar increases were to be awarded to all other uniformed employees, are not included in the above projections, as these funds are now being held in the labor reserve and will be transferred to pensions later, as necessary.

Some of the modifications the Chief Actuary may make to his FY 2005 recommendations are:

- *The World Trade Center Vicinity Legislation.* Chapter 104 of the Laws of 2005 provides accidental disability benefits to certain public employees who were in the World Trade Center vicinity between September 11, 2001 and September 12, 2002 and who subsequently become partially or wholly disabled due to certain diseases. The City estimates that this benefit will add $63 million each year to the City's pension expenses. The Chief Actuary intends to incorporate the impact of this legislation in his actuarial calculations as required by Section 430 of the Retirement and Social Security Law.[13]

- *FY 2005 Investment Returns.* Preliminary estimates indicate that pension fund investments earned about 9.8 percent for the year ended June 30, 2005. Under the new "one-year lag" methodology proposed by the Chief Actuary, this would not affect employer contribution calculations for FY 2006 as those would be based on asset values as of June 30, 2004.

- *PBA Arbitration Ruling on Contractual Salary Increases.* The Patrolmen's Benevolent Association (PBA) members were recently awarded salary increases through binding arbitration. The 24-month contract awarded two annually

[13] Section 430 applies when a new benefit or an improvement to any benefit is enacted that warrants an increase in actuarial contributions. It requires State and municipal employers to "commence payment for such increased cost … (in) the employer's fiscal year in which such benefit or improvement becomes effective."

compounded 5.0 percent increases on August 1, 2002 and August 1, 2003.[14] These increases are about 4.0 percentage points higher than those assumed in the Chief Actuary's projections as shown in Table 12, above, and would add roughly $32 million per year in pension costs. If similar agreements were to be reached with all uniformed personnel, pension costs would increase by about $100 million per year. While these added costs are not reflected in the City's pension contribution, the City has included funding for them in the labor reserve.

- *Independent Actuarial Audit by The Segal Company.* Pursuant to Chapter 96 of the New York City Charter, the Comptroller has engaged The Segal Company to conduct two consecutive biennial independent actuarial audits. The first independent audit will include an Experience Study that will compare actual experience through June 30, 2003 to the assumptions used in actuarial calculations of employer pension contributions. Preliminary results of the Experience Study, which will include the first concrete examination of data in the post 9/11 world, are expected by the end of September 2005. This is important, particularly for the uniformed groups, as it may indicate possible changes in behavior as a result of the terrorist attacks. The Chief Actuary has indicated that if in his judgment he finds strong evidence of significant long-term behavioral change, he may modify his new recommendations.

Labor

On June 27, 2005, PERB awarded a retroactive 10.25 percent wage increase to the PBA covering the two-year period from August 1, 2002 to July 31, 2004. The 10.25 percent increase comprises a 5.0 percent increase effective August 1, 2002, and another 5.0 percent increase compounded effective August 1, 2003. The increase is derived from a baseline of 3.2 percent, which was the amount agreed upon for City-wide collective bargaining, plus 5.5 percent from cost and productivity savings. The remaining difference reflects the traditional uniform differential.

The cost and productivity savings will be achieved as follows: 1) a revised salary schedule for officers hired after June 27, 2005, as shown in Table 13, 2) elimination of the annual personal leave day for all employees, and 3) an increase in the number of rescheduling tours from 10 to 15.[15]

The City has added $730 million to the FY 2005 labor reserve to fund the additional retroactive cost of settlement for all uniformed agencies patterned after the PERB decision on the PBA contract. For FYs 2006 to 2009, the City has allocated roughly $298 million, $224 million, $171 million, and $113 million to fund the increase.

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[14] For more details on the arbitration ruling, please see the "Labor" section on page 24 of this report.

[15] Rescheduling days allow the Police Department flexibility to reschedule employees without the payment of pre-tour or post-tour overtime.

The allocations decrease in the outyears as the City expects to achieve increasing productivity savings.

Table 13. Cost Savings for Rookie Officers[16]

	Rookie Officer Before PERB	Rookie Officer After PERB	Rookie Officer Savings
Months 1 through 6 (Police Academy)	$18,439.00	$12,550.00	$5,889.00
Months 7 through 18	$37,780.50	$32,700.00	$5,080.50
Months 19 through 30	$39,362.00	$34,000.00	$5,362.00
Months 31 through 42	$40,991.00	$38,000.00	$2,991.00
Months 43 through 54	$42,524.50	$41,500.00	$1,024.50
Months 55 through 66	$50,200.50	$44,100.00	$6,100.50
Months 67 through 78	$57,293.00	$62,833.00	($5,540.00)
Total:	$286,590.50	$265,683.00	$20,907.50

The teachers' contract, which expired on May 31, 2003, continues to be funded based on the DC 37 agreement. However, in the past, the teachers' contract has been more generous than DC 37's, and the recent PERB decision makes it more likely that this trend will continue. Every percentage point increase awarded to the teachers in excess of the increases in the DC 37 contract would cost the City $95 million more in back pay than it has funded and $80 million more per year going forward. In addition, the retroactive cost of the second increase of 2.0 percent on the 25th month of the DC 37 contract, which is funded through productivity actions, would total $30 million. This analysis assumes that the second increase, going forward, would be funded by productivity savings. If the teachers were to reach a settlement equivalent to the PBA contract it would cost the City an additional $980 million in retroactive costs over the amount funded in the labor reserve.

Adding to the potential shortfall in the labor reserve is the fact that all the contracts, including the recently awarded PBA contract, have expired. The City has funded wage increases averaging 1.2 percent, or half the expected inflation rate, over the financial plan period to fund the next round of collective bargaining agreements.

Overtime

Last year, in "The Comptroller's Comments on the FY 2005 Adopted Budget and the FYs 2005-2008 Financial Plan," the Comptroller's Office projected that overtime spending for FY 2005 would total $758 million, $121 million greater than the City's estimate. The City now expects FY 2005 overtime spending to be $792 million.[17]

[16] Since there is a six month differential between the new promotional schedule and the previous schedule, the twelve month earnings schedule before the PERB decision have been adjusted to reflect overlapping periods. Longevity salary is reflected after five years for the schedule before the PERB decision, and after five and a half years for the schedule after the PERB decision.

[17] The $792 million FY 2005 overtime estimate reflects a projected offset of approximately $60 million from personal services savings.

Currently, the Comptroller's Office estimates that FY 2006 overtime expenditure would total $794 million, $181 million more than the City's projection, as shown in Table 14. The City's projection of $613 million in overtime spending is about 22 percent below the FY 2005 estimates. The projection appears overly optimistic, since overtime has grown annually by an average of 6.0 percent over the last ten years.

Further, the settlement of outstanding collective bargaining agreements for uniformed employees will result in higher unit overtime spending since overtime compensation is based on the wage rate. As discussed in "Labor" above, the PERB increase translates to a 10.25 percent compounded increase in salaries. This increase, if eventually extended to all uniformed personnel, would increase overtime for FY 2006 by approximately $60 million. While this additional spending is not reflected in the City's overtime budget, the City has included the overtime cost in its labor reserve.

Table 14. Projected Overtime Spending, FY 2006

($ in millions)

	City Planned Overtime FY 2006	Comptroller's Projected Overtime FY 2006	FY 2006 Risk
Uniform			
Police	$245	$380	($135)
Fire	88	95	(7)
Correction	40	55	(15)
Sanitation	66	66	0
Total Uniformed	$439	$596	($157)
Others			
Police-Civilian	$16	$40	($24)
Admin for Child Svcs	17	17	0
Environmental Protection	21	21	0
Transportation	29	29	0
All Other Agencies	91	91	(0)
Total Civilians	$174	$198	($24)
Total City	**$613**	**$794**	**($181)**

NOTE: The Comptroller's overtime projection assumes that the City will be able to achieve some offsets to overtime spending from personal services savings.

Uniformed police overtime spending accounted for over 43 percent of the City's FY 2005 overtime cost. This expenditure grew at an average annual rate of 12 percent from FY 1994 to FY 2004, although overtime increases over the last four years are not surprising in light of terrorism issues and a reduction in the size of the uniformed police force. The Comptroller's Office estimates that police uniformed overtime spending will be approximately $380 million in FY 2006, almost 55 percent higher than the City's estimate of $245 million.

Even though the City adopts initiatives every year to curtail and/or reduce overtime, efforts have not been as successful as desired, and it remains a challenging task. However, the recent PBA arbitration ruling may lead to some increase in productivity and aid in controlling police overtime expenditures. The award eliminates one day of personal leave and gives the Police Department the ability to reschedule up to 15 tours, a significant increase from the ten tours in the previous agreement.

Headcount

Full-time City-funded headcount is expected to be 223,757 by June 30, 2006, as shown in Table 15. This represents a net increase of 2,884 employees, including 871 teachers, from the actual number on payroll as of May 31, 2005. Headcount is thereafter expected to increase 373 to 224,130 by June 30, 2007 and remain relatively stable through FYs 2008 and 2009.

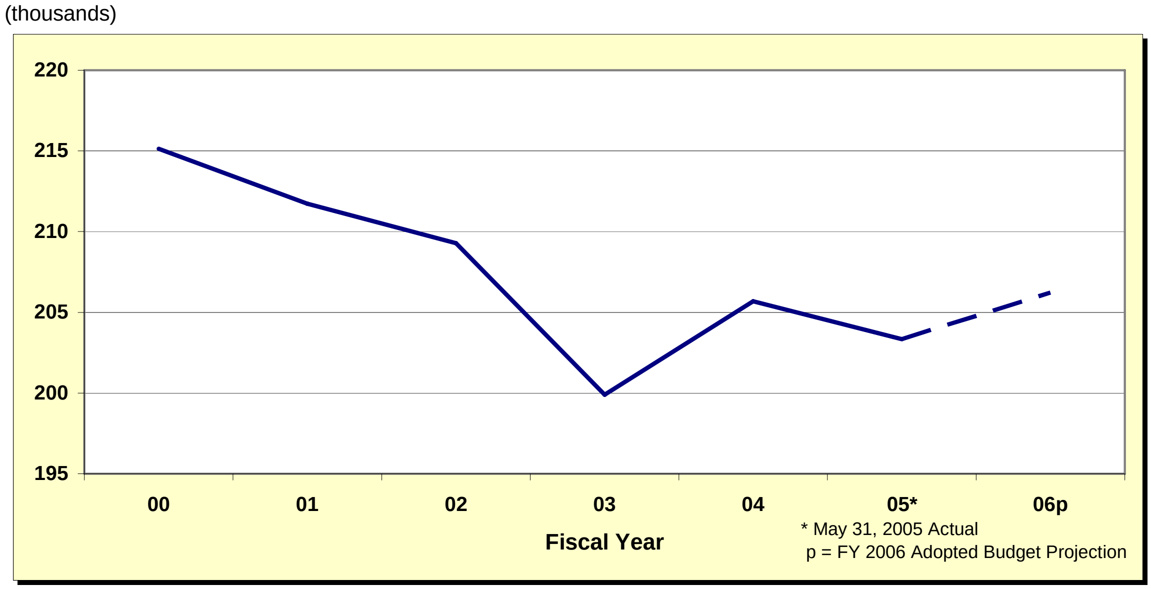
Table 15. City-Fund Full-Time Year-End Headcount Projections

	May 31, 2005 Actual	**FY 2006**	**FY 2007**	**FY 2008**	**FY 2009**
Agency Uniformed:					
Police	35,667	34,824	34,824	34,824	34,824
Fire	11,287	11,211	11,211	11,211	11,211
Correction	8,464	8,525	8,511	8,511	8,511
Sanitation	7,420	7,638	7,638	7,638	7,638
Sub-total	62,838	62,198	62,184	62,184	62,184
Pedagogical:					
Dept. of Education	88,019	88,890	88,873	88,873	88,873
City University	2,719	2,706	2,700	2,700	2,700
Sub-total	90,738	91,596	91,573	91,573	91,573
Civilian:					
Police	8,864	9,230	9,422	9,422	9,422
Fire	4,409	4,374	4,374	4,374	4,374
Admin for Child Svcs.	6,079	6,242	6,242	6,242	6,242
Dept. of Health	2,587	2,845	3,092	3,129	3,134
Social Services	11,035	11,333	11,373	11,373	11,373
All Other Civilians	34,323	35,939	35,870	35,845	35,801
Sub-total	67,297	69,963	70,373	70,385	70,346
Total	**220,873**	**223,757**	**224,130**	**224,142**	**224,103**

SOURCE: Office of Management and Budget, FY 2006 Adopted Budget.

City headcount was reduced sharply in the mid-1990's but grew again as the City prospered in the late-1990's. After FY 2000, headcount generally trended downward with the steepest drop in FY 2003, reflecting the City's early retirement program and hiring freeze in response to the fiscal crisis confronting the City at that time. However, as shown in Chart 5, the City's forecast for FY 2006 shows an increase from the actual May 31, 2005 level. This increase stems mainly from the planned hiring of additional pedagogical staff and social services agencies employees as shown in Table 15.

***Chart 5*. Full-Time City-Funded Headcount**



SOURCE: NYC Office of Management and Budget and NYC Office of the Comptroller
NOTE: For comparison purposes, FYs 2004 to 2006 headcount have been adjusted to exclude approximately 17,500 full-time employees who had previously been classified as FTEs.

City-funded part-time headcount are expected to total 32,422 full-time-equivalent (FTE) employees on June 30, 2006, about 2.0 percent greater than the actual 31,754 FTEs employed on May 31, 2005, and thereafter remain at comparable levels, as shown in Table 16. However, some changes are planned in individual agencies. Between May 31, 2005 and the end of fiscal year 2006, a planned increase of pedagogical part-timers in the Department of Education is expected to be offset by a decrease in City University part-timers. During the same time-frame, among civilian part-timers, a combined increase of 1,177 FTEs in the Police Department, the Department of Health and Mental Hygiene, and the Administration for Children's Services is expected to be partially offset by a combined decrease of 618 FTEs in the Department of Education, the City University and the Department of Parks and Recreation.

Table 16. City-Fund Full-Time Equivalent (FTE) Year-End Headcount Projections

	May 31, 2005 Actual	FY 2006	FY 2007	FY 2008	FY 2009
Agency Pedagogical FTEs:					
Dept. of Education	527	952	952	952	952
City University	1,900	1,468	1,468	1,468	1,468
Sub-total	2,427	2,420	2,420	2,420	2,420
Civilian FTEs:					
Dept. of Education	14,734	14,619	14,619	14,619	14,619
City University	912	800	800	800	800
Police	5,656	6,179	6,549	6,549	6,549
Dept. of Parks & Rec.	4,582	4,191	3,766	3,748	3,748
Dept. of Health	1,719	2,132	2,142	2,159	2,175
Admin for Child Svcs.	15	256	256	256	256
All Other Civilian FTEs	1,709	1,825	1,793	1,793	1,793
Sub-total	29,327	30,002	29,925	29,924	29,940
Total FTEs	**31,754**	**32,422**	**32,345**	**32,344**	**32,360**

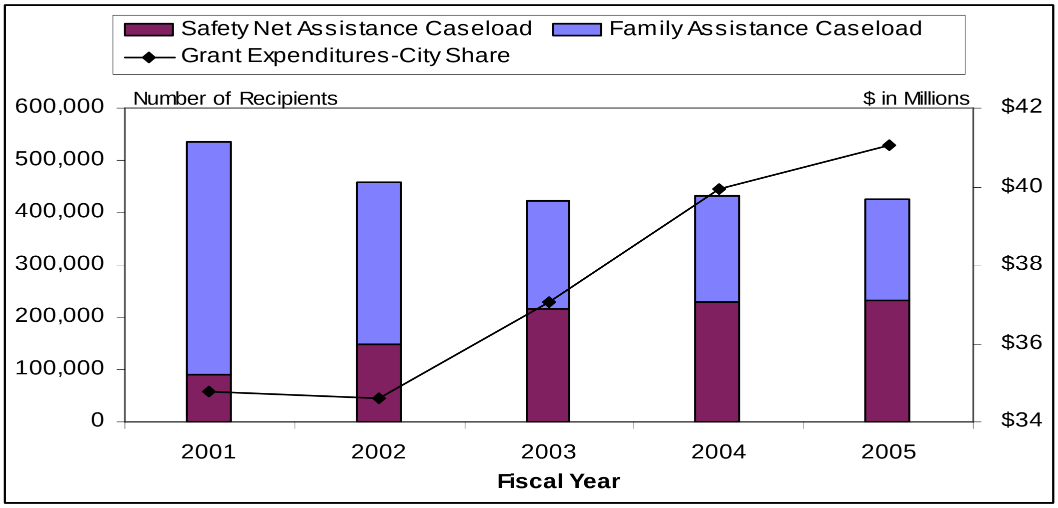
SOURCE: Office of Management and Budget, FY 2006 Adopted Budget.

Public Assistance and Medicaid

The City's public assistance caseload continued to drift lower in the final months of FY 2005, reaching its lowest level in about 40 years. Based on data provided by the Department of Social Services, the City's welfare caseload fell to 416,164 in June 2005, breaching a recent low of 418,770 reported in February 2003. The trend has reversed the entire caseload growth experienced in FY 2004, when the welfare rolls swelled by about 4.0 percent to 437,453. Since then, caseload has dropped almost 5.0 percent. The decline in caseload has not triggered a corresponding decrease in grants expenditures, as illustrated in Chart 6. Over the past five years, baseline grant expenditures have actually risen even as caseload level declined.

The rising grant expenditures are attributable to the higher proportion of welfare caseload constituting the Safety Net Assistance (SNA) program. The SNA component is a State-mandated program that serves primarily single adults, whereas the Family Assistance category is a Federally-mandated program that provides support to low-income families. SNA recipients currently comprise about 54 percent of public assistance caseload. In FY 2001, the SNA category represented only about 17 percent of the City's welfare population. This growth is due both to a rise in the traditional SNA population and the transfer of time-limits recipients from the Family Assistance (FA) program. Coming on the heels of the City's recession and the 9/11 disaster, the traditional SNA population has expanded almost 19 percent since FY 2001. In addition, as of June 2005, the SNA category includes close to 121,000 recipients—more than a quarter of the overall welfare caseload—who continue to require welfare benefits after having reached their five year time-limits in the FA program.

***Chart 6.* Average Monthly Public Assistance Caseload and Grant Expenditures, FY 2001-FY 2005**



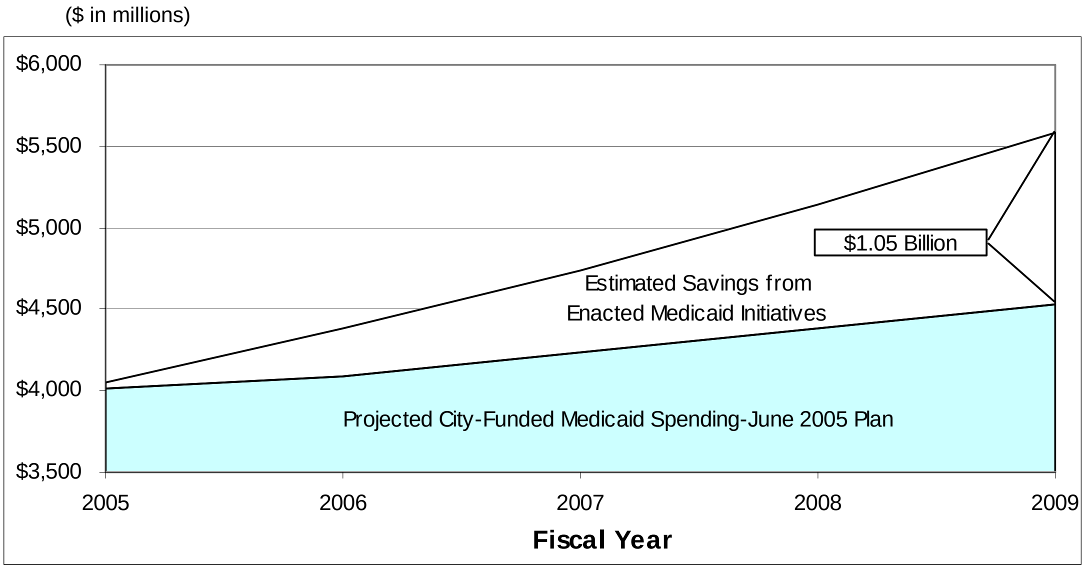
SOURCE: Department of Social Services, City of New York.

The SNA program is a more expensive program to support from the City's standpoint because it provides half of the funding for this category, compared with a 25-percent City share for the FA category. The additional City support for the higher SNA caseload has more than outstripped the savings realized in the FA category.

In the June Plan, the City projects caseload will reach 438,295 by the end of FY 2006 and remain flat thereafter. However, because actual FY 2005 caseload was significantly below forecast, it is likely that the City has overestimated future caseloads. Yet, the City appears to have adequately budgeted for baseline grants spending, providing about $512 million annually for its share of the overall costs. Despite the yearly increase in welfare grant expenditures shown in Chart 6, the City's share of these expenditures has stabilized at a monthly average of about $41 million over the past twelve months. Barring a significant increase in grant levels, the June Plan provisions for public assistance expenditures appear to be in line with the recent trend.

The June Plan projects City-funded Medicaid spending, excluding the Health and Hospitals Corporation (HHC), to grow 2.0 percent to $4.09 billion in FY 2006, from a projected FY 2005 base of $4.02 billion. The modest growth reflects savings from Medicaid initiatives enacted by the State during FY 2005. Chief among these actions is the phased-in State takeover of the Family Health Plus (FHP) program, estimated to save the City $254 million in FY 2006. In addition, the State has approved a 3.5 percent cap on local Medicaid spending growth for FY 2006. Although the cap would provide no savings in FY 2006 because the FHP takeover and other cost containment initiatives would bring City-funded Medicaid spending below the 3.5 percent threshold, its impact in the outyears will be substantial. The continuing provision, which caps local Medicaid spending growth at 3.25 percent in FY 2007 and 3 percent in FY 2008 and beyond, is projected to save the City between $110 million and $634 million annually in the outyears.

***Chart 7.* Budget Impact of Enacted Medicaid Initiatives**



SOURCE: NYC Office of Management and Budget.

As illustrated in Chart 7, savings from the local spending cap and State FHP takeover would reach a total of $504 million in FY 2007 and $756 million in FY 2008. By FY 2009, the projected savings would eclipse $1 billion, representing costs that would have been the City's responsibility if not for the approved Medicaid measures. Accordingly, the June Plan projects City-funded Medicaid spending to grow at an average of 3.4 percent annually, from $4.09 billion in FY 2006 to $4.53 billion in FY 2009. Aside from providing substantial budget relief to the City, the local spending cap will bring more predictability to the City's fiscal planning of Medicaid expenditures. The cap thresholds will stabilize significant swings in Medicaid growth that have taken place in recent years, when annual increases have ranged from 2.0 percent to 15 percent.

Department of Education

The FY 2006 Adopted Budget sets funding of $14.14 billion for the Department of Education (DOE), representing an increase of $364 million from projected FY 2005 spending. The bulk of this increase is projected to occur in spending for instructional services, pupil busing, and fringe benefits.

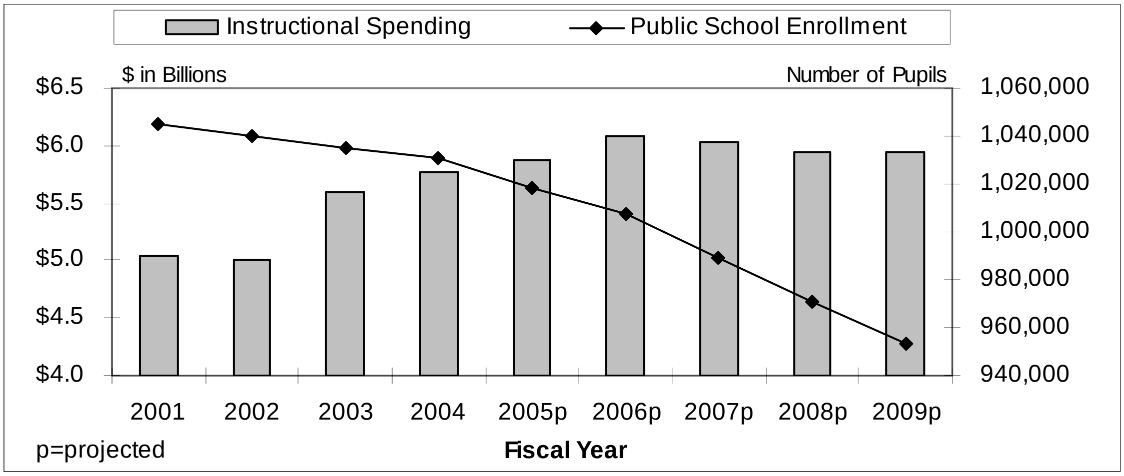
Compared with the Executive Budget, an additional $72 million has been reflected in FY 2006. A portion of the funding increase is attributable to the roll of a $37 million surplus from FY 2005 that the Department had identified since May. In addition to the surplus roll, major changes include a $17 million restoration for the Teacher's Choice program providing teachers and instructors with up to $200 each for purchases of classroom supplies and equipment, and $6 million for expansion of the Universal Pre-Kindergarten (UPK) program. However, with the exception of the UPK expansion, other changes in the Adopted Budget are increases on a one-year basis only that have no impact in the outyears.

The FY 2006 Adopted Budget also marks a new budget structure for the Department. Under the new structure, funds for instructional and administrative functions are allocated on a regional basis, to reflect the change in the DOE operating structure. Among the notable changes, the new regional format consolidates funding for kindergarten through 12th grade, replacing the old structure that contained separate units of appropriation (U/A) for community school districts and high schools. This change occurs in both general and education functions. In addition, new units of appropriation have been created to reflect various types of non-public school payments, including charter schools and special pre-kindergarten programs. While the realignment of U/As is reasonable in principle, it reduces the total number of U/As by nine and makes the Department's budget less transparent.

Over the financial plan period, DOE expenditures are projected to grow \$561 million from a FY 2005 base of \$13.78 billion to the FY 2009 estimate of \$14.34 billion. This growth reflects notable increases in two areas of spending. First, pupil transportation is expected to cost \$917 million by FY 2009, representing an increase of \$225 million, or 32 percent, from an estimate of \$692 million for FY 2005. The trend recognizes the costs for the extension of the Department's school bus contracts and includes adjustments for retroactive increases. Recent legislation allows the Department to extend the bus contracts without re-bidding for these services. According to DOE, the contract extension with existing vendors actually represents the low end of potential cost scenarios because of the nature of the industry. Second, projected spending for fringe benefits will increase by about \$337 million or 20 percent to \$1.98 billion by FY 2009 because of rising health insurance costs.

Instructional spending for general and special education is expected to fluctuate within a narrow range between \$5.95 billion and \$6.09 billion in the outyears, despite a projected decline in pupil enrollment. As shown in Chart 8, because of programmatic funding increases in recent years, instructional spending has risen even as enrollment fell. The City's current assumptions contain a sharper decline in pupil enrollment than previous projections. Over the term of the plan, public school enrollment, excluding pre-kindergarten, is expected to fall more than 6.0 percent, from 1,018,604 in FY 2005 to 953,507 in FY 2009. The decline is expected to occur in general education categories, with concentration heaviest in the middle grades. This decrease is offset partly by a moderate increase in special education enrollment. In comparison, the City has not projected an enrollment decline of more than 4.0 percent for any given four-year plan period in recent years.

Chart 8. **Instructional Spending vs. Public School Enrollment, FY 2001-FY 2009**



SOURCE: NYC Office of Management and Budget.

Health and Hospitals Corporation

In the FYs 2006-2009 Financial Plan, the City projects that the Health and Hospitals Corporation (HHC) will complete FY 2005 with a cash balance of $449 million, representing an increase of $105 million since the April Plan. While this improvement would provide a boost to the FY 2006 fiscal outlook, the Adopted Budget still shows a major budget shortfall of $600 million for HHC.

The projected deficit in the FY 2006 Adopted Budget is attributable to a significant drop in the Corporation's receipts, falling to $4.25 billion from $4.67 billion in FY 2005. Third party receipts, which comprise over 85 percent of total receipts, are expected to slip by more than $114 million due to weaker estimates for indigent care pool and Medicare revenues. In addition, the City's subsidy to the Corporation declines in FY 2006 mainly because a prepayment of $172 million was made to augment the FY 2005 cash balance. At the same time, disbursements are projected to increase $340 million to $4.85 billion mainly because of higher costs for fringe benefits and personal services.

In response, HHC has proposed gap-closing actions totaling $445 million. If fully realized, these actions would enable the Corporation to achieve a closing cash balance of $294 million. The chief components of the gap-closing actions are anticipated Federal and State actions of about $260 million. Although a certain portion of this estimate appears achievable, the uncertainty of these actions could still necessitate an increase in the City's subsidy to the Corporation to uphold the FY 2006 cash balance projection.[18]

[18] The City indicates that $65 million of the Federal and State actions could be realized through rate appeals.

The City may choose to fill the potential gap by prepaying subsidy earmarked for FY 2007, similar to actions taken in both FY 2004 and FY 2005. However, a more accurate reflection of expected City support would be to raise the FY 2006 subsidy without resorting to prepayments.

The Corporation faces similar prospects in the outyears of the plan. The size of HHC's budget gaps is expected to persist, as disbursements are projected to outpace revenue receipts by a wide margin each year. The June Plan shows operating deficits ranging from $520 million in FY 2007 to $664 million in FY 2009 for the Corporation. Meanwhile, HHC's projected cash balance is expected to decline from $294 million in FY 2006 to about $179 million in FY 2008, before dropping off to $85 million in FY 2009. To reach these targets, HHC will need to implement gap closing programs averaging more than $500 million each year. As in FY 2006, Federal and State actions figure prominently among the planned initiatives to reduce HHC's operating deficits in the outyears, constituting about 60 percent of the total value of gap-closing actions. The heavy reliance on these actions raises more uncertainty about the Corporation's fiscal assumptions. The Federal government will soon formulate plans for substantial cuts in Medicaid funding over the next few years. Pending the impact of the Federal Medicaid reductions, HHC may need to develop alternative measures to keep its gap-closing assumptions intact in the outyears.

Debt Service

Debt service in the FY 2006-2009 Financial Plan, including NYC Transitional Finance Authority (NYCTFA) and TSASC debt service and excluding prepayments, is estimated to total $4.38 billion in FY 2006 and is projected to grow to $5.93 billion by FY 2009, an increase of $1.55 billion or 35 percent over the financial plan period.

As shown in Table 17, General Obligation (G.O.) debt service is estimated to increase by $1.44 billion, or 48 percent, over FYs 2006-2009. This increase is driven primarily by projected new G.O. borrowing of approximately $18.3 billion in FYs 2006-2009, generating additional debt service of about $1.2 billion per year by FY 2009.

Table 17. FY 2006 Adopted Budget and Financial Pan Estimates FYs 2006-2009, June 2005

($ in millions)

Debt Service Category	FY 2006	FY 2007	FY 2008	FY 2009	Change FY 2006 to FY 2009
G.O.[a]	$3,023	$3,770	$4,095	$4,462	$1,439
NYCTFA	947	955	983	988	41
Lease-Purchase Debt	305	335	382	379	74
TSASC, Inc.	92	92	99	100	8
Municipal Assistance Corp.	10	10	10	0	(10)
Total	**$4,377**	**$5,162**	**$5,569**	**$5,929**	**$1,552**

SOURCE: FY 2005 June 2005 Financial Plan, June 2005, FY 2006 Adopted Budget, June 2005.
NOTE: Debt Service is adjusted for prepayments.
[a] Includes long term G.O. debt service and interest on short term notes.

NYCTFA and TSASC, Inc. have no planned new money borrowing over the financial plan period. Debt service for NYCTFA and TSASC, Inc. is projected to increase modestly from a combined $1.04 billion in FY 2006 to $1.09 billion in FY 2009, an increase of less than five percent. Lease purchase debt service is projected to increase $74 million from FY 2006 to FY 2009 primarily due to the assumed growth in Hudson Yards Infrastructure Corporation debt service.[19]

Financing Program

As shown in Table 18, the financing program for FYs 2006-2009 totals $26.4 billion. The only planned issuances of debt over the financial plan period are G.O. debt of $18.3 billion and the NYC Water Finance Authority (NYW) debt of $6.9 billion. Combined, these represent over 95 percent of the total financing program. Anticipated use of pay-as-you-go capital comprises $800 million, or 3.0 percent of the total share. At this point in time, there is no planned borrowing for the NYCTFA because debt issued to date has reached its maximum capacity under its current legislative authorization. In addition, there is also no scheduled borrowing for TSASC, Inc. and conduit (lease-purchase) debt.

Table 18. FY 2006 Adopted Budget Financing Program, FYs 2006-2009

($ millions)

Description:	Estimated Borrowing and Funding Sources FYs 2006-2009	Percent of Total
General Obligation Bonds	$18,260	69.2%
NYC Water Finance Authority	6,871	26.1%
NYC TFA	0	0.0%
TSASC, Inc.	0	0.0%
Conduit Debt	0	0.0%
Other Sources and NYW Pay-As-You-Go Capital	443	1.7%
Pay- As- You Go Capital	800	3.0%
Difference	**$26,374**	**100.0%**

SOURCE: FY 2006 Adopted Budget Debt Service Detail, Office of Management and Budget, June 2005.

[19] Although debt service is included for the Hudson Yards Development Corporation in the lease-purchase unit of appropriation, borrowing for this entity is not included in the Financing Program because of its uncertain issuance schedule.

Appendix — Revenue and Expenditure Details

Table A1. *FY 2006 Executive Budget Revenue Detail*

($ in millions)

	FY 2006	FY 2007	FY2008	FY2009	Change FYs 2006-09 Percent	Dollar
Taxes:						
Real Property	$12,609	$13,295	$14,229	$14,884	27.8%	$3,236
Personal Income Tax	$6,586	$6,455	$6,655	$7,121	(0.2%)	($13)
General Corporation Tax	$1,908	$2,052	$2,091	$2,249	13.8%	$272
Banking Corporation Tax	$497	$496	$456	$452	(22.3%)	($130)
Unincorporated Business Tax	$1,077	$1,123	$1,156	$1,212	9.3%	$103
Sale and Use	$4,345	$4,470	$4,418	$4,655	6.2%	$272
Commercial Rent	$456	$466	$480	$493	10.8%	$48
Real Property Transfer	$716	$608	$595	$609	(43.2%)	($463)
Mortgage Recording Tax	$736	$584	$554	$554	(55.9%)	($702)
Utility	$306	$309	$312	$314	(3.4%)	($11)
Cigarette	$120	$118	$114	$112	(10.4%)	($13)
Hotel	$267	$277	$291	$306	20.5%	$52
All Other	$420	$394	$396	$395	(12.4%)	($56)
Tax Audit Revenue	$512	$509	$509	$509	(3.1%)	($16)
Tax Reduction Program	($221)	($233)	($92)	($141)	N/A	($141)
Total Taxes	**$30,334**	**$30,924**	**$32,165**	**$33,724**	**7.8%**	**$2,439**
Miscellaneous Revenue:						
Licenses, Franchises, Etc.	$379	$371	$372	$369	(4.9%)	($19)
Interest Income	$159	$115	$123	$134	(11.3%)	($17)
Charges for Services	$530	$512	$512	$512	(14.2%)	($85)
Water and Sewer Charges	$998	$1,002	$1,017	$1,037	11.3%	$105
Rental Income	$177	$181	$179	$171	(81.8%)	($771)
Fines and Forfeitures	$692	$691	$691	$690	(6.8%)	($50)
Miscellaneous	$602	$343	$342	$344	(74.7%)	($1,016)
Intra-City Revenue	$1,289	$1,271	$1,270	$1,271	(3.6%)	($48)
Total Miscellaneous	**$4,826**	**$4,486**	**$4,506**	**$4,528**	**(29.6%)**	**($1,901)**
Unrestricted Intergovernmental Aid:						
N.Y. State Per Capital Aid	$327	$327	$327	$327	0.0%	$0
Other Federal and State Aid	$235	$235	$235	$235	0.0%	$0
Total Unrestricted Intergovernmental Aid	**$562**	**$562**	**$562**	**$562**	**0.0%**	**$0**
Anticipated State and Federal Aid:						
Anticipated State Aid	$0	$0	$0	$0	0.0%	$0
Anticipated Federal Aid	$50	$0	$0	$0	0.0%	$0
Total Anticipated Aid	**$50**	**$0**	**$0**	**$0**	**0.0%**	**$0**
Other Categorical Grants	**$927**	**$923**	**$928**	**$934**	**3.5%**	**$32**
Inter Fund Agreements	**$364**	**$355**	**$344**	**$343**	**(1.7%)**	**($6)**
Reserve for Disallowance of Categorical Grants	**($15)**	**($15)**	**($15)**	**($15)**	**0.0%**	**$0**
Less: Intra-City Revenue	**($1,289)**	**($1,271)**	**($1,270)**	**($1,271)**	**(3.6%)**	**$48**
TOTAL CITY FUNDS	**$35,759**	**$35,964**	**$37,220**	**$38,805**	**1.6%**	**$612**

Table A1 (Con't). *FY2006 Executive Budget Revenue Detail*

($ in millions)

	FY 2006	FY 2007	FY2008	FY2009	Change FYs 2006-09 Percent	Dollar
Federal Categorical Grants:						
Community Development	$269	$247	$247	$247	(23.8%)	($77)
Welfare	$2,131	$2,035	$2,035	$2,035	(14.2%)	($338)
Education	$1,808	$1,808	$1,808	$1,808	(7.0%)	($137)
Other	$901	$770	$760	$760	(40.6%)	($519)
Total Federal Grants	**$5,109**	**$4,860**	**$4,850**	**$4,850**	**(29.9%)**	**($2,071)**
State Categorical Grants						
Welfare	$1,837	$1,879	$1,879	$1,879	3.4%	$61
Education	$6,516	$6,549	$6,607	$6,643	7.5%	$462
Higher Education	$188	$188	$188	$188	7.4%	$13
Department of Health and Mental Hygiene	$430	$435	$439	$443	(1.8%)	($8)
Other	$349	$321	$319	$322	(20.7%)	($84)
Total State Grants	**$9,320**	**$9,372**	**$9,432**	**$9,475**	**4.9%**	**$444**
TOTAL REVENUE	**$50,188**	**$50,196**	**$51,502**	**$53,130**	**(1.9%)**	**($1,015)**

Table A2. FY 2006 Adopted Budget Expenditure Detail

($ in thousands)

	FY 2006	FY 2007	FY2008	FY2009	Change FYs 2006-09 Percent	Change FYs 2006-09 Dollar
Mayoralty	$71,280	$70,957	$70,478	$70,478	0.0%	$0
Board of Elections	$77,884	$68,884	$68,884	$68,884	(1.0%)	($802)
Campaign Finance Board	$62,997	$8,091	$8,091	$8,091	(87.2%)	($54,906)
Office of the Actuary	$5,311	$5,311	$5,111	$5,111	(3.8%)	($200)
President, Borough of Manhattan	$3,996	$3,121	$3,121	$3,121	(21.9%)	($875)
President, Borough of the Bronx	$5,594	$4,491	$4,491	$4,491	(19.7%)	($1,103)
President, Borough of Brooklyn	$5,146	$3,926	$3,926	$3,926	(23.7%)	($1,220)
President, Borough of Queens	$4,836	$3,685	$3,685	$3,685	(23.8%)	($1,151)
President, Borough of S.I.	$3,940	$3,127	$3,127	$3,127	(20.6%)	($813)
Office of the Comptroller	$60,737	$60,826	$60,526	$60,734	(0.0%)	($3)
Dept. of Emergency Management	$5,416	$5,732	$5,732	$5,732	5.8%	$316
Tax Commission	$2,325	$2,325	$2,325	$2,325	0.0%	$0
Law Department	$114,805	$106,468	$106,468	$106,468	(7.3%)	($8,337)
Department of City Planning	$20,286	$19,612	$19,612	$19,612	(3.3%)	($674)
Department of Investigation	$16,715	$16,715	$16,715	$16,715	0.0%	$0
NY Public Library-Research	$4,334	$15,891	$15,892	$15,892	266.7%	$11,558
New York Public Library	$12,593	$84,212	$84,252	$84,252	569.0%	$71,659
Brooklyn Public Library	$8,075	$62,928	$62,962	$62,962	679.7%	$54,887
Queens Borough Public Library	$7,575	$60,590	$60,673	$60,673	701.0%	$53,098
Department of Education	$14,135,612	$14,162,848	$14,224,473	$14,332,921	1.4%	$197,309
City University	$580,393	$523,210	$522,995	$523,012	(9.9%)	($57,381)
Civilian Complaint Review Bd.	$9,935	$8,862	$8,862	$8,862	(10.8%)	($1,073)
Police Department	$3,430,859	$3,425,959	$3,414,492	$3,398,529	(0.9%)	($32,330)
Fire Department	$1,183,143	$1,186,728	$1,186,553	$1,186,063	0.2%	$2,920
Admin. for Children Services	$2,163,957	$2,093,095	$2,092,733	$2,092,733	(3.3%)	($71,224)
Department of Social Services	$7,211,340	$7,353,177	$7,503,349	$7,648,916	6.1%	$437,576
Dept. of Homeless Services	$703,128	$678,629	$678,628	$678,628	(3.5%)	($24,500)
Department of Correction	$802,437	$792,905	$792,941	$793,049	(1.2%)	($9,388)
Board of Correction	$949	$853	$853	$853	(10.1%)	($96)
Department of Employment	$0	$0	$0	$0	0.0%	$0
Citywide Pension Contributions	$4,599,415	$4,949,897	$4,842,792	$4,714,976	2.5%	$115,561
Miscellaneous	$5,513,021	$6,083,683	$6,628,473	$7,182,763	30.3%	$1,669,742
Debt Service	$1,391,345	$4,105,588	$4,477,569	$4,840,894	247.9%	$3,449,549
M.A.C. Debt Service	$10,000	$10,000	$10,000	$0	(100.0%)	($10,000)
NYCTFA Debt Service*	$0	$761,729	$982,550	$988,161	0.0%	$988,161
Public Advocate	$2,858	$1,897	$1,897	$1,897	(33.6%)	($961)
City Council	$47,545	$46,518	$46,518	$46,518	(2.2%)	($1,027)
City Clerk	$3,040	$3,040	$3,040	$3,040	0.0%	$0
Department for the Aging	$254,020	$226,784	$226,784	$226,784	(10.7%)	($27,236)
Department of Cultural Affairs	$133,448	$105,010	$105,010	$105,010	(21.3%)	($28,438)
Financial Info. Serv. Agency	$48,971	$44,875	$42,356	$42,356	(13.5%)	($6,615)
Department of Juvenile Justice	$97,624	$98,395	$98,395	$98,395	0.8%	$771
Office of Payroll Admin.	$11,660	$10,578	$10,578	$10,578	(9.3%)	($1,082)
Independent Budget Office	$2,776	$2,746	$2,746	$2,746	(1.1%)	($30)
Equal Employment Practices Com	$808	$711	$711	$711	(12.0%)	($97)

Table A2 (Con't). *FY2006 Adopted Budget Expenditure Detail*

($ in thosuands)

	FY 2006	FY 2007	FY2008	FY2009	Change FYs 2006-09 Percent	Dollar
Civil Service Commission	$597	$597	$597	$597	0.0%	$0
Landmarks Preservation Comm.	$3,715	$3,715	$3,715	$3,715	0.0%	$0
Districting Commission	$0	$0	$0	$0	0.0%	$0
Taxi & Limousine Commission	$28,247	$25,338	$25,338	$25,338	(10.3%)	($2,909)
Commission on Human Rights	$6,804	$6,804	$6,804	$6,804	0.0%	$0
Youth & Community Development	$286,386	$222,392	$222,667	$222,667	(22.2%)	($63,719)
Conflicts of Interest Board	$1,544	$1,351	$1,351	$1,351	(12.5%)	($193)
Office of Collective Barg.	$1,626	$1,626	$1,626	$1,626	0.0%	$0
Community Boards (All)	$12,817	$12,663	$12,663	$12,663	(1.2%)	($154)
Department of Probation	$75,804	$75,209	$75,209	$75,209	(0.8%)	($595)
Dept. of Small Business Services	$102,735	$87,888	$87,888	$87,888	(14.5%)	($14,847)
Housing Preservation & Dev.	$485,076	$477,549	$477,439	$476,311	(1.8%)	($8,765)
Department of Buildings	$78,601	$69,422	$68,135	$66,570	(15.3%)	($12,031)
Department of Public Health & Mental Hygiene	$1,570,775	$1,490,734	$1,506,959	$1,522,824	(3.1%)	($47,951)
Health and Hospitals Corp.	$792,256	$952,640	$936,598	$922,913	16.5%	$130,657
Dept. of Environmental Prot.	$808,882	$791,073	$786,237	$786,297	(2.8%)	($22,585)
Department of Sanitation	$1,075,324	$1,110,405	$1,110,166	$1,109,606	3.2%	$34,282
Business Integrity Commission	$5,301	$5,301	$5,301	$5,301	0.0%	$0
Department of Finance	$199,284	$199,017	$199,086	$199,086	(0.1%)	($198)
Department of Transportation	$492,157	$484,398	$484,398	$484,398	(1.6%)	($7,759)
Dept. of Parks and Recreation	$240,446	$223,763	$217,276	$217,276	(9.6%)	($23,170)
Dept. of Design & Construction	$98,455	$98,454	$94,454	$88,454	(10.2%)	($10,001)
Dept. of Citywide Admin. Services	$265,535	$260,402	$259,343	$259,336	(2.3%)	($6,199)
D.O.I.T.T.	$168,426	$188,983	$186,224	$186,159	10.5%	$17,733
Dept. of Records & Info. Serv.	$3,801	$3,801	$3,801	$3,801	0.0%	$0
Department of Consumer Affairs	$13,136	$13,249	$13,249	$13,249	0.9%	$113
District Attorney - N.Y.	$68,787	$63,527	$63,527	$63,527	(7.6%)	($5,260)
District Attorney - Bronx	$40,368	$37,254	$37,254	$37,254	(7.7%)	($3,114)
District Attorney - Kings	$69,014	$64,489	$64,489	$64,489	(6.6%)	($4,525)
District Attorney - Queens	$35,985	$33,386	$33,386	$33,386	(7.2%)	($2,599)
District Attorney - Richmond	$6,156	$5,682	$5,682	$5,682	(7.7%)	($474)
Off. Of Prosec. & Spec. Narc.	$14,712	$13,571	$13,571	$13,571	(7.8%)	($1,141)
Public Administrator - N.Y.	$1,073	$1,020	$1,020	$1,020	(4.9%)	($53)
Public Administrator - Bronx	$391	$338	$338	$338	(13.6%)	($53)
Public Administrator - Brooklyn	$519	$465	$465	$465	(10.4%)	($54)
Public Administrator - Queens	$416	$363	$363	$363	(12.7%)	($53)
Public Administrator - Richmond	$335	$282	$282	$282	(15.8%)	($53)
Prior Payable Adjustment	$0	$0	$0	$0	0.0%	$0
General Reserve	$300,000	$300,000	$300,000	$300,000	0.0%	$0
Energy Adjustment	$0	$10,903	$2,475	($3,160	0.0%	($3,160)
Lease Adjustment	$0	$25,669	$43,331	$61,476	0.0%	$61,476
OTPS Inflation Adjustment	$0	$52,842	$107,007	$162,526	0.0%	$162,526
City-Wide Totals	**$50,187,615**	**$54,701,174**	**$55,971,083**	**$57,055,332**	**13.7%**	**$6,867,717**

Glossary of Acronyms

AIRA	Actuarial Investment Return Assumption
CFE	Campaign for Fiscal Equity, Inc.
COLA	Cost of Living Allowances
DC 37	District Council 37
DOE	Department of Education
FA	Family Assistance
FEMA	Federal Emergency Management Agency
FHP	Family Health Plus
FTE	Full-Time Equivalents
FY	Fiscal Year
GCP	Gross City Product
GDP	Gross Domestic Product
G.O. Debt	General Obligation Debt
HHC	Health and Hospitals Corporation
J&C	Judgments and Claims
MAC	Municipal Assistance Corporation

NAPM – NY	National Association of Purchasing Management - New York
NYC	New York City
NYCTFA	New York City Transitional Finance Authority
NYCWFA	New York City Water Finance Authority
OMB	Office of Management and Budget
OTPS	Other than Personal Services
PBA	Patrolmen’s Benevolent Association
PERB	Public Employment Relations Board
PS	Personal Services
PIT	Personal Income Tax
STAR	School Tax Relief Program
SNA	Safety Net Assistance
TSASC	Tobacco Settlement Asset Securitization Corporation
U/A	Unit of Appropriation
UPK	Universal Pre-Kindergarten
U.S.	United States
WTC	World Trade Center