Review of the Financial Plan of the City of New York

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Highlights

- **New York City's FY 2012 budget is balanced with $5 billion in nonrecurring resources.**
- **City-funded spending is projected to rise by 12.5 percent in FY 2012, driven by the expiration of federal stimulus aid and an increase in City funds to replace cuts in State education aid.**
- **The City projects a budget gap of $2 billion for FY 2013, which could grow to $4.9 billion by FY 2015. These estimates do not reflect potential cuts in federal and State funding.**
- **The City's actuarial consultant has recommended changes in the assumptions used to calculate City pension contributions, including a reduction in the annual investment earnings assumption from 8 percent to 7 percent.**
- **The securities industry lost nearly $3 billion in the third quarter of 2011, reducing year-to-date profits to $9.6 billion. As a result, profits are likely to fall significantly short of the City's forecast of $20 billion for all of 2011.**
- **In response to reduced profitability, the securities industry has resumed downsizing, and cash bonuses in New York City are likely to be substantially smaller than last year.**
- **City-funded debt service is expected to grow by 45 percent between fiscal years 2011 and 2015, consuming a higher share of City fund revenues.**
- **Over the next two years, the City intends to use the remaining $2 billion that it had set aside to fund post-employment benefits other than pensions (OPEBs) to balance the operating budget. In FY 2011, the unfunded OPEB liability grew by 11.9 percent to $84 billion.**
- **City-funded staffing declined by 13,878 employees between fiscal years 2008 and 2011. Staffing is projected to decline by another 4,213 employees by the end of FY 2013.**

On November 18, 2011, New York City issued a revised financial plan covering fiscal years 2012 through 2015 (the "November Plan"). Mostly as a result of unplanned spending in the uniformed agencies, the out-year budget gaps have grown by half a billion dollars to $5 billion in FY 2013 and about $5.5 billion in both FY 2014 and FY 2015.

The Mayor has proposed actions that would reduce the gaps to more manageable levels. These include implementing an agency cost-reduction program, which would generate $600 million in recurring resources; withdrawing the remaining $2 billion from the Retiree Health Benefits Trust; and selling additional taxi medallions, which would generate $1 billion if New York State approves legislation authorizing the sale.

Even assuming implementation of these actions, the City still projects budget gaps of $2 billion in FY 2013, $3.8 billion in FY 2014, and $4.9 billion in FY 2015. Moreover, the City faces a number of significant budget risks (see Figure 1), although some are difficult to quantify at this time.

The national and local economies are growing slowly, but remain vulnerable. The European sovereign debt crisis has deepened, and the likelihood of a recession on the continent has increased greatly. Wall Street is again under pressure, with significant losses in the third quarter. The fiscal challenges facing the federal government and New York State also pose threats to the City's budget.

The November Plan includes a $1 billion annual reserve, beginning in FY 2012, to cover the cost of changes in the assumptions and methods used to calculate City pension contributions. The City Actuary is expected to make his final recommendations to the City's five pension systems in February 2012. Implementation will require the approval of the boards of trustees and, in some instances, State approval.

The City has not reached new labor agreements with the unions that represent municipal workers. The November Plan assumes a three-year wage freeze for the current round of collective bargaining, but new agreements could result in unplanned costs. (The City still has not reached an agreement with its teachers for the prior round of collective bargaining.)

New York City was in a much stronger position than many states and other large municipalities coming out of the recession as a result of its financial planning process, conservative revenue forecasts, popularity as a tourist destination, and large reserves established during the prior economic expansion. It appears likely, however, that the City will exhaust most of those reserves over the next two years.

It has been the City's practice to generate large surpluses in the current fiscal year that can be used to help balance the following year's budget. In the past two fiscal years the City has generated surpluses averaging $3.7 billion, but for FY 2012 it projects a surplus of only $12 million.

Given the size of the remaining budget gaps and the significant budget risks faced by the City, it appears likely that the City will have to take additional actions later in the fiscal year to balance the budget. The impact of those actions would be reduced to the extent that the City can generate additional surplus funds in FY 2012.

Figure 1
OSDC Risk Assessment of NYC Financial Plan
(in millions)

	Better/(Worse)			
	FY 2012	**FY 2013**	**FY 2014**	**FY 2015**
Gaps Per November Plan	**$ - - -**	**$ (2,041)**	**$ (3,828)**	**$ (4,877)**
Tax Revenues	- - -	(300)	(300)	(300)
Taxi Medallion Sale	- - -	(1,000)	- - -	- - -
Pension Reform	- - -	- - -	(131)	(252)
OSDC Risk Assessment[1]	**$ - - -**	**$ (1,300)**	**$ (431)**	**$ (552)**
Gaps to be Closed	**$ - - -**	**$ (3,341)**	**$ (4,259)**	**$ (5,429)**
Additional Risks and Offsets				
Wage Increases at the Projected Inflation Rate[2]	(1,432)	(1,539)	(2,062)	(2,520)

[1] The Plan includes an annual general reserve of $300 million.

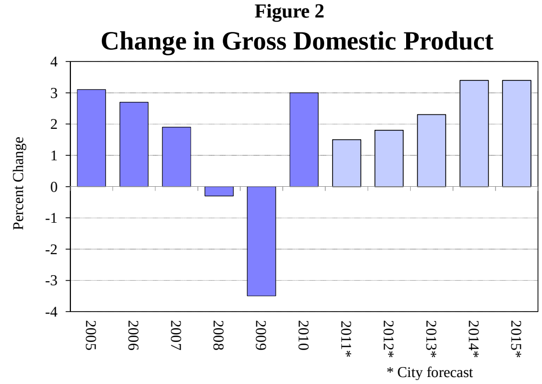
[2] The City has not reached agreement with the United Federation of Teachers for the prior round of collective bargaining. Wage increases at the pattern rate could increase costs by $900 million annually during the Plan period, excluding any retroactive costs.

Economic Overview

The national economy continues to grow at a slow pace and faces a number of significant risks, including weak labor markets, continued problems in the housing market, and fallout from the European sovereign debt crisis.

The Gross Domestic Product (GDP) grew by 3 percent in 2010, driven in part by the benefits from the federal stimulus program, but the November Plan forecasts that the GDP will grow by only 1.5 percent in 2011 (which is less than the 1.7 percent gain forecast by IHS Global Insight and Blue Chip Economic Indicators). The GDP is expected to remain weak until 2014 (see Figure 2).

Figure 2



Sources: U.S. Bureau of Economic Analysis; NYC Office of Management and Budget

In the past six months, the private sector added an average of 133,000 jobs per month, which is about one-quarter less than the average monthly job gains during the prior five months. Although the unemployment rate has fallen from a peak of 10.1 percent to 8.6 percent, it remains high. The November Plan assumes that national job growth will remain sluggish during the financial plan period, averaging slightly more than 1 percent annually through 2013, and then about 2 percent in each of the following two years.

New York City has recovered 82,000 of the 143,000 jobs (58 percent) it lost during the 2008-2009 recession, but total job growth has slowed in recent months. This reflects weakness in both the private and government sectors. The City's unemployment rate was 8.8 percent in October 2011, only 0.1 percentage point below the level at the start of the year.

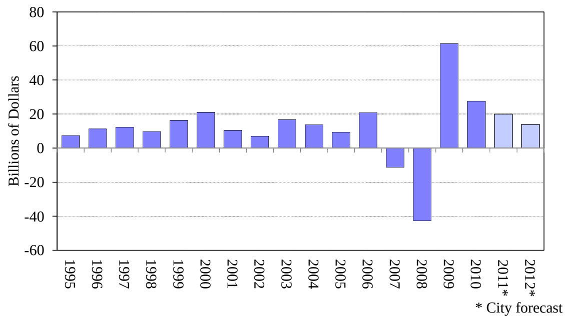
The November Plan assumes that growth in total employment will increase by 1.1 percent for all of calendar year 2011, ease to 0.6 percent in 2012, and then rise to 1.4 percent by 2015.

The November Plan's forecasts for the New York City economy show little change from those in the June Plan. Nevertheless, Wall Street is under renewed pressure, and weakness in the global economy could negatively affect tourism.

The broker/dealer operations of the member firms of the New York Stock Exchange (i.e., the traditional measure of Wall Street profitability) lost a record $54 billion in 2007 and 2008, but the industry earned oversized profits of $61 billion in 2009 fueled by federal assistance (see Figure 3). Industry profits totaled $27.6 billion in 2010, which was 55 percent less than a year earlier but still the second-best year on record.

Figure 3

Wall Street Profits



Note: Profits are for broker/dealer operations of NYSE member firms.
Sources: New York Stock Exchange; Securities Industry and Financial Markets Association; NYC Office of Management and Budget

Broker/dealer profits totaled $12.6 billion in the first half of 2011 (which was down 10.8 percent from the same period one year earlier), but the industry lost nearly $3 billion in the third quarter. Underlying profitability at the large firms was even weaker than reported because third-quarter profits were boosted by accounting adjustments.

The November Plan assumes that securities industry profits will decline to $20 billion in 2011 and $14 billion in 2012, which is unchanged from the City's June 2011 forecast. As profits have fallen, the industry has begun to cut costs, reducing employment and compensation.

In October 2011, the Office of the State Comptroller issued its annual report on the securities industry in New York City. The report concluded that industry profits may not reach $18 billion in 2011 (short of the City's forecast), but that estimate now seems optimistic given losses in the third quarter. The report also forecast that the industry may lose nearly 10,000 jobs in New York City by the end of 2012. The securities industry has lost 1,800 jobs since April 2011.

The City expects wage growth to total 5.1 percent in 2011 based mostly on projected job growth. The November Plan assumes that wage growth will slip to 2.6 percent in 2012 because job growth is expected to slow, and because Wall Street bonuses for 2011 (most of which will be paid in 2012) are likely to decline from the prior year's level.

Tourism remains a strong part of the City's economy, but shocks to the global economy could affect the number of visitors to New York City. For the time being, the relatively weak value of the dollar continues to attract international visitors. The City expects the number of visitors in 2011 to surpass the record of 48.8 million visitors in 2010.

The City's hotel industry remains strong. For the first ten months of 2011, the hotel occupancy rate averaged 84.8 percent, slightly less than the same period last year, while the average daily room rate reached $265.77, more than $16 higher than last year.

The commercial real estate market continues to improve. According to Cassidy Turley (a major real estate firm), the average asking rent in Manhattan's primary office market rose to $64.04 per square foot in November 2011, an increase of 10.2 percent from one year earlier; meanwhile, the vacancy rate averaged 9.9 percent, down from 11.3 percent one year ago. The November Plan assumes that rents for Manhattan's primary office market will rise to $75.39 per square foot by 2015.

Economic risks remain weighted toward the downside. The European debt crisis is intensifying, spreading beyond Greece into other parts of the region, and a solution remains elusive. The crisis has raised the risk of a European recession, which would affect trade flows and tourism, thereby slowing domestic growth.

Private sector job growth also remains weak, and government downsizing and the winding down of stimulus efforts is acting as a drag on the national economy. Congressional gridlock and concerns over deficit reduction are unlikely to change that situation. Finally, Wall Street is continuing to downsize and restructure in response to changes in its regulatory and economic environment. These pressures may increase near-term risks for the City's revenue collections and the local economy.

Changes Since the June 2011 Plan

The City's June 2011 financial plan projected a balanced budget for FY 2012, but gaps of $4.6 billion in FY 2013 and about $4.9 billion in fiscal years 2014 and 2015. While the City did not make any significant changes to its revenue forecasts, on a net basis, in the November Plan, it identified unplanned spending needs of about half a billion dollars, which opened a budget gap of $458 million in the current year and raised the out-year gaps to $5.1 billion in FY 2013, and $5.5 billion annually in fiscal years 2014 and 2015 (see Figure 4).

Figure 4
Financial Plan Reconciliation
November 2011 Plan vs. June 2011 Plan
(in millions)

	Better/(Worse)			
	FY 2012	**FY 2013**	**FY 2014**	**FY 2015**
Gap Per June 2011 Plan	**$ - - -**	**$(4,632)**	**$(4,844)**	**$(4,922)**
Revenue Reestimates				
Taxes	24	142	58	11
Non-Tax Revenues	1	(86)	(124)	(87)
Total	**25**	**56**	**(66)**	**(76)**
Expenditure Reestimates				
Uniformed Overtime	(300)	(302)	(281)	(254)
Other Uniformed Expenses	(107)	(122)	(118)	(102)
DOE Health Insurance	- - -	- - -	(71)	(106)
Other Expense Changes	(76)	(73)	(74)	(45)
Total	**(483)**	**(497)**	**(544)**	**(507)**
Revised Gap Forecast	**$(458)**	**$(5,073)**	**$(5,454)**	**$(5,505)**

Sources: NYC Office of Management and Budget; OSDC analysis

Spending in the uniformed agencies is now forecast to be higher by more than $400 million in fiscal years 2012 through 2014, and slightly less in FY 2015. Most of the additional resources were needed to fund overtime and failed cost-reduction initiatives. The Department of Education revised its health insurance forecasts for fiscal years 2014 and 2015 to match the assumptions used by the mayoral agencies for the growth in health insurance premiums, which increased its projected health insurance costs.

Closing the Projected Budget Gaps

To maintain budget balance in the current fiscal year and to narrow the projected budget gaps, the Mayor has proposed a number of gap-closing actions. These include an agency cost-reduction program, debt service savings from lower interest rates and refundings, and withdrawing the remaining $2 billion in the Retiree Health Benefits Trust over the next two years.

The City is also counting on the State to approve legislation that would permit the City to sell additional taxi medallions to generate $1 billion in FY 2013. Legislation was approved by the State Legislature in June 2011, but the Governor and City officials are discussing changes in the bill that would permit the sale to go forward.

As shown in Figure 5, the November gap-closing program would maintain budget balance in the current fiscal year and would narrow the out-year budget gaps to $2 billion in FY 2013, $3.8 billion in FY 2014 and nearly $4.9 billion in FY 2015.

Figure 5
November 2011 Gap-Closing Program
(in millions)

	FY 2012	**FY 2013**	**FY 2014**	**FY 2015**
Revised Gap Forecast	**$(458)**	**$(5,073)**	**$(5,454)**	**$(5,505)**
Agency Program	414	791	596	584
Debt Service Savings	56	229	30	44
Retiree Health Benefits Trust	- - -	1,000	1,000	- - -
Taxi Medallion Sales	- - -	1,000	- - -	- - -
Total	**470**	**3,020**	**1,626**	**628**
Surplus/(Gap)	**12**	**(2,053)**	**(3,828)**	**(4,877)**
Surplus Transfer	**(12)**	**12**	- - -	- - -
Gaps Per November Plan	**$ - - -**	**$(2,041)**	**$(3,828)**	**$(4,877)**

Sources: NYC Office of Management and Budget; OSDC analysis

The proposed agency program is valued at $414 million in FY 2012, $791 million in FY 2013 and nearly $600 million annually thereafter (see Figure 6). The City intends to mitigate the impact on basic municipal services by maximizing reimbursements from the federal and State governments, raising revenue from fees and tax audits, and reestimating costs. Nevertheless, the agency program would still reduce staffing by 1,215 positions by the end of FY 2013 (including 317 layoffs).

The Mayor would reduce funding to the Department of Education by $147 million in FY 2012, $301 million in FY 2013, and about $180 million in subsequent years. The reduction in funding, however, is not expected to affect educational services. The Transitional Finance Authority will transfer to the department $100 million in State building aid that it no longer needs to fund debt service in FY 2013. The department also plans to obtain additional federal and State aid, has reestimated special education costs, and will reduce funding for school repairs.

Figure 6
Agency Program
(in millions)

	Positions	FY 2012	FY 2013
Dept. of Education	- - -	$ 147.0	$ 301.2
Health and Social Services	69	114.0	60.3
Uniformed Agencies			
Fire	29	16.7	38.9
Sanitation	308	14.4	54.0
Correction	120	13.4	16.6
Police	- - -	8.3	74.6
Dept. of Citywide Admin. Svcs.	22	17.1	3.4
Dept. of Information Tech.	22	12.8	9.0
Transportation	112	12.3	28.5
Finance	(40)	8.0	43.5
Libraries	195	6.1	13.2
Cultural Institutions	109	3.1	6.1
Parks	137	2.7	21.7
Procurement Savings	- - -	- - -	55.5
All Other Agencies	132	38.0	64.7
Total	**1,215**	**$ 413.9**	**$791.2**

Sources: NYC Office of Management and Budget; OSDC analysis

The State Budget

In November 2011, the State estimated that it faced a budget gap of between $3 billion and $3.5 billion for the fiscal year beginning April 1, 2012. (The State also forecast a budget gap of $350 million in the current fiscal year.) In December 2011, the State approved new personal income tax brackets and other changes that will increase next year's income tax collections by $1.9 billion. The Governor's executive budget, scheduled to be released by January 17, 2012, will include actions to close the remaining budget gap. In the past, actions taken by the State to balance its budget have impacted the City's budget.

The Federal Budget

In August 2011, Congress agreed to raise the debt ceiling as long as the federal deficit was reduced. Congress established a committee to reduce the deficit by at least $1.5 trillion over ten years, but the committee was unable to reach agreement. Accordingly, automatic spending cuts of $1.2 trillion over nine years are scheduled to be implemented beginning in January 2013.

According to the Congressional Budget Office, planned defense spending would be cut by about 9 percent and nondefense programs by about 4 percent. Since some programs are exempt (e.g., Social Security and Medicaid), the cuts in domestic spending will fall more heavily on education and public housing, programs that are important to New York City. The State Division of the Budget estimates that New York State could lose $5 billion in federal funding over ten years.

Revenue Trends

Since the City released its adopted budget in June 2011, economic uncertainty has increased. Domestic growth slowed during the summer, and labor markets weakened. Political gridlock in Washington and the expanding debt crisis in Europe are adversely affecting the financial markets, and Wall Street, the engine of the City's economy, is restructuring and downsizing.

On a net basis, the City's tax revenue forecasts are virtually unchanged from June 2011. However, the City raised its forecast for collections from real estate transaction, sales, and bank taxes by, on average, about $280 million annually. These additional revenues were mostly offset by a reduction of, on average, $250 million annually in the forecast for personal income and general corporation taxes.

City fund revenues are forecast to grow by 3.9 percent in FY 2012 (after a 6.9 percent gain in FY 2011) and then rise by an average of 3 percent annually in fiscal years 2013 to 2015 (see Figure 7). In FY 2013, revenues are boosted from the anticipated receipt of $1 billion from the sale of new taxi medallions. Tax revenues are forecast to grow by 4.3 percent in FY 2012 (after an 8.5 percent gain in FY 2011) and then to increase at an average annual rate of 3.3 percent in fiscal years 2013 to 2015.

The November Plan anticipates a continuation of the modest recovery in real estate transactions, with collections forecast to grow by 10.7 percent in FY 2012 and an average rate of 10.8 percent during fiscal years 2013 through 2015. Although improving, the transaction tax forecast for FY 2015 ($1.9 billion) remains well below the FY 2007 peak ($3.3 billion).

Home prices have improved somewhat, especially in Manhattan, and there are signs of strengthening in the commercial real estate market. For example, during the first quarter of FY 2012 the value of transactions for large Manhattan offices (those valued at $25 million or more) totaled $1.7 billion, up from $1.2 billion for the same period in FY 2011 and $740 million two years earlier.

Figure 7
City Fund Revenues
(in millions)

	FY 2011	FY 2012	Annual Growth	FY 2013	FY 2014	FY 2015	Average Three-Year Growth Rate
Taxes							
Real Property Tax	$ 16,868	$ 17,646	4.6%	$ 18,238	$ 18,662	$ 19,092	2.7%
Personal Income Tax	7,644	8,037	5.1%	8,501	8,608	9,214	4.7%
Sales Tax	5,586	5,867	5.0%	6,068	6,313	6,584	3.9%
Business Taxes	5,300	5,721	7.9%	5,827	5,889	6,053	1.9%
Real Estate Transaction Taxes	1,229	1,361	10.7%	1,459	1,649	1,851	10.8%
Other Taxes	2,735	2,771	1.4%	2,853	2,901	2,956	2.2%
Audits	988	670	-32.2%	694	676	676	0.3%
Subtotal	**40,350**	**42,073**	**4.3%**	**43,640**	**44,698**	**46,426**	**3.3%**
Miscellaneous Revenues	4,587	4,550	-0.8%	5,541	4,560	4,618	0.5%
Unrestricted Intergovernmental Aid	39	25	-35.9%	- - -	- - -	- - -	NA
Anticipated State and Federal Aid	- - -	- - -	NA	- - -	- - -	- - -	NA
Grant Disallowances	(112)	(15)	NA	(15)	(15)	(15)	0.0%
Total	**$ 44,864**	**$ 46,633**	**3.9%**	**$ 49,166**	**$ 49,243**	**$ 51,029**	**3.0%**

Note: Miscellaneous revenues include debt service on tobacco bonds.
Sources: NYC Office of Management and Budget; OSDC analysis

The November Plan assumes that personal income tax collections will grow by 5.1 percent in FY 2012, less than half the rate in FY 2011. While year-to-date collections have been better than expected, these additional revenues are likely to be offset by the impact of lower Wall Street bonuses.

Personal income tax collections are forecast to grow by 5.8 percent in FY 2013 with continued job and wage growth. The City assumes that employment will grow by 24,000 jobs in calendar year 2012 and by another 37,000 jobs in 2013.

The November Plan assumes that a weaker economy and the European sovereign debt crisis will reduce consumption and tourism during the Plan period. The City expects sales tax collections to grow by 5 percent in FY 2012 (half the FY 2011 growth rate) and by an average of 3.9 percent over fiscal years 2013 through 2015.

The growth in business tax collections is expected to slow from 17.6 percent in FY 2011 to 7.9 percent in FY 2012, and then grow at an average of 1.9 percent in subsequent years. The bank tax is projected to decline by 3.6 percent in FY 2012 (after growing by 39 percent in FY 2011) and by similar amounts in fiscal years 2013 and 2014. The growth in general corporation and unincorporated business taxes is expected to slow beginning in FY 2013, when firms start to draw on credits for overpayments in earlier years.

Our analysis indicates that personal income tax collections could be lower by $200 million annually beginning in FY 2013 based on our forecast of lower securities industry employment and profits. The weakness on Wall Street could also reduce business and sales taxes by $100 million beginning in FY 2013.

Expenditure Trends

City-funded expenditures will grow by $5.6 billion in FY 2012 to $50.4 billion, an increase of 12.5 percent (see Figure 8). While projected spending is $3.7 billion higher than revenues, the budget is balanced with last year's surplus.

The growth is driven by the expiration of federal stimulus aid for education and Medicaid ($1.8 billion); an annual $1 billion reserve to cover the potential cost of changes in actuarial assumptions used to calculate City pension contributions; and an increase in City funds to replace cuts in State education aid ($812 million).

The November Plan assumes that spending will increase by only 1.7 percent in FY 2013 (even though debt service and health insurance costs are projected to continue to grow rapidly), because the City assumes a drawdown of $1 billion from the Retiree Health Benefits Trust, further staff reductions, and a three-year wage freeze. (The City has yet to reach agreement with the teachers' union for the prior round of collective bargaining.)

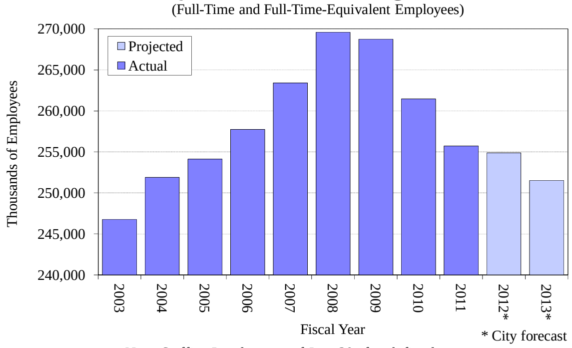
Staffing is projected to decline by 4,213 employees during fiscal years 2012 and 2013, to 251,507 employees (full-time and full-time-equivalents), after declining by 13,878 employees during fiscal years 2009 through 2011 (see Figure 9).

Figure 8
City-Funded Expenditures
(Adjusted for Surplus Transfers and TSASC)
(in millions)

	FY 2011	FY 2012	Annual Growth	FY 2013	FY 2014	FY 2015
Salaries and Wages	$11,935	$12,827	7.5%	$12,718	$12,858	$13,201
Pension Contributions	6,837	8,259	20.8%	8,405	8,284	8,529
Medicaid	4,614	6,091	32.0%	6,201	6,337	6,517
Debt Service	4,832	5,300	9.7%	6,083	6,639	6,986
Health Insurance	3,753	4,173	11.2%	4,613	5,081	5,610
Other Fringe Benefits	2,520	2,774	10.1%	2,835	2,960	3,023
Energy	886	952	7.4%	1,003	1,039	1,058
Judgments and Claims	664	655	-1.4%	685	718	754
Public Assistance	520	530	1.9%	540	540	540
General Reserve	- - -	300	NA	300	300	300
Drawdown Retiree Health Benefits Trust	(395)	(672)	NA	(1,000)	(1,000)	- - -
Prior Years' Expenses	(507)	- - -	NA	- - -	- - -	- - -
Other	9,103	9,174	0.8%	8,836	9,315	9,388
Total	**$ 44,762**	**$ 50,363**	**12.5%**	**$ 51,219**	**$ 53,071**	**$ 55,906**

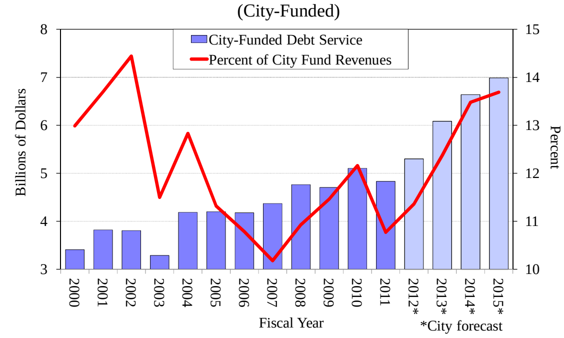
Note: Debt service includes bonds issued by TSASC.
Sources: NYC Office of Management and Budget; OSDC analysis

Figure 9
City-Funded Staffing Levels
(Full-Time and Full-Time-Equivalent Employees)



Note: Staffing Levels are as of June 30 of each fiscal year.
Sources: NYC Office of Management and Budget; OSDC analysis

Figure 10
Debt Service
(City-Funded)



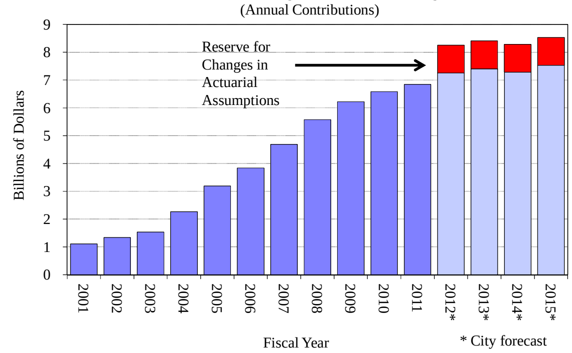
Note: Debt service amounts are adjusted for prepayments and debt defeasances.
Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

The pace of City-funded spending will pick up in FY 2014 (3.6 percent), primarily as a result of continued growth in debt service and health insurance premiums. Health insurance premiums for active employees are projected to rise at an average annual rate of more than 9 percent, and 8 percent for Medicare-eligible retirees; these are in line with historical rates.

City-funded debt service is expected to grow from $4.8 billion in FY 2011 to $7.0 billion by FY 2015 (see Figure 10) to fund the City's capital program. Debt service would grow at an average annual rate of 9.7 percent during this period, faster than the projected growth in City fund revenues. Consequently, debt service would consume an increasing share of revenues, rising from 10.8 percent in FY 2011 to 13.7 percent in FY 2015, the highest level since FY 2002.

Pension contributions grew during the past decade and totaled nearly $7 billion in FY 2011 (see Figure 11). As required under the City Charter, the City hired an actuarial consultant to review the assumptions and methods used to calculate City pension contributions.

Figure 11
New York City Pension Systems
(Annual Contributions)



Sources: NYC Comptroller; NYC Office of Management and Budget; OSDC analysis

The consultant has presented its report to the City's Actuary. The report recommends updating the assumptions for mortality, salary, and overtime to reflect recent trends, and reducing the annual investment earnings assumption from 8 percent to 7 percent to reflect current economic conditions.

If all of the recommendations are adopted, the report estimates that contributions from all employers would increase by a net of $2.6 billion annually. The City's contribution could rise by about $2.2 billion, which is more than twice the $1 billion reserve created for this purpose.

The City Actuary is contemplating changes that would mitigate the impact on the City's financial plan. The City Actuary is expected to make his final recommendations to the City's five pension systems in February 2012, when the impact on the City's financial plan will be detailed. Implementation will require the approval of the boards of trustees and, in some instances, State approval. If the changes are not implemented in FY 2012, the reserve in that year could be reallocated for other purposes.

The equities markets fell sharply at the beginning of the fiscal year due, in large part, to the European sovereign debt crisis. Even though the equity markets have improved in recent months, the pension funds have lost an estimated 4 percent on their investments as of December 9, 2011.

The November Plan continues to assume that the State will approve a lower-cost pension plan for new City employees, which will reduce pension contributions by $131 million in FY 2014, $252 million in FY 2015, and increasingly larger amounts in subsequent years. The State has yet to act on the City's request.

Department of Education

City funding for education has grown by $4 billion between fiscal years 2007 and 2012. This reflects the City's commitment under the Campaign for Fiscal Equity litigation, and an allocation of nearly $1.7 billion to replace expiring federal stimulus funds and cuts in State education aid. During the same period, State aid rose by $1.2 billion, far less than the promised $3.2 billion.

Even so, the Department of Education has reduced school budgets by a total of $1.1 billion over the past five years because resources were needed to fund rising costs for mandated services, fringe benefits and debt service. Consequently, class sizes have grown and other services have been cut.

An agreement, in June 2011, between the City and the United Federation of Teachers averted teacher layoffs in FY 2012. Still, the number of teachers on the payroll is projected to decline by 2,500 to 106,845 in FY 2012 (leaving 7,000 fewer teachers than in FY 2009). In October 2011, the department laid off 672 non-pedagogical employees.

The enacted State budget limits increases in State education aid to the rate of growth in the State's personal income. The November Plan does not anticipate any increase in education aid, but the City could receive about $300 million in additional education aid in FY 2013.

Metropolitan Transportation Authority

The Metropolitan Transportation Authority (MTA) provides services that are critical to New York City's economy, but the City's financial obligations are limited. The MTA's financial plan shows balanced budgets for 2011 through 2013, and relatively small budget gaps for 2014 and 2015. These estimates assume fare and toll increases of 7.5 percent in 2013 and 2015, and implementation of the MTA's cost-reduction program. The MTA faces other fiscal challenges including labor negotiations, the pace of the economic recovery, the potential for cuts in State aid, and rising pension and debt service costs.

The MTA must also address a $9.9 billion funding shortfall in its five-year capital program. The MTA has proposed borrowing $14.8 billion, the largest amount in its history, which would boost debt service by 64 percent, to $3.2 billion, by 2018. The MTA Board is scheduled to vote on the financing strategy in early 2012. If approved, the strategy will be submitted to the State Capital Program Review Board for its approval.

Health and Hospitals Corporation

The Health and Hospitals Corporation (HHC) could exhaust its cash reserves during FY 2013. To meet its cash needs through FY 2016, the HHC is seeking $1.9 billion in additional State and federal aid during the financial plan period. These resources may be difficult to obtain given current fiscal conditions, which could put pressure on the City to increase its contribution. The HHC also intends to reduce staffing by 1,200 employees.

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