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Report to Rep. William S. Moorhead, Chairman, House Committee on Banking, Finance and Urban Affairs: Economic Stabilization Subcommittee; by Elmer B. Staats, Comptroller General.

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The proposed \$1.3 billion increase in New York City's 1978 budget level runs counter to planned reductions in spending. Findings/Conclusions: The major increase in expenditures (about \$1 billion) was made possible by increases in Federal and State aid. This change was not fully analyzed because: the city estimates in the 1978 plan were not as detailed as those in its executive budget; changes were made in the accounting system; and the modified plan did not specify how the projected budget gap of \$433 million in 1978 would be eliminated. Despite these difficulties, the major revenue and expense variances were identified and were confirmed with the city's Office of Management and Budget. (DJM)

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548



B-185522

JUN 13 1977

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The Honorable William S. Moorhead
Chairman, Subcommittee on
Economic Stabilization
Committee on Banking, Finance
and Urban Affairs
House of Representatives

Dear Mr. Chairman:

In your letter of May 11, 1977, you requested that we provide additional information to supplement the briefing we gave your Subcommittee on April 29, 1977, on New York City's financial situation. Specifically, you requested information on (1) operating expenses in the capital budget; (2) increases in the City's budget above the amounts anticipated in the 3-year financial plan; and (3) illegal aliens in New York City as they affect the City's population base.

We have already responded regarding the matter of illegal aliens. This report responds to your request for information on the City's budget increases. We are looking into the matter of the operating expenses in the capital budget and that will be the subject of a subsequent report.

OVERALL BUDGET LEVEL

The City's proposed executive budget for fiscal year 1978, which begins on July 1, 1977, balances revenues and expenses at a level of \$13.9 billion, a \$1.3 billion increase over what was projected in its financial plan for 1978. This increase was made possible by revenue growth, primarily a higher level of assistance from the Federal and State governments than was anticipated in the financial plan.

The original plan projected a declining overall budget level between 1976 and 1978. Details of that projected decline, from \$13.2 billion in fiscal 1976 to \$12.9 billion in fiscal year 1978, are contained in enclosure I. Subsequent changes to the 1978 plan projected a continuation of the downward trend in overall city spending and the last plan modification anticipated a budget level of \$12.6 billion for 1978.

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The \$1.3 billion increase in the budget level proposed by the Mayor was your primary concern and our inquiry focused on the increase.

While the proposed 1978 budget is markedly higher than the financial plan projection, it exceeds the City's 1976 and 1977 expenditure levels to a much lesser extent. The City's 1976 operating expenditures totaled \$13.6 billion and its projected level for 1977 is \$13.8 billion. A breakdown of expenses for fiscal year 1976, the projected amounts for 1977, and the amounts proposed in the executive budget for 1978 are contained in enclosure II, and they illustrate the magnitude of City spending levels.

Nevertheless, the increase in budgeted spending for 1978 runs counter to the planned reductions in spending and we attempted to identify the reasons for the change.

As previously stated, it appears that the major increase (about \$1 billion) in expenditures was funded by increases in Federal and State aid and not by City generated revenues. Unfortunately, it was impossible to fully analyze this change because the City's estimates in its 1978 plan were not as detailed as those in its executive budget. For example, the revenue estimate in the plan for Federal and State aid was only one line item. That estimate was based on gross City projections of future Federal and State aid, rather than detailed estimates of each aid category. Because of this situation, we encountered some difficulty in trying to compare the detailed estimates in the 1978 executive budget with the more general financial plan estimates.

Two other factors also constrained our analysis of the differences between the plan and budget.

Since the fall of 1975, the City has been implementing its new accounting system and, as a result, certain of its revenue and expense categories have changed. For example, revenues classified under the category "Other" in the financial plan are classified as "General Fund" revenues in the 1978 budget.

In addition, the City's modified plan did not specify how it was going to eliminate a projected budget gap of about \$433 million in 1978. However, in its December 1976 monthly report to the Department of the Treasury the details were specified, and therefore, we used the Treasury report to make our comparison (see enclosure III).

Although the gap and the changes in the accounting system complicated the comparison you requested, we were able to identify the major revenue and expense variances which are indicated in the following schedule. We did not audit these variances but we confirmed our analyses with officials of the City's Office of Management and Budget.

COMPARISON OF FINANCIAL
PLAN AND PROPOSED EXECUTIVE BUDGET

	Modified financial plan <u>FY 1978 1/</u>	Proposed executive budget <u>FY 1978</u>	Variance Increase/ (Decrease)
<u>Revenues</u>			
	(in millions)		
General fund	\$ 4,466	\$ 4,870	\$ 404
Real estate taxes	3,218	3,166	(52)
Federal aid 2/	2,135	2,766	631
State aid 2/	2,102	2,477	375
Less: Disallowances for Federal and State aid	(125)	(125)	-
Other	281	-	(281)
Borrowings from the capital budget 3/	<u>515</u>	<u>713</u>	<u>198</u>
Total revenues	<u>\$12,592</u>	<u>\$13,867</u>	<u>\$1,275</u>
<u>Expenditures</u>			
Personal services and other than personal services	\$10,275	\$11,761	\$1,486
Debt service	1,821	1,616	(205)
MAC debt service	390	390	-
Budgeted reserve	<u>100</u>	<u>100</u>	<u>-</u>
Total expenditures	<u>\$12,586</u>	<u>\$13,867</u>	<u>\$1,281</u>

1/Includes allocation of budget gap. See Enclosure III.

2/Does not include Federal revenue sharing, countercyclical aid, or State revenue sharing. These items are included in the City's General Fund revenues.

3/These amounts are not revenues but borrowings to finance operating expenses in the capital budget.

REVENUE VARIANCES

The causes for the \$1,275 million overall revenue increase in the proposed 1978 budget were as follows.

General Fund - \$404 million net increase

The largest component of this increase, \$155 million, represents a reclassification of revenues from the "Other" category to the "General Fund" in the budget. This reclassification, required by the City's new Integrated Financial Management System, is offset by a decrease in the "Other" revenue category and therefore does not reflect a real growth in revenues but merely a change in how certain revenues are classified.

The next largest component, \$153 million, represents the City's estimate of additional revenues it will receive under the Federal countercyclical legislation. Also, the City projects a \$14 million increase in Federal general revenue sharing funds.

An increase of \$146 million represents tuition to be collected by the City University of New York in accordance with the City's new tuition policy. This revenue had not been anticipated in the modified plan.

Several other components of the general fund showed slight changes such as the unincorporated business tax (\$27 million increase), the personal income tax (\$12 million decrease), the corporate income tax (\$4 million increase), the financial tax (\$18 million decrease), the stock transfer tax (\$32 million increase) and the commercial rent tax (\$25 million decrease). These variances were due to revised forecasts based on new economic data, changes in collection patterns, and reductions made in certain City tax rates to encourage economic development.

A host of other minor variances resulted in a net decrease of another \$72 million.

Real Estate Tax - \$52 million decrease

This decrease resulted from the following:

- a projected reduction in the assessed value of taxable property which would result in a \$16 million decrease in tax revenue. This decline resulted from (1) the reclassification of publicly owned and publicly assisted housing as tax exempt, and (2) the lack of sufficient new construction to offset normal deterioration;

- --reductions in the real estate tax of \$83 million because of a lowering of the tax rate. Part of this reduction was necessitated by reductions in City debt service while the balance resulted from the City's decision not to tax at its constitutional limit, given lowered projections of City financed expenditures; and
- an increase of \$47 million in real estate tax collections.

Federal Aid (not including Federal revenue sharing and countercyclical aid) - \$631 million increase

The increase in Federal aid is primarily due to additional Federal funds for:

- programs under the Comprehensive Employment and Training Act (CEIA),
- community development activities, and
- increased public and medical assistance costs.

We were not able to quantify these increases over the plan amounts because the financial plan did not estimate Federal aid by individual program.

State Aid - \$375 million increase (not including State revenue sharing)

This increase in the executive budget resulted from additional State support for the senior colleges of the City University of New York as well as increased public and medical assistance costs. As with Federal aid, the absence of detailed estimates of amounts for State aid in the financial plan prevented any quantification of the increase by specific programs.

Other Revenues - \$281 million net decrease

This net decrease resulted in part from the reclassification of \$155 million of these revenues to the "General Fund" category as required by the new Integrated Financial Management System.

Another \$128 million of the decrease represents the elimination of revenues from the Municipal Assistance Corporation (MAC) and is offset

by a comparable decrease in debt service payments to MAC. Several miscellaneous variances accounted for a net \$2 million increase in this revenue category.

Borrowings from The Capital Budget -
\$198 million increase

This increase, according to City officials, resulted from a redefinition of expense items funded by capital borrowings. The stricter definition was mandated in a directive issued by the New York State Comptroller.

In gathering the data you requested on the capital budget, we will be looking at this matter in more detail. Our inquiries will cover the specific reasons for this increase as well as the question of whether the City is adhering to the State-legislated mandate to eliminate operating expenses from the capital budget.

EXPENDITURE VARIANCES

The causes for the \$1,281 million overall expenditure increase were as follows:

Personal Services and Other Than Personal
Services - \$1,486 million net increase

- a \$1,006 million increase reflects expected growth in expenditures for CETA programs; community development activities; public and medical assistance costs due to caseload, grant, and rate increases; and expenditures for support of City University senior colleges. These expenditures are budgeted to be offset by increases in Federal and State aid for these programs;
- a \$198 million increase in expenses supported by capital funds;
- a \$143 million increase in City University expenses which the City budgeted to be offset by increases in student tuition;
- a \$50 million increase for anticipated cost-of-living salary increases to match, on a dollar-for-dollar basis, the increases earned by workers through improved productivity;
- a \$46 million increase for additional subsidy to the Health and Hospitals Corporation;

- a \$26 million increase representing the City's share of salary costs over the CETA maximum salary levels;
- a \$74 million decrease in the City's share of pension costs arising from (1) increased reimbursements of pension costs under the Federal and State aid programs, and (2) a correction of a previous overestimate;
- a \$25 million increase due to the elimination of certain budget cuts previously projected in the plan;
- a \$29 million increase as a result of a reduction in the planned use of Federal community development funds to support City services; and
- a \$37 million net increase spread over a number of budgeted programs.

City Debt Service - \$205 million decrease

- a \$128 million decrease in City debt service to offset a comparable decrease in revenues from MAC. This is an accounting transaction which has no effect on City finances;
- a \$54 million decrease in debt service resulting from the early retirement of moratorium notes; and
- a \$23 million decrease in other debt service due to changes in the expected borrowing schedule.

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I trust this analysis of the increase in the proposed executive budget is responsive to your Subcommittee's needs. If you have any questions, or wish to discuss the information provided, we would be happy to meet with you at your convenience.

Sincerely yours,

SIGNED: HAYES B. STAATS

Comptroller General
of the United States

Enclosures - 3

ORIGINAL FINANCIAL PLAN

	Fiscal year		
	<u>1976</u>	<u>1977</u>	<u>1978</u>
<u>Revenues</u>	(in millions)		
General fund	\$ 4,041	\$ 4,198	\$ 4,423
Real estate taxes	2,967	3,265	3,234
State aid	2,316	2,325	2,307
Federal aid	2,143	2,136	2,126
Reserve for State and Federal aid disallowances	(295)	(290)	(150)
Other	<u>347</u>	<u>347</u>	<u>373</u>
Total revenues excluding capital funds	11,519	11,981	12,313
Capital funds <u>1/</u>	<u>697</u>	<u>647</u>	<u>597</u>
Total revenues including capital funds	<u>\$12,216</u>	<u>\$12,628</u>	<u>\$12,910</u>
<u>Expenditures</u>			
Expenditures not financed through capital budget	\$12,508	\$12,451	\$12,282
Expenditures financed through capital budget	<u>697</u>	<u>647</u>	<u>597</u>
Total expenditures	<u>\$13,205</u>	<u>\$13,098</u>	<u>\$12,879</u>
<u>Surplus/(Deficit)</u>	<u>\$ (989)</u>	<u>\$ (470)</u>	<u>\$ 31</u>

1/These amounts are not revenues but borrowings to finance operating expenses in the capital budget. It is GAO's position that the indicated deficit is understated by the amount of these borrowings.

COMPARISON OF 1976, 1977, AND 1978
EXPENDITURE LEVELS

	<u>FY 1976</u> <u>actual</u>	<u>FY 1977</u> <u>estimate</u>	<u>FY 1978</u> <u>executive</u> <u>budget</u> <u>proposal</u>
<u>(in millions)</u>			
Department of Social Services	\$ 2,926	\$ 2,989	\$ 3,047
Board of Education	2,092	2,066	2,094
Police Department	652	658	658
Board of Higher Education	479	445	437
Environmental Protection Administration	356	376	396
Fire Department	285	289	297
Health and Hospital's Corporation	663	680	706
Debt Service-MAC	462	608	390
Debt Service	1,847	1,775	1,616
Pensions	1,137	1,207	1,188
Other	<u>2,732</u>	<u>2,722</u>	<u>3,038</u>
 Total expenditure level	 <u>\$13,631</u>	 <u>\$13,815</u>	 <u>\$13,867</u>

THE FISCAL YEAR 1978 MODIFIED FINANCIAL PLAN AND
ALLOCATION OF THE BUDGET GAP
TO REVENUES AND EXPENDITURES

	<u>FY 1978 modified plan</u>	<u>Allocation of budget gap</u>	<u>Modified plan after alloca- tion of gap</u>
<u>Revenues</u>	<u>(in millions)</u>		
General fund	\$ 4,399	\$ 67	\$ 4,466
Real estate taxes	3,268	(50)	3,218
Federal aid	2,113	22	2,135
State aid	2,105	(3)	2,102
Less: Disallowances for Federal and State aid	(125)	-	(125)
Other	243	38	281
Borrowings from the capital budget	<u>515</u>	<u>-</u>	<u>515</u>
Total revenues	<u>\$12,518</u>	<u>\$ 74</u>	<u>\$12,592</u>
 <u>Expenditures</u>			
Personal services and other than personal services	\$10,372	\$ (97)	\$10,275
Debt service	1,886	(65)	1,821
MAC debt service	593	(203)	390
Budgeted reserve	<u>100</u>	<u>-</u>	<u>100</u>
Total expenditures	<u>\$12,951</u>	<u>\$ (365)</u>	<u>\$12,586</u>
 <u>Differences</u>	 <u>\$ (433)</u>	 <u>\$ 439</u>	 <u>\$ 6</u>