FUNDING THE CAPITAL AND EXPENSE BUDGETS: REPORT OF THE TEMPORARY COMMISSION ON NEW YORK CITY FINANCES

by

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ABSTRACT

In the summer of 1975, the City of New York experienced great difficulty in meeting financial commitments to its creditors and employees. Doubts about the economic well-being of the City and dissatisfaction with its financial policies caused the municipal bond markets to reject the debt offerings of New York. As a result of that rejection, payless paydays and a default on City notes appeared unavoidable. The Temporary Commission on New York City Finances was established in August 1975. Its mandate was to examine the length and breadth of city governmental operations, and to make recommendations for needed changes.

A major emphasis of the Commission, and the subject of the thesis, is the financing of government operations. The policies adopted by recent city administrations were not consistent with generally accepted principles of municipal finance. These inconsistencies were a factor contributing to the market's boycott of New York obligations.

The thesis presents an analysis of New York City tax and debt policy. The unorthodox fiscal policies of the city are described as are the steps taken to implement those policies. The thesis also describes the successful attempt to avert a technical default by the city. All levels of government had some involvement in reconstruction efforts-whether managerial, financial or otherwise. Important institutions and procedures created during the three-year recovery period are reviewed.

The Commission made a number of policy recommendations concerning public finance and other areas of city government. The thesis takes a critical look at the major recommendations of the Commission. The Commission's tax program, for example, seems to be based on an overestimation of the impact local taxes have on business' locational decisions. The political and economic obstacles to the implementation of the proposals are reviewed. In addition, the important public policy issues raised by the fiscal crisis are evaluated. Among them are: the role of banks in local public finance, the proper governmental response to a revenue shortfall, and the lack of public awareness of basic fiscal concepts.

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INTRODUCTION

The Mayor's Temporary Commission on New York City Finances was established by local law in August, 1975. Organized at the height of the city's fiscal crisis, the Commission was mandated to investigate several issue areas including management, fiscal policy, and other aspects of City government.

The Commission issued a total of 19 interim reports analyzing specific public policy issues. The final report includes material not covered within the narrow focus of each interim report. It comprehensively examines the city's population, economy, and political/governmental institutions.

The work of the Commission should be viewed in the overall context of combined public sector/private sector efforts to avert a 'technical' default by New York City. Contributions from all levels of government and from banking, labor, and academic institutions have been indispensible, financially and otherwise.

The news media's coverage of New York City finances has been oriented towards the crises that are just the outward symptoms of the problem-layoffs, the moratorium, bond boycotts, etc. Similarly, most governmental actions have been concerned with 'crisis management' of these media events. Necessary though they are, such activities do not identify the underlying causes responsible for the fiscal crisis.

From this perspective, the work of the Commission is seen to be complementary to the crisis management efforts of other agencies. This is because the Commission's focus was on the future direction of the city. Its recommendations suggest certain paths for New York policymakers to follow. The absence of any 'line responsibility' gave the Commission the freedom to analyse past mistakes and to prepare a much-needed, internally conducted form of criticism.

The internal or municipal nature of the Commission is as significant as its future orientation. Analysis by state, federal, and private agencies have already described the general nature of the city's fiscal/economic problems. The Commission's analysis represents the city's own admission (belated though it may be) of its past errors. The publication of such a critical report might help to increase the credibility of the local government.

A major concern of the Commission, and the subject of this thesis, is the fiscal policies of the city and the part those policies played in the fiscal crisis. The 'fiscal policy' in this instance is defined so as to include both the debt-contraction policy of the city and its revenue policy as well. The tax system is, of course, the revenue side of the capital and expense budgets. Together these two structures finance the operation of the city government.

<u>The Thesis</u>

A few words might be necessary to distinguish between the thesis document and the final report submitted to the Mayor. My original intent was to complete one document that would, with minor modifications, serve both the needs of the Commission and of the Urban Studies Department of M.I.T. As work progressed it became clear that such an arrangement would be impossible.

The report of the Commission is, in the final analysis, a very politically oriented statement. It is not a coincidence, I believe, that the final report was scheduled to be published during what is usually the month of the Mayoral Primary race (June, 1977). An unexpected action by Governor Carey (determined by his political agenda) changed the date of the primary to September, 1977. In spite of this shift, the Commission's report still had considerable impact on the Mayoral campaign.

The political considerations of the Commissioners often were not consistent with the legislative admonition to impartially analyze recent governmental operations. One of the major themes emerging from the analysis is the conflict between the political/short-term perspective and the economic/long-term viewpoint. Too often, recent city administrations responded to political imperatives. I feel the

Commission may be guilty of the same crime.

Many of their policy recommendations are not consistent with the problems identified by the time-series analysis of local fiscal trends. At the same time the recommendations are totally consistent with the business/political interests of the Commission members.

After many meetings and more than a few drafts, a document acceptable to the Commission was completed. This report was not, however, an apolitical description of the local revenue structure. The thesis, then, came to be a sort of revisionist view of the final report document. The parts common to both the Commission final report and the thesis are the quantitative analysis of revenue trends, and the discussion of policy implementation measures. The recommendations of the Commission are listed and critiqued with indications of economic and/or political obstacles to the implementation of the suggestions.

Data Sources

The basic data source for the thesis was the annual report of the New York City Comptrollers office. The time-series analyses were developed using the revenue and debt sections of these reports. The main reason for using the reports, was the need to have a consistent data base for all Commission staff members to use. There were many conflicts between the Mayoral annual budget and the budget as audited by the Comptroller, for example. And there were even greater discrepencies between city records and the calculations of the Financial Control Board and the Municipal Assistance Corporation. The decision to use one source for all revenue and expenditure figures was the most convenient/consistent path available.

Additional sources of information were the Advisory Commission on Intergovernmental Relations (ACIR) and the Citizens Budget Commission. ACIR data were used in the discussions of comparative tax burdens and of the extent to which particular tax measures are utilized nation wide. The Citizen's Budget Commission is a real estate industry-related organization, most of whose members I presume are citizens of New York. They prepared the calculation of capitalized expense budget items.

Working Definitions

The usage of a number of terms should be discussed to hopefully minimize confusion. Throughout the report, all references to "years" mean the New York City fiscal year, which starts on July 1st and ends June 30th. Revenue is another frequently used word. In the thesis, "Total revenue" refers to all local, state, and federal funding for municipal operations. The term "Local revenue" refers to the portion of "total revenue" that is raised within the city. "Tax Levy" funds refer to the property tax levy, although the city "levies" many non-property taxes. The word "levy" is also used in its verb form, in which case it may refer to any tax measure. The term "report" refers to the Final Report of the Temporary Commission, as opposed to the Thesis document.

Organization of the Thesis

The thesis is organized into four chapters. Additional, quantitative analysis of the revenue and debt structures of the local government are included in an appendix section. Chapter one of the thesis describes the debt management policies adopted by recent New York City administrations. It relates the city's debt contraction activities to the increasing level of expenditures occurring in recent years. The political and economic motivations for the debt management policies are reviewed, as well as the steps taken to implement the designated policy.

Chapter two presents essentially the same discussion concerning the tax policy of past city administrations. The overall tax policy goals are listed and the steps taken to implement the chosen policy are reviewed. In addition, the effects of the city's tax burden on individuals and businesses are analyzed.

Chapter three of the thesis describes the fiscal reorganization programs instituted in 1975 and 1976. All three levels of government participated in the effort to avoid a technical default by New York City. Chapter three discusses the institutions and policies adopted to bring the city's budget back into balance.

The fourth and final chapter of the thesis is an analysis of public policy issues raised by the fiscal crisis and by the government's response to that crisis. The first section of the chapter presents a critical evaluation of the recommendations developed by the Temporary Commission on City Finances. It describes the political and economic considerations that might block implementation of the Commission's proposals. The second section raises other important issues that are not addressed or inadequately addressed by the Commission.

A number of documents are included as an appendix to the text of the thesis. Appendix A is a detailed analysis of the city's bond and note holdings over the 1961-1975 period of concern. The various types of debt instruments utilized by the city are listed. Then, a time-series analysis of the changing size and composition of the city's funded debt is presented.

Appendix B includes similar information concerning the city's revenue structure. Each of the major tax measures are described and catagorized as either a property/non-property based or a personal/business oriented tax. Then, a time-series analysis of the revenue structure is presented. The contribution of individual taxes to the total revenue budget is listed.

Appendix D consists of a summary of the report adopted by the Temporary Commission on City Finance. The intent here is to provide an overall context in which to place the thesis document.

Appendix C includes the revenue data for the city over the 16-year period of concern. In addition, the tables and charts referred to in the text are included.

CHAPTER ONE: DEBT MANAGEMENT POLICIES

INTRODUCTION

Chapter One describes the public policy decisions that shaped the growth patterns of the city's funded debt (analyzed in Appendix A). The city decided to use its borrowing capacity to finance current operating expenditures. The steps taken to implement that decision are described. In addition, the state government's role in approving the incorrect policies is discussed. Finally, the municipal bond market's rejection of city paper is seen to be the "crisis event" that brought about much needed reforms.

The management policies of a locality are often the most crucial factors determining the cost of borrowing. The bond rating agencies supposedly reflect the likelihood that a bond offering would go into default. Since relatively few defaults have occured, a secondary judgement criterion weighs the honesty and efficiency of local government officials. A municipal government that is rated more reliable would consequently have less difficulty selling its bonds. The chapter points out that many practices adopted by New York City, while not illegal, were inconsistent with the policies of most localities. This undersirable form of uniqueness raised the interest rates charged on local debt.

A. DE FACTO POLICIES

There were four major policy decisions most directly responsible for abuses of the municipal borrowing power by New York City. Two of the policies concerned long-term debt instruments; two dealt with short-term notes.

A. The city failed to retire its short-term notes within the fiscal year in which they were issued. Instead, short-term notes were used as additional revenue.

B. The city liquidated its short-term notes by the contraction of new debt instead of by allocating sufficient amounts of funding from anticipated revenue sources.

C. The city borrowed up to its maximum capacity and sought means of enlarging its debt ceiling to the greatest extent possible.

D. The city financed some of its operating expenses by the sale of long-term bonds instead of by recurring revenues.

The improper debt management policies adopted by the city were the primary cause of the bond market's rejection of New York City obligations in 1975. In many respects, the city's lowered bond ratings and eventual exclusion from the bond market represented a lack of confidence in the municipal government's financial policies. Dissatisfaction with these policies was perhaps a more crucial determinant of the market's boycott than was the likelihood of a payment default.

The ability to market short-term and long-term debt is an absolutely indispensible requirement for the proper functioning of local governments. And the contraction of debt and its retirement directly influences and is influenced by the city's tax and expenditure levels.

The most basic concepts of municipal finance describe these interrelationships, pointing out the functions of the capital and expense budgets, the sources of revenue for each, and the safeguards or management procedures developed to insure the efficiency, effectiveness, and solvency of municipal government.

In brief summary, the expense budget consists of the annual operating expenses required by the subject locality in the delivery of public services. This budget is funded from the annual revenues generated by the city's tax system, along with intergovernmental aid from federal or state sources.

The capital budget funds those infrastructure needs (roads, schools, etc.) that have a useful life extending over many years.[1] These facilities are financed by the contraction of long-term debts that are paid off over many years. The capital budget is also funded by the recurring revenues of the city. Debt-service payments sufficient to cover the gradual retirement of debts are properly included as an operating expense in each year's budget.

Another part of the capital budget is the short-term note. With this debt instrument, the city can borrow money based on its expected revenue yields. This facilitates the operation of local government before tax collections are complete. As revenues are received, the short-term debt is retired. The "short-term" refers to the fact that such debt is paid off within the same year that it is contracted. The debt policies of New York City often were not consistent with the practices described here, as the following paragraphs explain.

The city, over a period of years, included increasing amounts of what were actually expense budget items in its capital budget. This was, in effect, a decision to pay for part of its annual operating costs from borrowed funds. The practice had become so entrenched in the city's accounts that an immediate end to the policy was considered impossible by the control or monitoring agencies working with the city's government since 1975. Instead, the gradual phasing-out of this practice over a ten-year period was considered the most practical way to eliminate that area of abuse.[2]

Every local government unit has established limits on its capacity to borrow money. These ceilings are designed to insure that, except for statistically improbable circumstances or occurrences, the city will be able to finance government operations and retire bonded debt from the amount of local revenues raised from all sources.

The New York City government consistently borrowed at or beyond its legal limits. In addition, the city sought authorizations or put forth definitions of limits so as to allow for increased borrowing wherever possible. The State Legislature was the body responsible for setting limits on borrowing. They were also required to approve any relaxation of or exemptions to the ceilings established.

The decision was made to use the short-term note as a means of deficit financing. That is, instead of using the short-term note as a cash-flow adjustment mechanism the city used its short-term borrowing as additional revenues. Two related practices were used to implement this policy decision. First, the city refused to retire its short-term debt in the year in which it was contracted. Secondly, the city would "roll over" its short-term debt by the issuance of new obligations to pay for the retirement of notes.

The short-term obligations of any municipality are usually retired in the year of their issue. The law allows for an additional year or two, (5 years for tax anticipation notes) in what are expected to be unusual and infrequent circumstances. The City, however, institutionalized a practice whereby the exceptional case became the everyday case. Most or all of the city's notes were left outstanding for the maximum period allowed by law. Few if any of its short-term obligations were retired within the same year of issue.

The retirement of short-term obligations was also handled in an improper fashion. The city would not pay off its note holders from the revenue sources against which the notes were issued. Instead the city would "roll-over" its debt. Rolling over described the practice where maturing obligations are paid off by the issuance of new debt obligations. The city would sell new short-term notes to acquire the funds to pay the holders of these notes outstanding for the longest period allowed by law.[3] Given the higher interest rates charged for more recent city paper, the roll-over practice sharply increased the cost of short-term borrowing.

The postponement of debt obligations does not provide additional funds, either to facilitate proper cash flow or to finance additional operating expenditures. Therefore, the city borrowed more in each succeeding year than it did in the previous year. The amount of short-term debt outstanding increased almost every year, causing increased amounts of "rolled-over" obligations. This was one city practice utilized for both short and long-term debt; the refusal to reduce the amount of outstanding obligations over the course of the fiscal year.

Table I-1 expresses new short-term debt obligations as a percentage of obligations redeemed in the same fiscal year. Whenever the ratio of new issues and redemptions is at unity (1.00 or 100 percent), the City has, in effect, rolled over its entire debt, since the outstanding amount remains unchanged. When the ratio is greater than unity, the outstanding debt has increased. The data show that in only two years during the 1961-75 period did the City actually reduce its short-term debt. In fiscal 1966 outstanding debt was reduced by almost $59 million from the preceeding year and fiscal 1973's outstanding short-term debt was reduced by $132.7 million. In every other year the City issued more short-term debt than it redeemed; that is, it rolled over its entire short-term debt and increased that debt by some amount. 1971 was the year of the greatest margin of new issues compared to redemptions. In that year new issues exceeded redemptions by almost 19 percent.

The same policies governed the contraction of long-term debt by the City. (See Table I-2) 1961 and 1968 were the only years where the City reduced its funded debt by redeeming more obligations than it issued. The ratio of new issues to redemptions for long-term bonds was greater than for short-term notes. In 1962, the City's borrowing exceeded its redemptions by 37 percent. In 1963, the margin was 39 percent. The year of the greatest excess in borrowing was 1971 when the City issued 79 percent more long-term bonds than it retired.

The excessive use of short-term financing is reflected in the increased percentage of total local debt represented by short-term instruments. Table I-3 shows the increase to be substantial. In 1961 the City's total short-term debt of $100.4 million was less than 3 percent of its long-term debt of $4.2 billion and an even smaller percentage of its combined short- and long-term debt. In fiscal 1966, five years later, outstanding short-term debt had grown to over 9 percent of long-term debt and 8.5 percent of total debt outstanding. In fiscal 1971 the ratio had increased further to 41 percent of long-term debt and almost 30 percent of total debt obligations. In fiscal 1975, the year of the fiscal crisis, short-term debt represented more than 1/3 of the total city debt.

When viewed as an extension of or complement to the expenditure decisions made by the New York City government, the viability of the debt policies adopted are clear. These policies provided the maximum of flexibility and possibilities. The combination of the four policies discussed, in an almost infinite number of variations, changed the impact of the capital obligations held by the city on its annual budget.

Under what might be called orthodox municipal finance, the capital budget acts as a constraint on expenditures for municipal services. That is, the greater the amount of debt, the greater the required debt-service payments and consequently the smaller the percentage of total revenues available for operating expenses. In the New York City context, the capital budget became a source of funds against which additional expenditures could be matched. The city's actions, in effect a deficit finance policy, expanded the level of expenditures and debt simultaneously and far in excess of what the city's recurring revenues could finance.

B. INSUFFICIENT FISCAL CONTROL MECHANISMS

To facilitate the efficient management of the city's general obligation debts, a system of controls was established to insure that the city could properly dispose of its obligations while at the same time allowing for the delivery of vital municipal services to residents. This system of debt management was based on three factors. First was a limitation on the amount of debt that the city could have outstanding at any one time. The second limit was on the type of activities that could be funded by the issuance of debt instruments. The third constraint was the requirement for legislative approval of alterations to established safeguards.

The limitation on the amount of debt the city could have outstanding was constitutionally mandated. The city's debt ceiling for each year was equal to ten percent of the average full value of the city's taxable real property as calculated over the five preceeding years.[4] This limit, generally called "the 10 percent limitation", was established at a time when most local revenue was raised through the property-tax levy, thus, the indexing of the city's borrowing capacity to the value of its real property. There is a separately calculated borrowing limit over bonds issued for the construction of housing. The borrowing limit for housing purposes (called the 2 percent limitation) is equal to two percent of the average value of the city's taxable real property as calculated over the preceeding five years. The housing limit is different from the general debt limit in that, while the average at full value is used to calculate the general obligation limit, the housing limit is determined by the average assessed value, which is considerably lower.

The second major limitation on the city's contraction of debt is based on the definition of what could properly be included in the capital budget, that is, what activities could be financed through the marketing of long-term debt. According to the generally accepted principles of municipal finance, proper capital budget items should include the acquisition, construction, or improvement of "major permanent facilities having a relatively long life."[5] By this definition, the intent is clearly to limit debt financing to activities directly related to construction of buildings, roads, bridges, or similar efforts. Labor costs directly contributing to the design or construction of valid capital projects are appropriate capital expenses. However, labor costs associated with the staffing of a building, for example, are expense items that should be funded through recurring revenue sources and included in the annual expense budget.

Discrimination between capital expenditures and operating expenditures limits the range of activities that can be financed through borrowing. In this way the size of the capital budget is minimized. The "useful life" of an item is an important determinant of its proper classification as an expense item or a capital item. The municipal bonds issued by New York City may not remain outstanding for a period of time that is longer than the useful life of the project that is financed through the sale of such bonds.[6]

The third constraint on the city's debt-incurring ability is the state legislative approval necessary for any borrowing inconsistent with the limitations on the permissible amount of debt or the activities financed through municipal bond sales. By requiring the approval of the state legislature, an external and hopefully impartial examination of city proposals could be achieved. The need for state approval also highlights the character of the city as a "creature of the state." This appellation points to the fact that New York City is an administrative device created by the state. The city is delegated certain powers as a convenient method of discharging the functions of the state. Requiring state approval confirms the ultimate responsibility of the state for the conduct of its created sub-divisions.

The expenditure decisions and policy of recent New York City administrations have been described in the Commission's final report. It has been pointed out that expenditure decisions were the major determinants of city revenue and debt policies. The city decided to use capital borrowing to finance noncapital, expense budget items. The implementation of that decision required the nullification of the external constraints or ceilings on the city's ability to contract debt. For each of the three state-mandated controls on debt financing, the city was able to secure exclusions, exceptions, or favorable interpretations that would allow for increased borrowing of funds.

The "10 percent limitation" for general purposes (nonhousing) proved to be an ineffective limit on the city's outstanding debt. This was due to the liberal use of the "excluded debt" classification as the focus for additional bond issues. The excluded debt classification includes municipal borrowings which, for various reasons, are permitted in addition to the allowable outstanding debt under the constitutional, 10 percent limitation. Capital projects that are expected to be self-sustaining are a major portion of the excluded debt. These are public enterprises whose user charges or fees are projected to be sufficient to cover the debt service (interest and principal) on the financing. Since these projects are assumed not to require debt-service payments from the expense budget, they are not included within the debt ceiling.

The city made use of this excluded debt classification to substantially increase its borrowing. And while the city's total debt far exceeded the general 10 percent limit, the use of the different accounts permitted the city to maintain an "unencumbered borrowing capacity" in each year up to and including fiscal 1975 when the market for city obligations evaporated.

Table I-4 shows that the debt ceilings were an ineffective means of limiting the city's contraction of debt obligations. The statutory debt ceilings were exceeded in every fiscal year reviewed. The excluded debt category and increased short-term borrowing were the major instruments used to expand the city's outstanding debt beyond constitutional limits. And state legislative approval made the policies legal. In 1971, for example, the city's outstanding debt was almost $8 billion, or $1.4 billion (21 percent) greater than its supposed debt ceiling of $6.6 billion. More recently, the 1975 city debt of $12.3 billion was over $4 billion or 50 percent larger than the legal debt limit of $8.2 billion. In spite of the overextension of the city's borrowing, the city technically did have an "unencumbered" margin within its housing and general debt limit.

The city was also able to obtain a relaxation of the limitations on the types of activities that could be funded in the capital budget. This change in policy was perhaps more significant than was the increase in the amounts of debt the city could contract. An increase in the city's capital funds would be useless if the additional funds were not able to finance operating expenditures - wages, non capital equipment, costs, etc. Since the operating budget was the intended area for increased expenditures, and the area where revenues were insufficient, the capital financing/operating expenditure shift was an integral part of the fiscal policy.

The city's objectives were met with the passage of the Local Finance Law. This law contained a much more liberal definition of what activities could be funded through the capital budget.[8] By using this statute, the city was able to finance many expense items from the capital budget, that is, through borrowed funds. The language of the Local Finance Law spoke of capital financing for "various municipal purposes." The city, in its annual report on outstanding debt, used the same terminology to list the expense items it financed through borrowing. Such activities accounted for almost 50 percent of the city's capital budget in recent years. The practice was so firmly entrenched that its immediate elimination would have resulted in serious hardships for the city and its residents. A ten-year time schedule was adopted to facilitate the gradual elimination of expense items from the capital budget.

Table I-5 shows the increasing amounts of capital funds being used to finance current operating expenditures. The practice began in fiscal 1965 when $26 million was used to finance manpower training programs. The original rationale for this procedure was the "human capital" nature of employment programs. Since job training would have long-term positive effects on a person's earning potential, this was used as a justification for calling the expenditure a "capital" item. The next major extension to this policy was the use of capital funds to finance a retroactive pay increase for City employees.

The size of the capital budget/expense item shift grew rapidly, especially after fiscal 1969. By the start of the fiscal crises, nearly 50 percent of the City's capital budget, more than $700 million, was being used to finance expense budget items.

The third constraint on the city's debt management policies was the state legislature. In spite of the well-publicized upstate/downstate antagonism and the presence of a distinct anti-New York City majority among the state legislature, that body must accept a major responsibility for the New York crisis. There was a clear failure of the legislature to exercise its proper role as the supervisor of local governments when necessary. The above-described increases in the city's debt-incurring powers would have been impossible without legislative approval. Similarly, the use of capital funds for operating expenses would have been impossible without legislative sanction. The state refused to say no when clearly improper policies were proposed by the city.

CITY-STATE RELATIONS

The state's reluctance to exercise its proper oversight function is a result of the peculiar relationship between New York City and State. From the City's perspective, the legislature was a gathering of an anti-city majority of upstate farmers. The City did not receive its fair share of state aid but got more than enough meddling in local affairs, fiscal and otherwise. If only the upstaters would leave the city alone, all would be well. Greater autonomy was demanded under the slogan of "home rule."

The noncity portion of the legislature saw city/state relations in a different light. The City was felt to receive an excessive amount of state aid while constantly claiming discrimination in the allocation of funds. In addition, New York City was seen as the spendthrift of the state, providing exhorbitant wages for City workers and too liberal welfare and other social programs. All of these expenditures the City sought to finance through the taxes of upstate New York residents.

Of course, neither perspective was all true or all false. However, the reconciliation of these views at budget-adoption time was in part responsible for the City's difficulties. The City would, as a matter of course, request additional state aid to finance the expenditures it felt necessary. When sufficient state aid was not forthcoming, the City's fallback position was the "home rule" argument. It requested the authorization to raise money locally in order to finance their expenditure programs without increased state aid.

It was this situation that permitted the development of the city's tax structure and its debt management policies. The state agreed to let the city cut its fiscal throat as long as such activities were contained within the five boroughs. This sentiment caused the state to approve the imposition of a tax structure that would contribute to the city's economic decline as surely as it would increase operating revenues in the short run. It authorized the city's borrowing of monies far in excess of its capacity to repay.

The state legislature incorrectly felt that New York City could go its own harmful way with little or no negative effect on the rest of the state or nation. But instead, the state (Urban Development Corporation) UDC's default contributed to the market's rejection of city bonds. And the city's fiscal crisis contributed to the difficulty in (and high costs of) marketing the state's obligations in spring 1976. These developments reaffirm, if painfully, the indivisibility of the state and its created subdivisions.

C. THE BOND MARKET REACTION

The constitutional and governmental constructs on New York City's debt policies were proven to have been an ineffective means of controlling its long-term borrowing. However, the workings of the marketplace, specifically the municipal bond market, provided a different set of constraints on the management of municipal obligations. In fact, the dramatic event that marked the "birth" of the fiscal crisis was the rejection of New York City Notes by the bond market. That rejection was not engineered by the proverbial "invisible hand" but by the quite visible and articulate hand of the NYC clearinghouse banks, the traditional underwriters of New York's municipal bond offerings.

The municipal bond market provided early criticism of NYC policies in the form of the less than optimal bond rating given to recent note offerings. The lowered city ratings resulted in increased borrowing costs for the city as interest payments necessary to attract investors increased. The major bond-rating services were two institutions most directly involved in the market's evaluation of NYC paper.

The two major bond-rating agencies are the Moody's Investors Service and the Standard and Poor's evaluation.[9] Both groups evaluate the thousands of tax-exempt bond issues annually offerred by state and local governments nation-wide. The ratings analyse the quality of bond issues as compared to the offerings of other governmental bodies. The ratings assigned after the completion of their analysis are the standard criteria utilized by investors when deciding among various municipal offerings. As such, the attainment of a higher or lower bond rating can have a measurable impact on the cost of borrowing money. The rating agencies utilize a number of objective and subjective criteria in their analysis of a particular bond offering.[10] Among the objective criteria examined are the overall economic conditions of the municipality, the legal constraints on the contraction and uses of debt, the efficiency and reliability of the locality's debt management policies. In each of these areas the conditions of New York City (from the rating agencies' point of view) did not argue for the granting of the highest bond rating.

The city's economy had suffered from the loss of private sector jobs and a drastic increase in social welfare expenditures. Retail sales were declining and the city's share of regional income had declined. In addition, the city's revenue system was extremely sensitive to fluctuations in economic trends. The relatively greater reliance on non-property taxes meant that revenues were less stable over the short run.

Municipal bond analysts also considered the impact of New York State legislation that permitted more liberal uses of capital funds than was the norm. The city policy of financing operating expenses with capital funds was legally sanctioned, however, the bond market frowned on such practices. There was also a widespread belief that the city used a number of accounting gimmicks to hide the existence of a revenue deficit. This practice and the city's excessive issues of short-term debt raised questions about the fiscal management of New York City.[11]

D. THE EFFECTS

There were a number of unfavorable outcomes that resulted from the improper debt management policies followed by the city. As described above, the abuses of the municipal borrowing power contributed to the deterioration of the city's physical plant, it increased the cost of municipal service delivery, and it siphoned additional funds from the expense budget in order to pay rising debt service charges.

The use of a substantial portion of capital funds for operating expenses meant that there was less money available for legitimate capital needs. The viability of any locality is in part determined by the maintenance of public facilities--buildings, roads, bridges, etc. The maintenance of old facilities and the construction of new ones were neglected since much of the capital budget was being used to finance expense budget items. Certain types of capital expenses, bridge or tunnel maintenance, pot hole repair and the like, can be delayed for a while without immediate negative impact. But a consistent policy that ignores the depreciation of the city's capital assets over the long run will surely result in greatly increased costs as continued neglect renders certain assets useless. The City's West Side Highway is the best example of this process.

The policy of using capital financing to fund operating expenditures had the effect of substantially increasing the cost of municipal service delivery without producing any corresponding improvement in the quantity or quality of such services. The use of borrowed funds for such expenditures meant that the city would also have to pay the long-term interest costs associated with such borrowing. Therefore, while the city might use one million dollars of capital funds for an operating expense, the actual cost to the city's residents is one million dollars plus whatever interest charges were required. Over the life of a 10-year bond, for example, such interest costs are substantial.

The increase in the outstanding amount of city debt causes less of the operating budget to be avialable for the funding of municipal service delivery. The long-term debt of a municipality is an obligation of the city's full faith, credit, and taxing power.[12] This means that bond obligations must receive first priority in the expenditure of city funds. The required debt-service payments are an uncontrollable budget item in the same way that welfare and Medicaid costs are since the city cannot unilaterally diminish debt service payments. The increasing amount of outstanding debt meant that required debt-service payments also had to increase. And the effect is that a larger and larger portion of the city's operating budget is utilized for uncontrollable debt service payments. This also means that a decreasing portion of that budget is available to fund the programs that actually provide services to the city's residents.

SUMMARY

Chapter One described the debt policy decisions of recent city administrations. It presented a picture of very innovative or very incompetent managers who were coping with a consistent pattern where expenditure needs (legitimate or illegitimate) far exceeded the available amount of revenues. The reaction to this mismatch of supply and demand was to violate the standard operating procedures utilized in the financing of governmental entities. The city used a number of unorthodox procedures to increase the available amount of current operating expenditures and to create the appearance of a balanced budget.

One often-heard criticism of New York City concerns the alleged incompetence of its fiscal managers. The development of its revenue structures is pointed to as an indication of this incompetence. A close look at the City's revenue operations suggests that this is not the case. It is clear that the decision to substantially increase expenditures was the "independent variable" that determines the level of all taxes and the extent of borrowing. It is also clear that this policy is the exact opposite of the usual public finance situation wherein the amount of available revenues determined expenditure levels. However, if one momentarily ignores the rightness or wrongness of the basic fiscal policy (and it was an unwise choice) its creativity is undeniable. The City decided to extract the maximum amount of revenue from it's tax and debt systems. And, the seemingly "incompetent" fiscal policies adopted were in every instance consistent with the furtherance of that policy.

The assertion, then, is that, far from being incompetent political hacks (or more precisely, aside from being hacks), the City's fiscal management really was efficient, really did "know the buck" as the Mayor's campaign slogan stated. Their policies were both market-conscious, and politically conscious, as they had to be to get past the state legislature. Part and parcel of the revenue generation strategy they followed was the tradeoff involving long-term contraction of the tax base as the price for increased revenue in the short run.

FOOTNOTES

1. James Maxwell and J. Robert Aronson, Financing State and Local Government (Washington: Brookings Institute), p.42.

2. City of New York, Financial Plan for the City of New York and Covered Organizations, p. 3.

3. Advisory Commission on Intergovernmental Relations, Understanding the Market for State and Local Debt (Washington: U.S. Government Printing), p. 11.

4. Op. Cit., Comptroller Report 1964-65, p. 443.

5. New York State Comptroller's Office, Accounting Systems Directive # Four (New York), p. 2.

6. Section 11, Local Finance Law of New York State.

7. Op. Cit., Comptroller's Report 1964-65, p. 428.

8. Section 11, Local Finance Law of New York State.

9. Op. Cit., Calvert, p. 26.

10. Ibid., p. 35.

11. Ibid., p. 36.

12. Ibid., p. 3.

CHAPTER TWO: LOCAL TAX POLICY

INTRODUCTION

Chapter two describes the tax policies developed by recent New York City administrations. The overall objectives of city policy are listed, and the steps taken to implement those policies are discussed. The effect of the local tax burden on individuals and on the business community is assessed. Political considerations, it appears, determined much or all of the city's tax policies. Some of the policital rationales behind the development of the local revenue structure are reviewed.

A. DE FACTO POLICY

An increase in the revenue generating capacity of the municipal tax system was the primary objective of the city tax structure. The city's tax policy was based on two practices;

a. The city substantially increased the rate of taxation on the major revenue-producing city taxes.

b. The city imposed new levies on previously untaxed forms of income or wealth.

A large part of the increased expenditures in recent

New York budgets was financed through increases in the rate of taxation on all major taxes levied by the city. The property tax rate, for example, has been subject to annual increases for each of the last fifteen years. The tax on business incomes has been increased three times since 1965, resulting in a rise in the effective tax rate of over 100%. The combined city/state cigarette tax is the highest in the nation. And, there were substantial increases in the sales tax, and the personal income tax over the past 15 years.[1] All of these levies are major components of total local tax revenue. The combined effect of these tax increases has raised the New York city tax burden higher than that in any other municipality nationwide.

The introduction of new taxes helped to finance expenditures that were in excess of those funded by tax rate increases. The city developed a number of new revenue sources, in some instances taxing activities no other municipality does. Many of these taxes were directed at particular segments of the economy, such as the hotel occupancy tax which is different from the more broadly-applicable commercial occupancy tax. Similarly, the tax on horse race admissions is another example of a very narrowly based tax. These are representative of other "gimmick" taxes levied by the city.

From a policy point of view, the benefits of having the ability to combine (in various proportions), tax rate increases with new taxes are obvious. The arrangement provides the maximum amount of flexibility to local government officials in the preparation of the budget.

Further increases in the tax rates of major local revenue sources were not feasible either politically or economically. Each major revenue source had a city-wide tax base and therefore a city-wide constituency opposed to such a policy. At the same time, the reaction of market forces to past tax increases strongly suggested that the city was at or near the limit of its ability to make further increases in the percentage rates of the major taxes. Each increase in the property tax rate contributed to the abandonment of taxable property and to an annually increasing percentage of uncollected property taxes.[2]

In summary, the most widely utilized forms of local finance (the property tax, and, increasingly, the sales and income taxes) were not capable of producing the amount of revenue necessary to finance the city government's expenditures.

It was this situation that created the need for the new, revenue-producing taxes, imposed by the city government. The primary reason for the imposition of the new, gimmick taxes, is that the levies provide additional revenue without requiring increases in the more broadly based tax measures.

The logic behind the imposition of the tax on horse race admissions is exemplary of the way in which the city's tax structure was developed. This levy produces revenue for the city and has the added political attraction of affecting the relatively small group of individuals who frequent race tracks.

In the same fashion, excise taxes, such as coin operated amusement device tax or the annual vault charges, were imposed. The introduction of any one nuisance tax, when proposed separately, may seem insignificant. But the combination of many small taxes can produce very significant amounts of revenue and can have significant and unanticipated effects on the city's tax structure and tax payments structure.

The implementation of the city's tax policies, especially after fiscal 1965, created a number of cause/effect relationships, with the result of one action becoming the cause of another. First, the increasing rate of taxation caused the tax burden borne by New York City residents and businesses to become the highest in the nation. The New York City tax rates became increasingly non-competitive with those in neighboring local government entities. Then, the loss of a competitive tax burden caused the out-migration of many businesses and individuals to those localities with lower tax rates. The decline in jobs and local personal income caused a drop in the value of the city's tax base. Finally, the losses in the tax base caused the need for higher tax rates to produce smaller amounts of revenue, at which point the cycle begins again.

B. THE INDIVIDUAL'S TAX BURDEN

The tax policies adopted by the city government placed a low priority on maintaining competitive rates vis-a-vis neighboring municipalities. This in spite of evidence suggesting that high taxes were a contributing factor to the economic decline of the city.

Table II-1 illustrates the un-competitive nature of New York's personal taxes compared to national and urban averages. The so-called big three taxes (property, sales, and income) are the major revenue sources utilized by local governments. The data show that for low, moderate, and upper income levels, NYC taxes are significantly higher than national or urban tax levels.

For the $7,500 income level family, the three major taxes claim 12.4 percent of total income. This tax burden is almost 30 percent greater than the average for U.S. cities and is almost twice the average for the U.S. as a whole. The same pattern holds for middle ($12,000) and upper ($50,000) income groups.

Of particular significance is the fact that the differential between average urban and New York City tax burdens is much greater for the upper income than for lower- or middle-income groups. While the low-income New York City tax burden is 30 percent above the urban average, upper-income tax burdens are over twice as high as the average.

Persons in the upper-income group are more mobile than lower-income persons, and are more likely to consider tax differentials as a basis for a locational (residential or business) decision.

While a tax rate that is near or below the national average is desireable, it is even more important for a municipality to be competitive with regard to the tax rates of neighboring localities. In the tri-state metropolitan area, no city or county had a local tax burden or, a total tax burden as high as New York City's. When considering the total tax burden or specific tax measures, the New York City tax structure encouraged the relocation of taxable activities outside the city limits.

Table II-2 compares the liability for the same "big three" taxes in New York City and neighboring localities in the Metropolitan area. It shows that the city is worst or next to the worst in each tax category. While Connecticut's property taxes are higher than New York's, the absence of a personal income tax serves to partially explain the high real property tax rate.

C. THE BUSINESS TAX BURDEN

The business community also was impacted by the revenue generation policy that overshadowed the economic development/maintenance function that is properly a role of a local tax system. The erosion of the city's tax base, was in part caused by the structural deficiencies in the region's economy. These structural problems were aggravated by the negative effects of the New York tax system. The manufacturing industry, for example, had been on the decline due to high wage costs, an obsolete physical plant, and the increased costs of energy. However, the City's tax system increased the speed of the manufacturing exodus instead of slowing the departure rate as much as possible. That industrial sector paid a disproportionately high share of the city's sales and commercial occupancy taxes. This contributed to the departure of manufacturing firms.

The burden of business income taxes also increased over the 16-year period of analysis. Table II-3 contains data collected by the New York State Economic Development Board (EDB). In a study prepared for the Governor, the agency compared the rates of return on a hypothetical investment in various New York counties. Since the applicable federal and state taxes were identical in every location, the difference on "bottom line profits" is considered to be a function of the local tax burden. As the data indicate, New York City is in every case the least profitable location in which to invest. An investor from California, for example, could earn as much as 12.15 percent on his investment if he located in Onondaga county. The same investment in New York City would yield 10.95 percent, almost 10 percent less.

Each increase in the sales tax rate has been responsible for reducing the value of taxable retail sales in the city. Shoppers preferred the lower sales tax rates charged in Westchester County, Connecticut or New Jersey. The excise tax on cigarettes, when combined with state taxes, is the highest in the nation. This has resulted in an estimated $50 million worth of tax losses to the city annually. This loss is partially caused by out-of-city purchases of cigarettes by individuals. The majority of lost taxes are caused by the massive importation of untaxed cigarettes by organized crime. The uncompetitive nature of the city's cigarette tax provides the incentive for these activities.[3] The city is also non-competitive in regards to its personal income tax, property taxes, and, of course, in its enactment of nuisance taxes.

The loss of middle- and upper-income residents was also caused in part by the city's tax burden. The flight to the suburbs caused further declines in retail sales in the city. There were also losses in the New York City income tax as a result of movements out of the city.

The adoption of many new taxes has caused the structure of the city's tax system to change. Local finance nationwide has changed considerably in the last 30-40 years, from the time when the property tax financed almost all local government expenditures. However, even with that qualification, the New York local tax structure has evolved into something unique among American local government bodies.

The use of common definitions for income, deductions and exemptions, etc., has been found to be more convenient for the tax collector and the tax payer. By conforming to the definitions used by higher levels of government, localities' collection costs are indirectly subsidized by the greater efficiency of the state or federal governments.

The New York City tax system, by its reliance on unique tax measures, enjoys none of the advantages of conformity. Many of its taxes require special forms and separate calculations of income, credits, and exemptions. For each unique tax the city must pay for the collection of information that will ensure compliance with the tax measure. The costs for collection of such taxes is much higher per dollar than is the cost for collecting more widely used tax instruments.[4]

SUMMARY

Chapter Two reviewed the public policy decisions that influenced the shape and size of the local revenue budget. The decision to increase municipal expenditures created a need for additional tax revenue. City officials decided to generate the maximum amount of revenue from the local tax base. To increase revenue collections, the City utilized two procedures, namely, increasing tax rates on old tax measures and, introducing new tax levies. The city created "packages" combining tax increases and new taxes. The maximum political flexibility was assured by targeting tax increases towards a politically weak constitutency. Additional revenues were generated in this way.

The combined effect of the City's tax policies caused the local tax burden to become the highest in the nation. For both businesses and individuals, a very uncompetitive tax structure was in place.

Many of New York City's fiscal problems can be explained by the so-called, "captive of events" theory. According to this conception, actions of the state or federal government, as well as the operations of the bond market have been most responsible for the city's difficulties. Local governments, in New York or elsewhere, are powerless to counteract the effects of these powerful forces, it is argued.

At the same time, many scholars maintain that the local tax structure is at best a secondary consideration when firms make locational decisions. Other, more important factors, include the availability and cost of energy, labor costs, and proximity to markets and transportation. Only after these more crucial inputs have been analyzed are local tax burdens evaluated.

Both of these points are raised to suggest that, in the absence of changes in more important cost areas, reductions in the local tax burden will not significantly reduce the outflow of businesses from any city. However, the local tax structure is still the most powerful economic tool in the hands of the city government. Therefore localities will continue to manipulate the local tax system, acting as if that system were the deciding factor in making locational judgements.

FOOTNOTES

1. See Interim Report on Nonbusiness Taxes.

2. See Table B-3.

3. See the discussion of cigarette smuggling in Interim Report #11.

4. See Interim Report on Personal Taxes (Report #11).

CHAPTER THREE: FISCAL RECOVERY EFFORTS

INTRODUCTION

Chapter three discusses the fiscal reconstruction program created during summer and fall, 1975. As the extent of the financial crisis became known, additional and more extensive procedures and institutions were developed. The chapter analyzes the political and financial considerations that determined the shape of the governmental response to the crisis. In the tax area, shifts in the local revenue structure and proposed reforms are reviewed. The institutions created to address the debt management problems of the city are also discussed.

The three-year period beginning with fiscal 1975-76 was designated a transition period for the City of New York. This time frame was established to permit the city to right itself fiscally and to reorient its operating procedures. The major aim of the three-year transition period was for the city to balance its budget in fiscal 1978. In addition, the city was to analyze its fiscal, managerial, and political processes, in order to function better when "home rule" was reinstituted. All three levels of government had some part (fiscal, managerial or analytical), during the three-year period of transition.

A. FEDERAL/STATE/LOCAL CONTRIBUTIONS

The Federal government's role was primarily fiscal. Its major involvement was as the sponsor of the seasonal financing agreement, a piece of legislation whose life coincides with the three-year reorganization program of the city.[1] The agreement allows the U.S. Treasury to lend a maximum of $2.3 billion to New York annually. The loan was for the purpose of regularizing cash flows since the short-term bond market was closed to city offerings. The extension of the loans was made contingent upon the city's repayment of outstanding borrowings within the same fiscal year that the loans were made. In other words, the city had to follow the short-term borrowing practices that were normal for most other governmental entities. New York City's debt policies in recent years, however, were not consistent with those norms. This created the need for an independent audit of city accounts before the Treasury would renew the loans.

In addition to its financial impact, the loan program, and the federal involvement it represented, had substantial impact on local politics. When negotiations concerning the financing of the city's moratorium settlement stalled, the Treasury's threat to "turn off" the seasonal loans was the major factor that brought the banks and pension funds together, thereby facilitating the redemption of the debt previously in moratorium. It was widely rumored that, public protestations not withstanding, the Mayor privately urged the Treasury Department to make the cutoff threats, as a means of forcing the banks and unions to reach an agreement.

New York State's role in the fiscal 1975-78 transition period was implemented primarily through the Emergency Financial Control Board. That entity, which has state and local representatives (although the state clearly dominates) was delegated the power to accept or reject the financial decisions made by the New York city administration. The EFCB's power is based upon the city's position as the "creature of the state." Given the city's apparent inability to responsibly manage its affairs, (as evidenced by the fiscal crisis and the unmarketability of city bonds) the EFCB is the state's delegated oversight body for New York City affairs.[2]

Since the major item in the city's budget is personal services (wages, salaries), a large part of the Control Board's attention is directed to the review of labor contracts. In addition, fiscal relations with the covered organizations have been a major area of concern. These are agencies whose funds come from the New York City Budget, but over which the Mayor has no direct control (Board of Education, Health and Hospital Corporation, etc.). The financial decisions of these semi-autonomous bodies have been subject to Control Board review.

Tax and debt management policies have also been reviewed by the Control Board. For both of these areas, the deliberations have been concerned with the impact of policy decisions on the city's ability to balance its budget within the designated three-year period.

As was the case with the Federal government involvement, the state's role was supposedly limited to fiscal oversight and the preparation of a balanced budget for 1978. As long as available revenues were sufficient to cover proposed expenditures, the control board was to have no say in what the expenditures were for. Within the constraints determined by available revenues, priorities concerning expenditures and necessary cutbacks were to be the prerogative of the city government. In practice, however, fiscal decisions had major impact on certain expenditure priorities that were inconsistent with the control board's best judgement. The management of the Health and Hospitals Corporation was one area where the control Board's review went beyond financing to address, implicitly at least, the policy decisions that were ostensibly the city's responsibility.[3]

The residual authority left intact and in city hands extended over intra-city reorganization, analysis, and reform. With financial matters subject to a Control Board veto, the city's major function was to look inward. Various study panels were created to discover what went wrong with the city's governmental processes. The findings of the various panels served as the raw material or analytical basis for the drastic reorganization of municipal service delivery.

B. TAX SYSTEM REFORMS

The major developments concerning the local revenue system during the fiscal crisis period have been:

(a) an increase in local revenue, at a rate less than the norm in recent years:

(b) a significant change in tax policy whereby the emphasis is on tax cuts, primarily in the business tax area.

Fiscal 1976 was the first year under the EFCB's supervision. During that year local revenue collections increased, although at an annual rate far less than the norm for recent years. In addition, 1976 marked the first year wherein property tax revenues were less than those realized in the previous fiscal year. For that tax and for the major revenue-producing non-property taxes, annual growth rates were markedly different from the averages over the last 16 years.

Total locally raised revenue for 1976 was $5.9 billion. This represented an increase over 1975 ($5.8 billion) local revenue of 2.6 percent. The fiscal 1976 rate of growth was the lowest for the 16-year period of analysis. Since 1967, locally raised revenues have increased by over 6 percent in each fiscal year except for fiscal 1974.

Property tax revenues for 1976 were $2,966 million. This figure represents a decrease in tax levy collections of 1 percent when compared to 1975 collections of $2,986 million.[4]

Although the rate of decrease and the absolute amount of the decline in revenue are relatively minor, the very existence of a revenue loss is significant. Property taxes, in the New York City context and in general, are considered the most stable source of locally raised revenues. In New York City, tax levy funds increased by an average annual rate of 7.9 percent over the 1961-75 period.

In the general fund (non-property taxes) category, revenue growth for the major taxes was generally lower than average rates of increase for the past 15 years. 1976 revenues from sales, personal income, and commercial rent occupancy taxes increased at a below-average rate. At the same time, revenues from the two largest business income taxes increased at an annual rate far above average. The general corporation tax and the financial corporation tax are the major revenue producers of the six business income taxes. (The others; the unincorporated business, transportation corporation, utility tax, and insurance corporation tax produce lesser amounts of revenue).

A change in the tax policy orientation of city officials has been the most significant development of the three-year transitional period. This shift of emphasis resulted in the placing of a high priority on lowering the local tax burden as a form of economic stimulus. This policy is almost the exact reverse of the emphasis during the last decade. During that period, the local tax burden increased steadily as new taxes were introduced as a means of generating additional revenue. That the beginning of the three-year retrenchment period coincides with the first reduction in New York City taxes in the 1961-1975 period is not coincidental. While the amount of reductions were relatively minor, the symbolic importance is nonetheless evident. Even more indicative of the new attitudes among city officials is the abundance of tax-reduction proposals being drafted by the local legislative and executive branches.

The apparent shift in emphasis from tax increase to tax reductions began approximately halfway through fiscal 1976. As late as November, 1975, the policy alternatives offered by the City administration were focussed on new tax measures as a revenue-generating strategy. And, an increase in local taxes was part of the fiscal package created to bolster New York's arguments in favor of the federal seasonal loan legislation.

The revenue proposals intended to show that intergovernmental assistance, if forthcoming, would be accompanied by an increased local tax effort. Although the proposed taxes would do further damage to New York's economic base, the state authorized the City to impose the tax measures. This evidence of local "belt tightening" was instrumental in securing the approval of the seasonal loan program.

Among the measures included in the 1975 budget-balancing proposals was the imposition of a new Estate tax. In addition, the legislature authorized increases in the rates for the

City's personal income, cigarette, sales, business income, and financial taxes. Thus these early moves to address the problems caused by the fiscal crisis were, in fact, a continuation of the very policies that had precipitated that crisis.

The granting of economically counter-productive tax rate increases was sharply criticized by the Commission on City Finances, among other public and private agencies. The criticisms of the tax increases led to the repeal of the estate tax authorization in spring, 1976, before the measure took effect.[5]

At about the same time, a proposal granting a local income tax credit for so-called "market makers" was approved by Albany and adopted by the city government. The credit was equal to the stock transfer taxes paid by the frequent and substantial securities transactions of the market makers. This legislation was passed in July, 1976.

The bond transfer tax proposal was enacted by the state legislature in 1975. Similar to the stock transfer tax, this levy was also repealed on the basis of arguments pointing out the decline in bond transactions that would result. Repeal of the authorization for this tax was accomplished in fiscal 1976.

The amount of foregone revenue resulting from the repeal of the three taxes discussed was approximately $100 million. While such a reduction in tax revenue represents less than one percent of total New York revenue, the real significance of the tax reduction is its symbolic value as an indication of a newly emerging tax policy. The beginning of a tax reduction policy had begun.

Although no additional cuts in local taxes have been enacted, the question now being debated by city policymakers is not <u>should</u> taxes be cut but <u>which</u> taxes should be cut and and by how much. There has been a drastic increase in the number of tax reduction proposals by a wide spectrum of the city/state political establishment. This suggests that the local tax burden for New York City will be lowered as a result of a rapidly forming consensus that such a reduction is necessary.

One question must be asked about the new tax policy or, indeed, for any of the new management policies adopted by the city since the fiscal crisis began. That question concerns the impetus behind the new policies. One possibility is that the new policies were forced upon the city by the control board and/or the federal government. Another possibility is that the new policies were the creation of the city administration. The answer to that question could have a serious impact on the development of the city once the three-year transition period is over. The city administration may have unwillingly adopted policies implicitly dictated by the financial decisions of the higher levels of government. If that is the case, then the end of the transition period in

June, 1978, will permit a shift to old policies. The city might also be in full support of the newly developed policies in taxes and other areas. If that is the case, then the trend of tax reductions may continue beyond the point when New York city's home rule powers have been reinstated.

C. DEBT MANAGEMENT REFORMS

The rearrangement of the city's debt management policies were probably a greater area of need than was the reform of the city's tax policies. The city's dependence upon excessively large amounts of debt obligations precipitated the fiscal crisis. Reentry into the national bond market is one goal of city policymakers and is also an explicit goal of the three-year transition plan.

A number of important developments have occurred concerning the reform of the city's borrowing powers. Among these developments has been:

a) the development of a plan for the reduction of the city's short-term debt,

b) the imposition of a moratorium on the repayment of outstanding city notes. State courts subsequently invalidated that moratorium.

c) the extension of short-term loans to the city via the Seasonal Financing Act of the federal government, and

d) the development of a schedule for the elimination of the city's capitalized expense budget items.

The creation of the Municipal Assistance Corporation (MAC) was presumed to be the only action necessary to facilitate a solution to the city's fiscal crisis. As the state was to find out shortly thereafter, New York City's problems were primarily, but not exclusively related to its inability to market debt obligations. This realization led to the creation of the Emergency Financial Control Board (EFCB) a few months after MAC's creation.

In spite of the corporation's inability to solve all of the city's problems, it has played a central role in the alleviation, if not solution, of New York City's problems. The creation of MAC was very important since that agency developed the first coherent scheme for the elimination of the short-term debt obligations of the city.

Prior to MAC's creation, the city had no real plan (or intention, some have charged) to reduce its outstanding short-term debt. That debt had increased to the point where short-term obligations represented over 30 percent of the city's total outstanding debt. The city's debt management policies consisted of periodically "rolling over" its short-term debts. New notes were issued to finance the redemption of old obligations.

The MAC short-term debt strategy called for the transformation of short-term notes into long-term bonds. Since the city was excluded from the bond markets, the obligations of the separately-financed Municipal Assistance Corporation were offered in exchange for the short-term city notes. This procedure would eliminate the need for the city to immediately and completely repay the principal of the matured short-term notes. Instead, the city (in the form of the MAC capital reserve fund) would have to pay only interest costs and a fraction of the outstanding principal.[6]

The success of the short-term/long-term bond swap was dependent upon the willingness of city note holders to trade in their city notes for MAC bonds. In order to make the swap more appealing to holders, the state legislature enacted a moratorium on the repayment of the city's short-term debts. The moratorium legislation was the second major development of the three-year transition period.

The moratorium was enacted in November, 1975. It imposed a three-year delay in the repayment of principal on the city's outstanding notes. The arrangement required the city to offer to exchange maturing notes for the long-term bonds of MAC. Those noteholders not accepting the MAC swap were to receive a unilaterally determined (by the same legislation) 6 percent interest payment on the notes in moratorium.

After the moratorium act was passed, the MAC immediately offered to exchange its long-term bonds for up to $1.6 billion of outstanding city notes. This policy, which combined the carrot (8 percent MAC bonds with more secure financing) with the stick (moratorium on principal and much less secure financing) was only partially successful. $458 million or slightly over 25 percent of the hoped for $1.6 billion in city notes were swapped.[7]

Then, the New York Court of appeals struck down the legislated note moratorium calling it unconstitutional. This was a serious setback for a number of reasons. First, the city, the Municipal Assistance Corporation, and the Emergency Financial Control Board had all supported the moratorium legislation. The legality of the moratorium had been upheld in two previous court tests. In both trials, the city and state argued that the moratorium was an indespensible part of the effort to avert technical default. Secondly, all the financial plans developed by the city assumed that the moratorium would be upheld. Therefore, no contingency plan was created in case the moratorium was not validated. The Emergency Financial Control Board had developed a reputation as a most conservative and unsympathetic oversight body for the city. Many city contracts and other financial commitments were vetoed by the Control Board because of a failure to develop contingency plans if the worst happened. However, in spite of their conservative orientation, the E.F.C.B. also had no contingency plan for use if the moratorium was overturned.

When the moratorium was judged to be unconstitutional, the decision stated that the matured notes would have to be redeemed but that the negotiated redemption program should not needlessly be disruptive of the well-being of New York

City residents.

The city indicated that the redemption of the notes in moratorium was an impossibility unless federal and/or state assistance was forthcoming. The state dismissed that possibility, pointing to its own financial difficulties and the proposed expenditure cuts in its own budget. The federal government rejected the proposal on policy grounds.

With default seemingly unavoidable, the city administration surprised the entire financial community by paying off the individual note holders from "cash on hand." This payment of almost $900 million confirmed many parties worst suspicions concerning the lack of credibility (or basic honesty) of statements by the city administration.

The city's mismanagement of its debt contraction policies were repeated in its debt expenditure policies. A major problem addressed during the transition period was the city's policy of using borrowed funds to finance part of its expense budget. The city agreed to a plan to be accomplished over a ten-year period terminating in 1985. The phase-out schedule was developed because of the difficulty (or impossibility) of abruptly removing the funding for almost $700 million in city expenses.[8]

The enactment of the seasonal loan program was another major development of the city's transitional period. That legislation allowed the New York government to acquire the short-term loans it needed to operate efficiently.

After initial reluctance on the part of the Ford administration and the Congress, the Federal government agreed to some participation in efforts to avert a formal default on the part of the city. The creation of MAC and the EFCB were in part intended to indicate that the state and local governments were doing all they could to solve the city's problems. Additional tax authorizations worth $500 million were passed as a further indication of local effort.

The federal government prepared its own analysis of the national impact on any New York City default. It was pointed out that average interest costs for municipal borrowing nationwide had increased substantially in response to the threat of a payment default by the city. Thus, an actual default of New York City bonds could be expected to have a substantial negative impact on the municipal bond market, and credit markets in general.

The seasonal financing legislation commits the Treasury Department to loan up to $2.3 billion to New York City annually. The interest rate for the loans was set at one percentage point higher than the Federal government's cost of borrowing at the time the loan was made.

SUMMARY

Chapter Three describes the three-year transitional period created by the city and state government. The effort to avert a "technical" default on New York City bonds was successful because of contributions by the city, state, and federal governments.

The federal governments involvement was primarily financial. The seasonal loan program provided the cash-flow regulating mechanism without which the City could not function. The state also provided financial assistance, but its more significant role as "fiscal watchdog" was exercised by the Emergency Financial Control Board. The board was created out of both fiscal and political necessity. Some form of oversight had to be engaged in by the state government. And a convenient "lightning rod" was needed to deflect criticism aimed at the administration in Albany. New York City's role in the transition program was limited to analysis and reorganization of local operations. The Commission on City Finance was one agency created to provide internal criticisms of local government.

In the tax area, a major development during the transition period was a sharp decline in the growth rate for local revenues. Another and much more important development was the shift to an emphasis on tax reductions. Previous administrations had increased the tax burden as part of the revenue generation strategy.

FOOTNOTES

1. The city government will argue for the extension of the program when it expires on June 30, 1978.

2. See the annual report of the Emergency Financial Control Board, 1976.

3. It was charged for example, that EFCB wouldn't approve the HHC budget until its executive officer was replaced.

4. See Table B-3.

5. See the Commission's interim report #3 on the Estate Tax.

6. The annual report of the Municipal Assistance Corporation (1976) describes bond swap procedure.

7. *Ibid.*

8. See Table I-5.

CHAPTER FOUR: POLICY ANALYSIS AND IMPLEMENTATION OF REFORMS

INTRODUCTION

Chapters One and Two of the thesis examined the development of the local revenue and debt structure. In Chapter One, the increasing use of short-term debt obligations and the use of borrowed funds for current operating expenditures is discussed. Chapter Two described how the city's tax structure was altered over the period of concern. Individuals and households paid a larger portion of total locally raised revenue as a result of the changes instituted. And, in general, the tax burden for all classes of tax payers increased substantially. (See Appendix sections A and B).

The first two chapters of the thesis describe the public policy decisions that influenced the shape of the revenue and debt systems. In both areas, the basic determinant of policy was the decision to increase local expenditures in response to a changing population and the changing service needs of that new population. An influx of poorer persons caused expenditures for welfare, Medicaid, daycare, and other social service needs to increase dramatically. This caused city administrators to develop policies whereby the maximum amount of revenue could be extracted from the local tax base.

The material contained in the first two chapters is mainly descriptive. It tells about the public finance policies adopted without explicitly characterizing the policies as positive or negative. While such a description is useful in and of itself, a complete analysis of the local finance structure must also relate the policy initiatives to the "real world" of residents, businesses, city workers, and politicians. What impact did the policy changes have, positively or negatively on various local interests and what part did these changes play in the "fiscal crisis?" The examination of these relationships begins with a discussion of the recommendations of the Commission on City Finances. The intent is to determine whether or not their recommendations were consistent with the problem areas identified in the analysis of the public finance structure. The specific recommendations in the revenue and debt policy areas are reviewed first. Then the six-point, "developmentalism" program is assessed. This is a group of recommendations that present the Commission's overall strategy for solving the fiscal crisis.

A. LOCAL REVENUE STRUCTURE

The local revenue structure grew in size due to tax rate increases and the introduction of new tax measures. The major use for the additional revenue was to finance the hiring of more city workers. In New York City, the outflow of private sector jobs has been and still is one of the major problems facing the local economy. An increase in government spending has had the effect of partially offsetting the loss in private employment opportunities. The increasing municipal payroll has helped those who receive jobs. However, the long-term effect has been to postpone the inevitable "day of reckoning" when the decline in the local tax base must be reflected in a decline in the local government sector.

The changing composition of the local revenue structure did not contribute to a more viable system of taxation. The major shift was an increasing utilization of non-property tax measures. As mentioned earlier, the non-property based forms of revenue are less stable sources of revenue. Thus, in 1966 for example, there was a decline in revenues from all the major general fund taxes. In the same year, however, property tax revenues increased when compared to 1965. In 1973-74, when the severe recession/depression occurred, New York City's economy was affected to a greater extent than would have been the case in a more property-oriented revenue system.

The shifting of a portion of the tax burden from the business community to individual residents was another negative development occurring within the period of analysis. The business community is of course, only a distributor of the tax burden to other portions of the economy. Taxes are a cost of doing business, and this cost is passed on to the consumers of each of the businesses products. Individuals on the other hand have no such option. By reducing the business sector's tax payments, the process by which the local tax burden is exported to non-local consumers is curtailed. This means that more of that local tax burden is confined to the local area.

The tax burden on individuals is the area in which local taxes are least competitive. While the business sector's local tax burden is heavy, the state's business taxes are more responsible for any tax-inspired relocation of businesses.

B. COMMISSION RECOMMENDATIONS-TAX POLICY

The Commissions recommendations concerning tax policy can be summarized as follows:

A. Property assessments should be equalized across residential/commercial/owner-occupied categories.

B. Rent control and rent stabilization should be phased out.

C. Corporate taxes should be cut by 50 percent over a five-year period; manufacturers' purchases of equipment should be exempt from sales taxes; and the commercial rent occupancy tax should be reduced by two-thirds.

D. The rates of taxation on the major personal taxes (sales, personal income) should not be increased as long as other localities in the SMSA have lower rates than New York's. Commuter taxes should be doubled.

The tax policy recommendations of the commission are clearly inconsistent with the data presented in Appendix B. It appears that a predilection for business tax reductions determined, a priori, the shape of the tax policy recommendations. The first recommendations ("A" and "B") present the property tax reduction proposals also included in the debt management area. While the effect of equalized assessments would be positive from the big business viewpoint, the negative impact on middle-income homeowners and small businesses is ignored. In addition, the Commission's proposals for equalized property tax assessments are in conflict with important political and economic realities that have in the past prevented reforms.

First, the Commission proposals do not adequately assess the effects of the proposed equalized assessments. The claim of tax relief for the "Business community" does not distinguish between big business versus small business; firms that own their real estate versus those that lease; space-intensive business versus those whose use little space. Within the undifferentiated "business community"; there are some firms who stand to gain from equalization and some who have a lot to lose. The Commission might have determined which businesses fall into which category before adopting such a position.

The political feasibility of the equalization proposal is doubtful. This is the second factor ignored by the Commission. In this instance, the democratic system is seen to be an obstacle to the Commission's plans. Given the numerical superiority of homeowners, it is highly unlikely that the elected governments in New York or Albany would support a policy that taxes General Motors and Archie Bunker at the same rate.

The analysis of the local revenue structure indicates that the personal tax burden has increased more than the business tax burden. A further personal tax increase (via the property tax) would be counter-productive. Such a shift would speed the out-migration of middle class individuals. Their tax contribution, purchasing power, and involvement in local affairs would be lost.

The recommendations of the Commission do not adequately state the case for possible reductions in personal tax measures. This, in spite of the fact that reductions in personal taxes would almsot immediately increase business transactions while reductions in business taxes only indirectly and over the long-run produce benefits for individuals. The one proposal concerning the taxes paid by individuals calls for the maintenance of present rates so long as neighboring localities have lower rates in effect. While seemingly a market-conscious recommendation, it is clear that a similar logic could apply to the business-tax burden as well.

The implicit message of the Commission is that whatever is good for business is good for New York City. This particular sentiment is a natural outgrowth of the Commission's business orientation, which is, in turn a product of the myth about "incompetent government/efficient private enterprise."

When the extent of the fiscal crisis became clear, there was much discussion of the "well known" incompetence of government in general and of local government in particular. There were calls for more "hard-nosed business-men" to take part in a reorganization of the government. This was followed by an influx of management consultants whose only qualifications were their successful administration of private corporations. Richard Shinn of Metropolitan Life became a management consultant, Leo Oberst of Bell Telephone was also loaned to the city by his firm. The same type of people were selected for the Temporary Commission. Robert Tishman and Lewis Rudin own two of the city's largest real estate management/construction firms. Bruce Llewellyn heads the nation's largest Black-owned supermarket chain. Given this information, the self-interest represented by the proposed policies is clear.

From the perspective of the Commission members, the recent history of the city has been marked by increasing obstacles to profitable business activity. These obstacles take the form of increased local taxes and cause profit maximizing investors to relocate in other areas. The resultant loss of investment and jobs (and the tax base these jobs represent) can be eliminated only if the city would cut expenditures, thereby permitting a cut in business taxes. Most of the Commission members came to the assignment holding these views. They did not have the objectivity necessary to weigh the relative merits of proposals that did not provide immediate relief (or the promise of relief) to the business sector, whose representatives they were. The "what's good for busines.." slogan is not an exageration, since that sentiment was accepted as true by the commission members.

C. THE LOCAL DEBT STRUCTURE

The debt structure of the city also shifted during the period of analysis. The increased use of short-term obligations and the "rollover" policy meant that what were described as short-term debts had been outstanding for more than the usual one year, that is, they were in fact long-term debts. This required changes in the volume and frequency of debt sales by the city. Where long-term bonds were sold once or twice yearly, the redemption schedules of "short-term notes required monthly sales; and the absence of any sinking fund or other debt-service mechanism for short-term notes caused increasing use of the "new debt for old" policy.

The problem with the city's debt management policies went beyond the amount of bonds sold. The improper uses of borrowed funds is another distinct problem, area. By financing operating expenditures with borrowed funds, the viability or marketability of New York City bonds was compromised. This was the immediate cause of the fiscal crisis.

D. COMMISSION RECOMMENDATIONS-DEBT POLICY

The Commission's recommendations concerning debt management policy can be summarized (see the appendix for the exact text) as follows:

A. Start reducing the city's outstanding debt by indexing new debt issues as a fraction of debt retirements in the same year.

B. Speed up the elimination of capitalized expense budget items by changing the present 10-year phaseout into a 6-8 year schedule.

C. Negotiate a "stretchout" of city (and MAC) bonds to facilitate lower annual debt-service payments.

D. The state should establish more effective and enforceable limits on the uses and amount of capital funds.

E. The federal government should extend the seasonal loan program beyond its present fiscal 1978 termination date.

The debt management recommendations are generally consistent with the problems covered in Appendix A. The recommendations basically call for a return to more orthodox uses of the debt-incurring power than the city has exhibited in the past. The use of borrowed funds for operating expenditures, and the massive size of the city's debt obligations are the two major problem areas. The proposed policies would effectively eliminate these abuses if implemented.

Close examination of the proposals indicates the emphasis on property tax reductions as a priority area for the Commission. Recommendations "A" and "B" are favored because of the decline in property taxes that would occur if these policies are implemented. Interestingly, these proposals are somewhat contradictory in that "A" calls for a speedy reduction in the total debt burden while "C" calls for a "stretch-out" of payments, which translates into a slower reduction in outstanding debt.

The recommendation for the faster elimination of capitalized expense budget items (proposal "D") is in reality a call for further budget cuts. Since Commission proposals argue against increased local revenue collections, no expense budget finding would be available to replace the capital funds. This would necessitate the elimination of programs presently funded through the capital budget.

Recommendations "D" and "E" call for actions on the part of the state and federal governments. The recreation of debt ceilings or limits is a good idea. But, the lesson of the past 16 years has been that any system created by a political body can be changed or ignored by that same body. That is, debt ceilings are only as rigid as is the commitment of the state legislature to abide by the established limits.

The extension of the seasonal loan program is probably the most pressing need. The city is still not in a position to market its own short-term obligations. Therefore, the cash-flow mechanism is still important.

The same pattern of subjectivity/self-interest is evident when examining the other Commission recommendations. The more general proposals suggest a grand strategy for handling the fiscal crisis.

The basic message of the final report suggests the implementation of a "developmental strategy" that would enlarge the city's economy. This strategy includes three major areas from which additional revenues may be generated and three major investment areas where the additional funds should be used.

The sources for additional revenue would be; "load shedding" of certain functions to the state or federal government, improved management resulting in the elimination of waste, further cuts in city services and personnel. The freed-up funds would be used for; reductions in outstanding debts, tax cuts to promote new investment, capital expenditures for infra-structure maintenance.

The major problem with the Commission's recommendations is a failure to set priorities concerning which of the six steps would be most important to take. The commission's refusal to set priorities is not so much the result of naivete as it is a political decision to ignore the difficulties, inconsistencies, and obstacles associated with their proposals. If the Commission placed a rank order on the six developmentalism strategies, and assigned a reasonable dollar value to each, it would almost immediately become obvious that only one or two of the proposals could be implemented at this time. The absence of any ranking suggests that all six strategies should be implemented simultaneously. For a number of reasons, that may not be possible.

Among the three revenue-generation strategies, for example, neither the Carter administration nor the Carey administration in Albany appear willing to assume the financing for specific "municipal overburden" services. President Carter has reneged on his campaign pledge to quickly move for federalization of localities' welfare costs. And, Governor Carey has sought substantial expenditure cuts in each state budget he has prepared.

Management improvement and additional cutbacks are two issues so closely related that they might easily have been included in one recommendation. Since the delivery of municipal services is a very labor-intensive undertaking, substantial savings can come about only through "increased productivity." This means that either the same number of workers will do more than before, or fewer workers will do the same amount of work that is presently done. In either case, agreements reached in labor negotiations have already committed 100 percent of any productivity savings to workers as substitutes for the COLAs (cost of living allowances) given up to avoid additional layoffs. This discussion is intended to suggest that additional or unallocated revenues may not be available for a period of time.

Of course, additional finances will be accepted from whatever source or sources. It is in the allocation of funds that the setting of priorities is required. Given the almost certainty of "scarce resources" which of the three investment strategies should be implemented first?

Reducing the city's outstanding debt would improve the chances for a successful sale of a New York City (as opposed to MAC) bond. Tax reductions might stimulate new investment. And infra-structure improvements would raise the quality of life, thereby making the city a more attractive place in which to work or reside.

Finally, there is the question of a balanced budget and how to implement such a budget for a number of years in succession. As part of the fiscal 1978 budget, the Mayor was required to submit projections of revenues and expenditures through fiscal 1981. These projections show substantial deficits occurring through 1981, at least. Even the "balanced" budget approved for 1978 is not "technically" balanced from an orthodox accounting perspective. Over $500 million in capital funds are being used in the expense budget. Over $150 million in non-recurring revenues are used to create the appearance of a balanced budget.

E. ISSUES OF PUBLIC POLICY

The question of a consistently balanced budget leads into a discussion of the public policy questions raised by the fiscal crisis and the response of government to that crisis. The rationale behind the substantial layoffs and cutbacks of 1975-76 was that a balanced budget had to be developed. If such a budget was not attained (and the projected deficits show that this is the case), what was the real reason for the fiscal reconstruction efforts undertaken?

Among the many important policy questions raised by the fiscal crisis, at least three seem of primary concern. First, what is the proper municipal response to declining revenues at a time when expenditure needs are rising? Second, what was the role of the financial sector in the New York City fiscal crisis and in the life of municipalities in general? Did their activities adequately reflect the public interest as well as self-interest? Finally, does the creation of EFCB-type institutions threaten the maintenance of democratic (that is, elected) government in New York City?

1. THE FISCAL CRISIS

Most analyses of older urban center's economies have indicated the approach of a point at which projected expenditure needs would surpass the amount of available revenues. The 1966 Temporary Commission on New York City Finances predicted such a shortfall would occur during the mid-1970s, for example. The question then arises as to what is the proper response to a revenue shortfall, once it is a reality? Recent city administrations adopted a policy whereby gimmicks and conveniently imprecise accounting methods hid the existence of a budget deficit. This strategy avoided the politically unpopular process of minor layoffs and cuts as finances dictated. However, this merely postponed the retrenchment effort, thereby necessitating the mass layoffs of 1975-76.

It has been argued that gradual cutbacks in services would have been preferable. On the other hand, it could also be argued that greater benefits to the citizenry were realized by delaying the "day of reckoning" as long as possible. Interested investigators might attempt to determine the effects of "pro-rating" the major cutbacks of 1975-77 across the 1961-1977 period of analysis. This would simulate the "gradual budget reduction" alternative rejected by New York City governments. By projecting a local tax reduction equal to the annual "budget cutback", and given present information on individual and business responses to tax rate changes, a rough comparison of the two strategies might be developed.

As discussed in the chapter on debt management policy, the crisis event that served to mark the "start" of the fiscal crisis was the bond market's rejection of New York City bonds. This was the result of the New York Clearinghouse banks refusal to act in its usual role as underwriter of New York's municipal bonds. Two questions arise from the financial sectors actions in the crisis. One concerns their activities associated with this particular fiscal crisis, the other examines the role of the municipal bond banker in general.

Recent SEC investigations have charged that many of the clearinghouse banks behaved unethically by attempting to "unload" their own holdings of city debt while at the same time not disclosing their knowledge that repayment was not certain. The banks' unloading of their large city debt holdings occurred at the same time as the city was trying to market new debt instruments. This increased the supply of city note offerings to an amount far in excess of the demand for those notes. Not surprisingly, prices dropped and record interest rates were needed to attract investors to the new short-term notes. These actions suggest that the banks were not <u>reacting</u> to the unmarketability of notes. Instead they <u>caused</u> the unmarketability of those notes by attempting to "dump" their city debt holdings.

The banks activities vis-a-vis the bond boycott were based upon a recognition of their indispensible role as the city's creditors. New York City, any city, literally cannot function without access to credit. The financial community has always been politically involved, supporting candidates whose policies they favor. However, the use of the bond boycott weapon goes beyond political advocacy. It indicates a more coercive attempt to influence ("dictate", some would say) city policy. Their program depends less on political persuasion then on the banks ability to shut off the city's credit if their fiscal retrenchment demands are not met.

Clearly the financial/business community prefers to maintain a low-profile political role to the extent possible. One area for further investigation would be to look at what constellation of events and circumstances motivated the financial community to-however reluctantly-put forth such a "robber baron" or "public be damned" public attitude.

The activities of the banks and the creation of the EFCB raise another important issue, that of the effects these institutions have on the functioning of a democratically elected local government. Does the fiscal crisis point out the potential for eliminating fundamental democratic institutions and principles in an attempt to restore "business confidence" in the city? The establishment of EFCB implies, among other things, that a democratic government is a luxury that cannot be afforded during times of fiscal crisis. According to this view, city government is like open admissions programs or low-cost day-care services -- tolerable during times of fiscal expansion but too expensive and inefficient when revenues are low.

A case can be made for the EFCB's temporary control during fiscal 1975-78, but that case rests on proven irregularities and illegalities (it is illegal for the city to have a budget deficit) associated with a finite number of recent city administrations. Wholesale indictment of the democratic system itself is not justified, but one proposal of the Clearinghouse banks called for the creation of an EFCB-type institution to control city finances for the next twenty years. The control body would be made up of persons well-respected by the business/financial community (that is, bankers, businesspeople and a minority of politicians--if any). The proposed body would exercise veto powers over fiscal agreements entered into by the city government.

Although the negative public response to the suggestion caused the Governor to reject the proposal, the issue will be discussed again in fall/winter 1977, when the city seeks to sell its own bonds. The twenty-year proposal raises the EFCB strategy to its logical next step. The "logic" flows from the notion that politicians are inherently incompetent and/or corrupt, a concept nurtured by events like Watergate, the New York State Urban Development Corporation bankruptcy, and the recent felony conviction of Maryland Governor Marvin Mandel, just to cite a few examples.

2. THE GOVERNMENTAL CRISIS

In addition to those policy issues raised by the fiscal crisis itself, another distinct set of issues was generated by the governmental response to that crisis. First there is the inadequate assistance offered by the higher levels of government to New York City. This question is related to a second issue, that of the erroneous suggestion that a bankrupt New York would have little or no impact on the economy of the state and nation. The third and final issue to be discussed concerns "John Q. Public's" ignorance of basic public finance concepts. This helps explain the absence of any historical perspective from which to evaluate the present fiscal/political crisis.

The local government's response to the fiscal crisis has been described earlier. Another issue concerns the federal/state response, once the crisis became impossible to ignore. Both entities were reluctant participants in efforts to prevent a default by New York City, even though their own policies played a significant role in the creation of the crisis situation. Federal Housing and Transportation policy, for example encouraged surburban development. The exodus by the white middle class resulted in a smaller tax base for New York City. Similarly, the New York State legislature forced the city to carry the heaviest welfare burden borne by any locality in the nation. In other words, federal and state policies were factors contributing to urban problems in general and New York's fiscal crisis in particular. Unfortunately, state/federal involvement in the crisis has been more concerned with identifying and correcting local causes of the problem. Insufficient efforts have been made to redress those state-controlled or federally-controlled contributors to the city's problems. The Albany legislature, for example has not moved to assume the financing of county-administrated services (courts and probation, etc.) it provides elsewhere in the state. The federal government has not "moved quickly" to assume all local governments' welfare costs as was promised during the Presidential campaign.

Unfortunately for the cause of developing a national and rational urban policy, the serious structural economic problems of New York were compounded by inefficiency and political patronage in city government. Had these factors not been present, the fiscal crisis would have put the spotlight on public finance issues of national concern. Instead, the public debate focused on less important questions, and too much on the supposed dishonesty of politicians as the cause of the crisis.

Part and parcel of the inadequate governmental response, was the notion originally put forth that the city's problems were its own problems--that a bankrupt New York would have little or no impact on the state or nation. In fact any such bankruptcy would have immediate, substantial, and adverse effects on the national and international economy. The Ford Administration put forth this view originally, to the delight of the New York City hate/envy crowd in Congress. Luckily, wiser judgements eventually prevailed and the seasonal loan package was adopted. What is significant--and dangerous--is the administration's and Congress' ignorance of the linkages between the national economy and the local economy of its "primate" city (to borrow the terminology of the LDC's). An even worse possibility would be that the government knew about the importance of "bailing out" the city but for political or other reasons decided to ignore the necessity.

3. THE "FISCAL ILLITERACY" CRISIS

Perhaps the single factor most responsible for the city's fiscal problems was the absence of any "fiscal common sense" by the public. The availability of important background knowledge would have enabled the public to more intelligently analyze all of the policy questions associated with the fiscal crisis.

One of the concepts basic to economics is the notion that information concerning available alternatives is necessary in order to maximize one's effectiveness. Sadly, information was in short supply during the fiscal crisis. On one hand, we have the failure to properly disclose the state of the city's finances. This led to the crisis situation. Then there was the lack of any public education concerning the self-interest associated with the political postures of the unions, banks, etc.

The Securities and Exchange Commission report on the City's financial management has been mentioned earlier. It criticized recent administrations for inadequate disclosures of the approaching possibility of default. The strategy of inadequate (ambiguous, contradictory, misleading) disclosure had been firmly entrenched for years. Indeed, the city's deficit finance policy would have been impossible without some sort of cover-up. The success of this process was based on the public's acceptence of the idea that a municipal budget is a document incomprehensible to the average person. By leaving the budget to the experts (to those who "know the buck"), the residents accepted, or more correctly did not recognize, an inadequate budget statement from the local government. The vicissitudes of the city's budgetary (political) process, for example, consistently required the Mayor to at the same time underestimate revenues to establish a labor negotiation posture and to overestimate revenues to establish a bond selling posture. Such contradictions were lost on the fiscally-ignorant New York City electorate.

Given this pattern of deceit, it was predictable that, when the bond boycott was instituted and drastic cutbacks were required, everyone accepted the city's crisis statements as just the annual jockeying for a strong negotiating position.

The other side of the disclosure question concerns the failure of centers of influence other than the incumbent administration-opposition politicians, the media, academia, etc., to provide the historical perspective so necessary for an understanding of the fiscal crisis.

The saying about "those ignorant of history" being doomed to repeat it is certainly germane to the discussion of the New York fiscal crisis. For, in addition to the public's ignorance about fiscal affairs, there is a similar ignorance (or more correctly short memory) concerning the fiscal crises in New York's past. The public's tolerance of the EFCB and other oversight bodies is based on the perception that board members are acting in a non-political, "good government" capacity. Adequate information about prior fiscal difficulties would help to place the present crisis in its proper perspective. It would also help to point out the political self-interest that determined the shape of the fiscal retrenchment program.

The fiscal crisis that occurred during the "Boss Tweed" era is an excellent example of this phenomenon. That crisis involved all of the factors (and actors) that make up the present day fiscal crisis. In the 1870's version of the crisis, an increase in the city's low-income population caused social service expenditures to rise. Given the political costs associated with tax increases, the administration decided to substantially increase bond sales and to convert short-term notes into long-term debt. This meant that annual debt service payments increased, requiring a corresponding increase in property tax rates.

Eventually, the tax payers, (mainly real estate interests owning taxable property), and the New York City banks formed a coalition that forced the City to make deep cuts in expenditures. The major tool used to force a retrenchment program on an unwilling city government was (what else?) the bond boycott threat. Later, after criticizing the management of city affairs, these two interests ran a successful candidate for Mayor. The candidate's platform was based on "the inefficiency and corruption" of political leaders.

What is of significance--in addition to the deja-vu reaction to the description of the crisis--is the enduring or repetitive nature of the strategies, group interests, and procedures by which a fiscal crisis is created and eliminated. The actors in a crisis situation, whether in 1871 or 1975 include the lower-income class which wants but cannot pay for municipal services. There is the tax-paying group whose major interest is in lowering taxes whenever and however possible. There are the municipal lenders, the banks who provide the credit necessary for efficient governmental operation. And finally there is a survival-oriented political leadership in office.

The lower-income group's political strategy was to support politicians who offered the greatest amount of jobs and services. The property-tax payers, on the other hand supported candidates holding a conservative, that is, low-spending philosophy. The bankers profited handsomely from increased sales of municipal bonds, but then abruptly threatened a bond boycott when they felt that city expenditures were getting out of hand.

When making a comparison between the 1871 and 1975 fiscal crises, very little appears to have changed. Unfortunately, the forgetful public cannot recognize the apolitical, good government arguments of the banks as the standard political rhetoric of that group. Far from being "apolitical", the fiscal crisis has helped to replace one set of political priorities with another. Significantly, while the spend-less political philosophy was consistently rejected by the voters prior to the crisis, after the trauma of mass layoffs and service cutbacks, public acceptance of conservative policies has increased.

The information issue may be the most important of the public policy issues discussed in this thesis. Unless a new appraisal of what types of fiscal information can be comprehended by the public is developed, and unless the media or others accept their responsibility to provide more information, the cycle of local inflation, and coerced retrenchment will continue.

APPENDIX A: THE LOCAL DEBT STRUCTURE

This appendix describes the debt obligations used by New York City. Long-term debt is contracted using serial bonds or corporate stock. Short-term debt is contracted by a number of anticipation notes, (the bond anticipation note, etc.).

The appendix explains each debt instrument and then presents a time-series analysis of the overall debt structure. The contribution of each debt instrument to the city's total outstanding debt is described. And the shifting composition of the city debt burden is traced over the 15-year period of concern.

A. LONG-TERM DEBT

The total funded debt of New York City is composed of two types of general obligation bonds. One is called the city's Corporate Stock. The interest on these obligations is paid over the life of the bond, but the principal is refunded in a lump sum upon the maturity of the debt instrument. The city sinking funds are accounts established to accumulate the lump sum payments needed. Annual contributions to the sinking fund are held until the obligations are redeemed.[1]

Presently the city has four sinking fund accounts. These are the Rapid Transit Sinking Fund, the Transit Unification Sinking Fund, the Water Sinking Fund, and the so-called New York City Sinking Fund.

The other long-term debt instruments issued by the city are called serial bonds. These debts are different from the corporate stock in that the principal amount is redeemed gradually over the life of the instrument instead of in a lump payment. Each payment to serial bond holders includes earned interest and a partial amortization of the principal loaned. The serial bonds issued by the city have staggered maturation dates. That portion of the series with the earliest maturation date, will have a correspondingly lower revenue yield than would the bonds with later dates of maturity. The earlier debts will be retired months or years before those at the end of the series. A small portion of the city's serial bonds are redeemable from the assessment funds collected along with property taxes. The overwhelming number, however, are redeemable from the debt-service payments included as part of the annual expense budget. The corporate stock and serial bonds together constitute what is called the "total funded debt" of New York City.

The funded debt of the city is the "general obligation" of the government and people. The city pledges its full faith, credit, and taxing power to insure the timely repayment of such debt. The city is thus legally, if not morally, committed to repayment of general obligations. All of the city's revenue production capacity must be used to repay such obligations if necessary. In a quite literal, legal sense bonded-debt obligations are in front of such lesser obligations as contracts with city employees, municipal service delivery, or social welfare expenditures.

The size of the city's long-term debt grew much less rapidly than did the amount of short-term debt outstanding over the 16-year period of analysis. During that period, the funded debt became a smaller and smaller portion of the city's outstanding debt. At the same time, of course, the portion of total debt outstanding represented by short-term notes grew significantly. Between 1961 and 1969, the city's long-term debt increased by 21.7 percent.[2] This was far less than the increase in short-term debt, which totalled 744 percent over the same period.

In the 1970's the rate of growth for outstanding long-term debt increased slightly. The rate was, however, nowhere near equal to the growth rate for short-term debt. Between fiscal 1970 and 1975, the amount of long-term debt increased by 141.8 percent. This increase, occurring over a five-year period, was seven times the overall growth in long-term debt during the entire decade of the sixties but was still much less than the 352.4 percent increase in the size of the short-term debt.

The clearest evidence of the changing structure of the city's debt obligations can be seen in the declining share of total debt represented by long-term bonds. In fiscal 1961, long-term debt accounted for over 96 percent of the city's total outstanding debt. By 1967, the share of total debt had been reduced to 89 percent. In 1970, three years later, long-term debt accounted for 80 percent of outstanding obligations. The same pattern continued through the 1970's. By fiscal 1975, long-term debt was only 60 percent of the city's total debt obligations. The increases in the city's short-term debt obligations caused the decline in the long-term bond's share of total outstanding debt.

B. SHORT-TERM DEBT

In addition to the long-term debt commitments issued by the city, a substantial amount of short-term borrowing is necessary for the efficient operation of the local government. The use of short-term debt is necessary in order to facilitate the uninterrupted delivery of municipal services pending the receipt of anticipated government revenues. Generally, the city's revenues are collected annually (the personal income tax, for example) or quarterly (as is the case with the local property tax.) The city borrows during the early part of the fiscal year when a smaller amount of total revenues are available. Then, as tax receipts are completed later in the year, the short-term debts are retired.

The short "term" of the notes refers to the fact that such obligations are to be redeemed within the same fiscal year in which they are contracted. The notes are different from municipal bonds because of their short life and also in terms of their proper use by localities. Short-term notes are intended to be used for current operating expenses, while municipal bonds should properly be used for the construction or rehabilitation of public facilities.

The city uses a number of short-term borrowing instruments for various purposes. These include Budget Notes, Tax Anticipation Notes, and Revenue Anticipation Notes. These notes are issued for receivable revenues or for revenue short-falls. Additional short-term borrowing takes the form of Bond Anticipation Notes, Capital Notes, and Urban Renewal Notes. These instruments are used to finance capital projects.

1. TAX ANTICIPATION NOTES

Tax anticipation notes are issued against the receipt of tax levy (property tax) funds. Section 2400 of the local finance law, authorizes such borrowing. The notes are callable, which means they may be redeemed prior to maturity, thereby allowing a savings in interest costs.[3] While the usual life of a tax anticipation note is one year, the renewal of such notes is permitted. This arrangement effectively allows the notes to remain out-standing for a maximum of five years.

The growth pattern for the Tax Anticipation Notes (TAN) is similar to that of the property tax, the revenue source against which the TANs are issued. The decline in the property tax's share of local revenue is paralleled by the decline of TANs as a portion of the city's short-term debt. For the TAN, as with most other city finance instruments, the time series analysis indicates fairly substantial growth in outstanding commitments occurring at the same time as the overall significance (percentage contribution) of the instrument is declining.

The amount of TANs issued in any fiscal year is a function of the uncollected property tax levy for that year. Thus, the greater the percentage of the total tax levy that is collected, the less need there is for Tax Anticipation Notes. The amount of TANs outstanding doubled over the 1961-1965 period, growing from $42.9 million to $88.8 million. The outstanding amount almost doubled again between fiscal 1965 and 1970, growing from $88.8 million to $170 million. And between 1970 and 1975 the outstanding amount more than doubled, this time, increasing by $210 million to $300 million dollars overall.

As a portion of the city's total short-term debt, the TAN accounted for over 40 percent in 1961, but had declined to less than 10 percent in fiscal 1975. The 1963 fiscal year was the locus of a great portion of the overall decline in the TAN's share of short-term debt.

In the preceeding year, the instrument accounted for 40.6 percent of such debt, but in 1963 the debt share had dropped to only 27.3 percent (see Table A-1).

2. REVENUE ANTICIPATION NOTES

Revenue anticipation notes (RANs) are issued against expected receipts of inter-governmental aid or other non-property tax revenues. The issuance of such obligations is authorized by the local finance law, section 25.00. Prior to 1971, revenue anticipation notes were required to be issued against a specific category of aid, as listed in the city's revenue budget. Subsequent to July 1, 1971 these notes were allowed to be issued against the overall federal and state aid total.[4] As is the case with the tax anticipation notes, the usual life of revenue notes is one year. Renewals are allowed for two years thereafter. The rapid increase in the use of RANs caused the amount of notes outstanding to increase by 6400 percent between 1964 and 1975 (see Table A-2). During the same 1964-1975 period, total short-term debt had increased by a comparatively small 1400 percent.

The Revenue Anticipation Note began to account for an increasing portion of total short-term debt. This occurred simultaneously with the growth in the absolute amount of notes outstanding. During the 1960's, the RANs were second in magnitude to the TANs as a source of short-term debt for expenditure purposes. Beginning in 1970 however, RANs became the largest component of the city's short-term debt.

The major shift in the RANs percentage share of short-term debt occurred in fiscal 1970. During that year the amount of outstanding RANs increased by over 400 percent. The instruments share of total short-term debt rose from 172. percent in fiscal 1969 to 41.7 percent in 1970. At this time RANs became the largest single source of short-term borrowing for operating purposes.

During the 1970's RANs have consistently accounted for over 40 percent of the city's short-term debt. From fiscal 1970-1974, the RANs debt share ranged from 41-47 percent of revenue. In fiscal 1974 and 1975 the correspon-ding figures surpassed 50 percent (52.6 and 56.4 percent respectively.)

3. BUDGET NOTES

Budget notes are the third type of short-term debt used to finance current operating expenses. Section 29.00 of the local finance law authorizes the issuance of these obligations. The tax and revenue anticipation notes are issued against revenues listed in the annual budget. The budget note, however, is intended to finance revenue shortfalls. The shortfalls or deficits result from unanticipated expenditures not listed in the annual budget.

Budget notes are supposed to be redeemed by an expense budget appropriation in the year following their issue. In the event that the subsequent year's budget has already been approved, they may be redeemed in the second year after issue.[5]

The budget note was the only short-term debt instrument that the City completely redeemed in a number of fiscal years. The City retired all of these notes in fiscal 1967 and in fiscal 1975, for example, and in 1969 and 1970 the budget note was not used at all by City policymakers.

The occasional use pattern for budget notes contributed to the large annual increases in budget notes outstanding. The City would issue large amounts of these obligations for a few years in succession, then retire the total amount outstanding. Thus in fiscal years 1962-65, the amount of budget notes outstanding increased by 88.7 percent (1962), 34.0 percent (1963), 29.7 percent (1964), and 56.0 percent (1965). These increases raised the amount of notes in circulation from $10 million in 1962 to over $68 million in fiscal 1965. Following the expanded use of the budget note, the City retired all such instruments over the next two fiscal years. In 1966 the amount of notes outstanding was lowered by over two-thirds (see Table A-2). The remaining budget notes were all redeemed in fiscal 1967, leaving no outstanding obligations of this type. The same pattern occurred in the seventies when the amount of notes outstanding increased by 495 percent in fiscal 1972. The following year the City retired one-third of the budget notes. In fiscal 1975 all $308.3 million of budget notes were redeemed; therefore, the City had none of the obligations outstanding at the start of the crisis period.

4. OTHER SHORT-TERM OBLIGATIONS

In addition to these cash-flow debt instruments, the City utilizes other forms of short-term borrowing to finance some capital expenditures. Capital notes, Bond Anticipation Notes, and Urban Renewal Notes are used for this purpose.

The issuance of Capital Notes is authorized by Section 28.00 of the local finance law. They can be issued to finance activities that are properly fundable by serial bonds.[6] This, in effect, means that the instrument may be used for capital expenditures. The notes are allowed a maximum life of two years subsequent to the year of issue, for a total of three fiscal years. In cases where the notes are used as the initial financing of a major capital project, the amount of the capital note must be credited against the overall debt limit (on the long-term bonds sold) for the particular project.

Bond anticipation notes are another form of short-term capital financing. Section 23.00 of the local finance law authorizes the use of these notes. They are issued in anticipation of long-term bond authorizations, and the notes are redeemed from the proceeds of bond sales. Funds acquired through bond anticipation note sales must be used for the same purpose as are the long-term bonds used to retire the notes.[7]

Urban renewal notes are authorized by Section 25.00 of the local finance law. The notes are issued against the proceeds of specific urban renewal projects. They are redeemed from proceeds of any real property sale associated with the project or from the federal or state contribution to the urban renewal effort.[8]

The primary focus of this section has been on the short-term debt instruments used to finance recurring operating expenses, that is, TANs, RANs, and Budget Notes. Misuse of these debt instruments has been identified as a cause of the fiscal crisis.[9] In spite of this focus, any discussion of the city's short-term borrowing policies would be incomplete without some reference to the city's Bond Anticipation Note.

Unlike the other short-term notes described, the Bond Anticipation Note (BAN) is issued to finance capital, as opposed to operating, expenditures. It has consistenly been a major contributor to the City's outstanding short-term debt.

The growth pattern for the BAN is similar to those of the major city revenue sources. There was a substantial increase in the number of BANs outstanding during the period of analysis, but the rate of growth was still lower than that of overall short-term debt and of the RAN in particular. Thus, the BANs' share of total short-term debt gradually declined.

The total amount of BANs outstanding increased by a factor greater than 26 (overall increase of 2,624.9%). During the 1961-1975 period of analysis, the amount grew from $52.2 million to $1.37 billion. As a portion of short-term debt, the BAN accounted for over 40 percent of total obligations outstanding during the entire decade of the sixties. BANs outstanding increased by 15.6 percent in fiscal 1970, as compared to a 416.7 percent increase for RANs. It was in this year that outstanding RANs surpassed the amount of BANs in circulation, becoming the largest component of the city's short-term debt. In the previous year (1969) outstanding BANs were worth $404.6 million. RANs were worth only $128 million, over $200 million less. In fiscal 1970, however, outstanding BANs amounted to $467.6 million, while RANs had grown to $536 million.

C. SUMMARY

Appendix A examines the changing size and composition of the local debt structure. During the period of analysis, the most significant change in that structure has been the tremendous growth in the use of short-term debt obligations.

The major impact of the changed debt structure is two-fold; the increase in the overall debt load meant that a corresponding increase in debt-service payments was required. More importantly the increasing use of short-term notes caused the City's temporary borrowing to take on many characteristics of long-term debt, i.e., the need to redeem such notes through sinking fund appropriations or other mechanisms. Short-term notes in most cases do not require debt service appropriations, since they are presumably borrowed against specific revenue sources. As the short-term debt of the city increased, even the most optimistic projections of receiveable revenues showed a deficit.

FOOTNOTES: APPENDIX A

1. Gordon L. Calvert, Fundamentals of Municipal Bonds (Baltimore: French Bray Printing Co.), p. 168.

2. The time series analysis of the Local Revenue Structure is based on data in The Comptrollers Annual Report.

3. City of New York, Annual Report of the Comptroller (New York: 1972-1973), 422.

4. Ibid., p. 440.

5. Ibid., p. 428.

6. Ibid.

7. Ibid.

8. Ibid.

9. See the discussion of debt management policies in chapter two.

APPENDIX B: THE LOCAL REVENUE STRUCTURE, 1961-1975

This appendix examines the local revenue structure. Following the same procedure as in Appendix A, a time-series analysis of the local tax system is presented. The increasing size of the tax structure and the change in the composition of that system is assessed.[1] The appendix first looks at the relationship between the local and non-local portions of the total revenue budget. Then the analysis of the local structure begins. The major tax measures are listed along with a description of the coverage for each tax and the present rates of taxation. The local revenue structure is then divided into three categories: Personal taxes, which are paid by individuals and households, business taxes, those taxes paid by the business sector, and, property taxes, paid by both residential and commercial landowners.

The analysis of the New York City revenue structure begins with a look at that overall structure in fiscal 1976. A look at the 1976 revenue totals shows the City's tax system as it was structured at the start of the fiscal crisis. The discussion of the 1976 revenue structure also shows the portion of city revenues contributed by all levels of government. The analysis proceeds by dividing each level of the revenue structure into its component parts. Throughout this appendix, the intent is to examine the changing size and composition of the local revenue structure.

This analysis revolves around two factors that have interacted to create the tax system now in effect: (1) the absolute growth rates for the various components of the local revenue system and (2) the shifting contribution of these components to the total and local revenue structure. From the perspective of the local revenue structure, for example, the major development during the 16-year period of analysis has been the growth in local revenue collections. However, while locally raised revenues have increased substantially, intergovernmental aid has increased at an even faster pace. This has resulted in local revenue growth rates that are lower than the growth rate for the total revenue system (local and intergovernmental funds).

The changes in the composition of the local revenue structure is another area of concern. In the analysis of growth rates, the changing size of the city's revenue budget is examined. In the analysis of compositional changes, the shifting contribution of various classes of taxpayers to the local revenue "pie" is assessed. The introduction of the personal income tax, for example, represented a policy decision to increase the portion of local revenues contributed by individuals and households. Similarly, the introduction of the commercial rent occupancy tax had the effect of increasing the tax burden on those businesses that lease space relative to those firms that own real property.

Much of the public debate surrounding the New York City crisis focuses on such issues as the perceived increase in the tax rates, and the growing share of local taxes paid by the business community, or by individual residents. Careful analysis of the local revenue structure shows that not all of the perceived trends in the local revenue system in fact exist. This in turn, might suggest that some city tax policy initiatives may be designed to solve problems that do not exist.

A. REVENUE BUDGET, 1976

Total revenue from all sources was $11.4 billion for the year 1976, as shown in Table B-1. This aggregate amount included $2.7 billion of state assistance from all categories and another $2.6 billion in federal intergovernmental aid. These figures accounted for 24 percent and 23 percent of total New York City funds respectively.

The $5.9 billion raised from local revenue sources was 52 percent of total revenue for the year. Within the locally raised revenue category, tax levy (property tax) funds of $2.97 billion and general fund revenues (non-property taxes) of $2.98 billion were almost equal, with each category accounting for 50 percent of local revenue or 26 percent of total city funds.

The City's General Fund is the account into which all non-property tax revenues are deposited. It includes the major personal taxes, the city's business taxes, special sales/use or excise taxes, and all other city revenue sources.

The major personal taxes are the retail sales tax and the personal income/non-residents earnings taxes. In fiscal 1976, these two categories represented 32 percent of general fund revenue and approximately 8 percent of total city revenues. Personal income tax collections were $527 million or 17 percent of general fund revenues. Sales tax receipts (as allocated to New York's revenue budget) were $445 million or 14 percent of general fund revenues. (As part of the financing for the Municipal Assistance Corporation, (MAC), the corporation has first claim on City sales tax revenues. After the subtraction of MAC debt service and operating expenses, remaining sales tax receipts are released to the City. Sales tax collections were $825 million. The $445 million sales tax figure is the residual after the subtraction of almost $380 million for the so-called Municipal Assistance Tax Fund.) The various business income taxes in aggregate contributed 26 percent of general fund revenues or approximately 7 percent of total city revenue for the fiscal year.

The general corporation tax was 53 percent of total business income taxes and 7 percent of local revenue collections. The tax on financial corporations was next in magnitude. That levy accounted for one-fourth of the total business income taxes. Receipts from the financial tax were slightly over $200 million in 1976. Utility tax collections were 12.0 percent of business income taxes collected and 1.6 percent of total locally raised revenue in 1976. The insurance corporation tax and the transportation corporation tax are the remaining corporate income taxes. These two levies provide smaller portions of local revenue.

The selective sales and use taxes are a group of taxes that are more narrowly based than is the virtually all-inclusive 8 percent city/state retail sales tax. The stock transfer tax is the largest revenue producer among the selective sales tax category, and is one of the major revenue sources in the city. Stock transfer tax receipts of $269 million accounted for 60 percent of the revenue in the selective sales tax groups. In addition, a number of automobile-related taxes (including gasoline taxes, registration fees, commercial motor vehicle tax and other) generate 17 percent of selective sales tax revenues (79.5 million). Another group of taxes directed towards consumers of cigarettes generates $50 million annually.

The balance of local revenue is generated by water charges of over $200 million (or 3.7 percent of total revenue), various fares, user charges, license fees (1.8 percent), tolls and other miscellaneous revenue sources

(2.2 percent). The "other" revenue cateogry in aggregate accounts for 6.2 percent of city raised funds.

B. LOCAL CONTRIBUTION TO TOTAL CITY REVENUE

The most significant feature of the New York City revenue system has been the decreasing share of revenues raised by the local government. In a section of the Commission's final report (and in the Interim Report devoted entirely to intergovernmental aid), the increasing amounts of state and federal assistance are analyzed. This external aid increased in absolute terms and also in terms of its contribution to the total amount of revenues available for New York City. An increase in Federal/State aid meant that a smaller and smaller portion of total revenue was locally raised.

Table B-2 shows that in the sixteen-year period between 1961 and 1976, the portion of city revenue raised locally decreased from 77 percent to 52 percent. The 1976 figure (52 percent of total revenue) was a shift from the preceeding year when for the first time locally raised revenue was less than 50 percent of the total revenue available to the City. 1975 was the last fiscal year before the imposition of financial controls on the City and its finances. The upward shift in the City's contribution to total revenues might therefore reflect the impact of external controls. Two other factors may also account for the increasing local contribution to total revenues when comparing fiscal 1975 and 1976. One factor is a sharp decrease in state assistance and the other is a decrease in total revenues during the fiscal 1975-76 period.

State assistance payments to New York City were decreased from $3.7 billion in 1975 to $2.7 billion in 1976. The state aid represented 31.1 percent of total city revenue in 1976. The 1976 fiscal year was also the only year during the 1961-76 period when total revenues available to the city were less than those available in the preceeding fiscal year. Total revenue was equal to $12 billion in fiscal 1975 and had dropped to $11.4 billion in 1976. The combination of decreased state aid, a drop in total revenues and the presence of the financial control board, increased the City's share of its total revenues to a level in excess of the 50 percent margin. This is significant because the 50 percent level of funding is often seen as a "tipping point" signalling the continued viability of a local government. If a municipal entity receives the majority of its funding from outside sources, the integrity and therefore the viability of that governmental entity is questioned.

C. PROPERTY-BASED AND NON-PROPERTY TAXES

The local revenues of New York City are generated by the tax levy (property tax) and the general fund (non-property taxes). As is the case with local revenues in general, both the property tax and non-property taxes are declining as portions of total revenue during the 1961-76 period.

The local property tax accounted for 41.9 percent of total city revenue in fiscal 1961. In 1976, the property tax accounted for 26.0 percent of local revenue.[2] This decline in the property tax's share of revenues occurred while property taxes receipts were rising annually, if at an unsteady rate of growth. In general, property tax revenues are more stable from year to year than are the proceeds from non-property tax sources.

The annual rate of growth in external assistance (state or federal aid) was greater than the rate of growth for the tax levy. Non-property tax revenues also increased at a more rapid rate than did property tax receipts. One of the effects of the varying growth rates for different revenue sources is indicated by the declining percentage share of property taxes to total New York City revenues.

The General Fund revenues of New York City accounted for 35.1 percent of total revenues at the beginning of the 1961-76 period of analysis.[3] At the end of that time span, in fiscal 1976, the General Fund share of revenue had declined to 26.2 percent of total revenues. The proceeds from general fund taxes increased far more rapidly than did revenues from the property tax levy over the same period. In addition, the growth pattern for general fund revenues was not as consistent as the more stable property tax levy. Increases in general fund revenues help to explain the relatively slower decline in the general fund's share of New York City revenues.

As was the case with tax levy funds and with the locally raised revenue category in aggregate, major shifts in the general fund's share of local revenue were occurring in the middle or late 1960's.

The significance of the mid/late 1960's in any analysis of the changing New York revenue structure is evidenced by the greater than average rate of change in the revenue composition occurring during that period. A combination of local and non-local policy initiatives were in part responsible for the changes in the city's contribution to its own finances.

The most important development in the local arena was the major tax reform implemented in 1966. The Lindsay Administration, relying in large part on the recommendations of the previous Commission on City Finances (1966), sponsored a revamping of the city's tax system. The changes were successful in generating additional operating revenues for the city government.

The increases in federal and state assistance were the complementary and equally significant developments occurring outside of New York. Intergovernmental aid from both sources was increased substantially during this period.

This led to an increase in local revenue due to city policy and an increase in state/federal aid. Both of these factors combined to rapidly expand the local government sector in New York.

This section of the thesis will analyse the local revenue structure of the city. The term local revenues refers to the part of the city's total revenue that is raised by the municipal government.

To facilitate the analysis of the local revenue system, the total local revenue will be broken down into its component parts. Generally, the local sources of municipal finance are classified as taxes on real property and all other revenues, which are called non-property taxes. This dichotomy is based on the historical fact that property taxes were (and are) the primary revenue source for local government entities. New York City was the leader in the development and imposition of non-property taxes, starting with the sales tax in 1934. The state constitution delegates the power to levy property taxes to its local government. However, any non-property taxes proposed by localities must be approved by the state legislature before they can take effect.

The overall classification of non-property tax can itself be further divided according to that segment of the economy upon which the tax burden is initially visited. Personal taxes, such as the tax on personal incomes, are paid by individuals. Business taxes, for example the commercial occupancy tax, are paid by corporations, partnerships, or other firms.

D. PROPERTY OR NON-PROPERTY TAXES: RELATIVE MERITS

The city of New York was one of the earliest users of non-property taxes as a significant part of the local revenue structure. However, non-property taxes have now become commonplace for municipalities throughout the nation as means were sought to diversify the sources of local revenue. The primary reason for this development was a rapid increase in municipal expenditures, and a resultant increase in local property taxes. In addition, the property tax is one of the least popular forms of taxation and is considered by some to be a very regressive or inequitable tax.

The various types of non-property taxes have a number of qualities that make them popular substitutes and/or supplements to the traditional property tax levy. There are three reasons usually cited as arguments for the use of non-property taxes. First, the use of non-property taxes can facilitate property tax relief. Such relief can take the form of a reduction in the percentage rate of taxation, or a reduction or elimination of anticipated tax rate increases. A second rationale for non-property taxes concerns the relatively high revenue yields associated with the imposition of the more widely used non-property taxes. In the case of the income tax or the sales tax for example, low percentage rates of taxation can produce large amounts of revenue, especially in urban areas.[4]

A third reason for the use of non-property taxes is the greater sensitivity of such taxes to economic changes, wehther positive or negative. The yield from an income tax automatically increases as the income of those in its area of coverage does. Similarly, losses in local income will result in lower revenue yields. Thus the non-property taxes are more immediately adjusted to changing economic conditions.

Finally, the use of non-property taxes enables localities to tax non-residents (commuters, tourists, etc.), and in that way to partially offset the cost of services provided to these groups. The New York City government accomplishes this by imposing an earnings tax on non-residents who work in the city.

While there are reasons favoring the use of non-property taxes, there are also many problems associated with the use of such devices.

The most important problem is caused by the local basis of non-property taxes. The non-property taxes are often levied by the smallest governmental subdivision instead of on a metropolitan or larger regional basis. This results in a tax-burden differential between neighboring municipalities, which in turn might affect the locational decisions of businesses and individuals. This is clearly the case in New York. Movements from the city to jurisdictions with lower taxes have, in large part, been responsible for the economic decline of New York.

The property tax is still the largest single source of local government revenue for New York City and for other localities nationwide. The use of real property as the basis for local taxes has been a practice as old as the United States itself. As late as 1940, the property tax was responsible for 40 percent of all taxes by all levels of government.[5] Since the 1930's the property tax's share of total governmental revenue has declined. The significance of the measure as a local tax source is still considerable, however. In fiscal 1973, property taxes produced over 80 percent of local tax revenue and over one-third (37 percent) of combined state/local revenue. States have gradually relinquished their portion of property tax collections as the tax became a more exclusively local basis for taxation.

The major quality that argues for the continued use of the unpopular property tax is its neutrality with respect to influencing the locational decisions of businesses and individuals. The major non-property tax revenue sources can cause differential tax burdens within regions. This in turn creates an incentive for tax avoidance by relocations. Real property is an immobile asset, incapable of relocating. Since businesses must locate near their markets, and workers must live near their places of work, the property tax will therefore continue as a major contributor to local revenues.

E. BUSINESS TAXES

The taxation of the city's business community was reorganized in 1966 as part of a major tax system reform. The use of the gross receipts type of business tax was eliminated in favor of an income-based tax. In addition, the taxation of business was organized around separate taxes levied on financial corporations, unincorporated businesses, utilities, and the general corporate income tax.

1. GENERAL CORPORATION TAX

The general corporation tax is authorized by the four-part city business tax. It is imposed on all corporate entities owning or leasing property, maintaining an office, or conducting business within the city. Firms subject to another business income tax are exempt from payment of the general corporation tax.[6]

The basis for taxation is the entire net income of the subject corporation. The city uses the New York State definition of net income. The state definition is in most respects similar to the federal standard, although there are a number of variations between the two. For example, interest on certain federal or municipal bonds may be tax exempt for federal tax purposes, but not for city income taxes. Such interest must be included in the computation of income. Similarly, where the federal government requires the inclusion of the value of gifts, such gifts are excluded from the city's computation of net income.

After the computation of taxable income, the rates of taxation are a flat 10.05 percent of calculated income. There are three alternate methods of calculating the required tax payments, involving capital investments, salaries of corporate officers, and other weighted factors. Most firms, however, pay the easier-to-calculate flat rate.

2. UNINCORPORATED BUSINESS TAX

The New York City tax on unincorporated businesses was enacted in 1966 as another part of the tax system reform package. The tax is applicable to any unincorporated entity that engages in commerce, business, or the professions, either wholly or partly in the city. The tax is patterned on a similar levy imposed by New York State. One significant difference between the city and the state measures is the inclusion of professions--law, medicine, architects, etc. among those liable under the city tax. The major exemption from the measure applies to that group of unincorporated businesses that are subject to the city's tax on utilities. The city also imposes a tax on vendors of utility services. Payment of this tax exempts businesses from the unincorporated levy.

The tax is levied against the taxable income of the business. The federal definition of gross income is the starting point in the calculation of city taxable income for this levy. A number of variations from the federal definition of income are used as is a modified federal exemption/deduction schedule.

After calculation of the taxable income, the rate of taxation is equal to 10.05 percent of income. Credits of all or part of the tax are available for businesses whose tax payments are less than $200.

3. FINANCIAL CORPORATION TAX

The tax on financial corporations is also part of the New York City business tax. Payment of the financial tax excludes the payee from obligations under the general corporation tax. The financial corporation tax is imposed on savings and commercial banks, trust companies, savings and loan associations, and other financial institutions chartered by the state.[7] National banks, federal savings and loan associations, and credit associations that do business in the city are also taxed according to a calculation of their New York City-earned share of income. The calculation of the tax-paying firm's income uses the same definition as does the general corporation tax. Similarly, where alternate methods of income calculation are available, the alternative that produces the highest taxable income is required to be used.

Once taxable income is determined, the tax rate is 13.8 percent of net city income for institutions other than savings banks and Savings and Loan Associations. An alternative method of tax payment calculation (to be used if a higher tax liability results) figures 2.6 mills on each dollar of apportioned issued capital stock.

For savings banks and loan associations, the tax rate is generally 12.1 percent of New York City income. The alternative method of calculating the tax is 2.6 percent of the amount of interest or dividends credited to depositors or shareholders.

4. UTILITY TAX

The city's tax on utilities is imposed on the operators of every utility or vendor of utility services. Any such establishment that owns property, holds a franchise, or does business in New York must pay this tax.[8]

Public utilities are those firms subject to the supervision of the State Public Service Department. They provide gas, electricity, steam, water, refrigeration, telephony or telegraphy or operate omnibusses. Vendors of utility services are those engaging in similar activities but not subject to the Public Service Department's supervision. Utility vendors, as opposed to operators, are subject to the general corporation tax in addition to the utility tax. Utility operators, are tax exempt from the general tax on the basis of their utility tax payments.

The tax is based on the gross income of the firm, which consists of all receipts prior to deductions for business expenses. The New York City acquired share of income is the basis for collections of firms operating in other areas.

The rates for the various types of utilities are as follows: For utilities and vendors of utility services, the tax rate is 2.35 percent of gross income. For the operators of omnibusses, the rate is 1.17 percent of gross income. And, for railroads, the tax rate is 3.52 percent of gross income.

5. COMMERCIAL RENT OCCUPANCY TAX

The city's commercial rent or occupancy tax is leveled on every tenant engaged in business, commerce or the professions. Although certain exemptions apply to very small and/or unprofitable businesses, the tax is paid by virtually all tenants in the city.[9]

The tax liability is calculated from the base rent payment of the tenant. After allowable adjustments to the base rent are calculated, the following rate/schedule is used to determine the tax.

ANNUAL RENTS

Rents	Tax Rates
$ 0-2,499	2-1/2 percent
$ 2,500-4,999	5 percent
$ 5,000-7,999	6-1/4 percent
$ 8,000-10,999	7 percent
$11,000 and over	7-1/2 percent

6. OTHER BUSINESSES TAXES

The General Corporation Tax, the Financial Corporation Tax, the Unincorporated Business Tax, the utility tax and the Commercial Rent Occupancy Tax are the largest revenue producers in the City's business tax structure. They are not, however, the only taxes whose initial burden falls on the business community. The City's corporate income tax laws include other levies that produce lesser amounts of revenue.

The tax measures listed above, excluding the commercial rent occupancy tax, accounted for over 95 percent of corporate income tax payments in fiscal 1976. (The commercial rent occupancy tax is not an income-based levy, as are the other business taxes discussed. However, it has been, since its introduction in 1963, a major contributor to the local revenue system.)

The remaining income-based business taxes are the Transportation Corporation Tax and the insurance Corporation Tax. In 1976, these two levies produced one million and fifteen million dollars, respectively. In addition, there are a number of selective sales taxes that impact on the business sector.

The vault tax and the conveyance of real property tax are exemplary of the smaller revenue producing taxes utilized by the city. The vault tax is often cited as an example of the nuisance taxes collected by New York. The tax is imposed for the "privilege" of having a vault, which is any subsurface opening that extends beyond the building line and into the public streets. Collections under this tax totalled $4 million in 1976. The conveyance of real property tax is levied on the transfer of deeds for any property worth more than $25,000. That tax produced $15 million in fiscal 1976.

F. THE BUSINESS SECTOR SHARE OF LOCAL REVENUE

The New York City business community pays its local taxes through three basic measures. Along with individuals and families, the businesses pay real property taxes. In addition, contributions to the city's general fund are made through the various business income taxes and the commercial rent occupancy tax. While these are not the only tax measures that are levied on businesses, these taxes in combination account for the overwhelming majority of business tax payments to New York City.

Business tax collections represented 24 percent of general fund revenues and 10.9 percent of total local revenues in 1961. In 1975, the year that the fiscal crisis became public, the share of taxes paid by the business community was virtually the same as that for 1961, 15 years earlier (23.7 percent). The share of total revenues was 11.5 percent.[10]

Although the aggregate difference of less than one percentage point is insignificant, in fact there have been substantial changes in the business sector's share of local revenues. The shift to the corporate income tax base from the previously-used gross receipts tax base was begun in 1967. That year serves as the dividing point between two distinct patterns of tax payments by the business sector. Prior to 1967, an increasing share of local taxes were being paid by businesses under the gross receipts system. The introduction of the income-based tax system resulted in a more stable proportion of business/total local taxes. The shift also resulted in a decline in the business community's contribution to local revenues.

During the "gross receipts era" of 1961-1966, the business tax share of general fund revenues increased steadily. In 1961 business tax collections accounted for 24.0 percent of general fund revenues and 10.9 percent of total local revenue. In 1966, the proportion had increased to 31.8 percent of general fund collections and 13.3 percent of total revenue.

The last fiscal year under the old business tax system was 1966. In 1967, the newly implemented income-based taxes resulted in the business community's share of revenue declining substantially. The business share of revenues dropped from 31.8 percent of general fund collections, to 25.7 percent. The share of locally raised revenue dropped from 13.3 percent in 1966 to 11.4 percent in 1967.

For the period from 1966-1975 the business community's revenue share declined from 31.8 percent to 23.7 percent of local revenue. This was almost the exact reverse of the gross receipts era when a rise from 24 percent to 31.8 percent occurred. The decline was fairly consistent with the business community's local revenue share equalling about 24 percent in 1968-1969, 23 percent in 1970-1971, and slightly more than 22 percent from 1972-1974. The aftermath of the fiscal crisis caused an increase in the business community's local revenue share, to the 30 percent level effective before the income tax-based system was introduced. In fiscal 1976, General Fund revenues included 30.5 percent of business tax payments. The business sector's contribution was 15.3 percent of local revenue.

The impact of new taxes on the business sector appears to have been to redistribute the tax burden within the business sector. The introduction of major new taxes did not cause any increase in the percentage share of local taxes contributed by the business community.

During the 1961-1975 period of concern, the two major initiatives in the business tax area have been the introduction of the commercial rent occupancy tax in 1964 and the restructuring of the business tax base in 1967. As a result of each initiative, the local revenue share contributed by the business sector declined.

Prior to 1964, the general corporation tax and utility tax were the major sources of business sector revenues. The entire business community, utilities excluded, paid their local taxes through the general corporation levy. In fiscal 1963, general corporation tax collections of $235 million accounted for 11.5 percent of local tax revenues.[11] Utility tax collections were $27 million in the same year. In combination, the two business sector taxes produced 28.7 percent of general fund revenue and 12.8 percent of total local revenue.

The introduction of the commercial rent occupancy tax had the primary effect of reducing collections under the general corporate tax. Revenues from that tax declined by 17 percent, from $235 million in 1963 to $195 million in fiscal 1964. Since utility tax collections maintained a 1.3 percent share of local revenues in both years, the occupancy tax collections served to partially offset the decline in the corporate tax's local revenue share. It did not increase the share paid by the business sector. The combined general corporation and occupancy tax collections in 1964 equalled 11.2 percent of locally raised revenue. The amount is almost identical (0.3 percentage points less, in fact) to the contribution in the previous year (11.5 percent).

The business sector's total contribution to local taxes declined slightly in 1964. As mentioned earlier, the 1963 contribution from all business tax sources was equal to 28.7 percent of general fund revenue and 12.5 percent of local revenue. In 1964, the corresponding figures were 26.2 percent of general fund revenue and 12.5 percent of locally raised taxes.

In fiscal 1967, a major reorganization of the local revenue structure took place. For the business sector, the most significant change was from the gross receipts to the income basis for taxation. The previously all-encompassing general corporation tax was supplemented by separate income taxes for the financial sector, the transportation industry, etc. As was the case with the introduction of the commercial rent occupancy tax, the system changes resulted in the business community's share of locally raised revenues declining. In fact, the decline between fiscal 1966 and 1967 was even more pronounced than was the earlier shift caused by the occupancy tax. The introduction of personal income tax as part of the tax system reform package provided additional revenues that permitted the business community's share of local revenues to decline.

In fiscal 1966, the business sector's share of revenues equalled 31.8 percent of general fund monies and 13.3 percent of local revenue. This aggregate amount includes payments under the general corporation tax (9.0 percent of local revenue), the utility tax (1.3 percent). The new tax structure introduced in 1967 caused the general corporation tax's revenue share to drop from 9 percent to 4.6 percent. The commercial rent occupancy tax's revenue share also declined slightly from 3 percent to 2.6 percent of local revenue. An increase in utility tax collections of over 30 percent caused that levy's share of local revenue to increase slightly, from 1.3 to 1.4 percent.

In aggregate, the business sector paid 25.7 percent of general fund revenues and 11.4 percent of local collections in 1967. This was substantially less than the previous year when payment accounted for 31.8 percent of general fund monies and 13.3 percent of total local revenue.

G. PERSONAL TAXES

Personal taxes are those whose initial impact falls on individuals or households. In New York City the major personal taxes are the retail sales tax and the personal income tax. These two levies are the largest non-property tax sources nationwide.

The use of the sales tax is widespread although the tax is levied on a statewide, as opposed to a citywide, basis in many cases. The personal income tax is less widely used by state and local governments.

In fiscal 1971, 13 of the nation's 48 largest cities imposed a personal income tax. Collections nationwide totalled $1.7 billion, of which $1.5 billion was raised by city governments.[12] Thus, the personal income tax is primarily a revenue source for urban areas. Often the income tax is adopted as a means of property tax relief.

Sales taxes are second to the property tax as a source of local revenue. In fiscal 1972, sales tax collections totalled $3.7 billion. More than one-half (precisely 26) of the nation's 48 largest cities, utilize the local sales tax as a source of revenue.

1. SALES TAX

The tax on retail sales, formerly the sales and use tax, is the original form of non-property tax used by the city of New York. The tax was instituted during the depression of the 1930's.[13] The state legislature at that time granted approval of the measure as a temporary means of financing the heavy public assistance expenditures required during that period. The original intent was to discontinue the authorization, and therefore the sales tax itself, when the public assistance needs of the city would decrease to a level capable of financing from the property tax levy. However, through a series of political compromises and due to the lobby efforts of the New York City government, the decision was made to let the city utilize sales tax revenues for purposes other than social welfare expenditures.

The sales tax is imposed upon the retail purchase of any tangible property. Sales of most services are also taxable. The city generally follows the definitions and exemption schedules included in the state's sales and use tax.[11]

The most significant difference between the state and city measures is that the city taxes the sale of manufacturing equipment and machinery while the state does not. Similarly, the state exempts the sale of fuel and utility services used in manufacturing processes while the city does not. The present rate of the sales tax is 4 percent of the retail price of goods. Since the state also has a 4 percent tax, the total New York City tax on sales is 8 percent.

The city's sales tax predates the state sales tax by quite a few years. However, the city's sales tax is now administered by the state government. Sales tax revenues are used to fund debt service (principal and interest) payments for the bond issues of the Municipal Assistance Corporation (MAC). After the subtraction of MAC's debt service and operating costs, whatever sales tax receipts are remaining are transferred to the city. These residual sales tax receipts are included in the city's general fund in the same manner as before the creation of MAC.

2. USE TAX

The use tax is complementary to the sales tax. All tangible personal property used in New York City and not subject to the city's sales tax is subject to the use tax, whose rate is identical to the sales tax.[14] The levy is intended to tax those retail purchases made outside of New York City but used within the city. Imposition of the tax removes the economic incentive for city residents to shop in surburban stores in order to avoid the sales tax. Most use tax collections are for auto sales in other parts of the metropolitan area.

Sales tax collections have been increasing at an average annual rate of 7.3 percent for the 1961-1975 period. In spite of the growth rate for the sales tax, the even faster growth of other revenue sources meant that the portion of the city's local revenues generated by the sales tax decreased. In 1975, sales tax collections represented 28.0 percent of general fund taxes (and 13.6 percent of total locally raised revenue). This represents a decline of 7 percentage points when compared to the 1961 contribution. In fiscal 1961, the sales tax accounted for 35 percent of general fund revenues and 16 percent of total local revenue.

The sales tax's contribution to total city revenue also declined over the last 15 years. In fiscal 1961, the $303 million of sales tax revenue was 12.3 percent of all revenues. In 1975 the percentage had dropped to 6.6 percent. The distinction between the local revenue share and the total revenue share is important to make. The sales tax's declining share of total revenues is primarily the result of intergovernmental contributions. The decline in the local revenue share is the result of policy decisions by the city administration.

3. PERSONAL INCOME TAX

The New York City tax on residents' personal income was first collected in 1966. Created as part of a major revision of the city's tax system, the levy was imposed concurrently with a tax on the New York City-earned income of nonresidents. Thus the tax on residents' incomes can be collected only so long as the complementary commuters tax is in effect. The tax is similar in most respects to the state personal income tax.[15] Rate schedules are different from the state levy, but the city uses the state's definition of income and also follows the same schedule of deductions and exemptions.

The personal income tax is administered by the state tax commission for the city. The tax is collected along with the state tax and refunds are mailed from Albany. Revenues are then transferred to New York City.

4. NON-RESIDENT EARNINGS TAX

The tax on earnings of nonresidents is the companion measure to the city's personal income tax. The city is authorized to impose such a tax only as long as the residents personal income tax is in effect.[16] The tax must be paid by anyone who earns a wage within the city and is not subject to the income tax. Salaries and the income of self-employed persons are also subject to the tax. Once the taxable income has been determined the tax calculated is equal to 45/100 of one percent of total city taxable earned income for wage earnings. The rate of taxation for self-employed persons is 65/100 of one percent.

Personal income tax collections have grown by an average annual rate of 16.5 percent for the 1967-1975 period. This is about 25 percent greater than the overall revenue growth rate of 12.1 percent.

The tax was introduced as a part of a tax-reform program designed to increase the revenue-generating capacity of the local tax structure. In this regard the effort was successful. The 16.5 percent average annual growth rate is composed of a very erratic pattern of large revenue increases and two fiscal years when collections under the tax declined.

As a share of general fund revenues, the income tax maintained a relatively stable share from its introduction in 1967 until 1971. In 1972 the tax's share of general fund revenues increased sharply. This was followed by another period of relative stability, which continued up to the start of the fiscal crisis period.

Over the 10 years that it has been in existence, the income tax has grown in importance was a contributor to total local finance. In 1967, collections of $130 million accounted for 10.4 percent of general fund revenues and

4.5 percent of total local revenues. By 1975, income tax collections were $466 million. That figure represents 16.5 percent of general fund revenues and 8 percent of local revenue.

5. OTHER PERSONAL TAXES

In addition to the sales tax and the personal income tax, there are a number of other city tax measures that impact upon the individual consumer. None of these older taxes produce the amount of revenue generated by the sales and income tax levies. They remain the major components of the personal tax area.

Another component of the personal tax burden is the tax on the use, possession, or operation of motor vehicles. The city has a number of different taxes that are imposed on automobile users. These are the tax on commercial motor vehicles, the auto use tax, and the parking tax. In addition, there is a tax on the use of gasoline, a separate tax on leaded gasolines, and the motor vehicle registration fee. The taxes on gasoline and the registration fees are paid by all state residents. New York receives a portion of these revenues and includes these revenues in its listing of selective sales/use taxes.

Of the total amount of auto-related taxes, the auto use tax and the gasoline and motor fuel taxes are the greatest producers of revenues.

The City also imposes two taxes on the purchase of cigarettes. The cigarette tax is payable by the consumer of cigarettes. It is a flat 8¢ tax per package of 20 cigarettes. The tax is paid in the form of stamps that are affixed to each package of cigarettes. The City also has a tax on the basis of the tar and nicotine content in cigarettes. The tax is progressively higher on cigarettes having greater amounts of the taxed substances.

H. THE PERSONAL TAX SHARE OF LOCAL REVENUE

Analysis of the business tax structure indicated that the perceived increase in the business community's share of local taxes did not really occur within the period of concern. A similar analysis of personal taxes indicates that there was some increase in the proportion of local revenues contributed by individual tax payers.

The combined sale and personal income tax collections can be used as an approximation of personal tax payments. From that perspective, the increasing share of local revenues contributed by individuals is seen to be the result of the personal income tax implemented in fiscal 1967.

Prior to 1967, the sales tax was the largest source of non-property tax revenue and the primary means of personal taxation. During the 1961-1966 period sales taxes accounted for between 16 and 18 percent of total local revenue. The introduction of the personal income tax had two impacts on the personal tax area. First, the levy caused a shift of the personal tax burden from the sales tax to the new tax measure. Second, the overall contribution of individuals to the local revenue structure began to increase slowly. As personal income tax collections grew, the share of local revenues contributed by individuals increased also.

Thus, in fiscal 1967, the sales tax's share of local revenue dropped from 16 percent to 13.4 percent. When adding the contribution of personal income tax, however, the overall revenue share for individual tax payers increased from 16 percent to 18 percent. By fiscal 1972, the local revenue share paid by individuals had increased to over 20 percent, with the personal income tax accounting for most of the additional contribution. Income tax collections in that year provided 9.9 percent of total local revenues as opposed to the 4.6 percent figure in 1967. Individual contributions to the local revenue structure were consistently greater than 20 percent in the post-1971 period. In 1976, the "MAC take out" of sales tax funds caused the relative share of personal taxes to decline.

1. REAL PROPERTY TAX

The property tax is the greatest single source of locally raised revenues. The power to levy the tax is the only taxing power specifically delegated to the City by the

New York State constitution. New York's property tax is administered by the Department of Finance. That agency is responsible for assessing the value of taxable property and with the collection of tax payments. Property assessments form the base for the tax levy.

The annual assessments must be completed by the 25th of January.[17] Property owners are permitted to file a review if they feel their property has been overassessed. The City Tax Commission is the body that has the power to adjust the Finance Department's assessments upon the complaint of the tax payer. Applications for an assessment correction must be filed by March 15th.

Property assessments are supposed to be made equal to the full market value of the property. This rarely occurs, however. Instead, property is assessed at various fractions of its full value. In general, commercial or business property is assessed at a higher assessed/full-value ratio than are residential properties. And, within the residential property category, one- and two-family houses are assessed at a lower ratio than are multiple dwellings.

The total assessed value of the City's real property and the amount of money to be raised by the tax levy are the two determinants of the annual property tax rate. The year's tax levy divided by the total assessed value of property produces the tax rate which is expressed as a payment for every \$100 of assessed value. The property tax is paid quarterly on the first day of August, October, January and April.

The State Constitution places limits upon the amount of the property tax levy. Although localities are responsible for determining the tax rate that rate must be equal or less than the so called "2½ percent limitation." This ceiling limits the property tax levy to 2½ percent of the average full value of taxable real property as calculated over the previous five years.

This limitation applies to tax levy funds that will be used to finance the City's operating budget. An additional and virtually unlimited tax levy is allowed for the debt service payments associated with the City's long-term debt obligations. New York's general obligation bonds are backed by the City's full faith, credit, and taxing power. Specifically, debt-service obligations are backed by a lien on the City's property tax revenues. Such obligations are a major part of the city's uncontrollable expenditures. As such, debt-service payments are categorized as tax levy payments "outside the 2½ percent limitation." The amount of the payments are a function of the interest and amortization payments required in any fiscal year.

Property tax collections increased at an average annual rate of 7.9 percent for the 1961-1975 period of analysis. The rate of growth was much slower than the growth in total revenues. Since overall revenue increased at an average annual rate of 12.1 percent, the portion of the total revenue represented by the property tax declined steadily.

Between 1966 and 1971, property tax revenues grew by 47.6 percent, less than one-half as fast as the total revenue growth over the same period. As a portion of local revenue, the property tax declined slightly over the period of analysis. While generating 54.4 percent of local revenue in 1961, the corresponding figure for 1975 was 51.5 percent. In fiscal 1966, a sharp decline in sales tax revenues and corporate tax payments occured. This had the effects of increasing the property tax's share of local revenue to 59.2 percent as compared to 53.6 percent in fiscal 1965. 1972 was the only fiscal year in which the property tax's share of local revenue dropped below the 50 percent level. In that year, general fund revenue increased by over 1/3 (34%) and property tax revenues grew by only 5.2 percent.

Of course, the general fund is complementary to the property tax in that a decreasing local revenue contribution by the property tax is tantamount to an increase in the general fund category's share. The aggregate shift over the 1961-1975 period caused the general fund's portion of local revenues to increase from 45.6 percent (1961) to 48.5 percent in 1975.

2. UNCOLLECTED TAXES

As mentioned in the analysis of property tax growth trends, 1967 was the first year in which a decline in property tax collections occurred. The $20 million dollar decline in revenues have more symbolic than fiscal impact. But, while a decline of 1 percent is marginal, the very existence of a property tax decline is not a positive sign for the future of the city's economy. Given the stability of the property tax over the short run, the slight decline of 1976 may be the beginning of a series of declines in subsequent years.

A problem of even greater fiscal importance is the large amount of uncollected property taxes still owed the city. In fiscal 1976, the amount of uncollected taxes from prior years was more than 100 times the 1976 decline in annual revenue collections. Over $240 million property taxes was due at the end of fiscal 1976.[18]

The large amount of uncollected property taxes influences the size of the short-term debt obligations issued by the City. Tax Anticipation Notes are sold on the basis of uncollected property taxes. The City assumes, (incorrectly it has recently admitted), that all back property taxes will eventually be paid off. It was this expectation that allowed the City to issue TANS backed by the never-to-be-collected property taxes.

In fiscal 1961 less than 5 percent of the City's property tax assessment was uncollected during the year it was due. By fiscal 1975 the amount of uncollected taxes was over 10 percent of total assessments. Disinvestments from many areas of the City are responsible for much of the tax delinquency. The abandonment of residential buildings and the City's policy of taxing idle lands at lower rates create the incentive for these activities (see Table B-3).

SUMMARY

In Appendix B a time-series analysis of the New York City revenue structure is presented. A major trend observed was: an increase in local revenues at a rate significantly lower than the growth rate for state and federal aid. The increases in intergovernmental assistance caused the locally raised portion of total revenues to decline. This is important because increased external assistance meant that city officials had less control over the areas where additional expenditures were to be made. The traditional local service areas (police, sanitation, fire, etc.) often were not the areas where increased state/federal aid was available. The "categorical grant" approach to federal aid in this way channeled "city" expenditures into new areas. Then when the fiscal crisis began, the city was criticized for providing many "non-traditional" city services.

The analysis also indicated that the business community's share of local revenues has declined over the 16 year period of concern. This decline has been offset by a rise in the portion of local revenues generated by personal taxes.

This finding is very interesting since it runs counter to the popular notion that the business community is being unfairly impacted upon in the local tax area. While taxes for all sectors of the economy have increased over the years, the impression of a <u>relatively</u> greater business tax burden does not appear to be valid.

In spite of the conclusions based on the comptroller's report data, most proposals concerning taxes call for business tax cuts as the area of priority.

APPENDIX B: FOOTNOTES

1. The data in this section is based on the Comptroller's Annual Reports of 1961-1976.

2. Ibid.

3. Ibid.

4. Robert Eisenmenger, et. al., Options for Fiscal Structural Reform in Massachusetts (Federal Reserve Bank of Boston), p.67.

5. Ibid., p. 68.

6. Commerce Clearinghouse Inc., Guidebook to New York Taxes (New York), p. 272.

7. Ibid., p. 137.

8. Ibid., p. 137.

9. Ibid., p. 288.

10. See Appendix C for business tax collections.

11. Ibid.

12. James Maxell and J. Richard Aronson, Financing State and Local Government, (Washington: Brookings Institute), p. 34.

13. Advisory Commission, On Intergovernmental Relations, Local Revenue Diversification (Washington: U.S. Government Printing Office), p. 42.

14. New York City Department of Finance, New York City Tax Guide, p. 31.

15. Op. Cit., Commerce Clearinghouse, p. 331.

16. Op. Cit., Local Revenue Diversification, p. 52.

17. Ibid., p. 31.

18. See Appendix C for property tax data.

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1961		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,028.3	41.9%	--
SALES TAX	303.0	12.3	--
PERSONAL INCOME TAX	--	--	--
GENERAL CORPORATION TAX	178.9	7.3	--
OTHER BUSINESS TAXES	26.3	1.1	--
Commercial Rent-Occupancy Tax	--	--	--
Utility Tax	26.3	1.1	--
Financial Corporation Tax	--	--	--
Unincorporated Business Tax	--	--	--
Insurance Corporation Tax	--	--	--
SPECIAL CITY TAXES	57.0	2.3	--
Cigarette Tax	22.0	0.9	--
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	3.6	0.1	--
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	
Others	31.4	1.3	--
WATER CHARGES	50.6	2.1	--
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	65.2	2.7	--
FARES, TOLLS, RENTS, INTEREST AND SERVICES	82.5	3.4	--
OTHER REVENUES	96.0	3.9	--
FEDERAL ASSISTANCE	110.3	4.5	--
STATE ASSISTANCE	454.9	18.5	--
TOTAL	$2,453.0	100.0%	--

Source Annual Report NYC Comptroller, 1960-61

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1962		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,070.9	41.5%	4.1%
SALES TAX	318.0	12.3	4.9
PERSONAL INCOME TAX	--	--	--
GENERAL CORPORATION TAX	191.1	7.4	6.8
OTHER BUSINESS TAXES	26.7	1.0	1.5
Commercial Rent-Occupancy Tax	--	--	--
Utility Tax	26.7	1.0	1.5
Financial Corporation Tax	--	--	--
Unincorporated Business Tax	--	--	--
Insurance Corporation Tax	--	--	--
SPECIAL CITY TAXES	54.8	2.1	-3.9
Cigarette Tax	24.4	0.9	10.9
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	4.6	0.2	27.7
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	25.8	1.0	-17.9
WATER CHARGES	51.4	2.0	1.5
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	76.5	3.0	17.3
FARES, TOLLS, RENTS, INTEREST AND SERVICES	88.4	3.4	7.1
OTHER REVENUES	73.1	2.9	-23.9
FEDERAL ASSISTANCE	144.3	5.6	30.8
STATE ASSISTANCE	483.7	18.8	6.3
TOTAL	$2,578.9	100.0%	5.1%

SOURCE ANNUAL REPORT, NYC COMPTROLLER
1961-62

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1963		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,134.5	40.9%	5.9%
SALES TAX	326.3	11.8	2.6
PERSONAL INCOME TAX	--	--	--
GENERAL CORPORATION TAX	234.6	8.5	22.7
OTHER BUSINESS TAXES	27.3	1.0	2.2
Commercial Rent-Occupancy Tax	--	--	--
Utility Tax	27.3	1.0	2.2
Financial Corporation Tax	--	--	--
Unincorporated Business Tax	--	--	--
Insurance Corporation Tax	--	--	--
SPECIAL CITY TAXES	55.5	2.0	1.2
Cigarette Tax	23.2	0.8	-5.0
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	4.5	0.2	-2.2
Off-Track Betting			
Tax on Leaded Gasoline	--	--	--
Others	--	--	--
WATER CHARGES	27.8	1.0	7.7
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	52.1	1.9	1.3
FARES, TOLLS, RENTS, INTEREST AND SERVICES	69.9	2.5	-8.7
OTHER REVENUES	95.5	3.4	8.0
FEDERAL ASSISTANCE	44.0	1.6	-39.9
STATE ASSISTANCE	165.9	6.0	14.9
	564.0	20.4	16.6
TOTAL	$2,769.6	100.0%	7.3%

SOURCE: ANNUAL REPORT, NYC COMPTROLLER 1962-63

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1964		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,220.2	39.2%	7.5%
SALES TAX	417.4	13.4	27.9
PERSONAL INCOME TAX	--	--	--
GENERAL CORPORATION TAX	194.9	6.3	-17.0
OTHER BUSINESS TAXES	95.2	3.0	248.7
Commercial Rent-Occupancy Tax	65.9	2.1	--
Utility Tax	29.3	0.9	7.3
Financial Corporation Tax	--	--	--
Unincorporated Business Tax	--	--	--
Insurance Corporation Tax	--	--	--
SPECIAL CITY TAXES	73.1	2.3	31.7
Cigarette Tax	39.0	1.2	68.1
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	4.5	0.1	0
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	30.6	1.0	10.0
WATER CHARGES	53.6	1.7	2.8
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	80.8	2.6	15.5
FARES, TOLLS, RENTS, INTEREST AND SERVICES	102.0	3.3	6.8
OTHER REVENUES	95.4	3.1	116.8
FEDERAL ASSISTANCE	182.6	5.9	10.0
STATE ASSISTANCE	599.1	19.2	6.2
TOTAL	$3,114.3	100.0%	12.4%

Source Annual Report, NYC Comptroller
1963-64

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1965 Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,313.9	39.5%	7.6%
SALES TAX	441.8	13.3	5.8
PERSONAL INCOME TAX	--	--	--
GENERAL CORPORATION TAX	247.5	7.4	26.9
OTHER BUSINESS TAXES	101.0	3.0	6.0
Commercial Rent-Occupancy Tax	70.0	2.1	6.2
Utility Tax	31.0	0.9	5.8
Financial Corporation Tax	--	--	--
Unincorporated Business Tax	--	--	--
Insurance Corporation Tax	--	--	--
SPECIAL CITY TAXES	79.1	2.4	8.2
Cigarette Tax	40.9	1.2	4.8
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	5.3	0.2	17.7
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	32.9	1.0	7.5
WATER CHARGES	53.4	1.6	-0.4
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	78.6	2.4	-2.8
FARES, TOLLS, RENTS, INTEREST AND SERVICES	101.8	3.0	-0.2
OTHER REVENUES	36.7	1.1	-61.6
FEDERAL ASSISTANCE	218.3	6.6	19.5
STATE ASSISTANCE	655.6	19.7	9.4
TOTAL	$3,327.7	100.0%	6.8%

SOURCE: ANNUAL REPORT, NYC COMPTROLLER 1964-65

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1966 Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,409.4	38.1%	7.2%
SALES TAX	382.1	10.3	-13.6
PERSONAL INCOME TAX	--	--	--
GENERAL CORPORATION TAX	213.5	5.8	-13.8
OTHER BUSINESS TAXES	102.5	2.8	1.4
Commercial Rent-Occupancy Tax	71.8	2.0	2.5
Utility Tax	30.7	0.8	-1.0
Financial Corporation Tax	--	--	--
Unincorporated Business Tax	--	--	--
Insurance Corporation Tax	--	--	--
SPECIAL CITY TAXES	53.1	1.4	-32.9
Cigarette Tax	32.5	0.9	-20.6
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	4.9	0.1	- 7.6
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--		--
Others	15.7	0.4	-52.3
WATER CHARGES	49.4	1.3	- 7.5
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	76.3	2.1	- 3.0
FARES, TOLLS, RENTS, INTEREST AND SERVICES	86.6	2.4	-15.0
OTHER REVENUES	8.8	0.2	-76.1
FEDERAL ASSISTANCE	307.9	8.3	41.0
STATE ASSISTANCE	1010.1	27.3	54.0
TOTAL	$3,699.7	100.0%	11.1%

SOURCE ANNUAL REPORT, NYC COMPTROLLER
1965-66

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1967		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,573.3	34.5%	11.6%
SALES TAX	379.6	8.3	-0.7
PERSONAL INCOME TAX	130.4	2.9	
GENERAL CORPORATION TAX	182.0	4.0	-14.8
OTHER BUSINESS TAXES	141.8	3.1	38.3
Commercial Rent-Occupancy Tax	72.5	1.6	0.9
Utility Tax	40.8	0.9	32.8
Financial Corporation Tax			
Unincorporated Business Tax	16.8	0.3	
Insurance Corporation Tax	11.7	0.3	
SPECIAL CITY TAXES	51.8	1.1	-2.5
Cigarette Tax	34.9	0.8	7.3
Tar and Nicotine Tax			
Conveyance of Real Property	4.7	0.1	-4.1
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	12.2	0.2	-22.3
WATER CHARGES	91.2	2.0	84.6
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	81.7	1.8	7.0
FARES, TOLLS, RENTS, INTEREST AND SERVICES	102.2	2.2	18.0
OTHER REVENUES	89.2	2.0	913.6
FEDERAL ASSISTANCE	576.8	12.6	87.3
STATE ASSISTANCE	1161.4	25.4	14.9
TOTAL	$4,561.4	100.0%	23.2%

SOURCE ANNUAL REPORT NYC COMPTROLLER
1966-67

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1968		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,648.1	31.2%	4.7%
SALES TAX	409.8	7.8	7.9
PERSONAL INCOME TAX	170.2	3.2	30.5
GENERAL CORPORATION TAX	203.6	3.9	11.8
OTHER BUSINESS TAXES	188.2	3.6	32.7
Commercial Rent-Occupancy Tax	78.6	1.5	8.4
Utility Tax	41.3	0.8	1.2
Financial Corporation Tax	26.4	0.5	
Unincorporated Business Tax	29.8	0.6	77.3
Insurance Corporation Tax	12.1	0.2	3.4
SPECIAL CITY TAXES	53.9	1.0	4.0
Cigarette Tax	34.7	0.7	-0.6
Tar and Nicotine Tax			
Conveyance of Real Property	5.7	0.1	21.2
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	13.5	0.2	10.6
WATER CHARGES	82.9	1.6	-9.2
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	77.0	1.5	-5.8
FARES, TOLLS, RENTS, INTEREST AND SERVICES	106.6	2.0	4.3
OTHER REVENUES	120.3	2.3	34.8
FEDERAL ASSISTANCE	746.0	14.1	29.3
STATE ASSISTANCE	1467.2	27.8	26.3
TOTAL	$5,273.8	100.0%	15.6%

Source: Annual Report, NYC Comptroller 1967-68

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1969 Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,737.9	28.3%	5.4%
SALES TAX	444.2	7.2	8.3
PERSONAL INCOME TAX	201.4	3.3	18.3
GENERAL CORPORATION TAX	215.8	3.5	5.9
OTHER BUSINESS TAXES	212.7	3.5	13.0
Commercial Rent-Occupancy Tax	81.1	1.3	3.1
Utility Tax	41.8	0.7	1.2
Financial Corporation Tax	40.3	0.7	35.2
Unincorporated Business Tax	38.0	0.6	27.5
Insurance Corporation Tax	11.5	0.2	-5.0
SPECIAL CITY TAXES	49.6	0.8	-8.0
Cigarette Tax	33.0	0.5	-4.9
Tar and Nicotine Tax			
Conveyance of Real Property	7.6	0.1	33.3
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	9.0	0.2	33.4
WATER CHARGES	91.2	1.5	10.0
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	80.1	1.3	4.0
FARES, TOLLS, RENTS, INTEREST AND SERVICES	120.5	2.0	13.0
OTHER REVENUES	95.8	1.6	-20.4
FEDERAL ASSISTANCE	899.9	14.6	20.6
STATE ASSISTANCE	1991.3	32.4	35.7
TOTAL	$6,140.4	100.0%	16.4%

SOURCE: ANNUAL REPORT, NYC COMPTROLLER 1968-69

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1970		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$1,892.7	28.8%	8.9%
SALES TAX	466.9	7.1	5.1
PERSONAL INCOME TAX	205.4	3.1	2.0
GENERAL CORPORATION TAX	205.1	3.1	-5.0
OTHER BUSINESS TAXES	207.8	3.2	-2.4
Commercial Rent-Occupancy Tax	93.5	1.4	15.3
Utility Tax	44.0	0.7	5.2
Financial Corporation Tax	42.9	0.6	6.4
Unincorporated Business Tax	15.8	0.2	-58.5
Insurance Corporation Tax	11.6	0.2	0.9
SPECIAL CITY TAXES	49.5	0.8	-0.3
Cigarette Tax	32.6	0.5	-1.3
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	7.6	0.1	0
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	9.3	0.2	3.3
WATER CHARGES	103.9	1.6	13.9
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	96.4	1.5	20.3
FARES, TOLLS, RENTS, INTEREST AND SERVICES	103.3	1.6	-14.3
OTHER REVENUES	185.3	2.8	93.4
FEDERAL ASSISTANCE	1059.8	16.1	17.7
STATE ASSISTANCE	1992.7	30.3	0.1
TOTAL	$6,568.8	100.0%	6.9%

SOURCE: ANNUAL REPORT, NYC COMPTROLLER
1969-70

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1971		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$2,080.4	28.0%	9.9%
SALES TAX	493.6	6.6	5.7
PERSONAL INCOME TAX	199.4	2.7	-3.0
GENERAL CORPORATION TAX	183.3	2.5	-10.0
OTHER BUSINESS TAXES	256.7	3.5	23.5
Commercial Rent-Occupancy Tax	139.5	1.9	49.1
Utility Tax	49.6	0.7	12.7
Financial Corporation Tax	38.3	0.5	-10.8
Unincorporated Business Tax	17.3	0.2	9.4
Insurance Corporation Tax	12.0	0.2	3.4
SPECIAL CITY TAXES	49.1	0.7	-0.9
Cigarette Tax	33.5	0.4	2.7
Tar and Nicotine Tax	--	--	--
Conveyance of Real Property	6.4	0.1	-15.8
Off-Track Betting	--	--	--
Tax on Leaded Gasoline	--	--	--
Others	19.2	0.2	106.4
WATER CHARGES	157.9	2.1	51.9
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	98.4	1.3	-2.1
FARES, TOLLS, RENTS, INTEREST AND SERVICES	85.2	1.1	17.6
OTHER REVENUES	185.8	2.5	0.2
FEDERAL ASSISTANCE	1286.6	17.3	21.4
STATE ASSISTANCE	2360.6	31.7	18.4
TOTAL	$7,437.0	100.0%	13.2%

SOURCE ANNUAL REPORT, NYC COMPTROLLER 1970-71

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1972		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$2,188.9	25.7	5.2
SALES TAX	519.7	6.1	5.2
PERSONAL INCOME TAX	443.1	5.2	122.2
GENERAL CORPORATION TAX	239.9	2.8	30.8
OTHER BUSINESS TAXES	341.8	4.0	33.1
Commercial Rent-Occupancy Tax	153.3	1.8	9.8
Utility Tax	54.0	0.6	8.8
Financial Corporation Tax	69.1	0.8	80.4
Unincorporated Business Tax	52.4	0.6	202.8
Insurance Corporation Tax	13.0	0.2	8.3
SPECIAL CITY TAXES	95.6	1.1	94.7
Cigarette Tax	30.9	0.4	-7.8
Tar and Nicotine Tax	21.0	0.2	--
Conveyance of Real Property	13.3	0.1	107.8
Off-Track Betting	2.4	0.1	--
Tax on Leaded Gasoline	8.0	0.1	--
Others	20.0	0.2	4.1
WATER CHARGES	180.2	2.1	14.1
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	152.5	1.8	54.9
FARES, TOLLS, RENTS, INTEREST AND SERVICES	119.8	1.4	40.6
OTHER REVENUES	206.2	2.4	10.9
FEDERAL ASSISTANCE	1524.4	17.9	18.4
STATE ASSISTANCE	2516.8	29.5	6.6
TOTAL	$8,528.9	100.0%	14.6%

SOURCE: ANNUAL REPORT, NYC COMPTROLLER
1971-72

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1973 Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$2,468.1	26.1%	12.7%
SALES TAX	551.3	5.8	6.0
PERSONAL INCOME TAX	439.5	4.6	-0.9
GENERAL CORPORATION TAX	247.2	2.6	3.0
OTHER BUSINESS TAXES	348.4	3.7	1.9
Commercial Rent-Occupancy Tax	166.1	1.7	8.3
Utility Tax	62.5	0.7	15.7
Financial Corporation Tax	61.8	0.7	-10.6
Unincorporated Business Tax	45.0	0.5	-14.2
Insurance Corporation Tax	13.0	0.1	0
SPECIAL CITY TAXES	138.1	1.5	44.4
Cigarette Tax	29.7	0.4	- 3.9
Tar and Nicotine Tax	22.5	0.2	7.1
Conveyance of Real Property	19.5	0.2	46.6
Off-Track Betting	34.2	0.4	1325.0
Tax on Leaded Gasoline	11.1	0.1	38.7
Others	21.1	0.2	5.5
WATER CHARGES	176.9	1.9	-1.9
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	139.5	1.5	-8.6
FARES, TOLLS, RENTS, INTEREST AND SERVICES	102.1	1.1	-14.8
OTHER REVENUES	258.7	2.7	25.4
FEDERAL ASSISTANCE	2,048.9	21.6	34.4
STATE ASSISTANCE	2,547.4	26.9	1.2
TOTAL	$9,466.1	100.0%	10.9

SOURCE: ANNUAL REPORT, NYC COMPTROLLER 1972-73

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1974		
	Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$2,655.5	26.7%	7.5%
SALES TAX	575.3	5.8	4.3
PERSONAL INCOME TAX	454.8	4.6	3.4
GENERAL CORPORATION TAX	254.6	2.6	2.9
OTHER BUSINESS TAXES	355.4	3.6	2.0
Commercial Rent-Occupancy Tax	177.1	1.8	6.6
Utility Tax	70.1	0.7	12.1
Financial Corporation Tax	58.9	0.6	-4.7
Unincorporated Business Tax	36.1	0.4	19.8
Insurance Corporation Tax	13.2	0.1	1.5
SPECIAL CITY TAXES	147.8	1.4	7.0
Cigarette Tax	29.9	0.3	0.6
Tar and Nicotine Tax	21.0	0.2	-6.7
Conveyance of Real Property	18.4	0.2	-5.7
Off-Track Betting	44.5	0.4	30.1
Tax on Leaded Gasoline	11.6	0.1	4.5
Others	22.4	0.2	4.6
WATER CHARGES	124.7	1.3	-29.6
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	153.8	1.4	10.2
FARES, TOLLS, RENTS, INTEREST AND SERVICES	116.8	1.2	14.3
OTHER REVENUES	319.5	3.2	23.5
FEDERAL ASSISTANCE	2,049.6	20.6	0.1
STATE ASSISTANCE	2,749.0	27.6	7.9
TOTAL	$9,956.8	100.0%	5.1%

SOURCE ANNUAL REPORT, NYC COMPTROLLER
1973-74

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Fiscal Year 1975 Amount	% of Total	% Increase
REAL ESTATE TAX LEVY	$2,986.1	24.1%	9.0%
SALES TAX	791.1	6.6	37.5
PERSONAL INCOME TAX	465.8	3.9	2.4
GENERAL CORPORATION TAX	268.1	2.2	5.3
OTHER BUSINESS TAXES	455.2	3.8	28.0
Commercial Rent-Occupancy Tax	190.5	1.6	7.5
Utility Tax	90.1	0.7	28.5
Financial Corporation Tax	114.2	0.9	93.8
Unincorporated Business Tax	42.3	0.4	17.1
Insurance Corporation Tax	18.1	0.2	37.1
SPECIAL CITY TAXES	156.8	1.3	6.0
Cigarette Tax	29.8	0.2	-0.4
Tar and Nicotine Tax	14.9	0.1	-29.1
Conveyance of Real Property	14.2	0.1	-22.9
Off-Track Betting	67.1	0.6	50.7
Tax on Leaded Gasoline	9.6	0.1	-17.3
Others	21.2	0.2	- 5.9
WATER CHARGES	190.5	1.6	52.7
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	155.3	1.3	0.9
FARES, TOLLS, RENTS, INTEREST AND SERVICES	118.4	1.0	1.3
OTHER REVENUES	303.6	2.5	5.0
FEDERAL ASSISTANCE	2,473.7	20.6	20.6
STATE ASSISTANCE	3,726.4	31.1	35.5
TOTAL	12,001.0	100.0%	20.5%

SOURCE: ANNUAL REPORT, NYC COMPTROLLER
1974-75

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Aggregate % Change 1961-75	Aggregate % Change 1961-66
REAL ESTATE TAX LEVY	181.6%	37.0%
SALES TAX	161.0	26.1
PERSONAL INCOME TAX	257.2[a]	--
GENERAL CORPORATION TAX	160.4	19.3
OTHER BUSINESS TAXES	1630.8[c]	289.7
Commercial Rent-Occupancy Tax	189.1[d]	9.0[e]
Utility Tax	242.6	16.8
Financial Corporation Tax	332.6[f]	--
Unincorporated Business Tax	151.8[g]	--
Insurance Corporation Tax	54.7[g]	--
SPECIAL CITY TAXES	175.1[h]	-6.9
Cigarette Tax	35.4	47.7
Tar and Nicotine Tax	-29.1[i]	--
Conveyance of Real Property	294.4	36.1
Off-Track Betting	96.1[j]	--
Tax on Leaded Gasoline	20.0[i]	--
Others	-32.5[k]	-50.0[k]
WATER CHARGES	276.5	- 2.4
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	138.2	17.0
FARES, TOLLS, RENTS, INTEREST AND SERVICES	43.5	5.0
OTHER REVENUES	216.2	-90.8
FEDERAL ASSISTANCE	2142.7	179.1
STATE ASSISTANCE	719.2	122.0
TOTAL	389.2	50.8

SOURCE: ANNUAL REPORT, NYC COMPTROLLER 1961-1975.

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Aggregate % Change 1966-71	Aggregate % Change 1971-75
REAL ESTATE TAX LEVY	47.6%	39.2%
SALES TAX	29.2	60.3
PERSONAL INCOME TAX	52.9[b]	133.6
GENERAL CORPORATION TAX	-14.2	46.3
OTHER BUSINESS TAXES	150.4	77.3
Commercial Rent-Occupancy Tax	94.3	36.6
Utility Tax	61.6	81.7
Financial Corporation Tax	45.1[l]	198.2
Unincorporated Business Tax	2.9[m]	144.5
Insurance Corporation Tax	2.6[m]	50.8
SPECIAL CITY TAXES	-7.6	219.3
Cigarette Tax	3.1	-11.1
Tar and Nicotine Tax	--	-29.1[i]
Conveyance of Real Property	30.6	121.9
Off-Track Betting	--	96.1[j]
Tax on Leaded Gasoline	--	20.0[i]
Others	22.2[k]	10.4[k]
WATER CHARGES	219.6	20.6
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	28.0	57.8
FARES, TOLLS, RENTS, INTEREST AND SERVICES	-1.7	39.0
OTHER REVENUES	2011.4	63.4
FEDERAL ASSISTANCE	317.9	92.3
STATE ASSISTANCE	133.7	57.9
TOTAL	101.0	61.4

SOURCE: ANNUAL REPORT, NYC COMPTROLLER
1966-75

City Revenue Structure (in millions)
Fiscal Period 1961-1975

	Average Annual % Change 1961-75
REAL ESTATE TAX LEVY	7.9%
SALES TAX	7.3
PERSONAL INCOME TAX	16.5[a]
GENERAL CORPORATION TAX	3.1
OTHER BUSINESS TAXES	21.8
Commercial Rent-Occupancy Tax	10.2[d]
Utility Tax	9.4
Financial Corporation Tax	21.6[f]
Unincorporated Business Tax	12.0[g]
Insurance Corporation Tax	5.7[g]
SPECIAL CITY TAXES	7.7[h]
Cigarette Tax	2.3
Tar and Nicotine Tax	-11.6[i]
Conveyance of Real Property	10.5
Off-Track Betting	34.0[j]
Tax on Leaded Gasoline	6.2[i]
Others	-3.0[k]
WATER CHARGES	10.1
LICENCES, FINES, FEES FRANCHISES, PERMITS AND PRIVILEGES	6.6
FARES, TOLLS, RENTS, INTEREST AND SERVICES	2.8
OTHER REVENUES	8.8
FEDERAL ASSISTANCE	23.7
STATE ASSISTANCE	16.1
TOTAL	12.1

Footnotes

A. FY 67 through FY 75.
B. FY 67 through FY 71.
C. The number of taxes in this group grew from 1 to 5 during this period.
D. FY 64 through FY 75.
E. FY 64 through FY 66.
F. FY 68 through FY 75.
G. FY 67 through FY 75.
H. The number of taxes included in this category varied for the period.
I. FY 72 through FY 75.
J. FY 73 through FY 75.
K. Includes 13 different taxes at different periods of time. See Addenda A.
L. FY 68 through FY 71.
M. FY 67 through FY 71.

SOURCE: ANNUAL REPORT, NYC COMPTROLLER 1961-75

(Best copy available)

City Revenue Structure - Addenda A
Fiscal Period 1961-75
Other Taxes and Years in Effect

	FY 61	FY 62	FY 63	FY 64	FY 65	FY 66	FY 67	FY 68	FY 69	FY 70	FY 71	FY 72	FY 73	FY 74	FY 75
ensating Use Tax	X	X	X	X	X	X	X	X	X	X					
ement Tax	X	X	X	X	X	X	X	X							
uit Tax	X	X	X	X	X	X									
on Occupancy of Hotel Rooms	X	X	X	X	X	X	X	X			X	X	X	X	X
on Commercial Motor Vehicles	X	X	X	X	X	X	X	X	X	X	X		X	X	X
e Race Admissions Tax	X	X	X	X	X	X	X	X	X	X			X	X	X
on Retail Liquor Licenses	X	X	X	X											
on Taxicab Rides	X	X													
on Coin-Operated Amusement vices	X	X	X	X	X	X	X	X	X	X					
pancy Tax (Transferred from ecial fund)	X	X	X	X	X	X	X	X	X	X	X	X	X	X	X
al Vault Charge			X	X	X	X	X	X	X	X		X	X	X	X
sportation Corporation Tax							X	X	X	X	X	X	X	X	X
ial Taxes - General											X	X	X	X	X

SOURCE: ANNUAL REPORT, NYC COMPTROLLER.
1961-75

TABLE I-1

New Issues, Redemptions

of Short-Term Debt

1961-1975
($ Millions)

Fiscal Year	Issued	Redeemed or Cancelled	Increase (Decrease) in Amount Out-standing	Notes Issued/ Redeemed
1961	$ 687.7	685.7	20	1.0029
1962	842.2	815.7	27.1	1.0331
1963	807.7	704.3	105.4	1.1463
1964	1,166.7	1081.8	85.0	1.0786
1965	1,470.0	1260.1	209.9	1.1658
1966	1,645.0	1704.5	(58.9)	0.9653
1967	2,076.0	1907.9	168.2	1.0886
1968	2,427.7	2369.4	58.3	1.0244
1969	3,271.0	3217.0	54.0	1.0167
1970	4,400.9	3860.0	540.9	1.1398
1971	6,512.2	5481.1	1031.2	1.1881
1972	5,749.0	4918.1	330.9	1.0673
1973	4,003.3	4136.0	(132.7)	0.9678
1974	7,305.9	6407.6	898.4	1.1403
1975	8,395.7	7271.4	1124.3	1.1547

Source: Annual Report of the New York City Comptroller, 1961-1975

TABLE I-2

New Issues, Redemptions

of Long Term Debt: Fiscal Years 1961-1976
($ Millions)

Fiscal Year	Issued	Redeemed or Cancelled	Increase (Decrease) in Amount Outstanding	Bonds Issued/ Redeemed
1961	293.7	326.2	1 32,5	0.9002
1962	458.7	333.6	125.1	1.3748
1963	450.4	126.6	126.6	1.3908
1964	472.5	361.0	111.5	1.3088
1965	530.1	364.8	165.3	1.4530
1966	717.1	402.6	314.5	1.7810
1967	489.1	438.0	51.1	1.1166
1968	484.0	510.0	(26.0)	0.9489
1969	513	476.9	36.3	1.0762
1970	653.8	498.3	155.5	1.3119
1971	904.2	504.7	399.5	1.7915
1972	1360.0	615.3	744.4	2.2010
1973	1155.2	618.4	536.8	1.8681
1974	1491.7	756.5	735.2	1.9717
1975	942.0	827.3	114.7	1.1385
1976	730.0	1069.9	(339.1)	0.068

Source: Annual Report of the Comptroller, 1961-1976

TABLE I-3

Short-Term Debt as Percentage of Long-Term, Total Outstanding Debt
($ Millions)

Fiscal Year	Short Term Out-stand-ing	Long Term Out-Stand-ing	Total (1+2)	Short Term % of Long Term	Short Term as % of Total
1961	100.4	4176.0	4276.4	2.4%	2.3%
1962	127.5	4301.1	4428.6	3.0	2.9
1963	230.9	4427.7	4658.6	5.2	5.0
1964	315.8	4539.2	4855.0	7.0	6.5
1965	525.7	4704.5	5230.2	11.2	10.1
1966	466.7	5018.9	5485.6[b]	9.3	8.5
1967	634.9	5070.0	5704.9	12.5	11.1
1968	693.2	5044.0	5757.2[a]	13.7	12.1
1969	747.3	5080.2	5827.7	14.7	12.8
1970	1288.2	5235.9	6524.1	24.6	19.7
1971	2319.4	5635.3	7954.3	41.1	29.2
1972	2650.2	6380.0	9030.0	41.5	29.3
1973	2517.5	6916.3	9434.3[b]	36.4	29.3
1974	3415.9	7652.0	11067.9	44.6	30.7
1975	4540.4	7766.6	12306.7	58.5	36.9
1976	4866.7	7427.5	12294.2[a]	65.5	39.6

Source: Annual Report of the New York City Comptroller, 1961-1975

[a]Decrease in long-term debt.
[b]Decrease in short-term debt.

TABLE I-4

Comparison of Outstanding Debt and Legal Debt Ceilings
($ Millions)

Fiscal Year	Debt Ceiling[1]	Total Debt Outstanding	Borrowing, Beyond Limits		Unencumbered Margin[4]
1961	$2814.9	$ 4276.4	$1461.5	(51.9%)	341.8
1962	3548.2	4428.6	880.4	(24.8)	224.4
1963	3893.3	4658.6	819.3	(21.3)	156.7
1964	4100.9	4855.0	754.1	(18.4)	154.8
1965	4378.1	5230.2	852.1	(19.5)	279.3
1966	4607.0	5485.6	878.6	(19.1)	248.0
1967	4823.6	5704.9	881.3	(18.5)	587.4
1968	5497.6	5737.2	239.6	(4.4)	746.5
1969	5766.3	5827.7	61.4	(1.1)	458.6
1970	6251.8	6524.1	272.3	(4.4)	659.2
1971	6551.5	7954.7	1403.2	(21.4)	220.4
1972	6935.8	9030.2	2094.4	(30.2)	603.3
1973	7701.8	9434.3	1732.5	(22.5)	444.3
1974	8161.7	11067.9	2906.2	(35.6)	558.2
1975	8207.7	12306.7	4099.0	(49.9)	256.4
1976	8370.3	122994.2	3923.0	(46.9)	1098.2

[1] Debt Ceiling includes combined housing (2 percent) and general

[2] Total debt outstanding includes short term obligations; long term debt within and outside the combined (housing and general) ceiling.

[3] Borrowing bdyond limits shows outstanding debt in excess of limits; i.e., in 1963 outstanding debt equalled 121.3 percent of combined ceilings.

[4] Unencumbered margin includes unencumbered housing and general obligation capacity.

TABLE I-5

Growth of Capital Funding for Operating Budget, 1965-1976
($ Millions)

Year	Amount	Year	Amount
1965	26	1971	195
1966	57	1972	226
1967	68	1973	274
1968	68	1974	564
1969	84	1975	724
1970	151	1976	697

Source: Citizen's Budget Commission Inc.

TABLE II-1

Estimated Burden-Combined State and Local Big Three Taxes

At Various Income Levels

New York vs. National, City Averages

Income	Tax	U.S. Average	City Average	New York City
$ 7,500	Real Property	3.6%	6.6%	7.8%
	Personal Income	1.1	1.2	2.0
	Sales Tax	1.6	1.8	2.6
	Total	6.3	9.6	12.4%
		N.Y./U.S. = 197%	N.Y./CITY = 129%	
12,000	Real Property	3.4%	4.6%	5.4%
	Personal Income	1.8	2.0	5.4
	Sales Tax	1.4	1.6	2.3
		6.6%	8.2%	11.1%
		N.Y./U.S. = 168%	N.Y./CITY = 204%	
50,000	Real Property	2.5%	2.1%	2.2%
	Personal Income	3.7	4.3	11.1
	Sales Tax	0.7	0.8	1.2
		6.9%	7.1	14.5
		N.Y./U.S. = 210%	N.Y./CITY = 204%	

TABLE II-2

"Big Three" Tax Rates

New York City vs. Selected Metropolitan Areas

	New Jersey	Connecticut	Westchester County	New York City
Sales Tax Rate	5%	7%	5%[a]	8%[b]
Personal Income Tax	2%-2.5%	N.A.	2%-2.5%[c]	0.9%-4.3%
Property Taxes Per Capita[d]	228.09	514.85	233.72	338.32

[a]City/State combined tax. County rate is 1%.

[b]City/State combined tax. Each receives 4%.

[c]Westchester has no local income tax. Listed rates are for State income tax which is also paid by New York City residents.

[d]Calculated for 1974.

Source: Advisory Commission on Intergovernmental Relations.

TABLE II-3

After Tax Rate of Return Resulting from Expansion in Selected New York Sites (Hypothetical Industry)

	Nassau	Onondaga	N.Y.C	Schenecta
Arkansas	11.85	11.90	10.70	11.85
California	12.05	12.15	10.95	12.05
Connecticut	11.30	11.40	10.20	11.30
Indiana	11.80	11.85	10.65	11.80
Kansas	11.85	11.90	11.70	11.85
New Jersey	11.25	11.35	10.10	11.25
North Carolina	11.15	11.20	9.90	11.10
Ohio	11.25	11.30	10.10	11.25
Pennsylvania	12.15	12.25	11.05	12.15
Tennessee	11.25	11.30	10.05	11.20
Texas	11.00	11.05	9.70	10.95
Washington	11.10	11.20	9.90	11.10

Source: New York Economic Development Board. 1977

(Continued on following page)

TABLE II-3

After Tax Rate of Return Resulting from Expansion in Selected New York Sites (Hypothetical Industry)

	Broome	Chautauqua	Erie	Monroe
Arkansas	11.85	11.95	11.90	11.80
California	12.05	12.15	12.10	12.00
Connecticut	11.30	11.40	11.35	11.25
Indiana	11.80	11.90	11.80	11.75
Kansas	11.85	11.95	11.85	11.80
New Jersey	11.25	11.35	11.30	11.20
North Carolina	11.10	11.25	11.15	11.10
Ohio	11.25	11.35	11.30	11.20
Pennsylvania	12.15	12.25	12.20	12.10
Tennessee	11.20	11.35	11.25	11.20
Texas	11.00	11.10	11.00	10.95
Washington	11.10	11.25	11.15	11.05

Source: New York Economic Development Board. 1977

(Continued on following page)

TABLE A-1

COMPOSISION OF NYC SHORT-TERM DEBT

	TOTAL (100%)	RANS	BANS	TANS	BUD. NOTE	OTHER
1961	$ 88.4	%	%52.0	%42.7	% 5.3	% 0%
1962	100.4		51.5	40.6	7.8	0
1963	127.5		49.3	27.3	14.7	8.2
1964	230.9	12.7	45.3	24.5	14.0	3.5
1965	315.8	22.6	42.9	16.9	13.1	4.5
1966	525.7	9.6	58.0	21.5	4.5	6.4
1967	466.7	14.8	59.0	21.5		4.7
1968	634.9	13.5	58.2	21.3		7.0
1969	693.2	17.2	54.1	20.8		7.9
1970	747.3	41.7	36.3	13.2		6.1
1971	1288.2	47.3	25.3	8.9	13.3	5.2
1972	2319.4	44.5	25.9	8.8	17.4	3.6
1973	2650.2	35.2	38.0	10.5	12.2	4.1
1974	2517.5	52.6	26.6	9.3	9.0	2.5
1975	3415.9	56.4	34.6	8.8		0.2

Source: Annual Report of NYC Comptroller 1961-1975.

TABLE A-2

Growth of Short-Term Debt for Operating Expenses 1961-1975
($ Millions)

	TAN	% INCREASE	RANS	% INC.	BUDGET NOTES	% INCR.
1961	42.9	-	-	-	5.3	-
1962	51.8	20.8	-	-	10.0	88.7
1963	63.1	21.8	-	-	34.0	34.0
1964	77.4	22.7	40.0	-	44.1	29.7
1965	88.8	14.7	118.6	-	68.8	56.0
1966	100.3	13.0	45.0	-62.1	21.0	-69.0
1967	236.5	36.1	93.8	208.4	-	-100.0
1968	147.5	8.1	93.8	-	-	-
1969	155.5	5.4	128.8	37.3	-	-
1970	170.0	9.3	536.7	416.7	-	-
1971	206.0	12.2	1096.3	204.3	308.3	
1972	232.0	12.6	1180.0	7.6	460.8	49.5
1973	265.0	14.2	887.1	-24.8	308.3	-33.0
1974	317.0	19.6	1798.3	202.7	308.3	0
1975	380.0	19.1	2560.0	42.4	0	-100.0
1976*						

Source: Annual Report of NYC Comptroller, 1961-1975

*NYC has been unable to market notes, since fiscal 1975.

(-) None outstanding

TABLE B-1

Total Local Revenue by Major Sources, Fiscal 1976

($ Millions)

		Percent of Total
State Aid	$2,732.2	24.0%
Federal Aid	2,689.7	23.6
Total Intergovernmental	5,422.0	47.6
Locally Raised Revenue	5,948.0	52.4
Total Revenue	11,380.8	100.0

Locally Raised Revenue		Percent of Local Revenue
Real Property Taxes	2,966.6	49.9%
General Fund Revenue	2,981.4	50.1
Personal Income Tax	527.6	8.9
Sales Tax	445.1	7.5
General Corporation Tax	417.0	7.0
Stock Transfer Tax	269.8	4.5
Financial Corporation Tax	202.3	3.4
Commercial Occupancy Tax	197.9	3.3
Utility Tax	93.4	1.6
Water Charges	218.5	3.7
Forfeits, Fines, Penalties	107.3	1.8
Miscellenous	132.3	2.2
Other Revenue	368.8	6.2

Source: Annual Report of the NYC Comptroller 1975-76

TABLE B-2

New York City Revenue Structure 1961-1976
($ Millions)

	Total Revenue	Fed/State Aid	Local Revenue	Local Prop. Tax	General Fund Revenue
1961	2453.0	565.2(23.0)	1888.0(77.0)	1028.3(41.9)	861.0(35.1)
1962	2578.9	629.3(24.4)	1949.6(75.6)	1070.9(41.5)	879.4(34.1)
1963	2769.6	731.2(26.4)	2038.4(736)	1134.5(40.9)	905.7(32.7)
1964	3114.3	781.7(25.1)	2332.6(74.9)	1220.2(39.2)	1111.8(35.7)
1965	3327.7	875.2(26.3)	2452.5(75.7)	1313.9(39.5)	1138.6(32.2)
1966	3699.7	1317.1(35.6)	2382.6(64.4)	1409.4(38.1)	973.2(26.3)
1967	4561.4	1733.4(38.0)	2828.1(62.0)	1573.3(34.5)	1254.8(27.5)
1968	5273.8	2209.7(41.9)	3064.1(58.1)	1648.1(31.2)	1416.0(26.9)
1969	6140.4	2885.9(47.0)	3254.4(53.0)	1737.9(28.3)	1516.5(24.7)
1970	6568.8	3047.9(46.4)	3520.9(53.6)	1892.7(28.8)	1628.2(24.8)
1971	7437.0	3644.1(49.0)	3792.9(51.0)	2080.4(28.0)	1712.5(23.0)
1972	8528.9	4042.7(47.4)	4486.2(52.6)	2188.9(25.7)	2297.3(26.9)
1973	9466.1	4591.1(48.5)	4875.0(51.1)	2468.1(26.1)	2406.9(24.2)
1974	9956.8	4799.2(48.2)	5157.6(51.8)	2655.5(26.7)	2502.1(25.1)
1975	12001.0	6204.5(51.7)	5796.5(48.3)	2986.1(24.1)	2810.4(24.2)
1976	11380.8	5440.0(47.8)	5947.8(52.2)	2966.6(26.0)	2981.2(26.2)

Source: Annual Report of the New York City Comptroller 1961-1976

TABLE B-3

Trend of Real Estate Tax Collections

Fiscal Year		Year of Levy	First Year After Year of Levy	2nd Year After Year of Levy
1960-1961..	$1,057.354.083	95.91	1.58	0.25
1961-1962..	1,103,513,183	95.34	1.58	0.17
1962-1963..	1,163,347,557	95.57	1.40	0.20
1963-1964..	1,255,810,783	95.63	1.52	0.17
1964-1965..	1,350,022,870	95.59	1.43	0.16
1965-1966..	1,432,640,320	95.31	1.38	0.30
1966-1967..	1,587,662,912	94.04	2.44	0.27
1967-1968	1,661,299,588	94.22	1.91	0.31
1968-1969..	1,748.601,102	94.40	1.52	0.26
1969-1970..	1,101,471,k72	94.98	0.88	0.30
1970-1971..	2,089,650,042	94.25	1.25	0.19
1971-1972..	2,204,595,908	94.10	1.04	0.14
1972-1973..	2,468,676,173	93.38	0.85	0.11
1973-1974..	2,657,256,842	92.77	0.90	0.40
1974-1975..	2,897,460,153	90.38	1.66	....
1975-1976..	3,246,786,520	89.11	....	....

Source: Annual Report of New York City Comptroller 1975-1976

D 1

SUMMARY OF

THE CITY IN TRANSITION:
PROSPECTS AND POLICIES FOR NEW YORK

The Final Report of the
Temporary Commission on City Finances

June 1977

Summary

The central conclusion of the Final Report of the Temporary Commission on City Finances may be summarized as follows: The City of New York must be fundamentally reformed before its fiscal problems and the larger economic problems of New York City can be solved; incremental reform of the local governmental process will not suffice, even in the event that the State of New York and the Federal government assume increasing responsibility for functions performed by the City of New York.

Until the local private economy reaches a new equilibrium, the prospects for the City of New York and New York City will remain cloudy. Economic development represents the critical link between reform of the local governmental process and improvement of the larger city. Economic development is dependent upon increased investment.

While the developmental strategy proposed in the Final Report concludes that increased private investment ultimately holds the key to the city's future, its central focus is on the need to reform local public policies and managerial practices so that they promote rather than, as in the past, retard private investment. The developmental strategy is a broad plan for political action that will increase private investment in New York City by first increasing public investment.

The basic idea of the developmental strategy is that slack or uncommitted resources must be acquired and then invested by the City of New York in ways that promote the competitiveness of the local private and public economies. The City can acquire slack resources by reducing expenditures, improving management, and obtaining fiscal relief from the State and Federal governments. The City's investment of slack resources, if it is to promote long-term developmental needs rather than short-term maintenance needs, primarily should be for the purposes of tax cuts, debt reduction, and improvement of the City's infrastructure or physical plant.

The effect of the developmental strategy would be to make the City of New York's public policies and managerial practices more rational in an economic sense. In the past, particularly after the mid-1960s, the local political system behaved in an economically irrational fashion by attempting to contravene some fundamental economic forces. The attempt failed, as demonstrated by the onset of fiscal crisis in 1975. Further attempts to conserve the existing structure of local political costs and benefits also will fail.

The Final Report of the Temporary Commission on City Finances is divided into three parts. Part One identifies the causes of the fiscal crisis. Part Two analyzes New York City's prospects. Part Three contains recommendations for the future. In addition, three appendices are included in the Report. Appendix I lists the major recommendations of the Final Report. Appendix II summarizes the sixteen Interim Reports issued by the Commission between November 1975 and June 1977. Appendix III presents historical data on New York City finances.

A. Causes of the Fiscal Crisis

Part One of the Final Report examines the nature and causes of the City of New York's problems. The central finding is that the City's problems are not essentially fiscal but manifestations of deep-seated problems stemming from highly interactive developments in the socioeconomic structure of the city, intergovernmental relations, and the local governmental process. These three underlying causes are examined, respectively, in Sections II, III, and IV.

1. Socioeconomic Developments

The recent history of New York City as a socioeconomic entity is divided into three periods: an "equilibrium" period during the 1950s; a "modest growth" period during the 1960s; and a "depression" period which began in 1969 and has not ended. The composition, but not the size, of the city's population changed throughout the post-World War II era. The central characteristic of population change was the out-migration of largely white, middle-class New Yorkers and the in-migration of persons with lower incomes, less education, and different job skills. During the 1950s and 1960s, high birth rates and heavy in-migration offset the out-migration of an estimated two million New Yorkers and produced relative stability in the size of the population. However, when the local economy entered its depression period, the city began to lose large numbers of people for the first time in its history. Between 1970 and 1975, New York City's population declined 4 percent.

The composition of the local economy also changed throughout the post-World War II era. During the equilibrium period of the 1950s, decline in manufacturing was offset by growth in other sectors of the local economy, primarily the private service and financial sectors. The city's export base, those firms or individuals that sell their goods or services to customers located outside the city, continued its secular transformation from the production of goods to the production of services. In the 1960s, several forces combined to produce modest growth in the local economy: a very strong national economy; "one-shot" events, like Wall Street's "go-go" years, that boosted selected sectors of the private economy; and a substantial increase in local revenues and intergovernmental assistance that permitted large employment gains in the public sector, particularly in the local government. In the 1960-1969 period, almost 80 percent of the jobs added to the local economy were government jobs. However, when the 1969-1970 recession began, the city's economy started a sharp contraction that has not stopped. In the 1969-1977 period, employment has fallen nearly one-sixth from its historic high of 3.8 million to under 3.2 million.

Demographic change in New York City increased the share of persons who needed government services and decreased the share of persons able to finance government services. The effect of demographic change on the local public economy was offset somewhat by the modest growth of the local economy in the 1960s; however, the sharp contraction of the local economy after 1969 contributed to a serious imbalance in local government finances.

2. Intergovernmental Relations

The City of New York's unique intergovernmental problems were a major reason for its near-collapse in 1975. The City's unusually broad functional and financial responsibilities are not entirely the product of recent origin or Federal and State mandates. In the 19th century, partially in response to the needs of its huge immigrant population, the City initiated, among other things, municipal university and hospital systems. When consolidation of Greater New York City occurred in 1898, the City assumed the functional responsibilities of the five counties it now comprises as well as those of the old City of Brooklyn. The City entered the post-World Was II period with heavy service responsibilities plus a strong home-rule tradition that encouraged local functional and financial responsibility.

When the Federal government defined urban problems as a national responsibility in the 1960s under the general rubric of the Great Society, the City began to receive enormous amounts of new intergovernmental funds, particularly for social welfare programs. In the 1960s, the share of the City's expense budget funded by intergovernmental aid doubled from 23 percent to 46 percent. While intergovernmental aid permitted the City to expand services for its rapidly growing dependent population, it also put the City in a unique financial bind compared to other major American cities. The overwhelming share of Federal aid was provided through programs that required state matching grants (or state and local matching grants at the discretion of the state). The State of New York required local governments to finance higher shares of nonfederal costs than any other state in the nation. This requirement created an enormous financial problem for the City of New York, particularly in the areas of public assistance and Medicaid where the City was required to finance 25 percent of total program costs. In addition, the State mandated the highest welfare and medical assistance benefits in the country. State financing and benefit mandates, coupled with the "open-ended" nature of welfare and medical assistance programs, ensured enormously high social welfare costs for the City.

The effect of evolving intergovernmental programs was not limited simply to increasing the City's expenditures. Partly in order to finance its share of matching grant requirements the City substantially increased local taxes and engaged in heavy deficit financing. Also, the City began to reduce the share of local financial and manpower resources it allocated to the four most basic functions of local government: police, fire, sanitation, and education. Thus the effects of intergovernmental change compounded those of socioeconomic change, providing service-demanders with additional incentives to stay in or come to New York City and revenue-providers with additional incentives to leave.

3. <u>The Local Political Process</u>

Certain key policies and practices of the City of New York constituted, collectively, one of the underlying causes of the fiscal crisis. Between fiscal years 1966 and 1971, the City of New York's expenditures increased at an average annual rate of 15.9 percent compared to 8.6 percent in the 1961-1966 fiscal period and 10.2 percent in the 1971-1975 fiscal period. Rather than focus its attention on expenditure reduction, which always is difficult politically, the City sought to increase the supply of money by raising local taxes and borrowing beginning in the mid-1960s.

The City's tax policy gradually shifted the local revenue structure away from its traditional bases -- the real estate and sales taxes -- to more progressive and business-oriented taxes. Not surprisingly, this contributed to the exodus of people and businesses with the means to finance the local government and invest in the local economy. By 1974, municipal taxes in New York City were more than three times higher on a per capita basis than in Chicago and Los Angeles. Compounding the local tax burden was the fact that the State also had the highest per capita taxes in the nation.

The City's debt management policies also facilitated maintenance of existing expenditure commitments at the expense of important future interests. In the 1966-1971 fiscal period, the City's short-term debt jumped from less than $.5 billion to over $2.3 billion, and in the next four years it almost doubled to $4.5 billion. In the 1966-1975 fiscal period, short-term debt grew from 8.5 percent to 36.9 percent of total City debt. Long-term as well as short-term debt was used to sustain day-to-day operations. In fiscal year 1965, $26 million of operating expenses was capitalized; by fiscal year 1975, when the City's finances almost collapsed, $724 million of capital funds, over one-half of the entire capital budget, was used to finance operations.

The third important failure of the local political process was the City's loss of influence over both the compensation and management of its employees. In the 1966-1971 fiscal period, labor costs almost doubled from $2.1 billion to $4 billion. The largest percentage increases occurred in fringe and pension benefits rather than salaries. The cost of liberalizing pensions, of course, can be deferred into the future, as evidenced by the $8.5 billion of unfunded pension liability that exists today. However, the pay of City workers also increased rapidly, particularly in contrast to workers in the city's private sector. Between 1970 and 1976, during the worst years of the local depression period, real pay of patrolmen increased 10.3 percent, a higher rate of increase than during the largely expansionary 1965-1970 period. Real wages of selected private sector workers in the 1970-1976 period ranged from an increase of 4.5 percent to a decline of 7.9 percent.

The City's inability or unwillingness to moderate gains in the compensation of City employees in the midst of obvious (and increasing) financial scarcity resulted in a political, or managerial, trade-off of serious consequence when the City in the 1970s chose to finance negotiated wage and benefit increases by reducing the work force, particularly in the essential services.

During the 1971-1975 fiscal period, for example, local taxes for police services increased almost 50 percent, and compensation of individual police officers increased over 50 percent. The number of police officers, however, fell 2 percent, and the number of hours of police service actually delivered fell 4 percent.

The financial implications of the City's management failures were enormous. During the 1961-1975 fiscal period, the annual average increase in labor costs was 10.65 percent. If through a combination of slightly better collective bargaining and slightly more efficient management, the City somehow had been able to hold the average annual increase in labor costs to just one-half of one percent less than actually occurred, the City would have saved $1.9 billion cumulatively.

The socioeconomic and intergovernmental changes could be construed to support a "captive-of-events" theory of the fiscal crisis in which the City of New York is viewed as having little or no control over the events that caused the crisis. The "captive-of-events" theory is a popular interpretation that is true in some important respects. Certainly, the City of New York was incapable of influencing socioeconomic and intergovernmental change in a substantial fashion during the post-World War II era.

However, the "captive-of-events" theory also is popular because it tends to absolve the local political process of responsibility for the fiscal crisis and buttresses the also-popular view that solution to the City's financial problems lies in increased State and Federal aid rather than local political reform. The "captive-of-events" theory has a stronger political underpinning than it does a theoretical underpinning. Practices and policies of the City of New York also contributed substantially to the fiscal crisis, particularly in the post-1965 period: tax policies increased the financial incentives for mobile businesses and individuals to leave New York City; debt management and labor relations policies drove up the cost of local government (and thus local government taxes) and reduced the supply of essential public services, thereby diminishing the "quality of life" in New York City.

In order to understand better the extent to which the City of New York contributed to its own fiscal crisis, it is useful to examine the City's expenditure pattern in the year the fiscal crisis began, 1975. Over 85 percent of the City's total expenditures were for three groups -- the recipients of public and medical assistance benefits, 27.9 percent; City employees, 42.4 percent; and the holders of City bonds and notes, 14.9 percent. Mandated public assistance and medical assistance costs were $3.6 billion; but combined debt service and pension costs of $3.1 billion were not mandated in the same sense as welfare and Medicaid. Beyond that, the State and Federal governments picked up 75 percent of welfare and Medicaid costs. The overwhelming share of the $3.1 billion expenditure for debt service and pensions was provided from the City's own tax-levy funds. If the City had not bargained or borrowed so liberally, <u>or</u> if the Federal and State governments, particularly the latter, had not discriminated against the City with respect to welfare and Medicaid financing, the fiscal crisis would not have occurred in 1975 and perhaps never would have occurred.

B. Prospects for New York City

Part Two examines the same three factors analyzed in Part One from a prospective rather than retrospective basis. The assumption in Part Two is that the same factors that caused the fiscal crisis also will affect the future in important ways. Moreover, Part Two assumes planning should be based on reasonable assumptions about the future. Socioeconomic prospects, prospects for intergovernmental fiscal relief, and strategic policy options for the future are discussed in Sections V, VI, and VII, respectively.

1. <u>Socioeconomic Prospects</u>

Several important conclusions are reached concerning the city's socioeconomic prospects. First, the city's future is indeterminate. The view that the future of the city is not a foregone conclusion is contrary to the views of many, including pessimists who believe the city is either dead or dying and optimists who believe recovery is "right around the corner." Second, there is no reasonable basis to assume that the city's economy will experience a major recovery in the next decade. Third, there is a reasonable basis to assume that the decline of the local economy can be slowed significantly and perhaps even halted in the next decade.

Fourth, the City of New York can play a major role, positively or negatively, in determining the future of the local economy.

The fourth conclusion is critically important. The performance of the local economy is explained by two variables, the performance of the national economy and the "competitiveness" of New York City as a location for business enterprise. Three estimates of local employment in 1980 and 1985 are provided. In each estimate, the assumption about the performance of the national economy (slow recovery from the 1973-1975 recession) is held constant. The Commission's "most-likely" employment forecast assumes improvement of competitive conditions but of small proportions. Under this assumption, the 1976 employment level, 3.18 million, will fall to 3.105 million in 1980 and 3.05 million in 1985. Under the assumption that rapid deterioration of local competitiveness will continue, the low employment forecast was 2.99 million in 1980 and 2.78 million in 1985. However, if pronounced improvement in New York City's competitive position is assumed, the high forecast, employment will reach 3.27 million in 1980 and 3.32 million in 1985.

Most significant is the considerable variance between the high and low employment forecasts: 280,000 jobs in 1980 and 540,000 jobs in 1985. This does not mean, of course, that the City's policies alone can affect an employment swing of over one-half million jobs by 1985. Some factors that determine the competitiveness of New York City as a location for business activity are beyond the influence of the local government. However, many determinants of competitiveness are directly affected by the decisions of the City of New York: the "quality of life" in the city, including schools, other essential services, and the condition of the city's infrastructure; local tax, labor, rental and energy costs; and municipal budgetary conditions, to mention several.

Analysis of the city's socioeconomic prospects provides some important policy assumptions. On the one hand, there is no reasonable basis for policy-makers to assume that the local economy will experience a major recovery; on the other hand, there is strong evidence that policy-makers can substantially improve the performance of the local economy. However, it is clear that a reorientation of City policies is required if the City is to improve the local economy. The City's public policies and managerial practices, if not fundamentally changed, will continue to contribute to economic decline in New York City.

2. Intergovernmental Prospects

The prospects for major reform of intergovernmental relations in the next few years are not bright. Public assistance financing and medical assistance financing represent the two most important intergovernmental fiscal problems; neither appears likely to be resolved until at least the early 1980s. Other intergovernmental programs, particularly Federal programs, are yielding additional monies to the City but not in amounts required to improve materially either the City's fiscal problems or the performance of the local economy.

3. A Developmental Strategy for the City

If substantial change in the local economy or substantial reform of intergovernmental relations are not likely, the chances for correction of the City's fiscal problems are extremely low in the absence of substantial change in the local political system. Section VII introduces the Commission's developmental theory for the City of New York and contrasts it with two other strategic options, bankruptcy and decrementalism.

The developmental strategy would require reform of the local political process for the explicit purposes of improving the local economy and maximizing the impact of whatever additional intergovernmental monies the City receives. The nexus between the developmental strategy and improvement in the local economy is straightforward: by investing slack public resources in ways that promote the competitiveness of the local economy, private investment will increase. Increased private investment ultimately holds the key to stability in the local economy.

The developmental strategy does not assume that reform of intergovernmental relations is likely within the necessary time period. But in the event that fundamental reform of the intergovernmental system does occur, the developmental strategy does not see this as a sufficient basis for meeting the city's future investment needs without fundamental reform of the local political process also occurring.

The critical issue is the use to which the City of New York would put slack resources resulting from increased intergovernmental assistance. If slack resources are used in the future as they have been used in the past, that is, in an attempt to maintain an inherently imbalanced local governmental system, the long-term potential of intergovernmental reform largely and quickly will be dissipated. However, if slack resources are invested to promote the economy, intergovernmental reform will have a positive and enduring impact. This is why the City of New York must be fundamentally reformed before its fiscal problems and the economic problems of New York City can be solved; and why incremental reform of the local political process will not suffice, even in the event the State of New York and the Federal government assume increasing responsibility for functions provided by the City of New York.

Bankruptcy is the most radical of the three strategies. Its proponents assume that the City's fiscal problems are so enormous, and its adaptive potential is so limited, that judicial intervention is required. The Final Report concludes that, while bankruptcy may occur in the future, it is not presently a constructive option. First, it is not a democratic solution. Second, it would prevent the City from reentering the credit market for an extended period of time. Third, the substantial uncertainties about the formal and informal characteristics of bankruptcy suggest that it may not solve anything.

Decrementalism is the most conservative of the three strategies. It is also the prevailing strategy, primarily because it emphasizes change in intergovernmental relations and preservation of the existing governmental system in New York City. The decremental strategy clearly has roots in the "captive-of-events" theory of New York City's decline. Its underlying assumption is that fiscal reforms such as those implemented in the past two years, will buy the time required to restructure intergovernmental relations, thereby negating the need to change fundamentally the local governmental process.

The developmental strategy lies between the radicalism of the bankruptcy approach and the conservatism of the decremental strategy. Unlike the bankruptcy option, the developmental strategy assumes that the local governmental process still retains the capacity to adapt constructively to the larger developmental needs of New York City. Unlike the decremental option, the developmental strategy calls for fundamental reform and questions whether intergovernmental reform is a likely or sufficient basis for meeting the city's future investment needs. The developmental strategy emphasizes the interdependency of reform locally and intergovernmentally.

C. Developmental Policies for the Future

Sections VIII and IX identify three of the basic purposes to which slack resources should be invested -- tax reduction, debt reduction, and maintenance of the city's infrastructure. Sections X, XI, and XII examine the three principal means of acquiring slack resources -- management improvement, expenditure reduction, and increased intergovernmental fiscal relief through the assumption by the State and Federal governments of responsibilities presently assumed by the City.

1. Tax Reduction

Economic development considerations increasingly should inform local tax policy, and fiscal considerations, the historically dominant concern, should be less important. Three underlying principles must guide future tax policy. First, tax reduction must be substantial because of the size of existing tax disincentives. Second, tax reduction must be selective, aimed at those areas where stimulative effects will be greatest. Third, the commitment to tax relief must be long-term. The Commission's proposals represent a "bullet" approach to tax relief rather than a "shotgun" approach whereby small amounts of tax relief are distributed to relatively large numbers of taxpayers.

Five major tax reforms are proposed in the Report: (1) a five-year reduction in the corporate income tax from its present rate of 10.05 percent to 5.05 percent in order to reduce costs in and demonstrate the City's commitment to the core of its vitally important export base; (2) a substantial and immediate tax cut for manufacturers in order to stimulate goods production, which is particularly sensitive to local taxes; (3) phased elimination of rent control and rent stabilization in order to increase real estate taxes and improve the long-term quantity and quality of the city's housing stock; (4) elimination of discriminatory real property assessment practices that discourage investment in commercial and industrial properties and result in substantial subsidies by the owners of such properties to the owners of residential housing and vacant land; (5) reduction of the State personal income tax over the course of five years from its current rate of 15 percent on taxable incomes in excess of $25,000 to 10 percent on taxable incomes in excess of $15,000.

The basic purpose of the tax policies recommended by the Commission is to improve the competitiveness of New York City as a place in which to do business. The underlying assumption, of course, is that maintenance of existing taxes will diminish the existing business and individual tax base, thereby producing lower tax receipts and reduced private investment. The proposals concerning rent control and real estate assessment practices would, if implemented, increase local revenues, thereby providing some cushion against the short-term fiscal impact of the other tax cuts.

2. Debt Reduction and Infrastructure Maintenance

Prior to the fiscal crisis, the City had two basic debt problems, the total size of its outstanding debt and the huge amount of short-term debt that constantly needed to be rolled over because it could not be repaid. The ability of the Municipal Assistance Corporation (MAC) to convert a substantial amount of the City's short-term debt into long-term obligations of its own, plus the Federal seasonal financing program, have resolved the short-term debt problem, at least temporarily. However, the City's total outstanding debt, including MAC debt which is secured by City revenues, has increased over $1 billion since the beginning of the fiscal crisis.

The Commission recommends that the City pursue a debt management policy whereby it issues less debt each year than it amortizes. Reduction of outstanding debt in this fashion gradually will reduce debt service costs that inhibit the City's ability to provide essential services. Also, debt reduction will make it possible to reduce substantially real estate taxes, a key developmental goal that presently is frustrated by excessive debt service costs, over $2.3 billion in fiscal year 1977. Finally, reduction of outstanding debt will speed the City's return to credit markets at competitive interest costs.

The mechanism for reducing outstanding debt, each year borrowing a fraction of the amount that is amortized, requires linking the City's debt management to its capital budget process. The essential goals of reducing outstanding debt and maintaining the City's infrastructure are interrelated. New York City's infrastructure is one of its most important resources for the future. The city's physical plant badly needs the maintenance that was deferred during the post-1965 period when a substantial share of capital monies was diverted for operating purposes and the bulk of legitimate capital expenditures was for construction rather than renovation or maintenance.

In order to reduce outstanding debt, it is necessary to constrain the issuance of bonds (assuming, for the moment, that the City regains the ability to sell its bonds competitively). At the same time, the city's legitimate capital needs are enormous. In order to increase the likelihood of achieving both goals, the Commission recommends that the process of phasing out expense budget items from the capital budget be accelerated. The Commission also recommends that the focus of capital expenditure be on maintenance rather than new construction except in instances like the Convention Center where an important economic development interest would be served.

Finally, the Commission recommends that the Federal seasonal loan program be extended beyond the end of fiscal year 1978. If the developmental strategy recommended in the Final Report of the Commission is pursued, there is no reason why the extension of the Federal seasonal loan program should be dependent upon the extension of the statutory powers of the present Emergency Financial Control Board.

3. Management Improvement

The basic challenge facing management in the City of New York is to provide adequate services (which is essential to maintaining the "quality of life" in New York City) at reduced levels of expenditure (which is essential to freeing up resources for investment). Unfortunately, the key element in the City's retrenchment program, reduction of the municipal work force through a combination of attrition and layoffs, has negatively affected the City's work force in some basic ways. The collective impact of these changes greatly complicates the managerial challenge facing the City of New York. As a result of the City's policies since the beginning of the fiscal crisis, the work force is 21 percent smaller, older, less representative of the City's people in terms of race and sex, and better compensated than in 1975.

Four basic reforms must occur if the City is to be able to maintain services at reduced levels of expenditure. First, at the mayoral level, fiscal and managerial control must be centralized. Second, an effective management service must be created. Third, the formal and informal rules that govern the selection, training, and deployment of the work force must be modernized. In connection with this, the Commission recommends that the City develop a new municipal wage policy. City employees should receive general wage increases in return for the City's regaining managerial control over deployment and utilization of the work force. Fourth, experimentation in the means of organizing and delivering municipal services must occur.

To illustrate that management improvement can yield substantial savings while maintaining services, the Commission identifies eight reforms that, if implemented, would permit maintenance of police services at a savings of $100 million a year. The fact that none of the eight reforms has yet been accomplished even in the midst of fiscal crisis indicates that resistance to change in the City's managerial and bureaucratic processes is substantial.

4. <u>Expenditure Reduction</u>

Expenditure reduction is the second major method of acquiring resources for investment in the future. The City of New York lacks the resources to maintain its existing cost structure and functional scope. The most obvious area for expenditure reduction is the nearly $2 billion the City spends on the fringe and pension benefits of its employees. In the past two years, while the City was pursuing a conscious policy of reducing its work force and its services, only one substantial reduction has occurred in the fringe and pension benefits of City employees, a halving of the Increased-Take-Home-Pay (ITHP) benefit by which the City made its actuarial retirement systems virtually noncontributory for employees.

The Commission recommends the elimination of three pension benefits that cost the City a total of $135 million annually: the remainder of the ITHP benefit, the Heart Bill, and those union annuity funds that are not constitutionally protected. These three recommendations, if implemented, would reduce overall retirement costs by a modest 8 percent. Furthermore, five recommendations are made to reduce or eliminate selected fringe benefits that, if implemented, would save the City approximately $100 million annually.

The City's subsidy policies also are examined in the areas of mass transit and municipal hospitals, where the City's subsidy provides over one-quarter of revenues, and public housing. In all, the annual cost of City subsidies is nearly $600 million for these three functions. The strongest case that can be made for expenditure reduction in these areas is in the City's private and public hospital systems. Every independent study that has been made in recent years indicates the existence of excess bed capacity in New York City ranging from 4,000 to 7,000 beds. The closure of 5,000 beds, as recommended by the Commission, would reduce City tax-levy expenditures by $13 million to $37 million immediately (the range depends on whether individual beds or entire hospitals are closed). This could be done without adversely affecting patient care, and the savings would increase each year. One-half of the beds should be closed in the municipal hospital system, which has an occupancy rate of only 75 percent, and one-half should be closed in the proprietary and voluntary systems.

The Commission identifies approximately $300 million of expenditure reductions that should be made. While this is a substantial sum, expenditure reduction accomplished by functional load-shedding is a potentially more important area.

5. <u>Intergovernmental Reform</u>

The principal recommendation of the Commission in the area of intergovernmental relations is for assumption of local public assistance and Medicaid costs by the State and Federal governments. Ideally, both programs would be financed by the Federal government because of its inclusive, progressive tax structure and its ability to relate benefits to cost-of-living differences. Until this happens, and it appears to be something that will happen in the 1980s rather than in the 1970s the State of New York should assume gradually increasing shares of the City's welfare and Medicaid costs. While the State's finances are not trouble free, they are in much better condition than the City's.

Beyond the issue of the relative ability to pay, is the basic fact that the State of New York is responsible for the City of New York's financial problems to the extent that they reflect welfare and Medicaid costs. There are many areas in which the City of New York not only warrants criticism for its past and present failures and bears the primary responsibility for reform as well; in the areas of welfare and Medicaid, the State and Federal governments are responsible, not the City.

The Commission also recommends that the State assume the full cost of the senior colleges of the City University system. However, the University should remain an independent system oriented to the special higher educational needs of New York City. It is also recommended that the State honor its earlier decision to assume the cost of the local court system over a four-year period. Correction and probation services also should be assumed by the State, not only to improve the City's finances but to provide better over-all administration of the presently fragmented court, corrections, and probation systems in New York.

If the Commission's recommendations for intergovernmental reform are followed, over $1.2 billion in City expenditures would be absorbed by the State and Federal governments. Eventually, most if not all of these functional transfers will occur. The question is how fast they will occur.

With respect to the various Federal and State block grant programs, including revenue sharing, the City generally receives a fair proportion of funds. This is more the case with respect to Federal programs than it is to State programs. The most serious inequities in State programs concern aid to education and, less importantly, mass transit.

The conclusion of the Final Report examines the issue of whether or not the developmental strategy it proposes is politically viable. Pursuing the developmental theory involves a reordering of local political priorities. The developmental approach would engage the City of New York in policies that may not be rational in a political sense if the political values of the post-1965 period continue. How well public officials in the City, State and Federal governments are able to integrate economic and political rationality in the next few years will determine much about New York City's future.

In planning for the future, care should be taken not to define the city's recovery in terms of regaining the past. From the perspective of New York City, what it needs most from the City of New York are policies and practices that will contribute to the future rather than mistakenly attempt to recapture the past or even maintain the present.

Major Recommendations of the Temporary Commission on City Finances

The 22 major recommendations of the Commission for implementing its "developmental strategy" are as follows:

A. Tax Reduction

1. The City's General Corporation Tax should be reduced by one percentage point a year over the next five years from its present rate of 10.05 percent to 5.05 percent.

2. Tax reductions and credits for the city's manufacturers should be implemented. Specifically:

   a. The general corporation (business income) tax as it applies to manufacturers should be reduced from 10.05 percent to 5.05 percent immediately.

   b. The 4 percent sales tax on the purchase of machinery, equipment, fuel and utilities should be eliminated.

   c. A 5 percent investment credit against the general corporation (business income) tax should be instituted for the purchase of new manufacturing machinery, equipment and structures.

   d. The commercial rent occupancy tax should be reduced from its present effective rate of 7.5 percent to a flat 2.5 percent on all rentals in excess of $1,000 per annum.

   e. The exemptions from the property tax for newly constructed manufacturing facilities provided under the recently enacted Padovan-Steingut legislation should be increased to 95 percent of the assessed value added to the property, declining by 5 percent annually over 19 years from the present 50 percent exemption which declines by 5 percent annually over 10 years.

(more)

3. Rent control and rent stabilization should be eliminated. The City should move to eliminate assessment disparities that discriminate against commercial, industrial and apartment properties.

4. The maximum rate of New York State's Personal Income Tax should be reduced by one percentage point a year over the next five years from its present maximum rate of 15 percent on taxable income over $25,000 to 10 percent on taxable income over $15,000.

B. Improving Debt Management

1. The City should gradually reduce its outstanding debt by issuing less debt than it retires each year.

2. The Federal government should continue its seasonal financing program to the City of New York after June 10, 1978.

3. The State Legislature should reexamine the debt limits in the New York State Constitution to ascertain whether, in the light of the City's experience, they should be revised.

C. Improving the City's Infrastructure

1. The limited amount of funds available for capital expenditures in the coming years should primarily be used to rehabilitate and maintain the city's physical plant. Exception should only be made

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for projects like the Convention Center where new construction would provide a definite stimulus to the city's economic development.

2. The City should accelerate the rate at which it withdraws expense budget items from the capital budget.

D. Management Improvement

1. Fiscal and managerial control must be centralized in the hands of officials who are politically accountable.

2. The City must ensure that an effective managerial service is created.

3. The City's personnel policies should be reformed to enable it to deploy its labor force in as productive and cost efficient a manner as possible.

4. The City must support innovative means of organizing and delivering municipal services in ways that promote greater citizen responsiveness and lower costs.

E. Expenditure Reduction

1. The City's pension and fringe benefit systems should be revised. Specifically:

a. The Increased-Take-Home-Pay (ITHP) benefit should be permitted to expire by the State Legislature.

b. The Heart Bill should be permitted to expire by the State Legislature.

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c. Union annuity benefits should be ended.

d. Health insurance costs should be shared by the City and its employees at a 75-25 percent ratio while health insurance should be provided for retired employees only when they reach age 62.

e. Welfare fund benefits now provided to retired employees should be discontinued.

f. Uniform allowances should be reduced by one-half after five years for uniformed employees and three years for other municipal employees.

2. The City should consider methods of limiting the subsidies it presently provides for housing, mass transportation and the municipal hospital system.

3. The city's hospital capacity should be immediately reduced by 5,000 beds, one-half of which should be closed in the municipal hospital system and one-half in the city's private and voluntary hospitals.

4. The City should make substantial reforms in its leasing, purchasing and contracting procedures.

F. Intergovernmental Relations

1. The Federal and State governments should assume the cost of public assistance and Medicaid presently borne by the City.

2. The State should assume corrections and probation costs in conjunction with the four-year staged assumption of local court costs already in progress.

3. The State should move to assume the full cost of the City University system.

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4. The Federal government should commit itself to developing and implementing a comprehensive national urban policy to deal with the economic and social problems afflicting not only New York City, but cities everywhere in the nation.

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