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INTRODUCTION

This report assesses the debt condition of the City of New York ("the City") pursuant to Section 232 of the New York City Charter which requires the Comptroller's Office to render an opinion as to how much debt the City may soundly incur for capital projects during the current fiscal year and each of the three succeeding fiscal years.

The City exhausted its general debt limit in FY 98 and was able to finance its capital program only by dint of the new $7.5 billion debt-incurring power provided by the Transitional Finance Authority (TFA). Faced with the eventual exhaustion of the TFA's debt capacity in FY 00, the City has created a local development corporation, namely the Tobacco Settlement Asset Securitization Corporation (TSASC) to issue debt secured by proceeds from the settlement with the major U.S. tobacco companies. As a result, the Comptroller's Office estimates the City's debt-incurring power at $4.1 billion at the beginning of FY 00. By the beginning of FY 01, however, the City's debt-incurring power will drop to just under $3.0 billion. With capital contract registrations of more than $4.0 billion planned for FY 01, this debt-incurring capacity will fall short of what is required by the City to continue its Capital Program.

How best the City deals with this problem is still a matter of debate. One solution is to amend the State Constitution by redefining and expanding the general debt limit. While this option addresses the symptom of the City's general-debt-limit constraint, it worsens the underlying ailment of the growing debt, which has risen by 108 percent between FY 89 and FY 99. Another option is to raise the debt-incurring power of the TFA. But this solution also contributes to the City's growing debt problem, and may provide only temporary relief. Alternatively, the City can limit the growth of its debt by adopting a "pay-as-you-go" capital-financing program. But this option has pitfalls, since it takes budgetary resources away from operations.

This report also raises the issue of debt affordability. As debt service consumes a rising share of the City's budget, program choices become harder to fund. At $3.2 billion in FY 99, debt service consumed 15 cents of every tax dollar collected by the City. This was more than three times the Fire Department budget of $1 billion and over half of the City's contribution to the Board of Education budget. This pressure on the City's resources will only intensify if the currently favorable macroeconomic environment of low inflation, low interest rates, and robust growth were to turn unfavorable. Already rising commodity prices, a weakening dollar, and labor-market imbalances have raised concerns about inflationary pressures and have led the Federal Reserve to raise interest rates three times in 1999. Rising interest rates add to the City's borrowing costs and slow down the economy, which curbs tax-revenue growth.

Put simply, the City's growing debt and its related costs not only hamper the sustainability of the capital program, but also dictate budgetary decisions in a recessionary environment. The time to take preventive measures is now, when the City coffers are flush. This report proposes a number of solutions that address the City's need to provide adequate funding for its capital program, its debt-limit constraint, and its growing debt burden. Among the most prominent are: a pay-as-you-go capital program funded by non-recurring resources; a

debt-retirement program; and a mechanism to charge back debt service to individual agency budgets to encourage the use of current resources for maintenance to moderate the incidence of large future capital expenditures.

The report is presented in five sections. Section I profiles the City's debt outstanding and its institutional use. Section II provides a comparative analysis of the City's debt with that of 13 other large U.S. cities. Section III raises issues of the affordability of the City's debt. Section IV discusses the debt limit problem. Finally, Section V offers some potential solutions to the City's growing debt.

I. PROFILE OF NEW YORK CITY DEBT

This section examines the composition and uses of New York City (NYC) debt. For the period between FY 98 and FY 99, NYC debt has grown by 7.6 percent from $35.024 billion in FY 98 to $37.695 billion in FY 99.

A. Composition of Debt

At the end of FY 99, NYC debt totaled $37.695 billion, including general obligation bonds (G.O.), Municipal Assistance Corporation (MAC) debt, TFA debt, the Samurai Funding Corporation (SFC) debt, and capital lease obligations. (See Table 1.)

Table 1. *Gross City Debt Outstanding as of June 30, 1999 ($ millions)*

	General Obligation Bonds	**Municipal Assistance Corporation**	**Transitional Finance Authority**	**Samurai Funding Corporation**	**Capital Lease Obligations**	**Total Gross Debt Outstanding**
Tax-Exempt						
Fixed Rate	$23,383	$3,832	$3,180	-	$2,112	$32,507
Variable Rate	1,979	-	750	-	-	2,729
Derivatives*	218	-	-	-	-	218
Subtotal	$25,580	$3,832	$3,930	-	$2,112	$35,454
Taxable						
Fixed Rate	$962	-	$220	-	-	$1,182
Variable Rate	$899	-	-	$160	-	$1,059
Subtotal	$1,861	-	$220	$160	-	$2,241
Total	**$27,441**	**$3,832**	**$4,150**	**$160**	**$2,112**	**$37,695**
Percent of Total	**72.8 %**	**10.2 %**	**11.0 %**	**0.4 %**	**5.6 %**	**100.0 %**

*Derivative bonds are those bonds that derive their interest rate from an underlying financial instrument that is composed of an indexed formula.

Source: City of New York, Office of the Comptroller, Comprehensive Annual Financial Report, 1999, p. 266.

1. *General Obligation bonds,* which totaled $27.441 billion at the end of FY 99, account for 72.8 percent of total debt outstanding. The FY 99 G.O. debt represents an increase of $562 million over the FY 98 total, or 2.1 percent. The City pledges its full faith and credit to secure G.O. debt, which is limited by the State Constitution to ten percent of the average full value of taxable real estate for the most recent five years. In FY 98, the City nearly exhausted its debt-incurring power and prevailed upon New York State to create the TFA, whose debt is not subject to the general debt limit of the City.

2. *Municipal Assistance Corporation debt,* which totaled $3.832 billion at the end of FY 99, drops by $234 million from FY 98, or 5.8 percent. MAC debt accounts for 10.2 percent of the City's debt. MAC was created by the State in 1975, following the City's fiscal crisis.

MAC's role was to provide financing assistance for the City by issuing bonds and notes for the purpose of paying or loaning the proceeds of such sales to the City and to exchange the Corporation's obligations for those of the City. MAC also monitors and reviews the City's finances. MAC debt is secured by the City's share of the State sales tax derived in the City, the stock transfer taxes, and State per capita aid. MAC is not covenanted to issue new debt; its debt outstanding will continue to decline until final maturity on July 1, 2008.

3. *Transitional Finance Authority* debt totaled $4.150 billion at the end of FY 99, an increase of $2.0 billion over FY 98, or 93 percent. TFA debt represents 11 percent of the City's debt. TFA debt is secured by a first lien on personal income tax collections. Because TFA debt is not an obligation of the City, it is not included in the computation of the City's general debt limit. The TFA enabling legislation recognizes the need for $12 billion in debt-incurring capacity, but the State Legislature authorized only $7.5 billion.

4. *Capital Lease Obligations* rose by 22.2 percent in FY 99 to $2.112 billion, or 5.6 percent of total debt outstanding. The City is required to make annual appropriations from its general fund for its capital lease obligations. These leaseback obligations are included in the City's outstanding debt, but are excluded from the City's indebtedness when calculating outstanding debt under the general debt limit as stipulated in the State Constitution. Capital lease obligations cover such issuers as the Dormitory Authority of the State of New York for the New York City Courts Program ($409 million), the City University Construction Fund ($436 million), the Education Construction Fund ($150 million), the Primary Care Development Corporation ($353 million), the Housing Finance Agency ($264 million), the Urban Development Corporation ($54 million), and general city lease obligations ($445 million).

Additionally, independent authorities have financed a large number of capital projects in the City. Among the most prominent are the New York City Municipal Water Finance Authority (NYWFA), the Metropolitan Transit Authority (MTA), and the Port Authority of New York and New Jersey (PA). These authorities issue bonds secured by the pledge of certain revenues and user fees. (See Table 2.)

As the financing arm of the New York City Water Board, NYWFA funds the Department of Environmental Protection's capital program, which is responsible for the maintenance and operation of the City's water and sewer system. The NYWFA had $9.372 billion of debt outstanding as of June 30, 1999, an increase of $491 million or 5.5 percent from June 30, 1998. This debt is secured by revenues from water and sewer user fees.

The MTA is composed of four major agencies, including the New York City Transit Authority (NYCTA), the Long Island Railroad (LIRR), the Metro-North Railroad (MNR), and the Triborough Bridge and Tunnel Authority (TBTA). With $13.064 billion in debt outstanding as of June 30, 1999, including $4.883 billion for the TBTA, the MTA has the most debt outstanding of the three major independent authorities. MTA debt is, in general, secured by a combination of passenger revenue and other governmental funds.

Table 2. *Independent Authorities in New York City: Debt Outstanding as of June 30, 1999 ($ millions)*

	Water Finance Authority	**Metropolitan Transit Authority**	**Port Authority of New York and New Jersey**
Tax-Exempt			
Fixed Rate	$8,050	$12,314	$5,736
Variable Rate	1,322	750	937
Subtotal	$9,372	$13,064	$6,673
Taxable			
Fixed Rate	-	-	$49
Variable Rate	-	-	-
Subtotal	-	-	$49
Total	**$9,372**	**$13,064**	**$6,722**

Sources: The New York City Municipal Water Finance Authority, Metropolitan Transportation Authority and Port Authority of New York and New Jersey.

The PA is a municipal corporate instrumentality of the States of New York and New Jersey. It operates and finances, among other things, certain interstate crossings, tunnels, and harbor projects. Only a portion of the PA's debt is related to capital projects completed in New York City. The PA had $6.722 billion in debt outstanding as of June 30, 1999, an increase of $351 million or 5.5 percent from June 30, 1998.[1]

B. Institutional Use of Debt

The City uses its bond proceeds to build and rehabilitate schools, roads and bridges, correctional and court facilities, etc. In recent years, education has become the top capital priority of the City as a large share of its bond proceeds is allocated for education purposes. At June 30, 1999, debt used to finance capital projects for educational purposes accounted for 24.5 percent of G.O. debt outstanding, followed by housing at 14 percent, mass transit at 9.8 percent, and roads and bridges at 8.9 percent. Debt outstanding for correctional facilities, court facilities, the Police Department, and Fire Department accounted for 7.9 percent. (See Table 3.)

[1] Data provided by the Treasury Department, Division of Debt Management of the Port Authority of New York and New Jersey.

Table 3. *Use of G.O. Debt*

Categories	Debt Outstanding as of June 30, 1999*** ($ millions)	Percent of Total	Debt Outstanding as of June 30, 1989 ($ millions)	Percent of Total
Education	$6,766	24.5 %	981	8.6 %
Housing and Urban Development	3,854	14.0	1,095	9.6
Mass Transit	2,693	9.8	1,586	13.9
Bridges, Tunnels, Highways and Streets	2,440	8.8	1,152	10.1
Public Safety, Correction and Courts	2,177	7.9	1,023	9.0
Sanitation	1,447	5.3	777	6.8
Parks, Recreation and Culturals	1,232	4.5	431	3.8
Water Pollution Control, Water Mains and Sewers*	950	3.4	1,673	14.7
Health Services	783	2.8	432	3.8
Public Buildings	789	2.9	276	2.4
Social Services	394	1.4	96	0.8
Off-Street Parking, Airports, Ferries and Markets	289	1.0	261	2.3
Undistributed and Other	3,787	13.7	1,629	14.3
Total**	**$27,601**	**100 %**	**$11,412**	**100.0%**

* Represents debt issued for water and sewer purposes prior to June 30, 1985.
** Includes $160 million of Samurai Funding Corporation Bonds and excludes MAC, TFA, and Capital Lease obligations.
*** Over the past two years the TFA has supplanted much of G.O. borrowing and has issued $4.150 billion of bonds. The Chart above does not include debt issued by the TFA.
Sources: City of New York, Office of the Comptroller, Comprehensive Annual Financial Report, 1999, and the Office of Management and Budget, Adopted Budget Debt Service Statement II, FY 2000 and FY 1990.

Dictated by overcrowded classrooms, the City had to increase the share of its capital program dedicated to schools. Education, which accounted for only $981 million of G.O. debt outstanding in FY 89 or 8.6 percent, has risen to $6.776 billion or 24.5 percent of debt outstanding in FY 99. Another area that experienced a significant increase is Housing and Urban Development. Housing's share has increased to a 14 percent share in FY 99 from 9.6 percent in FY 89. On the other hand, Mass Transit has decreased to 9.8 percent in FY 99 from 13.9 percent in FY 89.

Since FY 86 capital expenditures for DEP are no longer financed by G.O. bonds; thus DEP's share of G.O. debt will continue to decline until its final G.O. maturity on or about FY 2023. For the category on table 3, "Water Pollution Control, Water Mains and Sewers", in FY 99 its share of the total decreased to 3.4 percent or $950 million from 14.7 percent or $1.673 billion in FY 89. NYWFA finances the majority of DEP's capital projects, but since 1986 its debt is not considered legally part of the City's debt.

II. COMPARISON WITH OTHER SELECTED MUNICIPALITIES

New York City has the largest population of all the cities in the U.S., and it must maintain the most complex and aging infrastructure in the nation. Given its population size, it has more school buildings, firehouses, health facilities, community colleges, roads, bridges, libraries and police precincts than any other municipality in the country. Moreover, the City has responsibilities that in other cities are distributed more broadly among states, counties, unified school districts and public authorities.

In order to compare the level of NYC's debt with other large cities, the data must be adjusted appropriately. In this section, the City is compared with 13 other large U.S. cities. For each City, relevant county and school district information was included to derive comparable debt-per-capita statistics. The debt-per-capita statistics for each municipality have been uniformly calculated from each City's Comprehensive Annual Financial Report (Annual Report) using data from the table typically entitled "Direct and Overlapping Debt Outstanding." At $4,400 debt per capita, New York is 2.7 times the sample city average and 1.76 times the city with the next highest level of debt per capita. The cities of Minneapolis and Chicago are a distant second and third at $2,501 and $2,320, respectively. (See Table 4.)

Table 4. *Debt Per Capita Measures for Selected Cities, 1998*

City	Population	Direct and Overlapping Debt Outstanding* ($ 000)	Debt Per Capita*
Minneapolis	368,383	$921,487	$2,501
Chicago	2,783,726	6,459,526	2,320
Philadelphia	1,451,372	2,988,863	2,059
Detroit	1,000,272	1,730,188	1,730
Seattle	539,700	876,163	1,623
Las Vegas	448,000	709,775	1,584
Houston	1,841,000	2,832,375	1,538
Phoenix	1,238,120	1,841,807	1,488
Los Angeles**	3,722,500	5,415,496	1,455
Boston	558,000	654,374	1,173
Dallas	1,052,300	1,176,179	1,118
San Diego	1,224,848	1,296,160	1,058
San Francisco	788,297	818,794	1,039
Average of All Other Cities***	1,308,963	$3,330,312	$1,629
New York City#	7,342,636	$32,304,000	$4,400

* This table is based on data from each city's Comprehensive Annual Financial Report. While diligence was used to render comparable results, the Comptroller's Office cannot guarantee, in every case, that the data are complete.
** This represents an estimate of the City of Los Angeles June 30, 1998 condition from Table 37 in the Official Statement dated July, 1998.
*** Figure represents a population-weighted average.
# This reflects assets on hand at fiscal year-end, which reduce gross debt outstanding.
Source: Comprehensive Annual Financial Reports from the cities listed.

Certain factors might explain some of the large divergence between NYC's debt-per-capita and that of the other large sample cities. One prominent factor is NYC's high cost of labor, which contributes to its high cost of capital projects. For August 1999, for example, non-seasonally adjusted hourly earnings for the construction sector in New York City was $29.46 per hour compared with the national average of $17.27, or roughly 71 percent higher than the national average.

Although the City's debt per capita is the highest of all the cities sampled, the debt per capita of eight cities grew at a faster rate than that of New York City for the period between 1988 and 1998. San Diego grew the fastest at 466 percent, followed by Las Vegas at 446 percent. (See Table 5.)

Table 5. *Debt Per Capita Comparisons for Selected Cities – 1988 and 1998*

City	Debt per Capita in 1988	Debt per Capita in 1998	Percent Change 1988-1998
San Diego	$187	$1,058	465.8 %
Las Vegas	290	1,584	446.2 %
Los Angeles*	435	1,455	234.5 %
Minneapolis	825	2,501	203.1 %
San Francisco	344	1,039	202.4 %
Phoenix	594	1,488	150.6 %
Chicago	953	2,320	143.4 %
Philadelphia	851	2,059	141.9 %
Boston	701	1,173	67.2 %
Seattle	986	1,623	64.6 %
Detroit	1,156	1,730	49.6 %
Houston	1,189	1,538	29.4 %
Dallas	1,213	1,118	-7.9 %
Average of All Other Cities**	$767	$1,629	112.4 %
New York City	$2,041	$4,400	115.6 %

* City of Los Angeles information from Table 37 of their official statements.
** Represents a population weighted average.
Source: NYC Comptroller's Office, based on Comprehensive Annual Reports and/or official statements of various cities.

Other Cities Complement G.O. Debt with User Fee Supported Bonds

Many of the cities surveyed dedicate specific revenues to finance a portion of their capital program, using mechanisms as diverse as School Finance Authorities, Park Districts, Hospital Districts, Community College Districts, Parking Authorities, Street and Highway User Revenue Bonds, Airport Revenue Bonds, Stadium Authorities, Sanitation Districts and Library Districts. Of the 13 cities sampled, general obligation bonds comprise approximately 44 percent of total debt issued in comparison with New York City's estimated 67 percent.[2] In addition, all the other cities make use of enterprise funds or special revenue funds. Enterprise funds are defined as those funds which are used to account for operations that are financed and operated in a manner similar to private business enterprises. Typically, it is the intent of the governing body where the

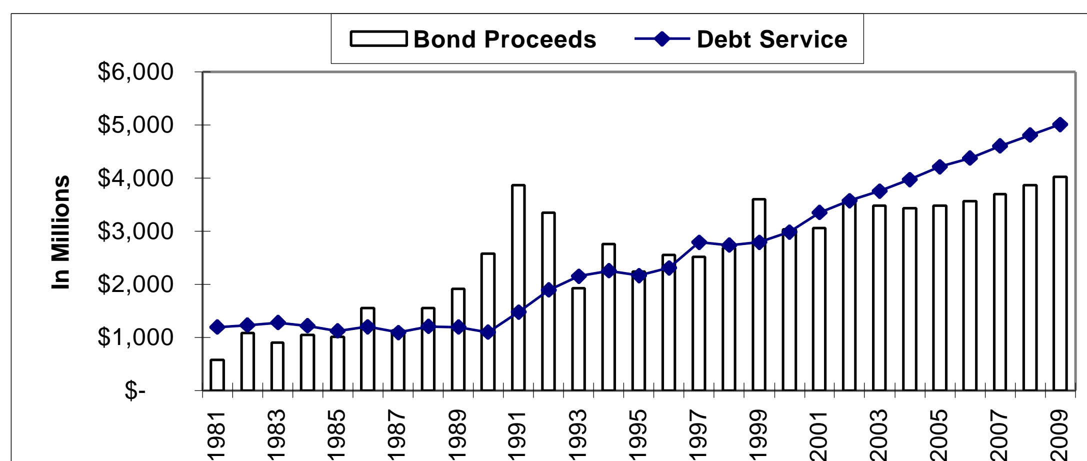
[2] The ratio of G.O. to total debt includes the NYWFA and TFA debt.

provision of goods or services to the general public is financed or recovered primarily through user charges. Revenue funds are defined as funds used to account for the proceeds of specific revenue sources, other than debt service, trust funds or capital projects, that are legally restricted for specific purposes. These revenues need not be user fee based and are often federal grants, community development block grants and revolving funds.

III. AFFORDABILITY OF CITY DEBT

Driven largely by the need to keep the City's infrastructure in a state of good repair after years of neglect following the 1970s fiscal crisis, the City undertook a very ambitious capital program in the 1990s. Borrowing to finance the City's capital program, which averaged $988 million between FY 78 and FY 89, jumped to a yearly average of $2.8 billion in the 1990s that has resulted in a large increase in debt service. (See Chart 1.)

Chart 1. *Bond Proceeds and Debt Service, FYs 1981-2009*



Sources: City of New York, Office of the Comptroller, Comprehensive Annual Financial Reports, 1981-1999 and Office of Management and Budget, FY 00 Adopted Financial Plan, June 1999.

On July 1, 1999, the City's total debt outstanding was $37.396 billion, an increase of 108 percent over FY 89.[3] Annual debt-service payments are expected to increase by approximately 6.3 percent between FY 99 and FY 08, rising to $4.814 billion in FY 08 from $2.789 billion in FY 99.[4] Even after adjusting for the effect of population changes and the relatively strong assessed value of taxable real property, debt grew at robust rates. Debt per capita, which amounted to $2,202 in FY 89, has risen to $4,667 in FY 99, an increase of 112 percent. The City's high level of indebtedness raises some serious questions about its affordability. The real estate tax is the primary source of funds used to pay debt service. From 1989 to 1999, billable assessed value of taxable real property – the basis of the real estate tax – has grown at an average annual rate of 2.65 percent, which is 3.9 percent less than the rate of growth of debt.[5] Consequently, the ratio of debt to assessed value of taxable real property stood at 42.2 percent in FY 99, up from 25.4 percent in FY 89. (See Chart 2.)

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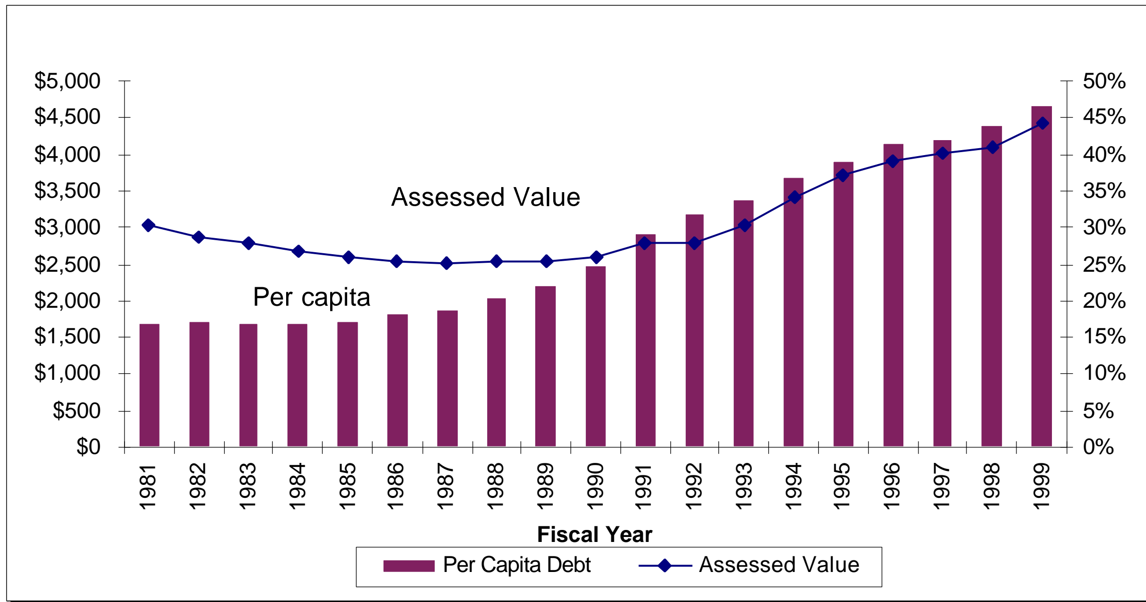
[3] This includes $4.15 billion of debt issued by the TFA, capital lease obligations of $2.112 billion and $297.7 million of U.S. Treasury securities that reduce debt outstanding from approximately $37.7 billion to approximately $37.4 billion.

[4] Adjusted for prepayments and excluding debt-service payments on debt issued by MAC, the repayment of interest and principal on short-term notes, debt service on debt issued by the NYC Municipal Water Finance Authority, and debt service on lease-purchase debt, but includes projected G.O., TFA, and the TSASC debt service.

[5] Assumes total gross debt of $19.98 billion in FY 89 compared with $37.7 billion in FY 99.

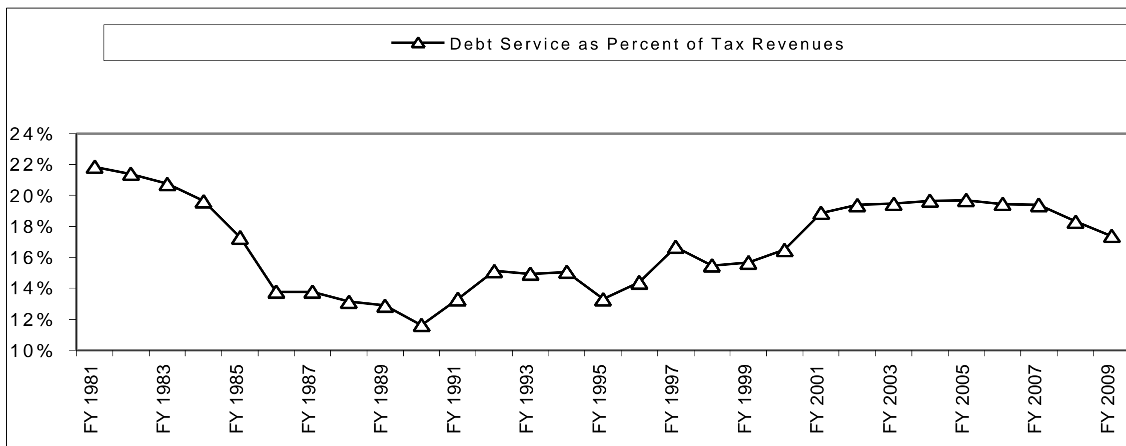
Chart 2. *Debt Per Capita and Debt as a Percentage of Assessed Value of Taxable Real Property*



Source: City of New York, Office of the Comptroller, Comprehensive Annual Financial Report, FY 1981-1999.

Another measure of affordability is the ratio of debt service to tax revenues, which indicates the share of tax revenues that is consumed by debt service. The City's tax revenues, fueled by a robust economy, have grown at an average annual rate of 4.0 percent between 1989 and 1999. But G.O. and TFA debt service, after adjusting for prepayments, has expanded faster at 8.9 percent a year. This is in spite of the City's aggressive refinancing program to take advantage of low interest rates without increasing debt-service costs in future years. As a result, the ratio of debt service to tax revenues is approaching levels not experienced since the aftermath of the fiscal crisis of the 1970s. The ratio of debt service to tax revenues reached 15.2 percent in 1999 from its low of 11.6 percent in FY 90, and is forecast to reach 19.5 percent by FY 03. (See Chart 3.)

Chart 3. *Debt Service as a Percent of Tax Revenues, FYs 1981-2009*



Sources: City of New York, Office of the Comptroller, Comprehensive Annual Financial Reports, 1981-1999 and Office of Management and Budget, FY 00 Adopted Financial Plan, June 1999.

IV. DEBT LIMIT

The growing level of the City's debt raises questions on the sustainability of its capital program. The City has exhausted its general debt limit and has relied on creative financial solutions like the TFA and the TSASC to provide short-term answers to a systemic problem. Even with the addition of the TFA and TSASC, the City will run out of debt-incurring power sometime in FY 01.

A. City Debt-Incurring Power

New York City's general debt limit, as stipulated in the New York State Constitution, is calculated as 10 percent of the 5-year average of the full value of taxable real property. Excluding the debt-incurring power provided by the TFA, the City had exhausted its general debt limit by $3.6 billion at the beginning of FY 99 and $5.8 billion at the beginning of FY 00.

Table 6 depicts the Comptroller's Office forecast of the debt-incurring power at the beginning of each fiscal year beginning with FY 01.[6] Estimates of the City's debt-incurring power on July 1, 2000 (FY 01), July 1, 2001 (FY 02), and July 1, 2002 (FY 03) are based on preliminary data provided by the State Office of Real Property Services (SORPS). Following a trend that began in FY98, the City's general debt-incurring power is projected to be: $30.746 billion in FY 01, an increase of 4.8 percent over FY 00; $32.248 billion in FY02, an increase of 4.9 percent over FY 01; and $33.927 billion in FY 03, an increase of approximately 5.2 percent over FY 02.

Excluding the debt-incurring power of the TFA and TSASC, the City has exceeded its general debt limit by $5.814 billion at the beginning of FY 00 and it is estimated that it will exceed its general debt limit by $6.909 billion at the beginning of FY 01, by $8.146 billion at the beginning of FY 02, and by $8.761 billion at the beginning of FY 03.

B. City's Short-Term Solutions to the Exhaustion of the General Debt Limit

The City has pursued a number of strategies to circumvent the constraint imposed by the general debt limit. Upon request of the City, the State created the TFA, which provided $7.5 billion of debt-incurring power. By the end of FY 99, the City had used $5.9 billion in TFA debt capacity or 78.6 percent of the total. Thus, $1.6 billion or 21.4 percent of TFA debt-incurring capacity remains available as of July 1, 1999. Before the end of FY 00, the $7.5 billion debt capacity of the TFA will be exhausted.

In order to ensure that the City's capital program continues unabated in the near term, the City is using the proceeds from the tobacco settlements to secure bonds issued by the TSASC. TSASC is planning to issue $2.8 billion in debt, but the City is expecting to realize an estimated

[6] General Debt Limit projections are based on data provided by the State Office of Real Property Services (SORPS).

Table 6. *NYC Debt-Incurring Power ($ millions)*

	July 1, 1999	**July 1, 2000**	**July 1, 2001**	**July 1, 2002**
Gross Statutory Debt-Incurring Power	$29,332	$30,746*	$32,248*	$33,927*
Actual Bonds Outstanding as of June 30, (net) **	26,542	25,451	24,214	22,868
Plus: New Capital Commitments				
FY 2000***		3,765	3,765	3,765
FY 2001***			4,101	4,101
FY 2002***				3,640
Less: Appropriations	(1,093)	(1,241)	(1,351)	(1,337)
Subtotal: Net Funded Debt Within the Limit	25,449	27,975	30,729	33,037
Plus: Contract and Other Liability****	9,697	9,680	9,665	9,651
Subtotal: Total Indebtedness Within the Limit	35,146	37,655	40,394	42,688
Exceeded Debt-Incurring Power within the General Debt Limit	(5,814)	(6,909)	(8,146)	(8,761)
Plus: Total Authorized TFA Debt-Incurring Power	7,500	7,500	7,500	7,500
Remaining Debt-Incurring Power within General Limit and TFA Capacity #	1,686	591	(646)	(1,261)
Plus: Total Authorized TSASC Debt-Incurring Power	2,400	2,400	2,400	2,400
Remaining Debt-Incurring Power within General Limit, TFA Capacity, and TSASC Capacity	4,086	2,991	1,754	1,139

* Based on preliminary data from the State Office of Real Property Services.

** Net adjusted for Original Issue Discount, Capital Appreciation Bonds, G.O. bonds issued for the water and sewer system, and Business Improvement District debt.

*** Reflects Capital Commitments as of the FY 00 Adopted Commitment Plan and includes cost of issuance and Inter-fund Agreements.

**** Contract liability is increased by $4.103 billion financed by TFA debt.

The Debt Affordability Statement released by the City in April, 1999 presents data in an end-of -year format in lieu of the beginning-of-year format in this table. In FY 01, for example, the City forecasts that the debt-limit would be exceeded at the end of the fiscal year by approximately $1.8 billion.

$2.4 billion in debt-incurring power depending on interest rates at the time of the sale of the remaining three bond issues. The discrepancy is attributable to the funding of a liquidity reserve and capitalized interest. The TSASC's additional debt-incurring power afforded the City the ability to register capital contracts for almost two fiscal years. Sometime in FY 01, the City will run out of debt capacity as contracts of $4.1 billion projected for FY 01 exceed the projected debt-incurring capacity on July 1, 2000 of $2.991 billion.

The TSASC incurs debt to finance the City's capital program, but remains as a separate legal entity. The TSASC issued its first bonds in November 1999 for a par value of $709.3 million and received net proceeds of $603.7 million. The $105.6 million difference is

attributable to: 1) $53.7 million for a liquidity reserve account; 2) $28.6 million for capitalized interest costs; 3) $8.3 million in original issue discount; 4) $5.0 million for underwriter's discount; and 5) $10 million in structuring fees and costs of issuance. The TSASC is scheduled to make three subsequent bond issues, each in the range of $700 million. The bonds of the TSASC are secured by revenues from the Master Settlement Agreement (MSA) with certain tobacco companies, including Philip Morris, R. J. Reynolds, Brown and Williamson, and Lorillard. The MSA, approved in November 1998, is a tobacco industry-wide settlement of litigation between the settling states and the participating manufacturers (PMs). Under the MSA the PMs are required to make five initial payments ranging from $2.4 billion to $2.7 billion each January 10, 2000 through 2003. The first of which, in an amount of $2.4 billion, was deposited with an escrow agent in December 1998. The PMs are required to make annual payments, inclusive of the initial payments, ranging from $4.5 billion in 2000 and increasing annually, up to $9 billion in 2018 and thereafter. The State of New York is projected to receive 12.762 percent of total annual payments, with the TSASC estimated to receive 26.67 percent of the State's share.

C. City's Long-Term Solutions to the Debt Limit Problem

Currently, the City is analyzing different options to deal with its debt-limit problem. One of the options involves an amendment to the State Constitution that would add 10 percent of total New York City personal income to the general debt limit. New York City personal income, estimated at about $290 billion in FY 00, would raise the limit by approximately $29 billion. Approval by two separately elected State Legislatures and ratification of the amendment by the citizens of New York would be required. Therefore, the additional debt-incurring capacity granted by the proposed amendment could not be implemented until January 2002.

Another option involves raising TFA's debt-incurring capacity. This solution requires an amendment to existing legislation. Although the TFA was authorized in March 1997 with a debt-incurring power of $7.5 billion, the indenture provided the authority to amend the TFA's debt-incurring power up to $12 billion of senior bonds without impacting its covenant with bondholders.

V. RECOMMENDATIONS

As stated in the Comptroller's Infrastructure and Capital Needs Report ("Dilemma in the Millenium", August 1998), in order for the City to bring its major physical assets to a state of good repair and address new capital needs, the City would have to spend money far in access of what is outlined in the City's current Ten-Year Capital Strategy. Though this report calls for either restraint in the City's capital program or a curtailment of its debt, the incongruity between needs and resources can be best dealt with during prosperous years when budget surpluses can be used as part of a pay-as-you-go capital program or a debt-retirement program. If nothing is done during years of record budget surpluses, the City's growing debt will impose severe future pain if the City's economy enters a recession. A debt-service burden that seems manageable in good times may become unbearable in bad times. Thus far, the City's focus has been entirely on its

ability to finance its capital program. Consequently, nearly all solutions that have been proposed address ways and means around the debt-limit constraint. The City can improve its debt position by adopting one or more of the following four recommendations.

A. Pay-As-You-Go Capital Financing Account

Currently, the City's capital program is financed exclusively by the issuance of bonds. Sound practice would be to set aside 5 to 10 percent of annual budget surplus and proceeds from bond refundings, asset sales, and tax-lien sales for pay-as-you-go capital. If a modest portion of the City's Ten-Year Capital Program were funded by a pay-as-you-go program, such as $200 million per year for ten years, the City would recoup its $2.0 billion investment from the operating budget with cumulative debt-service savings by the year 2016. It would thereby achieve overall cumulative debt-service savings of approximately $4.4 billion by 2039.

The use of pay-as-you-go financing is not unprecedented. The State of New York and municipalities such as Chicago, Dallas, Seattle, and San Diego use such a mechanism to fund a portion of their capital expenditures. In FY 81, barely out of the grip of the fiscal crisis, the City included $147 million in its operating budget for capital purposes.

Critics of such a program traditionally argue that current operating resources are simply not available to pursue this endeavor. This argument carries less weight when the City is recording historically high budget surpluses.

B. Charging Debt Service to Agencies

Under current practice, debt service is appropriated to a central account, namely the debt-service fund, and debt-service costs for a particular agency's capital projects are charged to that account. This procedure at times encourages agency heads, faced with competing demands for resources, to defer maintenance of assets. Deferred maintenance has resulted in the deterioration of assets, ultimately necessitating their replacement or rehabilitation that has to be funded from the City's capital budget at a much greater cost than maintenance would have cost. Charging debt service to City agencies for capital work they undertake might encourage them to provide adequate funding for maintenance, thereby reducing the incidence of unnecessary capital expenditures.

C. Repeal of the Wicks Law

The Wicks Law is out-dated and costs the City money. When capital projects are $50,000 or greater, the Wicks Law requires that the City issue four separate contracts for electrical work, plumbing, heating, ventilation, and air conditioning, and all other services. The Wicks Law adds approximately 13 percent to the cost of construction projects in New York

City.[7] The City's Capital Commitment Plan assumes savings of approximately $1.4 billion over the next ten years or about 3 percent of total projected capital commitments.

D. Debt Retirement Program

A debt-retirement program is a viable way to reduce debt. If $200 million of the City's budget surplus were used to retire debt maturing in 10 years with a coupon rate of 5 percent, the City would save interest payments totaling $100 million for the 10-year period. The $200 million initial investment earns interest in an escrow of Treasury securities, which offsets the coupon payments of the debt retired over the same period. Thus, the City would achieve zero present-value savings and would benefit by reducing its debt by $200 million on the day the transaction was finalized.

[7] According to a March 1993 study conducted by Ashenfelter & Ashmore on the impact of the Wicks Law on public construction projects in NYC.