

New York City Office of Management and Budget

To: Michael Bloomberg
From: Patrick Peterson
RE: Budgetary Implications And Political Strategy For PlaNYC
Date: April 29, 2007

Situation:

PlaNYC envisions a number of changes to City policies and advocates the creation of several new programs. The following discusses the budgetary implications of these changes.

Recommendations:

You must execute a robust public relations campaign to sell PlaNYC to the public, specifically in the areas of housing and transportation.

You should secure and institutionalize state commitment on funding for an enhanced water network and on transportation. The latter can be accomplished through the SMART Authority, but you must be aware of the difficulties in such a maneuver.

Much uncertainty exists regarding the financing of PlaNYC over the long term, particularly as it relates to the dedicated funding streams to the SMART Authority where it is unclear how the announced funding levels will finance the \$31 billion funding gap.

PlaNYC seems to particularly put pressure on the capital budget. Attention must be paid to the City's debt load especially given the sacrifices made in paying down the City's debt.

There are many programs and policy changes in PlaNYC that are likely to cost a significant amount of money, but for which no funding plan currently exists.

Last week you unveiled PlaNYC, which (if passed) will cement your legacy as one of New York's most innovative Mayors. This document will help you implement PlaNYC without sacrificing your record as the Mayor who rejuvenated the City's fiscal health.

PlaNYC stems from a number of long-term challenges. By 2030, the city will add a million new residents, for whom the cost to provide medical care will rise¹. Most of these costs will stem from public health diseases resulting from a poor environment. The population increase will stress the City's physical infrastructure system requiring significant repair. And the city will face unforeseen challenges to its environment (stemming in part from global warming). None of these challenges can be solved in one budget cycle, but as Mayor it is your task to guide the city towards addressing them.

¹ The City of New York. *PlaNYC: A Greener, Greater New York*. Office of the Mayor, 2007. Page 5.

The following will proceed in three components. First, I will outline key details of your plan. Next, I will discuss how your proposals affect the City's budget. Finally, I will offer recommendations on how you should pursue your political strategy as you seek to implement PlaNYC.

Your Housing Proposal

In all, you recommend 127 significant changes to the way the City operates. Many of these, like planting more trees throughout the city, are not controversial. However, your proposal to increase the stock of affordable housing will generate many local veto players. Your plan to expand the City's transportation network will generate conflict among many actors and incur significant capital costs. And your program to modernize the City's water infrastructure suffers from an unclear funding mechanism. Because these proposals are significant in terms of costs and because their success or failure will ultimately steer the direction of the entire plan, I will focus my attention here.

Existing City plans call for constructing housing for an additional 200,000 residents,² but by 2030 an additional 700,000 homes will need to be built for the expected population increase. In your 2005 Housing Marketplace report, you plan to provide an additional 165,000 units of affordable housing by 2013³. *The New Housing Marketplace's* strategy is to achieve most of the units through rezoning and more adaptable partnerships between City agencies and private and non-profit actors. The City has appropriated some money (\$4.3 million from the capital budget and \$1.2 million from the expense budget⁴) to build units directly, but the bulk of your plan is to offer incentives to the private sector to spur the housing projects.

However, PlaNYC's estimates of the City's long-term population growth mean that your existing housing strategy is insufficient. To increase housing starts and affordability, you plan to use City and State-owned land for housing developments, increase development near transit centers as a method to attract new residents, and to zone areas for more housing. And all of this development should be done in a green way (for example, your goal is to put a park within 10 minutes of all New Yorkers).

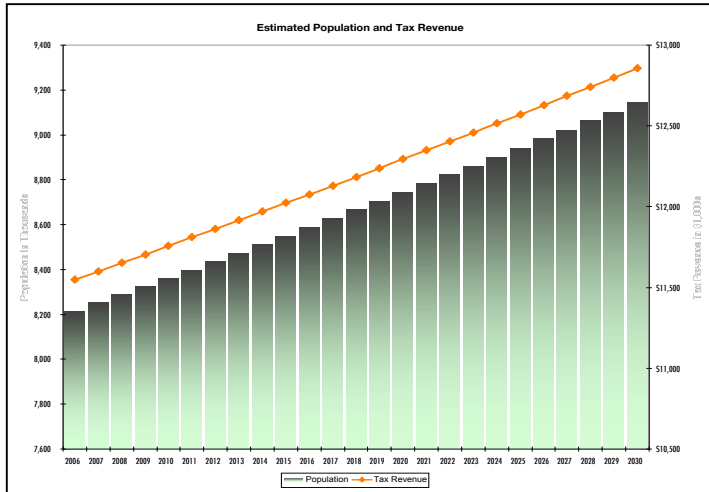
Unfortunately, the existing documentation does not show that this can be done without significant City investment. You state in PlaNYC that the city will use the property it owns to spur development. However, in the 2005 Housing Marketplace study, it is indicated that only 20,000 housing units can be generated from these types of transfers⁵. PlaNYC too leaves much of the responsibility for affordable housing development in the hands of the private sector, noting that there are a total of about 500,000 units available for development. Since we do not know

² Ibid. Land Section.

³ The City of New York. *The New Housing Marketplace: 2004-2013*. Office of the Mayor, 2005. Page 3.

⁴ Ibid, page 17.

⁵ The City of New York. *The New Housing Marketplace: 2004-2013*. Office of the Mayor, 2005. Page 7.



the characteristics of the population increase, we cannot know 500,000 units is enough for the 1 million new residents. That the City will grow increasingly unaffordable is a near certainty.

Frankly stated, the City benefits when housing is more expensive. A 2002 NY State Comptroller study on tax burdens found that the average property tax paid by New York City

residents was \$1,406 (in 2002 dollars) per-capita⁶. If population grows by the same rate that the City has projected⁷, and the property tax burden remains the same, the City can expect property tax revenue of nearly \$13 billion (in current dollars) in 2030.

As the City learned in the 1970's⁸, we are far better off with more residents than with fewer. And, according to your executive budget, City-specific industries like finance and tourism forecast medium- and long-term job growth. Of course, with new residents comes higher infrastructure costs, but these costs are not linear. An n^{th} city resident does not require an x^{th} portion of infrastructure. Rather, once the number of city residents passes a threshold, the infrastructure system is over-capacity and requires a major upgrade. This is a problem if the number of City residents is approaching that point, but if the number of residents is not, an opportunity to hold revenue for future spending exists.

An additional City resident is likely to be a contributor to City revenue rather than a drain on it. During the past decade the City economy has proven its strength: it largely withstood a direct attack on two of its major industries (finance and tourism), emerged from a recession and property tax increase unscathed, and continues to be a center where new industries (media, telecom, and biotech) grow. This demonstrates the City's ability to continue generating wealth and tax revenue in the future⁹. And New York's relatively high cost of living (which includes rent) means that wages will remain high and will continue discouraging residents relocating to the City only

⁶ Hevisi, Allen. *Property Taxes in New York State*. Division of Local Government Services & Economic Development. Office of the State Comptroller, 2006. Available at: <http://www.osc.state.ny.us>.

⁷ See Paul Campbell's *Population Projections: States, 1995-2025*, Current Population Report Number P25-1131 (May 1997) published by the US Census Bureau for population projections. One hardly needs to mention the difficulties in projecting population out thirty years, much less estimating the property tax revenue these would generate. Nevertheless, it serves as a useful example of some of the benefits of population growth.

⁸ A number of excellent sources report on how the City's problems multiplied during the 1970s crises, a recent notable book is Jonathan Mahler's *Ladies and Gentlemen, the Bronx is Burning* (Picador, 2006).

⁹ Your 2007 Capital Budget narrative makes the point that City residents tend to be more affluent and educated than residents of other cities around the country. See Page, Mark. *Ten-Year Capital Strategy FY2008-2017*, New York City Office of Management and Budget, 2007, page 16.

for its public services. Combined, this means that the City can depend on tax revenue, and that increasing the size of the City will increase the amount of revenue collected.

According to PlaNYC, your housing proposals will cost \$2 million in the 2008 capital budget and \$11.7 million in the FY 2008 operating budget, relatively paltry sums¹⁰. The chief difficulty in securing passage of your housing proposal will be to navigate the politics of housing. As you are no doubt aware¹¹ where and for whom housing is built and how projects are financed are issues that tend to generate numerous local supporters and opponents. By letting the private sector take the lead on most projects, you will be insulated from some opposition. But your plan to transfer City-owned property will be seen by opponents as corporate welfare, and given near certainty of higher average rents you will be accused of making New York less affordable.

Your Transportation Proposal

Another area where PlaNYC's success depends on the political situation is in your transportation proposals. But in contrast to your housing plan, which will require minimal City outlays and will generate mostly local veto players, your transportation plan envisions massive City, State, and Federal spending and is likely to hinge on your ability to pacify actors among all three levels of Government (not to mention convincing New Yorkers that the plan is necessary and feasible).

The transportation plan both repairs the existing transportation network and seeks to expand it. The plan imagines upgrading the Subway's signal service, repairing the City's Muni-Meters, investing \$50 million in operating funds to restore the City's tunnel and bridge system, and "seeking a grant from the SMART Authority to cover the MTA funding gap."¹² And you plan on expanding service: new express bus service to the outer boroughs, more traffic enforcement cameras, improving MetroNorth service, and spending \$6.2 million in capital and \$8.1 million in operating funds to complete the bike master plan.

The cornerstone of your transportation plan is to pilot a congestion pricing scheme which would charge drivers to pass through Manhattan's Central Business District¹³. Modeled on London's program, your analysis projects that traffic in the CBD would decrease by 6.7%, and the \$8 car/\$21 truck fare would generate \$400 million of revenue per year. The results of this program would be a new revenue stream that could finance the above-mentioned long-term transportation projects, cost-savings through reduced congestion, and a reduction of pollution in the area¹⁴.

¹⁰ The City of New York. *PlaNYC*. Office of the Mayor, 2007. Appendix B, page 141.

¹¹ Lee & Johnson. *Public Budgeting Systems*. Jones and Bartlett, Seventh Edition (2003). Pages 458, 492.

¹² *Ibid*, page 151.

¹³ Michael Bloomberg. *Mayor Bloomberg Delivers PlaNYC: A Greener, Greater New York*. Transcript of a Speech, Office of the Mayor, PR-120-07, April 22, 2007.

¹⁴ *Ibid*.

Much of your transportation is financed through the creation of the Sustainable Mobility And Regional Transportation (SMART) Authority, which is an innovative way to commit political will from intergovernmental actors. The Authority would collect revenue from the City, the State, and from congestion pricing and invest in projects led by transportation agencies. The Authority would be independent and intergovernmental, its mandate would be to clear the gap between what the City has already invested in transportation and what is required to implement the details of your plan.

The SMART Authority will be responsible for generating this \$31 billion gap through financing, but it is not clear that this is possible given the City's existing debt obligations. The City will commit \$200 million per year for the SMART Authority and ask the state to match its commitment. The remainder of the money needed to finance SMART's investments is projected to come from congestion pricing revenue. However, at the True Interest Cost similar to the City's 2006 Series AA General Obligation bonds (which have a similar load and maturity date as expected by the SMART investments¹⁵), the amortized cost of a \$31 billion package would be approximately \$1 billion each year over 25 years. But in PlaNYC, you estimate only \$400 million will be generated per year¹⁶, not the nearly \$700 million needed to reach the \$1 billion needed to pay off the bond. At a 4% interest rate, the \$32.4 billion total cost of the bond would take 47 years to pay off at a constant rate of \$700 million each year (\$200 million each from State and City sources and \$400 million from congestion pricing). With these back of the envelope calculations, it seems clear that congestion pricing will either need to raise more revenue than you predict, SMART bonds will have a longer maturity period, or State and City funding to SMART must increase.

A recent *Crain's Business* article noted that the City's debt load has decreased under your administration, but if SMART is implemented debt loads would surely increase¹⁷. The SMART program would mitigate the effects of using the FY2008 surplus to prepay some of the City's existing debt obligations¹⁸ by increasing the net debt load born by the City (currently less than %13.5 of City revenue and projected to increase to 15.3% in FY2017¹⁹). Simply stated, your transportation proposal will increase the City's exposure to debt after a period where you have acted aggressively to reduce our debt vulnerability.

If the State refuses to increase the debt capacity of the City's Transitional Financing Authority, the City would need to issue SMART Authority debt via General Obligation Bonds, which would imply higher borrowing costs. Under the TFA, the average interest rate is 3.46% of the tax-free bond, but this capacity has been exhausted by the

¹⁵ According to the City's Budget detail, the rate on 2006 AA Bonds is 4.59% and will mature in 2037, with a par of about \$2 billion. See: Mark Page. *January 2007 Financial Plan: Fiscal Years 2007-2011*. 2007, page 59.

¹⁶ The City of New York. *PlaNYC*. Office of the Mayor, 2007. Transportation, page. 91

¹⁷ Phillips, Ted. *Plan Would Use NYC Surplus for Debt Service*. *Bond Buyer*, Vol. 360, No. 32619 (Friday, April 27, 2007). Page 1.

¹⁸ Page, Mark. *Financial Plan Summary: Fiscal Years 2007-2011*. New York City Office of Management and Budget, January 25, 2007. Page 30.

¹⁹ *Ibid*, page 6 and 19.

City²⁰. If SMART issues GO bonds, the interest rate is higher; existing GO bonds average 5.26%. The State has the ability to increase the true costs of your plan which means that you must engage in deft lobbying at Albany to get the State on your side.

Water infrastructure Proposal

The City's debt position will be further stressed from your water infrastructure proposal, but unlike the transportation plan (where the system is at or approaching capacity) the water network is not over-extended²¹. Instead, the water network faces long-term sustainability challenges, which you have tried to address²² by investing in both new infrastructure and in finishing boondoggle projects that have cost far more than anticipated. The construction of Water Tunnel 3 was anticipated to take 16 years and cost \$300 million; it has taken 50 years and cost over \$6 billion. Key features of your water infrastructure plan budget \$5.6 billion for current projects, including \$1.66 billion to complete the final two stages of Water Tunnel 3, \$1.6 billion for an ultraviolet disinfection program, and implementing a 2004 law requiring the construction of a Croton Water Filtration Plant²³ for \$248 million. These projects will be financed through Water Authority Bonds, which are separate from the General Obligation bonds discussed above but still affect the City's debt exposure. Neither PlaNYC nor the Capital Budget²⁴ discusses how your water network proposals will be financed, but one can assume that they will include the issuance of more Water Authority debt. But without vigorous oversight and a clear idea of what your water infrastructure proposals will cost and how much time they will take, these programs risk sharing the fate of the Water Tunnel 3 project.

Your water network proposal indicates that many studies and plans will be funded, but PlaNYC does not discuss how the results of these plans will be funded. According to PlaNYC's appendix²⁵, you call for 34 plans, studies, and documentations (plan-wide) that are likely to result in new programs or changes to existing ones. And you seek 18 changes to City law or regulation, which are also likely to result in transition and implementation costs. None of these costs have been outlined in PlaNYC or requested in the capital budget. Thus it is likely that that the true final cost of PlaNYC will grow as implementation begins, laws are changed, and studies (once completed) demand new programs.

Another feature of your water network proposal found throughout PlaNYC is its intergovernmentality. A number of the plan's initiatives (and particularly those which require a significant investment) seek to partner with State, Federal, or private sector actors. This strategy distributes the total burden of the plan's cost among more

²⁰ Ibid, page 21.

²¹ The City of New York. *PlaNYC*. Office of the Mayor, Water Network section, 2007. Page 63.

²² The role played by executives in the budget process is (in part) to support these politically-orphaned but strategically essential projects necessary for the city's long-term stability. See Lee & Johnson (2003), pages 130-138, 217-218, 400, and 265-75.

²³ Page, Mark. *Ten Year Capital Strategy: FY2008-2017* New York City Office of Management and Budget, April 2007. Pages 41-43.

²⁴ Ibid, page 19.

²⁵ The City of New York. *PlaNYC*. Office of the Mayor, 2007. Appendix B.

actors, but adds a number of veto players who can more easily derail the progress. As noted in Lee and Johnson (437-447), even while local actors take the primary responsibility for administering many programs, the State exercises control via the funding process and at this level the City must negotiate with other co-equal actors as well as competing with the pet initiatives of State legislators. But fundamentally, both actors have an interest in coming to some agreement. However, when the City works with the private and non-profit actors, its challenge is to preserve its dominant position (dictating the terms of the action) while keeping the actors invested in making a deal. An interesting article in Public Choice found that these non-governmental actors can take their local cases to the super-ordinate government level (i.e. a local dispute being heard at the State level) requiring the City to fight its battle at both levels of government²⁶ The consequences to the City government if it fails to get approval of its agenda at the State level while convincing local actors that the agenda is the right course of action is either a delayed, more expensive, or cancelled plan. PlaNYC is no exception to this finding.

Political Strategy

PlaNYC is innovative and inspired, but it is incomplete without a political strategy that secures the support of stakeholders. It is with this in mind that I offer you some recommendations on the political strategy for achieving your agenda

You are using Governor Spitzer as an asset in passing PlaNYC at the statewide level, but many overestimate Spitzer's political capital. In your speech introducing PlaNYC, you called Spitzer a great supporter and since then have enlisted his assistance in getting PlaNYC's initiatives that require State approval passed during the next legislative session. But Spitzer is not an inexhaustible political asset: in 2006 a healthcare worker's union took him on aggressively when their interests were threatened. The Legislature and the Governor have clashed repeatedly, most recently over the appointment Thomas DiNapoli as the State Comptroller. These fights will continue. Despite the fact that Spitzer was elected with nearly 70% of the vote, his approval rate will fall. I recommend that your state political strategy include as many supporters as possible rather than counting on a few strong advocates.

Indeed, the political strategy at the State level will be extraordinarily complex. You will face a number of legislators who will use passage of PlaNYC to further their unrelated agendas and will hold the plan hostage. Beyond the suburban legislators who will oppose the Plan because it taxes their residents and conservative Republicans who will oppose it on ideological grounds, you must convince legislators to grant the City more policymaking authority than it has had post-1975.²⁷ An effective strategy would be to first assemble a solid base of

²⁶ Grossman, Phillip. *A Political Theory of Intergovernmental Grants*. Public Choice, Vol.78, No. 3-4 (March 1994). Pages 295-303.

²⁷ Glanz, James and Eric Lipton. *City in the Sky*. Times Books (2003), page 48

Democratic support, while working to convince suburban legislators that the plan is in their interest. The easiest way to accomplish this is to reorder the implementation plan such that the early expansions in transportation are to politically-sensitive districts.²⁸ But you should not doubt the difficulty in convincing suburban legislators to support your agenda.

The SMART Authority is an innovative way to lock in commitment from actors, but the election of Board members will challenge the unity of PlaNYC and could result in increased costs. One challenge to a program as ambitious as PlaNYC is that it requires a sustained commitment at both an intergovernmental level and by the Mayors who will ascend to office once you have left. This commitment cannot be ensured, and in the case of future Mayors (who will likely seek to make their *own* mark on the City) one can predict that implementation of PlaNYC would stall. But by creating SMART, you have institutionalized this commitment. Once SMART's funding sources are established and investments in transportation projects are made, it will be supremely difficult to disband the Authority or alter its mission significantly. Laws can be repealed, priorities can be reordered, but organizations (especially those in the business of funding projects) generate advocates who will resist attempts to disband the Authority.

The security of the Authority, the relative power of the Board, and the sensitivity of the projects it will fund²⁹ means that the competition to get on the board will be fierce and politicized. Indeed, in 2007 conflict arose over the appointment of Cheryl Buley to the State Public Utilities Commission between Spitzer (who wanted her to resign) and state Republicans (who wanted her to stay)³⁰. On an independent Board such as SMART with far more political exposure and on which a number of powerful executives have staked their legacies (not to mention their egos), is polarization of the appointments not likely? And SMART is likely to find an institutional enemy in the MTA, who by the power of investment could accelerate or decelerate the MTA's projects. This politicization could affect the mission of the Authority, elevating some priorities and subordinating others as part of a political deal.

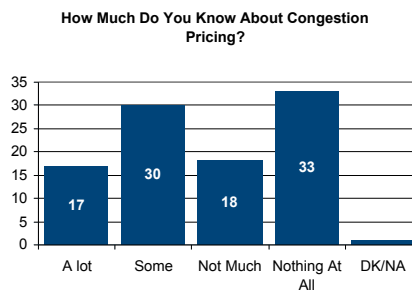
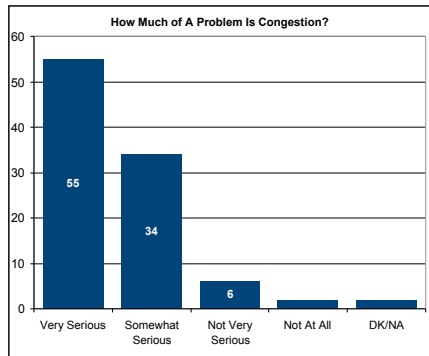
Indeed, the whole point of independent boards is to get the politics out of policymaking. But SMART's purview, intergovernmental status, and the money it will wield make this nearly impossible. I would recommend that you be prepared expend significant resources maintaining the integrity of the Board, and in its establishment routinize as many decisionmaking processes as possible, preventing them from being used as political levers when conflict over project investment arises.

²⁸ Recall how New York City Mayor Ed Koch threatened to close fire houses in precincts where opposition State Legislators had their districts during a budget battle in the 1980s as an example of using funding to affect one's political goals. Budgeting-Government Class Notes, Marc Shaw, March 19, 2007.

²⁹ It is rare that expensive, community-changing projects like public transportation do not generate intense political action. See Johnson & Lee (2003), page 373, 503-4 or W. Bartley Hildreth's *Case Studies In Budgeting and Financial Management* (CRC Publishers, 2003), 379, and 704-5.

³⁰ Gormley, Michael. "Commissioner: Spitzer Aide Threatened Me." *Forbes*, April 18, 2007.

If your state agenda is not difficult enough, you will be forced to contend with significant City opposition to PlaNYC. The following data was taken from a January 18 Quinnipiac University Survey on congestion pricing³¹:



Support	31%
Oppose	62%
DK/NA	7%

City residents believe that traffic is a serious problem and they oppose congestion pricing by a two-to-one margin, even if a bare majority of residents do not know anything about it. The survey also found that New Yorkers believe that congestion pricing will unfairly target suburban residents and that it would be bad for the City economy. While you note that congestion pricing in London once had a 60% disapproval rating and today is widely popular, the fact remains that you must convince New Yorkers that congestion pricing is in their interest..

Beyond that, your proposal to alter the City's transportation network and park system will generate local resistance and support, which you must be able to manage. This is in addition to the political issues surrounding the creation of entirely new neighborhoods through rezoning and the opposition you are likely to face by residents who feel that the City is becoming a less affordable place to live. Only a sustained and effective public relations campaign will be effective in securing local passage of your plan.

Mayors are generally rewarded when they take political risks on behalf of the long-term quality of the City. You have proven this maxim as you ferried your smoking and trans fat bans through a skeptical Council and sold the proposal to an antagonistic public. More importantly, you were unafraid to raise taxes when the City needed to make difficult choices about the City's fiscal situation. PlaNYC is your boldest endeavor, and it will have the longest-term effect of any of your previous policies. If implemented, the plan will change the very fabric of the City. If successful, your work will truly restore New York's place in the pantheon of global cities: the policies in PlaNYC will be studied and implemented in polities around the globe. But as you seek to transform New York, you must keep in mind the implications of your changes, and be prepared to make the fiscal choices necessary to preserve your legacy as a relentless guardian of the City treasury.

³¹Carroll, Maurice. *New York City Voters Oppose Congestion Pricing 2-1, Quinnipiac University Poll Finds*. Press Release, January 18, 2007.