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Report to Rep. Frederick W. Richmond; by Elmer B. Staats, Comptroller General.

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The major Federal programs contributing large amounts of funds to New York City were analyzed to determine the impact of reductions in New York City expenditures on the flow of Federal aid. Federal programs aiding New York City have particular purposes and objectives, and the amount of Federal funds the city receives is primarily determined by the formulas used in distributing the funds. Findings/Conclusions: Historical experience does not demonstrate a relationship between budget reductions and changes in Federal aid. It is unlikely that reductions in the city's budget will result in large reductions in Federal aid. In the short term, State and Federal regulations constrain the city's ability to make budget cuts. New York City's ability to control the flow of Federal funds is limited, and the Mayor's control over the city's total budget is constrained. The areas where the city can make major reductions are in city-controlled programs not largely supported by Federal assistance. Attention is called to the impact of State-level decisions, particularly in public assistance and education programs. (RRS)

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1/28/77



REPORT OF THE COMPTROLLER GENERAL OF THE UNITED STATES

Most Federal Assistance To New York City Unlikely To Be Affected By City-Initiated Budget Cuts

GAO was asked to find out what effect reductions in expenditures by New York City have upon its receipt of Federal financial assistance.

The areas where the city can make major reductions are in city-controlled programs not largely supported by Federal assistance. Moreover, budget cuts in federally aided programs are frequently constrained by State and Federal mandates. Thus, it is unlikely that reductions in the city's budget will result in large reductions in Federal aid.

GAO is preparing other reports on related aspects of the city's financial difficulty and the city, State, and Federal policies affecting budget preparation and expenditures.



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

E-185522

The Honorable Frederic W. Richmond
House of Representatives

Dear Mr. Richmond:

On April 26, 1976, you asked us to analyze the impact of reductions in New York City expenditures upon the flow of Federal aid. Several hundred Federal programs support activities in New York City. After discussions with your office, we agreed to analyze in depth the major Federal programs contributing large amounts of funds to the city. The programs selected constitute about 75 percent of all Federal aid the city expected and included in its Financial Plan Statements of September 1976.

FEDERAL AID TO NEW YORK CITY

According to its Financial Plan Statements New York City anticipates \$2.3 billion in Federal aid, not including Federal Revenue Sharing funds estimated at \$291.0 million. The major Federal-aid programs analyzed follow.

<u>Federal aid</u>	<u>Amount</u>
	(millions)
Can be expended for most budgetary categories:	
Revenue Sharing	\$291.0
Comprehensive Employment and Training Act of 1973	<u>212.3</u> \$ 503.3
Related to activities in the city budget:	
Aid to Families with Dependent Children	493.0
Medicaid	867.4
Elementary and Secondary Education Act of 1965, title I, part A	126.9
School lunch programs	<u>67.9</u> <u>1,555.2</u>
Total examined	\$2,058.5
Federally aided programs not examined	<u>508.5</u>
Total Federal aid	<u>\$2,567.0</u>

In addition, Federal aid related to multiyear appropriations for the Federal-Aid Highway Program, estimated at \$160.8 million, and for the Urban Mass Transportation Act, estimated at \$202.0 million, was examined.

WHAT DETERMINES THE AMOUNT OF FEDERAL AID?

The Federal programs aiding New York City have particular purposes or objectives. The amount of Federal funds the city receives is primarily determined by the formulas used in distributing the funds. In some cases, funds are allocated directly to cities without matching requirements and, in other cases, with matching requirements. Furthermore, the Federal funds cities receive are greatly influenced by program decisions made at the State level. State aid to New York City is estimated at \$2.8 billion for fiscal year 1977--slightly more than the estimated \$2.6 billion in Federal aid. Following is a brief discussion of the city's major Federal programs which are more fully explained in appendix I.

The Comprehensive Employment and Training Act and Revenue Sharing directly allocate the city Federal funds without matching requirements. Other programs involving large amounts of Federal aid, such as Aid to Families with Dependent Children and Medicaid, must be matched by a certain percentage. However, State laws and regulations require New York City to maintain a level of services or expenditures which precludes reducing expenditures from its own source (tax-levy) funds to any degree that would lead to major reductions in Federal aid. In some cases, the State also establishes the share or payment required from the city for nonfederally funded reimbursement costs. For the Aid to Families with Dependent Children and Medicaid programs, the State requires the city to pay about 25 percent of eligible costs.

Funds for the Elementary and Secondary Education Act, title I, part A, are allocated by a formula which multiplies the number of disadvantaged students by a per pupil reimbursement rate. This rate is a percentage of the average per pupil expenditure for the State, and as further explained in appendix I, no likely New York City budget cut would affect it. Federal funds received for the School Lunch Program are also not likely to be affected by city action. In the transportation sector, which involves capital projects, the city has not used all the Federal funds available under the Federal-Aid Highway Program or certain programs authorized under the Urban Mass Transportation Act of 1964. While the State also establishes the State/local percentage sharing arrangement for most

projects, the city has greater latitude in choosing which capital projects to fund or defer and whether to stress obtaining capital or operating expense funding.

State and Federal regulations constrain, in the short run, the city's ability to make budget cuts. The city's and State's ability to control the flow of Federal funds is summarized in appendix II.

As discussed in appendix I, New York City's ability to control the flow of Federal aid is limited. Furthermore, the Mayor's control over the city's total budget is also constrained. For example, one estimate of uncontrollable portions of the city budget suggests that \$8.7 billion, or 72 percent, of the Mayor's fiscal year 1976 budget was not directly controllable by the Mayor. It should be noted that 40 percent of the controllable items of this particular calculation was for police and fire protection--areas which received very little Federal aid.

Some of this \$8.7 billion went for debt service, retirement benefits, and the State and federally aided programs discussed in this report. Over time, however, debts may be repaid, pensioners die, and almost every aspect of the city's fiscal operations can be affected by changes in State or Federal legislation.

PROBLEMS IN ASSOCIATING BUDGETARY REDUCTIONS WITH THE FLOW OF FEDERAL AID

We reviewed recent estimates of reduced Federal aid because of city budget cuts. Most estimates began with the amount of anticipated Federal aid used to prepare the 1976 budget. This budget was revised several times, and each revision presented a different estimate of Federal aid. Since the estimated Federal aid was usually reduced, these reductions were called losses.

Furthermore, historical experience does not demonstrate the relationship between budget reductions and changes in Federal aid. Available accounting data does not facilitate the identification of changes in Federal and State aid for existing federally aided programs. If the city Office of Management and Budget estimates hold true, 1977 will be the first fiscal year since the crisis that there were actual reductions in Federal aid in comparison to prior years. Thus, information relevant to the relationship between New York City expenditure reductions and Federal-aid reductions will not be available until after June 1977.

Our review of major federally supported programs (see app. I) calls attention to the impact of State-level decisions. The State's role is particularly important in public assistance and education programs. For example, for the Aid to Families with Dependent Children and Medicaid programs, State regulations established under Federal guidelines determine who will receive benefits and how much these benefits will be. Furthermore, New York State requires the city to pay one-half of the matching requirements. State law also mandates both compulsory education and particular services. Most Federal aid in the transportation sector is also channeled through a State agency and frequently involves a State and city financial decision.

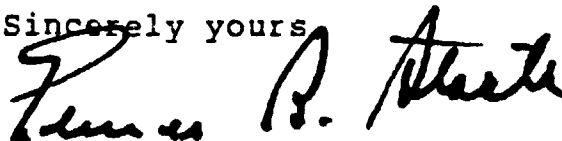
As you are aware, the Congress recently took action on matching requirements for public works projects. Section 103 of the Public Works Employment Act of 1976 (Public Law 94-369) includes no matching requirements, and section 104 provides funds that eligible State or local governments can use to meet their shares of other Federal matching grant public works projects.

During our review, we held informal discussions with officials in New York City's Office of Management and Budget, Office of the Comptroller, and the New York State Office of Special Deputy Comptroller. Their views were considered.

Furthermore, we are preparing other reports on New York City that address issues closely related to those raised in your letter. When these reports are completed, we will send them to you.

This concludes our work on your request.

Sincerely yours

A handwritten signature in black ink, appearing to read "James P. Stucke". The signature is written in a cursive style with a large initial "J" and "S".

Comptroller General
of the United States

COMPREHENSIVE EMPLOYMENT AND TRAINING ACT

The Comprehensive Employment and Training Act of 1973 (CETA) (Public Law 93-203) and the Emergency Jobs and Unemployment Assistance Act of 1974 (Public Law 93-567) authorize four major programs. Title I is for training and work experience, titles II and VI are for public service employment, and title III, section 304(a)(3) provides for the summer program for economically disadvantaged youths. New York City is eligible for all CETA titles, and as a prime sponsor, it usually deals directly with the Federal Government, not through an intermediary State agency. City estimates of fiscal year 1977 CETA receipts follow.

<u>Title</u>	<u>Amount</u>
	(millions)
I	\$ 77.8
II	100.0
III, section 304(a)(3)	28.5
VI	<u>6.0</u>
Total	<u>\$212.3</u>

Most CETA funds are allocated by formulas based on factors which include the number of unemployed persons in the prime sponsor's area.

Unlike the Medicaid and Aid to Families with Dependent Children (AFDC) programs, CETA programs have no matching requirements, nor does State law require the city to provide a specified level of public service employment. Again different from other programs, it is possible that city budget cuts may marginally increase the city's share of CETA funds because these cuts reduce public service employment and, thereby, increase unemployment--one variable upon which CETA funds depend.

Restrictions on using CETA funds limit the city. Persons employed in public service jobs with CETA funds may not receive over \$10,000 a year from CETA, but the city, in some cases, supplements these funds. Consequently, CETA funds may be used to support entry level positions; at the same time, the city may be laying off regular and experienced employees. A maintenance-of-effort clause of the act also restricts the use of CETA funds. In theory, New York City as a prime sponsor might lose CETA funds if it substitutes CETA moneys for its own to fund regular employment, a practice described as paper layoffs.

The Department of Labor has, however, with regard to title VI, issued regulations providing that:

"Former employees who lost their jobs due to a bona fide lay-off may be hired into positions supported under this Part provided that such hiring does not constitute a violation of the maintenance of effort provisions of the Act and these regulations."

Similar regulations apply to title II.

City officials have said that courts in cases involving New York City and Detroit, Michigan, have upheld a city's right to rehire laid-off regular employees. Although CETA maintenance-of-effort requirements may affect city priorities, there are no indications that New York City will lose CETA funds.

REVENUE SHARING

In fiscal year 1976, New York City received \$263 million in Revenue Sharing funds from the Federal Government. The city's Office of Management and Budget estimates that funds from this source in fiscal year 1977 will be \$291 million. The amount a city receives is determined by complex formula as specified in the State and Local Fiscal Assistance Act of 1972 (Public Law 92-512). The formulas generally increase a government's funds as its population and tax efforts increase and its per capita income decreases.

Because Revenue Sharing eligibility does not depend on a government's meeting matching fund or maintenance-of-effort requirements, changes in the amount or purpose of New York City's expenditures will not affect its Revenue Sharing funds. On the other hand, if its taxes increase proportionately more than those of competing governments, its Revenue Sharing funds should also increase.

AFDC AND MEDICAID

Title IV of the Social Security Act, as amended, provides for AFDC, and title XIX, as amended, provides for Medicaid--aid to the medically needy. In fiscal year 1977, Federal payments to New York City are expected to be about \$493.0 million for AFDC and \$867.4 million for Medicaid.

These programs have similar formulas based primarily on per capita income, which determine to what extent expenditures

are reimbursed from Federal funds. For New York State, the Federal Government's share is 50 percent. Currently, the remaining 50 percent is divided equally between the city and the State. For both programs, the crucial issues of eligibility and level of payments are determined by the State plan that meets broad Federal standards.

A superficial examination of these programs' matching requirements might lead to the conclusion that reducing city expenditures would cause a loss of three State and Federal dollars for each city dollar saved. Because the State plan mandates a high level of services, the city is unable to reduce greatly its program expenditures. The city can reduce only those services exceeding those mandated by the State and administrative costs. Since about 75 percent of these expenditures, generally, are reimbursed by the Federal and State Governments, these city reductions may cause a loss of Federal funds. Compared with overall program expenditures, however, these amounts are small.

ESEA TITLE I

In fiscal year 1977, New York City expects to receive about \$126.9 million under the Elementary and Secondary Education Act of 1965, title I, part A (ESEA, title I). This act gives financial aid to local educational agencies serving areas with children from low-income families. Basic grant funds are allocated through a formula which multiplies the number of disadvantaged students by a per student reimbursement rate. The number of disadvantaged students is the sum of (1) the number of 5- to 17-year-olds in families with incomes below the Bureau of the Census-defined poverty level, (2) two-thirds of 5- to 17-year-olds in AFDC families with incomes above the poverty level, and (3) the number of 5- to 17-year-olds living in institutions for neglected or delinquent children or being supported in foster homes with public funds. The per pupil reimbursement rate is 40 percent of the average State per pupil expenditure within a range of not less than 80 nor more than 120 percent of the average U.S. per pupil expenditure. This rate is applied across the board to every county in the State, but a hold harmless clause provides that each county will receive at least 85 percent of the previous year's allocation.

Acting on its own, New York City can do little to affect the amount of title I funds it receives. Assuming that State school districts maintain their current level of expenditures, even if New York City reduced its per pupil expenditures by 25 percent (a considerable and unlikely reduction inhibited

by Federal maintenance-of-effort requirements), New York State and therefore New York City would still be entitled to the maximum per pupil reimbursement.

Major changes in the amount of New York City's aid under this program would require congressional action. The 1974 changes in the title I formula reduced the city's allocation as a result of the lowered per pupil reimbursement rate and the reduced weight of AFDC eligibles in determining the number of disadvantaged students.

School Lunch Program

In fiscal year 1977, the city expects to receive about \$67.9 million in Federal funds under the National School Lunch Act, as amended. To be eligible to participate in this program, a school must agree to operate a nonprofit lunch program, to provide free or reduced-price lunches to children of families unable to pay the full price, and to serve lunches meeting the Department of Agriculture's type A nutritional standards. The Federal program places no total dollar limit on program costs; however, it limits the Federal reimbursement by providing 13 cents for each lunch served, plus an additional 48.5 cents for a reduced-price lunch or an additional 58.5 cents for a free lunch.

Except for a decision not to participate in the Federal program, the only program variable affecting Federal funds is the eligibility for free or reduced-price lunches. School authorities make this decision using State criteria, which are based on Federal guidelines.

TRANSPORTATION

Federal-Aid Highway Program

Funds from the Federal-Aid Highway Program are available through the State according to formulas based on such factors as population, land area, and intercity mail route mileage. Federal-Aid Urban Systems (FAUS) projects under this program, the formula for which is based upon urban population ratios, require 30 percent matching funds from the State or local government. State law and the type of project determine how the 30 percent will be divided between the two governmental levels. In New York, the State provides (1) all of the matching grant for State-maintained highway projects, (2) 25 percent of the total project cost as a matching grant for mass-transit substitution projects--New York City provides 5 percent, and (3) no matching assistance for local highway projects.

As of October 31, 1976, \$160.8 million in FAUS funds from fiscal years 1974-77 was available to New York City--of this sum \$102.4 million remained unobligated. A senior New York State Department of Transportation official thinks the primary reason for this large unobligated balance was the city's difficulty in providing matching funds.

Urban Mass Transportation Grants

The Urban Mass Transportation Act of 1964, as amended, provides funds to assist in acquiring, constructing, re-constructing, and improving mass transportation facilities and equipment. We analyzed funds distributed to New York City under sections 3 and 5 of the act. These funds are distributed both for specific projects and by formula. Capital grants may equal 80 percent of the net project cost--a cost which could not reasonably be financed with project revenues. The remainder of the project cost must come from other than Federal funds. In New York, the State provides 15 percent and the city supplies the remaining 5 percent of net project costs.

In fiscal year 1976, under section 3 of the Urban Mass Transportation Act of 1964, as amended, the New York Transit Authority received \$202 million. Section 3(h) allows a grantee to use as much as one-half of its capital grant to pay mass transit operating expenses, provided equal State or local funds are available by the end of the fiscal year following the fiscal year in which the funds were borrowed from the capital grant project, to substitute for the Federal funds. New York City has borrowed about \$204.5 million under this section--\$124.5 million in 1975 and \$80.0 million in 1976.

In addition, section 5 authorizes formula grants. This formula allocates one-half in proportion to urban area population, and one-half in proportion to population weighted by density for use in mass transit capital or operating assistance projects.

Section 5 funds are allocated by urbanized area. The New York urbanized area allocation for fiscal year 1976 was \$88.9 million, of which \$71.1 million was awarded to New York State and \$17.8 million to New Jersey.

Much of New York State's funds is available to the city. Formula grants for capital assistance may not exceed 80 percent of net project costs; grants for operating expenses may not exceed 50 percent of total operating costs.

Because of the Transit Authority's large operating deficit it is likely that most, if not all, of the city's share of section 5 funds will be used to meet operating expenses--if the city can meet the maintenance-of-effort requirements embodied in the law. New York City may have problems meeting these requirements.

CHARACTERISTICS OF FEDERAL-AID PROGRAMSTO NEW YORK CITY

<u>Program</u>	<u>Federal funds</u> (millions)	<u>Required city matching percent</u>	<u>Controllability over the flow of Federal funds</u>	
			<u>City</u>	<u>State</u>
CETA	\$212.3	none	-	-
Revenue Sharing	<u>a</u> /291.0	none	-	-
AFDC	<u>a</u> /493.0	<u>c</u> /25	low	high
Medicaid	<u>a</u> /867.4	<u>c</u> /25	low	high
ESEA, Title I	<u>a</u> /126.9	none	low	high
School lunch and free lunch	<u>a</u> /67.9	none	low	medium
Federal-Aid Highway Program	<u>b</u> /160.8	various	medium	high
Urban Mass Transportation Act	<u>b</u> /202.0	various	high	-

a/Fiscal year 1977 estimates from New York City's Office of Management and Budget, Nov. 1976.

b/Not included in the New York City expense budget, includes multiyear funds estimates from Federal sources.

c/Federal regulations require a nonfederal contribution of 50 percent. State regulations divide this contribution equally between city and State.