PART II

EXPLANATION OF RECEIPT ESTIMATES

EXPLANATION OF RECEIPT ESTIMATES

In accordance with the requirements of Article VII of the State Constitution and section 22 of the State Finance Law, there is submitted herewith an explanation of the receipt estimates by fund type.

These estimates have been prepared by the Division of the Budget with the assistance of the Department of Taxation and Finance and other agencies concerned with the collection of State receipts. To the extent they are material, income sources not noted below are discussed in the presentations of the agencies primarily responsible for executing the programs financed by such receipts.

CASH RECEIPTS
ALL GOVERNMENTAL FUNDS
2000-2001
(millions of dollars)

	General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Personal income tax	23,566	3,076	0	250	26,892
User taxes and fees	7,404	427	636	2,203	10,670
Sales and use tax	6,272	369	0	2,092	8,733
Cigarette and tobacco taxes	528	0	0	0	528
Motor fuel tax	17	58	324	111	510
Motor vehicle fees	338	0	157	0	495
Highway Use tax	0	0	155	0	155
Alcoholic beverages taxes	179	0	0	0	179
Alcoholic beverage control license fees	31	0	0	0	31
Auto rental tax	39	0	0	0	39
Business taxes	4,328	1,029	489	0	5,846
Corporation franchise tax	2,336	295	0	0	2,631
Corporation and utilities tax	817	192	0	0	1,009
Insurance taxes	584	60	0	0	644
Bank tax	505	86	0	0	591
Petroleum business tax	86	396	489	0	971
Other taxes	795	0	112	293	1,200
Estate tax	717	0	0	0	717
Gift tax	42	0	0	0	42
Real property gains tax	6	0	0	0	6
Real estate transfer tax	0	0	112	293	405
Pari-mutuel taxes	29	0	0	0	29
Other taxes	1	0	0	0	1
Total Taxes	36,093	4,532	1,237	2,746	44,608
Miscellaneous receipts	1,553	6,646	1,674	860	10,733
Federal grants	0	24,273	1,509	0	25,782
Total	37,646	35,451	4,420	3,606	81,123

CASH RECEIPTS
ALL GOVERNMENTAL FUNDS
2001-2002
(millions of dollars)

	General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Personal income tax	26,977	1,310	0	250	28,537
User taxes and fees	7,082	463	885	2,153	10,583
Sales and use tax	6,120	368	0	2,038	8,526
Cigarette and tobacco taxes	514	0	0	0	514
Motor fuel tax	0	65	345	115	525
Motor vehicle fees	202	30	389	0	621
Alcoholic beverages taxes	177	0	0	0	177
Highway Use tax	0	0	151	0	151
Alcoholic beverage control license fees	33	0	0	0	33
Auto rental tax	36	0	0	0	36
Business taxes	3,829	1,042	557	0	5,428
Corporation franchise tax	1,755	243	0	0	1,998
Corporation and utilities tax	987	204	0	0	1,191
Insurance taxes	630	64	0	0	694
Bank tax	457	86	0	0	543
Petroleum business tax	0	445	557	0	1,002
Other taxes	780	0	112	263	1,155
Estate tax	740	0	0	0	740
Gift tax	4	0	0	0	4
Real property gains tax	6	0	0	0	6
Real estate transfer tax	0	0	112	263	375
Pari-mutuel taxes	29	0	0	0	29
Other taxes	1	0	0	0	1
Total Taxes	38,668	2,815	1,554	2,666	45,703
Miscellaneous receipts	1,609	7,179	1,731	606	11,125
Federal grants	0	25,497	1,471	0	26,968
Total	40,277	35,491	4,756	3,272	83,796

CASH RECEIPTS
ALL GOVERNMENTAL FUNDS
2002-2003
(millions of dollars)

	General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total
Personal income tax	23,292	2,630	0	0	25,922
User taxes and fees	7,069	513	996	2,208	10,786
Sales and use tax	6,285	370	0	2,094	8,749
Cigarette and tobacco taxes	501	0	0	0	501
Motor fuel tax	0	65	343	114	522
Motor vehicle fees	65	78	464	0	607
Alcoholic beverages taxes	178	0	0	0	178
Highway Use tax	0	0	155	0	155
Alcoholic beverage control license fees	40	0	0	0	40
Auto rental tax	0	0	34	0	34
Business taxes	3,775	1,056	565	0	5,396
Corporation franchise tax	1,761	251	0	0	2,012
Corporation and utilities tax	995	203	0	0	1,198
Insurance taxes	516	54	0	0	570
Bank tax	503	97	0	0	600
Petroleum business tax	0	451	565	0	1,016
Other taxes	783	0	112	247	1,142
Estate tax	751	0	0	0	751
Gift tax	0	0	0	0	0
Real property gains tax	2	0	0	0	2
Real estate transfer tax	0	0	112	247	359
Pari-mutuel taxes	29	0	0	0	29
Other taxes	1	0	0	0	1
Total Taxes	34,919	4,199	1,673	2,455	43,246
Miscellaneous receipts	1,606	9,166	2,067	626	13,465
Federal grants	0	28,560	1,576	0	30,136
Total	36,525	41,925	5,316	3,081	86,847

CASH RECEIPTS
GENERAL FUND
2000-2001 THROUGH 2002-2003
(millions of dollars)

	2000-2001 Actual	2001-2002 Estimated	2002-2003 Recommended	2002-2003 Compared with 2001-2002
Personal income tax	23,566	26,977	23,292	(3,685)
User taxes and fees	7,404	7,082	7,069	(13)
Sales and use tax	6,272	6,120	6,285	165
Cigarette and tobacco taxes	528	514	501	(13)
Motor fuel tax	17	0	0	0
Motor vehicle fees	338	202	65	(137)
Alcoholic beverages taxes	179	177	178	1
Alcoholic beverage control license fees	31	33	40	7
Auto rental tax	39	36	0	(36)
Business taxes	4,328	3,829	3,775	(54)
Corporation franchise tax	2,336	1,755	1,761	6
Corporation and utilities tax	817	987	995	8
Insurance taxes	584	630	516	(114)
Bank tax	505	457	503	46
Petroleum business tax	86	0	0	0
Other taxes	795	780	783	3
Estate tax	717	740	751	11
Gift tax	42	4	0	(4)
Real property gains tax	6	6	2	(4)
Pari-mutuel taxes	29	29	29	0
Other taxes	1	1	1	0
Total Taxes	36,093	38,668	34,919	(3,749)
Miscellaneous receipts	1,553	1,609	1,606	(3)
Total	37,646	40,277	36,525	(3,752)

CASH RECEIPTS
SPECIAL REVENUE FUNDS
2000-2001 THROUGH 2002-2003
(millions of dollars)

	2000-2001 Actual	2001-2002 Estimated	2002-2003 Recommended	2002-2003 Compared with 2001-2002
Personal income tax	3,076	1,310	2,630	1,320
User taxes and fees	427	463	513	50
Sales and use tax	369	368	370	2
Motor fuel tax	58	65	65	0
Motor vehicle fees	0	30	78	48
Business taxes	1,029	1,042	1,056	14
Corporation franchise tax	295	243	251	8
Corporation and utilities tax	192	204	203	(1)
Insurance taxes	60	64	54	(10)
Bank tax	86	86	97	11
Petroleum business tax	396	445	451	6
Total Taxes	4,532	2,815	4,199	1,384
Miscellaneous receipts	6,646	7,179	9,166	1,987
State university income	1,656	1,759	1,878	119
Lottery	1,587	1,684	2,086	402
Indigent care	873	847	1,020	173
HCRA Transfer fund	246	372	720	348
Provider assessments	0	0	413	413
EPIC	178	260	500	240
Child health plus	259	325	431	106
All other	1,847	1,932	2,118	186
Federal grants	24,273	25,497	28,560	3,063
Total	35,451	35,491	41,925	6,434

CASH RECEIPTS
CAPITAL PROJECTS FUNDS
2000-2001 THROUGH 2002-2003
(millions of dollars)

	2000-2001 Actual	2001-2002 Estimated	2002-2003 Recommended	2002-2003 Compared with 2001-2002
User taxes and fees	636	885	996	111
Motor fuel tax	324	345	343	(2)
Motor vehicle fees	157	389	464	75
Highway Use tax	155	151	155	4
Auto Rental Tax	0	0	34	34
Business taxes	489	557	565	8
Petroleum business tax	489	557	565	8
Other taxes	112	112	112	0
Real estate transfer tax	112	112	112	0
Total Taxes	1,237	1,554	1,673	119
Miscellaneous receipts	1,674	1,731	2,067	336
Authority bond proceeds	1,579	1,587	1,875	288
State park fees	16	25	22	(3)
Environmental receipts	27	45	94	49
All other	52	74	76	2
Federal grants	1,509	1,471	1,576	105
Total	4,420	4,756	5,316	560

CASH RECEIPTS
DEBT SERVICE FUNDS
2000-2001 THROUGH 2002-2003
(millions of dollars)

	2000-2001 Actual	2001-2002 Estimated	2002-2003 Recommended	2002-2003 Compared with 2001-2002
Personal income tax	250	250	0	(250)
User taxes and fees	2,203	2,153	2,208	55
Sales and use tax	2,092	2,038	2,094	56
Motor fuel tax	111	115	114	(1)
Other taxes	293	263	247	(16)
Real estate transfer tax	293	263	247	(16)
Total Taxes	2,746	2,666	2,455	(211)
Miscellaneous receipts	860	606	626	20
Mental hygiene patient receipts	258	232	231	(1)
SUNY dormitory fees	224	262	284	22
Health patient receipts	87	86	85	(1)
Tobacco settlement receipts	250	0	0	0
All other	41	26	26	0
Total	3,606	3,272	3,081	(191)

ECONOMIC BACKDROP

OVERVIEW

The nation's longest economic expansion has ended. On November 26, 2001, the National Bureau of Economic Research (NBER) Business Cycle Dating Committee officially declared that the national economy's 10-year expansion peaked in March of 2001. The collapse of the high-tech investment bubble in 2000 severely weakened the manufacturing, finance and other sectors, causing U.S. corporate profits to plummet. In an effort to avert a recession, the Federal Reserve switched aggressively to an expansionary monetary policy in early January 2001. Then, on September 11, the already struggling U.S. economy was shocked by a terrorist attack, and the economy fell rapidly into recession.

The New York economy was also slowing in 2001, primarily from the twin impacts of falling corporate profits and a declining financial services sector. Following the destruction of the World Trade Center, economic activity was brought to a temporary halt in lower Manhattan. Operations within the finance, transportation, and communications industries were disrupted, and tourism was severely affected. The impact of the disaster was much more severe for New York City and New York State than for the rest of the nation. The New York economy is expected to undergo a sharp but relatively short contraction, with a substantial loss of jobs and a steep decline in income.

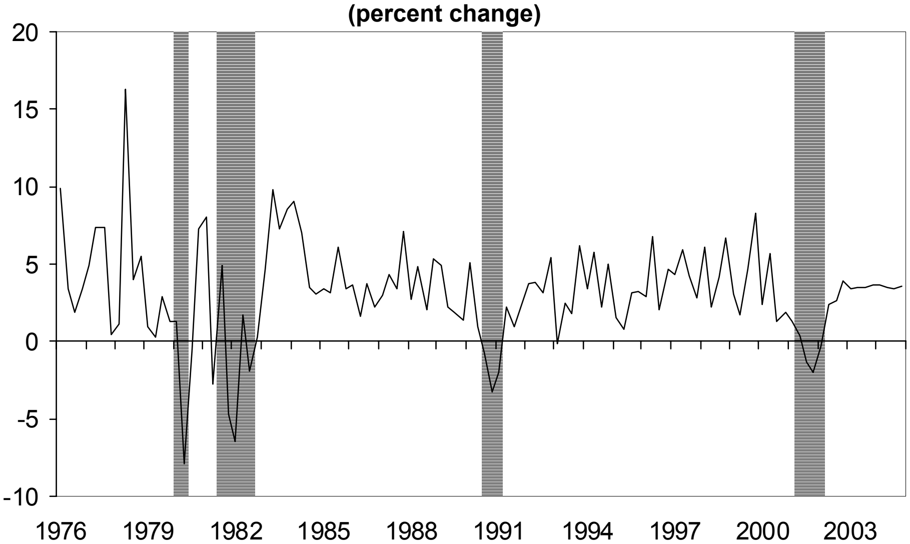
Federal spending increases associated with the September 11 attacks, combined with enacted tax cuts, are expected to provide fiscal stimulus to the ailing economy. At the same time, the Federal Reserve has continued to aggressively reduce interest rates in the wake of the September 11 disaster. Together, these expansionary monetary and fiscal policies are expected to engender a recovery by the middle of this year. The rebound in the national economy should produce growth for New York State before the end of 2002.

The level of uncertainty among forecasters as to when the economy will emerge from the current recession extends well beyond that of a typical downturn. This uncertainty is particularly pronounced for New York State. The attack of September 11 and subsequent events have obscured traditional economic reference points. Given the uncertainty in the current environment, a cautious approach to estimating future economic growth is warranted.

THE NATIONAL ECONOMY

The Division of the Budget is forecasting a continuation of the national economic recession through the beginning of 2002, resulting in two quarters of decline in the second half of 2001 and another decline in the first quarter of 2002 (see Figure 1). The U.S. economy, as measured by real U.S. Gross Domestic Product (GDP), is expected to grow 1.0 percent for 2001, followed by growth of 0.4 percent for 2002. The extraordinary growth in investment during the late 1990's has resulted in excess capacity in the manufacturing, telecommunications and high-technology sectors, contributing to declining profits. In light of these conditions, the current recession would likely be longer and deeper without the extensive monetary and fiscal policy initiatives now in place.

Figure 1
Real Gross Domestic Product
(percent change)



Note: Shaded areas represent US recessions; length of current recession is based on DOB forecast.
Source: DRI-WEFA; DOB staff estimates.

THE RETURN OF THE BUSINESS CYCLE

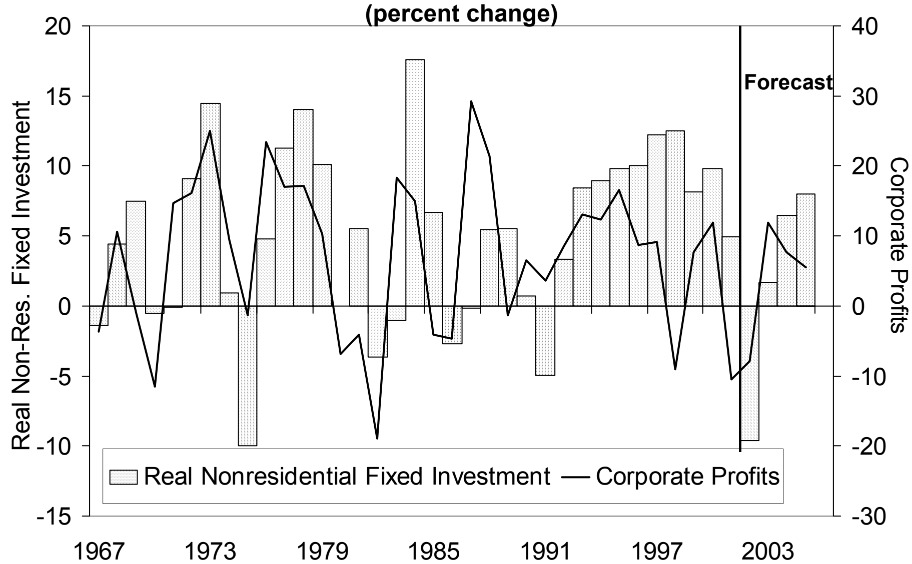
During the late 1990's, many of the nation's economists debated whether the U.S. economy had undergone a revolutionary transformation into what became known as the "New Economy". Proponents of this view held that the business cycle would no longer be a pronounced characteristic of the national economy. Supporting this belief was the Federal Reserve's seemingly improved capability to fine-tune the U.S. economy, demonstrated by the 1995 soft landing and confirmed by the monetary authority's handling of the Asian financial crisis during the fall of 1998.

Many economic analysts also argued that the importance of the business cycle had been diminished by the gradual shift of employment from goods production to the production of services, since the demand for the latter has always been less cyclical. High rates of productivity growth, related to the incorporation of internet-related technology into both the marketing and production process, seemed able to permit economic growth at rates of between 4 percent and 5 percent without generating inflation. Practices such as just-in-time inventory control and supply chain management, and the high depreciation rate of computer-related equipment, were expected to dampen the more traditional boom-and-bust investment cycle. However, recent events call a great deal of this analysis into question and suggest that traditional economic forces remain at work in the economy.

Preparations for the Millennium bug and the desire to incorporate the internet into production and marketing processes fueled a six-year investment boom, lasting until the second half of 2000. The rapid rise in equity prices, low borrowing costs, and the high depreciation rate on computer equipment produced high levels of investment spending, particularly on telecommunications, computer, and related equipment. While existing firms were investing in so-called "Y2K compliant" technology, strong growth in the numbers of internet start-ups produced additional demand for technology-related goods. A significant portion of these purchases were financed through the strong initial public offerings (IPO) market, which permitted firms with few prospects for near-term profits to acquire large amounts of capital.

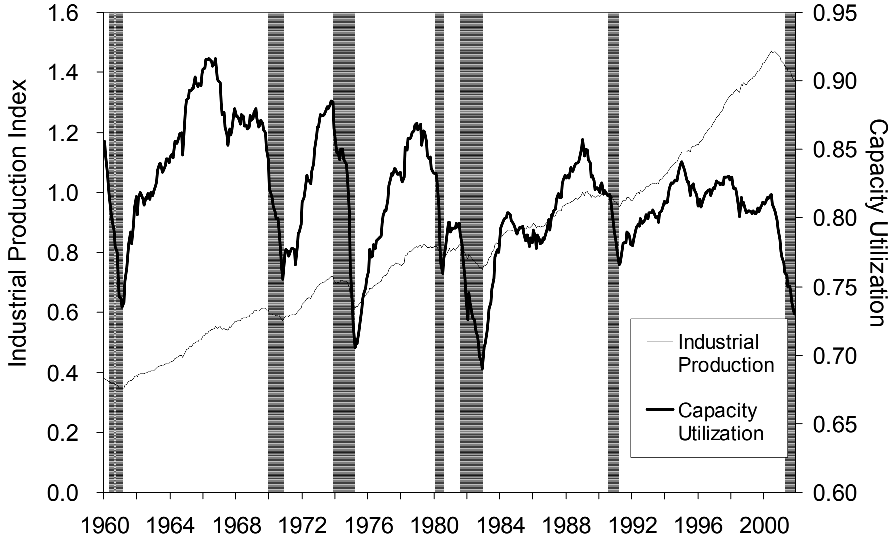
This upward spiral in the demand for internet-related and Y2K-compliant technologies prompted strong investment on the part of technology sector firms. Real nonresidential fixed investment grew at an average annual rate of 11.3 percent between the first quarter of 1996 and the second quarter of 2000. Real computer-related investment alone grew at an average annual rate of 43.1 percent over the same period. As indicated in Figure 2, real nonresidential fixed investment exhibited strong rates of growth for an unusually protracted period by historical standards. Strong investment growth, in turn, accelerated the growth in industrial production. The brisk addition to the nation's capital stock kept the rate of capacity utilization below the historical average rates for prior economic expansions (see Figure 3), helping to dampen inflationary pressures.

Figure 2
Real Nonresidential Fixed Investment and Corporate Profits
(percent change)



Source: DRI-WEFA; DOB staff estimates.

Figure 3
Industrial Production and Capacity Utilization



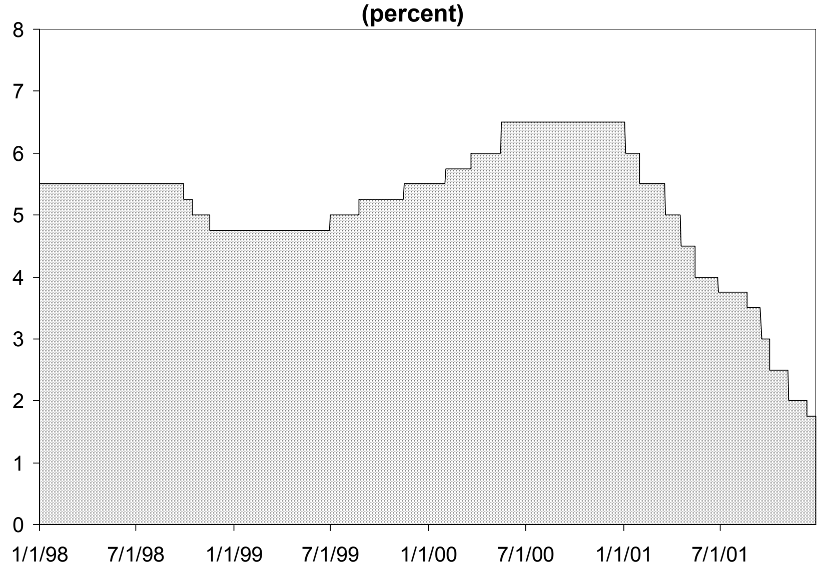
Note: Shaded areas represent US recessions.
Source: DRI-WEFA.

Although inflation remained relatively low throughout the late 1990's, the high-tech investment boom was accompanied by substantial growth in labor costs. With the unemployment rate falling to, and even briefly below, 4 percent, shortages of labor with specialized skills emerged. The skills shortage fueled growth in bonus income in the form of both cash and stock options as firms competed to retain talented workers. Anecdotal evidence was frequently cited of internet start-up firms using proceeds from over-valued stock prices to pay high salaries and bonuses, with little expectation of generating near-term profits.

The investment/equity market boom lasted several years with little interference from government policy makers. The Federal Reserve fired a warning shot in March 1997, in the form of a 25 basis point increase in its target short-term interest rate.[1] However, the promise of the "New Economy" had successfully obscured more conventional market principles, engendering the expectation that future high rates of productivity growth would compensate for the high asset prices of the day. In June 1999, the Federal Reserve discarded its 17-month-old neutral policy stance in favor of a more restrictive monetary policy (see Figure 4). By the end of the second quarter of 2000, equity prices were already well below their peaks. By the fourth quarter of 2000, investment growth had fallen to 1.0 percent, its last positive quarter to date.

[1] The Chairman of the Federal Reserve had warned in early March 1997 that equity markets were being guided by "irrational exuberance". However, in subsequent speeches, he often referred to the role of productivity-enhancing technologies in transforming the economy, perhaps reinforcing the notion that the business cycle had been tamed by technology and wisely executed monetary policy. Stock prices continued to rise for three years beyond March 1997.

Figure 4
Federal Funds Target Rate
(percent)



Source: Federal Reserve.

Although the internet and associated productivity enhancing technology remain an engine for future economic growth, the dramatic declines in investment, profits, and equity prices, have led many analysts to reassess the notion of the "New Economy."[2] Recent downward revisions by the U.S. Department of Commerce, Bureau of Economic Analysis (BEA) to the National Income and Product Accounts (NIPA) data may also be contributing to this reassessment. The Bureau of Economic Analysis recently released revised estimates of NIPA data beginning with the first quarter of 1998.[3] The revisions are normally released each July to incorporate source data that are more complete, more detailed, and otherwise more pertinent than previously available.

The largest revision to real GDP growth was for 2000, which was revised down 0.9 percentage points from 5.0 percent to 4.1 percent. It can no longer be said that high productivity growth was permitting the U.S. economy to achieve growth rates on the order of 5 percent without generating a rise in inflation. In addition, growth in corporate profits — before tax and with inventory valuation and capital consumption adjustments — was revised down for 2000 by 3.6 percentage points, while investment spending was revised down by 3.4 percentage points.

The recent NIPA revisions have also produced lower estimates for productivity growth, as measured by output per labor hour in the nonfarm business sector, for 1999 and 2000 (see Table 1). These revisions suggest that potential real GDP growth for the U.S. is lower than previously believed (see Box 1). Figure 5 compares the Division of the Budget's current estimate of potential real GDP growth with estimates constructed prior to the revision. Potential GDP growth was revised down for every quarter since 1997. Although several series used in the estimation of potential GDP have been revised in the last year, the NIPA

[2] For example, see Robert J. Gordon, "Does the 'New Economy' Measure up to the Great Inventions of the Past?", NBER Working Paper No. W7833, August 2000.

[3] See Brent R. Moulton, Eugene P. Seskin, and David F. Sullivan, "Annual Revision of the National Income and Product Accounts: Annual Estimates, 1998-2000 and Quarterly Estimates, 1998:I-2001:I,"*Survey of Current Business"* (August 2001): 7-32.

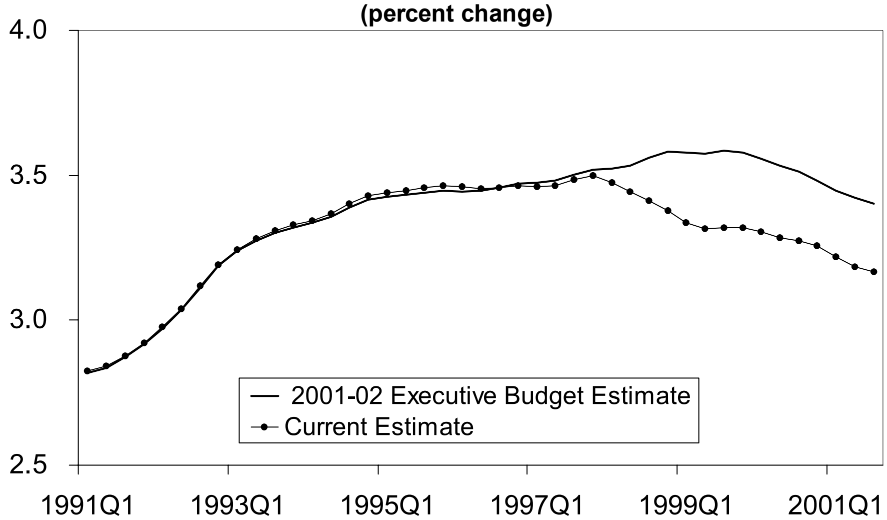
revisions have been the most influential. For given quantities of capital and labor, lower output growth implies that the most comprehensive measure of productivity in the economy — total factor productivity — is lower than originally estimated.

TABLE 1
2001 ANNUAL REVISION TO NATIONAL INCOME AND PRODUCT ACCOUNTS AND LABOR PRODUCTIVITY DATA
(percent change)

	1998	1999	2000
Real Gross Domestic Product			
Current	4.3	4.1	4.1
Previously published	4.4	4.2	5.0
Difference	(0.1)	(0.1)	(0.9)
Consumption			
Current	4.8	5.0	4.8
Previously published	4.7	5.3	5.3
Difference	0.1	(0.3)	(0.5)
Gross Private Domestic Investment			
Current	11.8	6.6	6.8
Previously published	12.5	6.6	10.2
Difference	(0.7)	0.0	(3.4)
Personal Income			
Current	7.0	4.7	7.0
Previously published	6.5	5.4	6.3
Difference	0.5	(0.7)	0.7
Wage and Salary Disbursements			
Current	7.8	6.7	8.2
Previously published	7.8	6.7	6.7
Difference	0.1*	0.0	1.5
Corporate Profits			
Current	(9.0)	7.7	8.9
Previously published	(4.3)	8.5	12.5
Difference	(4.7)	(0.9)*	(3.6)
Output Per Hour Nonfarm Business			
Current		2.3	3.0
Previously published		2.6	4.3
Difference		(0.3)	(1.3)

*Difference may appear imprecise due to rounding.
Source: U.S. Department of Commerce, Bureau of Economic Analysis; U.S. Department of Labor, Bureau of Labor Statistics.

Figure 5
Impact of the NIPA Revisions on Real Potential GDP Growth
(percent change)



Source: DRI-WEFA, DOB staff estimates.

Although the central bank can point to several successes in the 1990's, the ability of monetary policy to stabilize the economy remains limited. It can cushion but not eliminate the impact of economic shocks. Similarly, the potential for new technologies to dampen inventory cycles has also been shown to have its limitations. Indeed, as has happened many times in the past, the introduction of an important new technology can foment instability in the short run by inducing a round of "exuberant" speculative activity. The experience of the last few years of the 1990's may someday be looked upon as yet another example of history repeating itself, rather than as the emergence of a new economic paradigm.

BOX 1
THE DETERMINATION OF
POTENTIAL GROSS DOMESTIC PRODUCT

Potential Gross Domestic Product (GDP) is the level of output which the economy can produce when all available resources are being utilized at their most efficient levels. The economy can produce both above and below this level, but when it does so for an extended period, economic agents can expect inflation to either rise or fall, although the precise timing of that movement depends on many factors.

Some knowledge of the economy's productive capacity is fundamental to the decision-making process for households, firms, and the monetary authority. Households partially base their expectations surrounding their lifetime accumulation of wealth upon their estimates of the output potential of the economy. Firms choose a profit-maximizing level of labor and capital based on their estimates of the economy's long-run productive potential. An estimate of potential GDP also enables these agents to form expectations regarding the direction which inflation will take in the future. Such expectations might induce the central bank to shift the course of monetary policy.

Measurement of potential GDP requires a formalization of the aggregate production process. Economists refer to this formalization as an aggregate production function, which stipulates that total output is related to the amount of resources which are applied to production. The precise nature of the production function depends upon which sector of the economy one is trying to model.

Following the Congressional Budget Office (CBO), the Division of the Budget divides the economy into five sectors: nonfarm business, farm, government, nonfarm housing, and households and nonprofit institutions.[1] The nonfarm business sector is by far the largest sector of the economy, comprising 84.1 percent of total GDP during 2000. To model this sector, the DOB again follows CBO and adopts the neoclassical growth model incorporating three inputs to the production process: labor as measured by the number of hours worked, the capital stock, and total factor productivity.

Over the course of an economic expansion, we expect periods during which labor and capital are utilized in magnitudes which are above their most efficient levels. Similarly, during recessions, we expect periods when these inputs are underutilized. Therefore, we can adjust the inputs to the production process to their "potential" levels by removing the historical movements in these series which can be associated with the business cycle. To measure the total potential capital stock, DOB multiplies the U.S. Bureau of Economic Analysis' measure of the real capital stock by the capacity utilization rate, after removing the cyclical component of the latter series by using a standard smoothing method known as the H-P filter.[2] To measure the potential level of the number of hours worked, we remove the cyclical component using a methodology developed by the CBO.

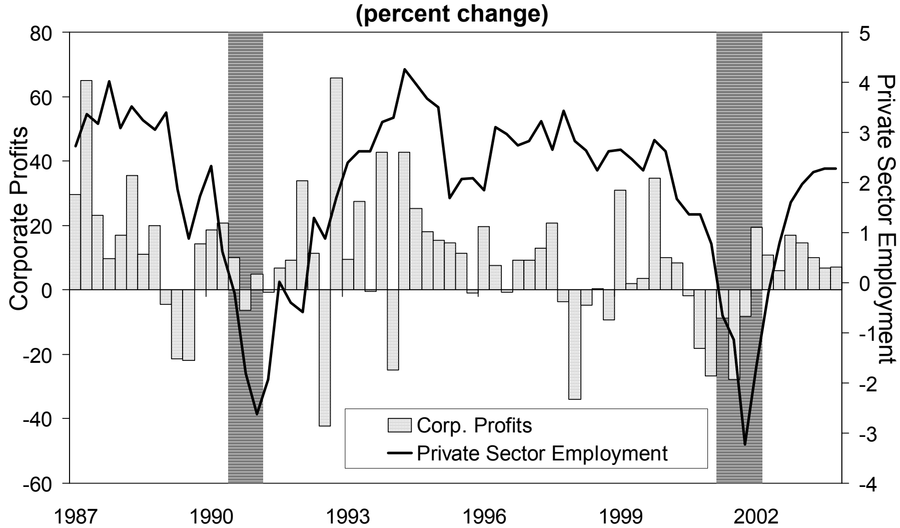
To estimate the potential level of total factor productivity, the actual values of labor and capital are substituted into a fixed-coefficient production function, where a coefficient of 0.7 is applied to labor and 0.3 is applied to capital. The residual obtained by subtracting the value of output obtained from this substitution from the historical value of output is assumed to represent total factor productivity. Removing the business cycle component from this residual yields its potential level. Substituting the potential levels of all of the inputs back into the fixed-coefficient production function, where total factor productivity is given a coefficient of one, yields a measure of potential nonfarm business GDP. For the other sectors of the economy, the cyclical component is removed directly from the series itself in accordance with the method used by CBO.

[1] See "CBO's Method for Estimating Potential Output," Congressional Budget Office, October 1995, and "CBO's Method for Estimating Potential Output: An Update," Congressional Budget Office, August 2001.
[2] See Robert J. Hodrick and Edward C. Prescott, "Postwar U.S. Business Cycles: An Empirical Investigation," Discussion Paper No. 451, Carnegie Mellon University, 1980.

THE HEART OF THE CURRENT SLOWDOWN: CORPORATE PROFITS AND INVESTMENT

The first indication of weakness in the economic environment was a moderation of consumption growth in the second quarter of 2000. The highly leveraged business sector was unable to surmount even a modest reduction in demand. Lower demand, combined with high interest and labor costs and falling stock prices, put significant downward pressure on corporate profits. The accumulation of technological investment resulted in significant overcapacity. Many of the aforementioned internet startups ran out of cash and vanished, thereby reducing the demand for media and telecommunications services, as well as for computer and related equipment. As a result, corporate profits have been falling since the third quarter of 2000 (see Figure 6).

Figure 6
Private Sector Employment and Corporate Profits
(percent change)



Note: Shaded areas represent US recessions; length of current recession is based on DOB forecast.
Source: DRI-WEFA; DOB staff estimates.

U.S. corporate profits are projected to begin a modest recovery in the first quarter of 2002. With the global economy growing slowly at best and domestic demand weak, conditions of excess capacity are expected to persist through most of the current year. The Division of the Budget is projecting a decline in pretax corporate profits of 16.0 percent for 2001, followed by growth of only 1.7 percent for 2002.

Real nonresidential fixed investment is expected to continue to fall through the second quarter. Given current conditions of declining output and excess capacity, the economy's optimal capital-output ratio can be expected to decline in the near-term, further discouraging business investment. In addition, the financial cost of capital, adjusted for inflation, may not fall as rapidly or deeply as current monetary policy might suggest. While it is true that the Federal Reserve reduced short-term interest rates 4.75 percentage points in 2001, the rate of inflation fell over the course of the year. Lower inflation, combined with only moderate declines in long-term rates, is projected to result in a real yield on Baa corporate bonds for 2002 almost a full percentage point above the estimated average for 2001.

Equity market prices are projected to rise gradually over the course of 2002. However, on an annual average basis, the stock market, as measured by Standard & Poor's index of 500 common stocks (S&P 500), is projected to decline 1.0 percent for 2002, following an estimated decline of 16.5 percent for 2001. Therefore, equity markets will likely be a much less significant source of funding for domestic investment relative to the late 1990's. Moreover, the real cost of corporate borrowing is expected to rise in 2002. Consequently, real nonresidential fixed investment is expected to fall 5.3 percent for 2002, following an estimated decline of 2.9 percent for 2001.

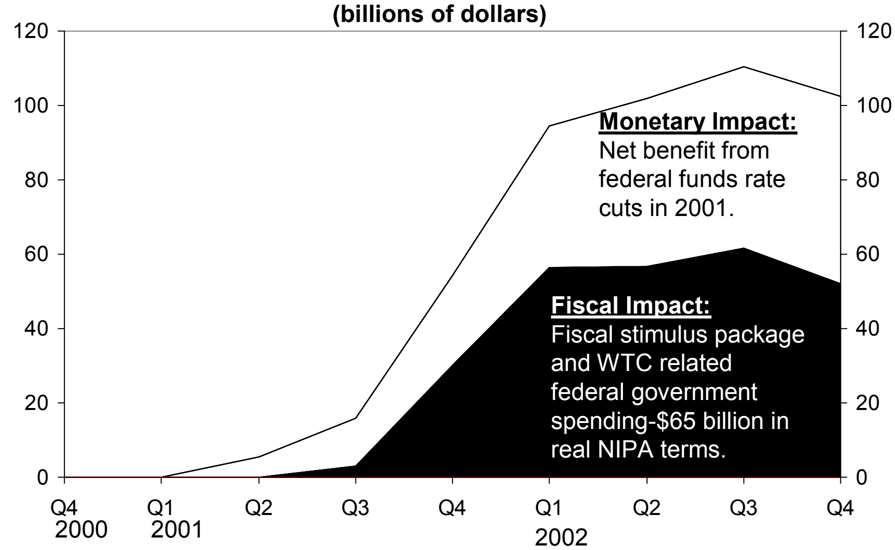
MONETARY AND FISCAL POLICY STIMULUS

The Division of the Budget's forecast for U.S. economic growth for both the fourth quarter of 2001 and 2002 includes the impacts of both monetary and fiscal policy initiatives. Absent these actions, GDP growth for calendar year 2002 would have been projected to be negative. Federal fiscal initiatives expected to stimulate the economy's recovery include the funding of recovery efforts related to the events of September 11, subsidies to the airline industry, as well as tax cuts enacted in June 2001. These measures are projected to add $65 billion to real GDP over the period from the fourth quarter of 2001 to the fourth quarter of 2002.

Monetary policy is imparting a significant stimulus as well. Interest rates were cut rapidly and dramatically during calendar 2001, by a total of 475 basis points. Historically, the full impact of interest rate cuts occurs with an average lag of one year. However, a number of factors may be offsetting the benefit of lower short-term interest rates, including the continued strength of the dollar, the increasing weakness in overseas economies, and perhaps most significantly, the reduction in consumer and business demand.

Nevertheless, simulation studies conducted using the DOB U.S. macroeconomic model indicate that the economy would have been even more sluggish during the first three quarters of 2001 without the Federal Reserve's monetary easing (see Figure 7). Simulation results indicate that without the Federal Reserve's interest rate cuts and the expected amount of fiscal stimulus, real GDP growth for 2001 would be 0.9 percent rather than the 1.0 percent now projected. Moreover, a decline of 0.5 percent in real GDP would be forecast for 2002, rather than the currently projected 0.4 percent growth.

Figure 7
Impact of Monetary and Fiscal Policies on Real Gross Domestic Product
(billions of dollars)



Source: DOB staff estimates.

The Federal Reserve is expected to begin tightening again during the second half of 2002, as the national economic recovery gets under way. In part, the Division of the Budget is guided in its projection of monetary policy shifts by a model of monetary actions known as

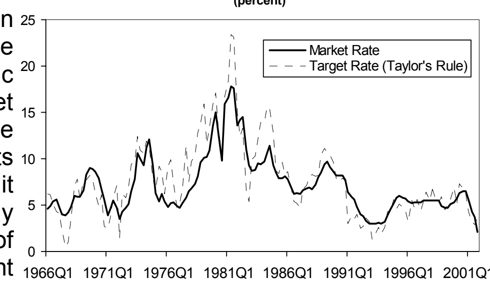
Taylor's Rule (see Box 2). Next year's expected monetary tightening should prevent any inflationary momentum which might occur as a result of the recovery and the expected elimination of the Federal budget surplus.[4]

BOX 2
FORECASTING MONETARY POLICY USING TAYLOR'S RULE

In recent years, the Federal Reserve has executed shifts in its monetary policy stance by changing its target for the federal funds rate. The federal funds rate is the interest rate which banks charge each other in the market for overnight loans. In reality, the Federal Reserve takes information from many sources into account when it formulates policy decisions. However, Taylor's Rule captures this process with a simple model by isolating two factors which are likely to be prominent in the decision-making process. The first factor is the gap between the central bank's target rate of inflation and the expected actual rate given prevailing economic conditions. If the expected actual rate is above the target rate, then the central bank is likely to adopt a tightening bias, sending the target federal funds rate up and reducing inflationary pressure. The second factor is the gap between the actual and the potential rates of output growth. If actual GDP growth is below the Federal Reserve's estimated potential rate, then it is likely that the central bank will lower its policy target for the federal funds rate to stimulate growth. More precisely, Taylor's Rule adds a weighted average of these two factors to the estimated real rate of interest and the expected actual rate of inflation to obtain a target federal funds rate.

DOB assumes that the central bank's target rates for inflation and potential GDP growth are 2.0 percent and 3.4 percent, respectively. DOB uses the historical average as an estimate for the underlying real interest rate, instead of the 2.0 percent rate which is generally used in economic literature. Figure 8 compares the federal funds policy target rate implied by the DOB application of Taylor's Rule with the actual federal funds rate. Although Taylor's Rule represents only a simplification of the monetary policy process, it appears to capture the central bank's behavior acceptably well for most of the period. The Federal Reserve's policy of monetary easing that prevailed throughout 2001 is consistent with Taylor's Rule, as is the monetary tightening projected to occur toward the end of 2002.

Figure 8
Taylor's Rule: Federal Funds Rate
(percent)



Source: DRI-WEFA.
Note: Fourth quarter of 2001 is DOB staff estimate.

OUTLOOK FOR U.S. EMPLOYMENT AND INCOME

Falling corporate profits have also translated into employee layoffs (see Figure 6). In the present strong-dollar low-inflation environment, firms are facing diminishing demand for their products abroad and are largely unable to raise prices at home. Consequently, the need to cut costs has resulted in a reduction in employment. About 1.4 million jobs were lost between March and December of 2001, more than half of the jobs lost during the early 1990's recession.

The sector bearing the heaviest losses has been manufacturing, losing 1.5 million jobs since July 2000. Due in part to the impact of a strong dollar on foreign demand for U.S. exports, employment in the nation's manufacturing sector was never able to stage a strong recovery from the 1998 Asian crisis. The slowdown in investment growth during the second half of 2000 and the subsequent declines during the first three quarters of 2001 also have contributed to job losses in manufacturing. Of the 1.5 million manufacturing jobs lost since July 2000, 1.1 million were eliminated from durable goods-producing industries.

[4] The Office of Management and Budget now projects that the current recession, revised growth forecasts for future periods, and increased Federal spending following the September 11 attacks are likely to result in Federal budget deficits for the current year and for at least two additional years. <http://www.whitehouse.gov/omb/pubpress/2001-61.html>

The loss of jobs officially classified as manufacturing may understate employment losses in that sector, since many manufacturing firms have turned to temporary service agencies to supplement their workforces. Employment in personnel supply services had been growing steadily since the 1995 soft landing, adding 1.5 million jobs between June 1995 and April 2000. However, between April 2000 and December 2001, personnel supply services employment fell by 719,000, making it one of the hardest hit industries during the current slowdown. It is estimated that many of the jobs added by that industry in the late 1990's, as well as those lost since early 2000, were in manufacturing.[5]

Since September 11, the nation's employment malaise has spread well beyond the goods-producing sectors. Although there was evidence that the business sector had been cutting back on expenses even prior to that date, travel and tourism came to a virtual halt immediately after the September 11 disaster and have far from fully recovered. Recent employment reports have shown significant losses in all industries related to travel and tourism, such as transportation services, hotel and motel services, and retail trade. Moreover, these industries are perhaps the most vulnerable to the almost daily news of potential terror attacks and threats to the public health.

The Division of the Budget projects a decline in nonagricultural employment of 0.6 percent for 2002, following growth of 0.4 percent for 2001. With the levels of output and investment projected to remain low, employment is not expected to rebound to its pre-recession level until early 2003. For the first time, the Division of the Budget is classifying and forecasting employment and wages for both the nation and the State according to the North American Industry Classification System, or NAICS (see Box 3). Nonagricultural employment losses are projected for 2002 for many of the major industry groups, as defined under NAICS.

The decline in output and employment will result in much lower wage growth than recorded for the late 1990's. The collapse of the high-tech sector, with an average wage rate, including bonuses and stock options, substantially higher than the overall national average, will contribute significantly to this decline. Lower bonuses and layoffs in the finance sector will have a similar impact. The Division of the Budget is projecting wage growth of 5.4 percent for 2001, followed by growth of only 2.0 percent for 2002, the lowest growth in wages since 1991. Similarly, total personal income growth is expected to grow 5.0 percent for 2001, followed by 2.8 percent growth for 2002.

[5] Manpower Inc., a large temporary placement agency, reports that 40 percent of its revenues come from the manufacturing sector (*New York Times*, November 3, 2001, C3).

BOX 3
NORTH AMERICAN INDUSTRY CLASSIFICATION SYSTEM

The Standard Industrial Classification System (SIC) system — the system used for many years to classify most U.S. economic data by industry or type of business — will soon be replaced. All U.S. government data collection agencies are adopting the North American Industry Classification System, or NAICS. The purpose of this overhaul is to better reflect the current industrial composition of the U.S. economy and to make the classification system more compatible with those of Canada and Mexico.

NAICS differs from the older SIC system in its use of the type of production activity as its organizing principle. In contrast, the SIC system tends to focus on the type of output or end-use. For example, under the SIC system, retail trade businesses were those who sold directly to households, while wholesale trade often referred to sales to businesses. However, in today's economy, many firms sell to both households and businesses. Hence, under NAICS, retail trade businesses are those who sell merchandise in small quantities, while wholesale trade businesses sell goods in large quantities. While the SIC system was created for an economy which is primarily manufacturing based, the NAICS system is more suited to today's U.S. economy, which is more service and technology oriented.

Under NAICS, the broadest classification category is the 2-digit industry code, of which there are 20. Some sectors are very recognizable from the SIC classification system, such as construction. Other sectors include industries from a variety of SIC codes, such as the information sector. Another new NAICS grouping, accommodation and food services, includes both SIC categories of eating and drinking establishments and hotels. Some new detailed NAICS classifications that did not exist as independent SIC codes are: fiber optic cable manufacturing, convenience stores, telecommunication resellers, HMO medical centers, telemarketing bureaus, casinos, and bed-and-breakfast inns. Each industry now has a 6-digit NAICS code as well as a 4-digit SIC code.

The NAICS system is being applied to a variety of economic data, including employment, wages and industrial production data. Employment data will be released on a NAICS basis starting in 2003 at both the national and State level. Historical employment data that has been released over the years on a SIC basis was not expected to be released on a NAICS basis. However, as a result of a state appropriation to the New York State Department of Labor, historical SIC based data will be converted to the NAICS, providing historical continuity, initially back to 1990, and eventually back to 1975.

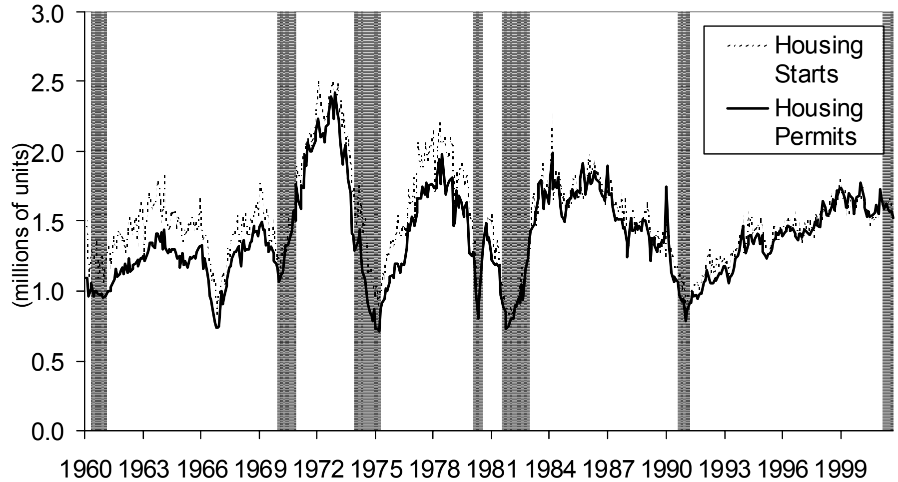
The historical NAICS series currently under development at the New York State Department of Labor will provide detailed data at both the industry and geographical levels. In anticipation of the release of these data, DOB has constructed estimates of NAICS employment at the 20-group 2-digit level for employment data going back to 1975. The basis for the data construction is a "bridge" table developed by the Census Bureau from the1997 Economic Census data.[1] This table allocates the 1997 level of employment for each 1-digit SIC major industry classification to the appropriate 2-digit NAICS sectors. The implied employment shares are applied to employment for the entire historical period, producing a consistent historical time series classified in accordance with the NAICS.

[1] See U.S. Census Bureau, "1997 Economic Census: Bridge Between SIC and NAICS," Table 2. <http://www.census.gov/epcd/ec97brdg>

CONSUMERS RETRENCH

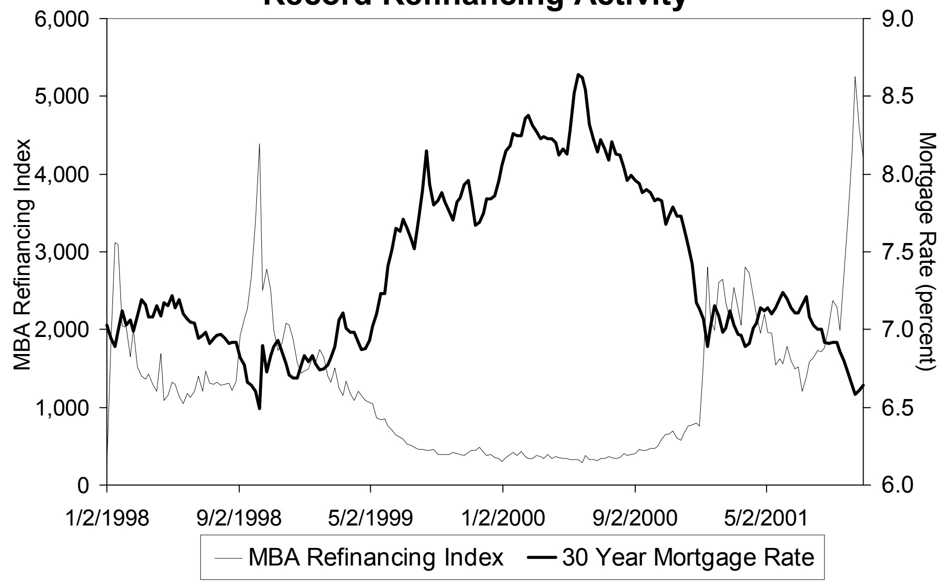
With the steady decline in equity prices since March 2000, the household sector has begun to reassess its long-term income prospects. With the Federal Reserve still increasing short-term interest rates, consumers began to retrench during the second quarter of 2000, although only modestly. Quarterly consumption growth had averaged 4.9 percent from the first quarter of 1997 to the first quarter of 2000, but only 3.3 percent from the second quarter of 2000 to the second quarter of 2001. Higher short-term rates affect consumption directly by increasing the interest rate on short-term consumer loans. Moreover, long-term mortgage rates were following the Federal Reserve's lead, resulting in declines in housing starts and applications for mortgage refinancings by late 1999 (see Figures 9 and 10). In an environment of rising home values, the refinancing of a mortgage often produces a cash windfall which can, in turn, fuel additional consumption. The combination of fewer refinancings and falling equity values put significant constraints on consumption growth.

Figure 9
U.S. Housing Market



Note: Shaded areas represent US recessions.
Source: DRI-WEFA.

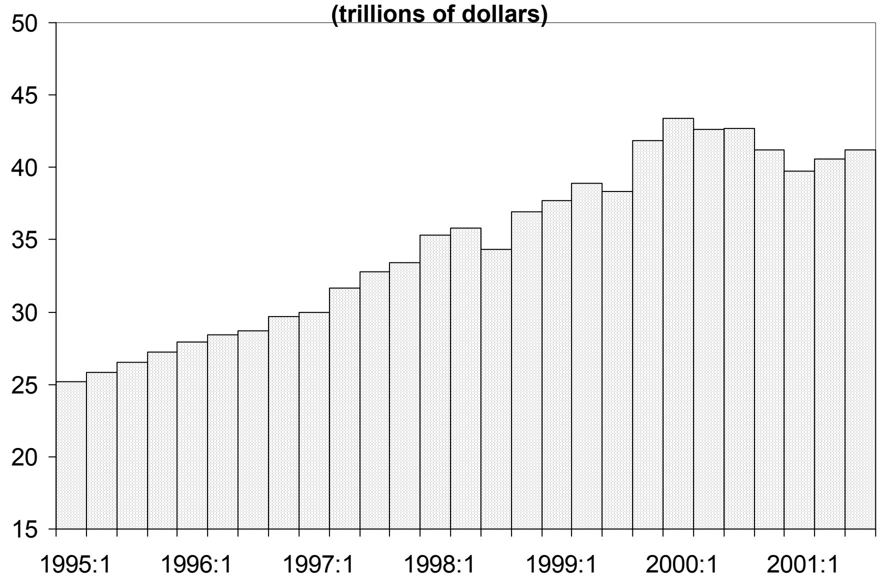
Figure 10
Record Refinancing Activity



Source: DRI-WEFA and Mortgage Bankers Association of America.

Equity prices continued to fall through the first nine months of 2001, despite the Federal Reserve's policy shift in January. Real household net worth fell by $2.2 trillion between the first quarter of 2000 and the third quarter of 2001 (see Figure 11). With consumption growth already on the decline, the events of September 11 brought consumer spending to a near halt. U.S. retail sales fell by a sharp 2.2 percent on a month-over-month basis in September. In November, consumer confidence fell to its lowest level since October 1993, but rebounded in December.

Figure 11
Real Household Net Worth
(trillions of dollars)



Source: DRI-WEFA.

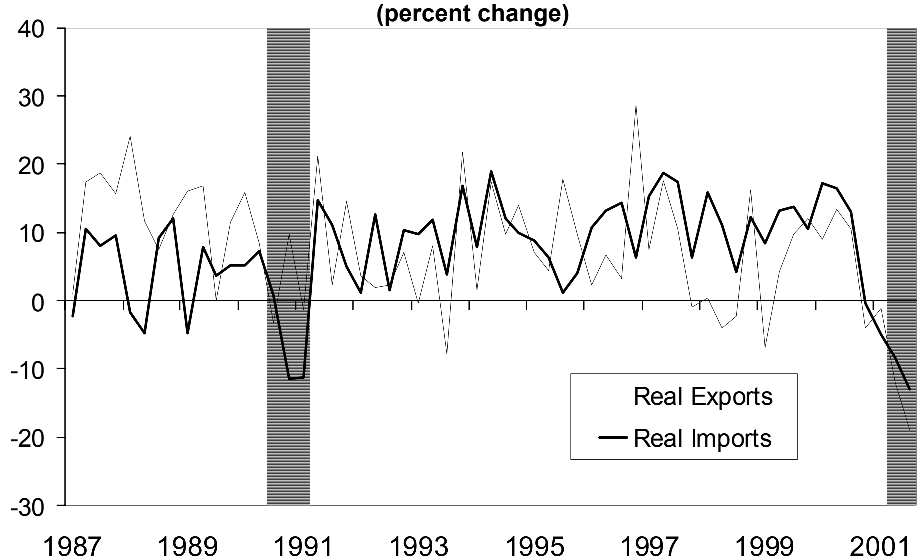
The Division of the Budget expects a decline in real consumption spending of just over 3 percent for the first quarter of 2002. This compares favorably with the last recession, when consumption fell by 3.3 percent and 1.8 percent, respectively, during the fourth quarter of 1990 and the first quarter of 1991. Toward the end of 1990, consumers were distracted by the war with Iraq. Real incomes were depressed by the spike in energy prices engendered by that conflict. Both short-term and long-term interest rates were significantly higher than today. In addition, the collapse of the real estate market in the Northeast reduced the value of what for many households is their most important asset, their homes.

Today, households are weathering declines in employment and real wages, as well as the reduction in financial net worth since the spring of 2000 (see Figure 11). However, of the total increase in financial wealth that has accrued since 1995, when the equity market started on its remarkable upward trend, only a portion has been lost. Moreover, home values have risen consistently over the same period. Today's relatively low inflation low interest rate environment is expected to cushion the blow to household purchasing power in the face of declining employment. In addition, many firms, particularly automakers, are offering incentives, such as low-cost financing, to induce consumers to spend. The October spike in retail sales indicates that these tactics are meeting with some success. Consequently, growth in consumer spending is expected to resume in the second quarter of 2002, fueled by lower interest rates, and additional growth in mortgage refinancings. Real U.S. consumption spending is projected to grow 2.7 percent for 2001, followed by growth of 0.5 percent for 2002.

GLOBAL SLOWDOWN

A world-wide economic slowdown is underway. Following the Asian financial crisis in 1998, the role of the U.S. economy as the world's economic growth engine became apparent. When the U.S. economy began to slow toward the end of 2000, that engine stalled and the impact on world economic growth became significant. The rate of decline in real non-oil U.S. imports has accelerated steadily since the fourth quarter of 2000, falling 12.0 percent during the third quarter of 2001 (see Figure 12). U.S. exports show a similar pattern of decline, indicating that foreign demand for U.S. goods has fallen simultaneously with the decline in U.S. demand for imported goods. In addition to the global recession, there is anecdotal evidence that the U.S. war on terrorism may also have a negative impact on global trade.

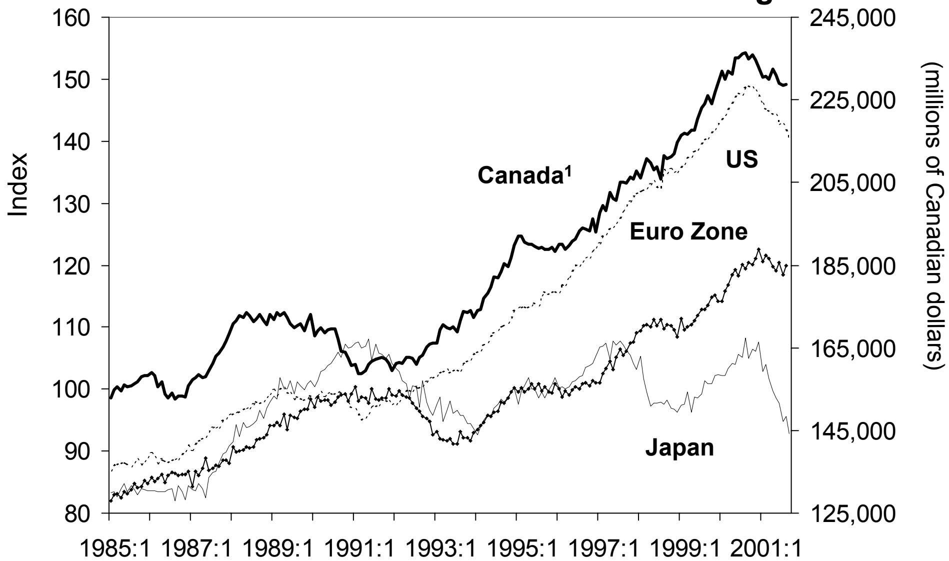
Figure 12
Real Imports and Exports
(percent change)



Note: Shaded areas represent US recessions.
Source: DRI-WEFA.

As indicated in Figure 13, the movements within the economies of the U.S. and its largest trading partners have become much more synchronized. During the recently concluded expansion, industrial production measures for the U.S., Canada, Japan, and the Euro zone peaked within five months of one another. In the early 1990's, industrial production for Japan and for those countries now participating in the common European currency continued on their upward trends through the end of the U.S. recession in early 1991.

Figure 13
Industrial Production in Manufacturing



[1] Real industrial output.
Source: DRI-WEFA.

The Division of the Budget forecast for U.S. exports assumes a long-run stable relationship between export growth and growth in the global economy. With much of the global economy in recession, exports are expected to fall during the fourth quarter of 2001 and the first quarter of 2002, followed by weak growth for the remainder of the year. In addition, declining inflation will tend to strengthen the U.S. dollar, thereby increasing the price of U.S. exports and putting additional downward pressure on real export growth. Moreover, with the world business cycle becoming more synchronized, there is less hope of a significant decline in the value of the U.S. dollar relative to the currencies of the nation's trading partners, which would stimulate demand by foreigners for U.S. goods.

The Division of the Budget is projecting a decline in real U.S. exports of 4.7 percent for 2001, followed by larger decline of 6.0 percent for 2002. Similarly, real non-oil imports are expected to decline by 3.1 percent for 2001, followed by a decline of 2.3 percent in 2002. Assuming no major disruption in the international oil market, real oil imports are expected to grow 3.8 percent for 2001 and 6.5 percent for 2002.

DATING THE RECESSION

On November 26, 2001, the National Bureau of Economic Research Business Cycle Dating Committee declared that the nation's longest expansion peaked in March 2001. Although official statistics on real U.S. GDP indicate that the national economy grew 0.3 percent during the second quarter, the Dating Committee determined that the nation has been in recession since April. This seeming inconsistency has engendered significant interest in the Dating Committee's method for dating business cycles.[6]

Despite what is commonly believed, the Dating Committee does not define a recession as two consecutive quarterly declines in real GDP. Rather, it defines a recession as a significant and prolonged downturn in economic activity, which is spread out over many sectors. Because a downturn must continue for at least several months, the Committee does not

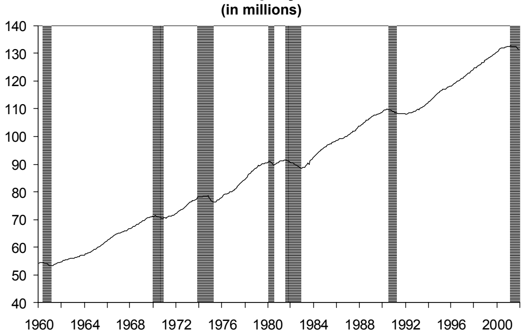
[6] For a detailed discussion of NBER's recession dating procedure, see "The NBER's Recession Dating Procedure", <http://www.nber.org/cycles/recessions.html>.

make the determination of a business cycle peak until many months after the peak actually occurs. For example, the official designation of the current period as a recession did not occur until eight months after the peak. Similarly, the Committee did not announce until April 1991 that July 1990 was the expansionary peak immediately preceding the last recession.

In fact, the Committee does not use GDP data to determine business cycle turning points because it is "measured only at a quarterly frequency and is continually revised." Rather, the Committee uses monthly data to determine business cycle peaks and troughs, focusing on four major indicators. Two of those indicators — employment and real personal income less transfer payments — offer economy-wide coverage. The other two measures — industrial production and real manufacturing and retail trade sales — cover trends in manufacturing and goods markets. The Committee considers other measures as well.

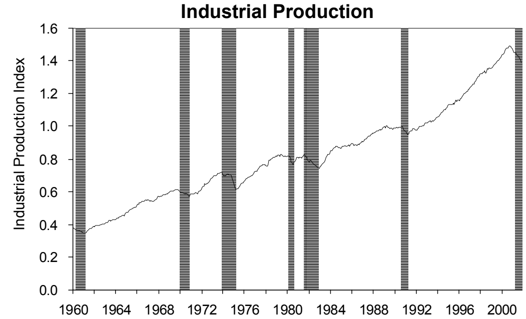
The Dating Committee considers employment to be the most informative monthly indicator covering the entire economy. Data through December indicate a decline in national employment of 1.0 percent since March of 2001 (see Figure 14). This compares to an average decline of 1.1 percent over the past six recessions.

Figure 14
Total Employment
(in millions)



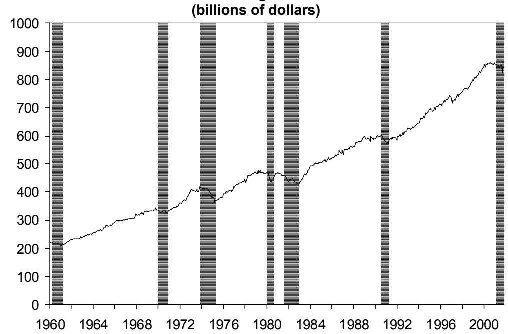
Note: Shaded areas represent US recessions.
Source: DRI-WEFA.

Figure 15
Industrial Production



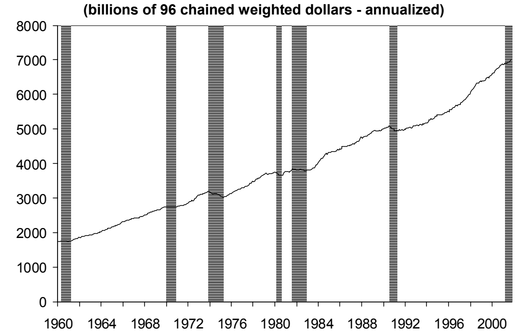
Note: Shaded areas represent US recessions.
Source: DRI-WEFA.

Figure 16
Real Manufacturing and Trade Sales
(billions of dollars)



Note: Shaded areas represent US recessions.
Source: The Conference Board.

Figure 17
Real Personal Income Minus Transfers
(billions of 96 chained weighted dollars - annualized)



Note: Shaded areas represent US recessions.
Source: The Conference Board.

It appears that the manufacturing sector has been in recession for more than a year. Industrial production, which measures manufacturing activity, has been declining since October 2000 (see Figure 15). From its peak in September 2000, the industrial production index has declined 6.6 percent through November 2001. This compares with a 4.2 percent decline during the 1990-91 recession and an average decline of 4.6 percent over the past six recessions. Similarly, real manufacturing and retail trade sales have declined in 8 months of the last 13 months since September 2000 (see Figure 16).

The last major indicator to signal a recession was real personal income minus transfers. That indicator declined significantly in October, followed by another small decline in November (see Figure 17). Although real personal income minus transfers has not dropped substantially during past recessions, it is projected to fall during the first two quarters of 2002.

TABLE 2
U.S. SELECTED ECONOMIC INDICATORS*
(calendar year)

	2000 (actual)	2001 (estimate)	2002 (forecast)	2003 (forecast)	2004 (forecast)	2005 (forecast)
Gross Domestic Product (current dollars)	6.5	3.3	1.9	5.2	5.3	5.5
Gross Domestic Product	4.1	1.0	0.4	3.4	3.5	3.5
Consumption	4.8	2.7	0.5	4.2	3.8	3.2
Residential Fixed Investment	0.8	1.5	(0.9)	3.4	4.2	3.1
Nonresidential Fixed Investment	9.9	(2.9)	(5.3)	4.1	7.0	8.7
Change in Inventories (dollars)	50.6	(52.1)	11.4	41.1	30.3	34.0
Exports	9.5	(4.7)	(6.0)	8.7	9.6	8.2
Imports	13.4	(2.8)	(1.7)	12.1	9.4	8.3
Government Spending	2.7	3.2	3.3	2.0	1.9	2.0
Pre-tax Corp. Profits	8.9	(16.0)	1.7	11.3	6.6	5.3
Personal Income	7.0	5.0	2.8	6.1	5.9	5.8
Wages	8.2	5.4	2.0	7.1	6.6	5.7
Nonagricultural Employment	2.2	0.4	(0.6)	1.7	2.3	2.0
Unemployment Rate (percent)	4.0	4.8	6.6	6.4	6.0	5.7
S&P 500 Stock Price Index	7.6	(16.5)	(1.0)	9.1	9.1	9.1
Federal Funds Rate	6.24	3.89	2.01	3.38	3.98	4.37
Treasury Note (10 year)	6.03	5.02	5.27	6.14	6.50	6.71
Consumer Price Index	3.4	2.8	1.5	2.3	2.3	2.5

* All indicators are percent changes except change in inventories, the unemployment rate, and interest rates; all GDP components refer to chained 96 dollars, unless otherwise noted.
Source: U.S. Department of Commerce; U.S. Bureau of Labor Statistics; Projections for 2001-05 by New York State Division of the Budget.

COMPARISON WITH OTHER FORECASTERS

Table 2 presents the Division of the Budget's forecast for selected U.S. economic indicators. The Division of the Budget's macroeconomic model underwent substantial revision in 2000. A brief description of the model is presented in Box 4.

Table 3 compares DOB's forecast for several major indicators with those of other forecasting groups. The Division of the Budget's forecast of 0.4 percent for 2002 is below the 1.0 percent forecast of the January Blue Chip Economic Consensus.

Among the participants of the January Blue Chip consensus, forecasts for 2002 range from growth of 2.9 percent to a decline of 0.5 percent. The width of that range underscores the degree of uncertainty that typically surrounds the onset of a recession. Those who forecast U.S. economic activity must rely upon data that are subject to reporting lags, and subsequently to revision. Consider the recession of the early 1990's, which officially began in August 1990. We can gauge the uncertainty facing forecasters during that time by examining the evolution of the Blue Chip Consensus forecast for 1991. Figure 18 (see Box 5) shows how the consensus forecast changed between January 1990 and December 1991. Ultimately, revised data shows the economy contracted by one-half of one percentage point in 1991. However, that information did not become available to economists until early the next year. In addition, many forecasters may not wish to stray too far from the prevailing wisdom on the direction of the economy. Figure 18 indicates that few forecasters had correctly estimated the extent of the 1990-91 recession, even by the end of 1990. The consensus forecast for 1991 GNP growth remained positive or flat until May 1991.[7]

TABLE 3
U.S. ECONOMIC FORECAST COMPARISON — 2001-2005

	2001 (preliminary)	2002 (forecast)	2003 (forecast)	2004 (forecast)	2005 (forecast)
Gross Domestic Product (GDP) (1996 chain percent change)					
DOB	1.0	0.4	3.4	3.5	3.5
DRI- WEFA	1.0	0.6	3.7	3.7	3.0
Blue Chip Consensus	1.0	1.0	3.4	N.A.	N.A.
Consumer Price Index (CPI) (percent change)					
DOB	2.8	1.5	2.3	2.3	2.5
DRI- WEFA	2.9	1.9	2.6	2.6	2.5
Blue Chip Consensus	2.9	1.7	2.4	N.A.	N.A.
Unemployment Rate (percent)					
DOB	4.8	6.6	6.3	5.8	5.5
DRI-WEFA	4.8	6.2	5.9	5.3	5.2
Blue Chip Consensus	4.8	6.1	5.7	N.A.	N.A.
Treasury Bill Rate (3 month)					
DOB	3.4	2.2	3.5	4.0	4.3
DRI-WEFA	3.4	2.0	3.7	4.6	4.6
Blue Chip Consensus	3.4	2.1	3.4	N.A.	N.A.
Corporate Profits (before tax percent change)					
DOB	(16.0)	1.7	11.3	6.6	5.3
DRI-WEFA	(16.2)	2.6	11.7	3.1	3.1
Blue Chip Consensus	(16.1)	0.2	9.8	N.A.	N.A.

Source: U.S. Forecast Summary, DRI-WEFA, January 2002; Blue Chip Economic Indicators, December 2001 and January 2002; projections for 2001-05 by New York State Division of the Budget.

[7] The Department of Commerce Bureau of Economic Analysis switched from Gross National Product (GNP) to Gross Domestic Product (GDP) as its primary measure of U.S. economic activity in 1992.

BOX 4
THE DIVISION OF THE BUDGET
U.S. MACROECONOMIC MODEL

Macroeconomic modeling has undergone a number of important changes during the last 25 years, primarily as a result of developments in economic and econometric theory. These developments include the incorporation of both rational expectations and micro-foundations based on the long-run optimizing behavior of firms and households. In addition, analysts now employ more flexible specifications of behavioral relations within a vector autoregressive (VAR) model framework. Recent developments also include a more rigorous analysis of the times series properties of commonly used macroeconomic data series, as well as the implications of these properties for model specification and statistical inference. There has also been much study of the long-run equilibrium relationships among macroeconomic data series and the predictive power of these relationships in constraining economic dynamics.

The Division of the Budget's U.S. macroeconomic model (DOB/U.S.) incorporates the theoretical advances described above in an econometric model used for forecasting and policy simulation. The model contains 98 core equations, of which 29 are behavioral. In addition, there are hundreds of auxiliary forecasting equations which incorporate the results from the core model as inputs. The current estimation period for the model is 1965:1 through 2001:3. Our analysis borrows heavily from the Federal Reserve Board model which has been redesigned over the past five years and was constructed using the most up-to-date advances in modeling techniques.[1] We are grateful to Federal Reserve Board economists for providing guidance and important insights as we developed the DOB/U.S. macroeconomic model.

DOB/U.S. could be termed a neoclassical model in economic parlance. Agents optimize their behavior subject to economically meaningful constraints. Households exhibit maximizing behavior over consumption and labor supply, subject to a wealth constraint. Expected wealth is, in part, determined by expected future output and interest rates. Firms maximize profits over labor demand and investment. The value of investment is affected by the cost of capital, as well as expectations about the future path of output and inflation. The economy's long-run growth path converges to an estimate of potential GDP growth. Monetary policy is administered through adjustments to the federal funds rate, as guided by Taylor's Rule. Current and anticipated changes in this rate influence agents' expectations and the rate of return on various financial assets.

DOB/U.S. incorporates three key theoretical elements into this neoclassical framework: expectations formation, equilibrium relationships, and dynamic adjustments (movements toward equilibrium). The model addresses expectations formation by imposing rational expectations as follows: the model specifies a common information set available to economic agents who then incorporate all relevant information when forming their expectations. The model structure incorporates an error correction framework which ensures movement back to an equilibrium which is a solution to a dynamic optimization problem carried out by households and firms.

The model structure reflects the microeconomic foundations which govern optimizing behavior, but is sufficiently flexible to capture the short-run fluctuations in employment and output caused by economic imbalances. DOB/U.S. incorporates dynamic adjustment mechanisms which reflect the fact that while agents are forward-looking, they do not adjust to changes in economic conditions instantaneously. The presence of frictions (costs of adjusting productive inputs, sticky wages, persistent spending habits) governs the adjustment of non-financial variables. These frictions, in turn, create imbalances which constitute important signals in the setting of wages and prices. In contrast, the financial sector is assumed to be unaffected by frictions due to the negligible cost of transactions and the presence of well-developed primary and secondary markets for financial assets.

[1] "A Guide to FRB/US A Macroeconomic Model of the United States," edited by F. Brayton and P. Tinsley. Federal Reserve Board, Version 1.0, October 1996.

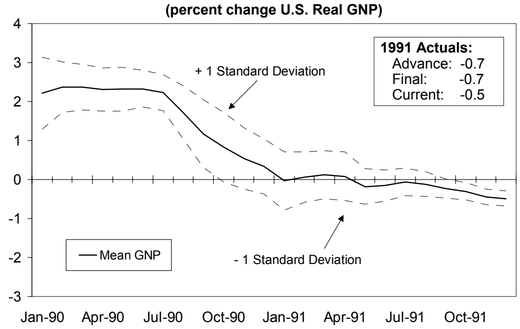
BOX 5
FORGING A CONSENSUS DURING UNCERTAIN ECONOMIC TIMES

At the beginning of every month, *Blue Chip Economic Indicators* reports the forecasts of about 50 major forecasting groups for 15 individual national economic indicators, including the growth rate of real GDP. The average of these forecasts is referred to as the "Blue Chip Economic Consensus Forecast." Each month's report contains the forecasts for both the current year and the following year. The Blue Chip consensus forecast is widely used by both private and public organizations for planning purposes.

The popularity of the Blue Chip forecast rests on the notion that an average over a range of independently produced forecasts, based on disparate sets of methods, information sets, and cost functions, should have a high probability of being accurate. However, the accuracy of the consensus forecast may be severely limited in certain situations. For example, the consensus forecast has tended to fail to accurately forecast business cycle turning points. This is not particularly surprising, in light of lags in the reporting of economic data, as well as the frequency and magnitude of revisions to the data. The problem is illustrated in Figure 1, which shows the evolution of the consensus forecast for real GNP for 1991, starting with the forecast published in January 1990 and ending with the forecast published in December 1991. It is evident that the consensus failed to foresee the seriousness of the slowdown until the beginning of 1991, and did not forecast a significant decline in real GNP until the middle of the year.

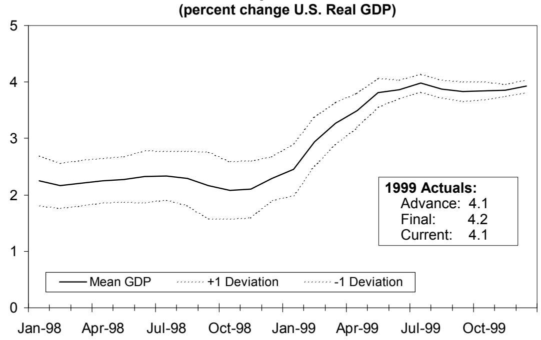
Figure 18 also shows the lag with which the consensus forecast incorporates the release of the most recent quarterly GDP growth rate and its revision. By the time the BEA's first estimate of quarterly growth is released, the economy is a full month into the next quarter. By the time that estimate becomes incorporated into the Blue Chip consensus, over two months have passed. Consequently, not until the March report was released would the consensus forecast include the information that real GNP had declined in the fourth quarter of 1990. The length of that lag should urge caution among users of the consensus forecast, particularly at times like the present, when the U.S. economy is at a turning point. Figure 19 indicates a similar problem when the economy is booming.

Figure 18
Evolution of the Blue Chip Consensus Forecast for 1991
(percent change U.S. Real GNP)



Source: Federal Reserve Bank of Philadelphia; Blue Chip Economic Indicators.

Figure 19
Evolution of the Blue Chip Consensus Forecast for 1999
(percent change U.S. Real GDP)



Source: Federal Reserve Bank of Philadelphia; Blue Chip Economic Indicators.

As suggested above, the value of the consensus forecast rests on independence among the individual forecasters. However, in reality, individual forecasters may not want to deviate too widely from the prevailing view. The resulting lack of independence could produce some very undesirable results. A preliminary study by DOB staff, of the Blue Chip consensus forecasts for the real GDP growth rate from January 1989 to December 1999, indicates that a "copycat" phenomenon may well exist among the Blue Chip forecasters.[1] The results of the analysis suggest that last month's consensus forecast has a very significant impact on the group's current forecast. Separate analyses based on data for individual forecasters produce similar results. Given these preliminary findings, DOB believes that caution should be exercised when using the Blue Chip consensus forecast as a guidepost for fiscal planning purposes, especially in the neighborhood of a business cycle turning point.

[1] See Gallo, Giampiero M., Clive W. J. Granger and Yongil Jeon, "Copycats and Common Swings: The Impact of the Use of Forecasts in Information Sets," October 2000.

RISKS TO THE U.S. FORECAST

The greatest risk to the U.S. forecast pertains to the length and severity of the recession. Demand for goods and services for the economy may be weaker than expected. Insufficient demand by the consumer, government, and foreign markets could cause investment spending to decline further than projected. Declining corporate profits and continued layoffs could result in even weaker wage growth and less consumer spending than expected. Also, lower than expected equity prices and the advent of declines in housing prices could well have a strong negative impact on the willingness of the consumer to spend.

Many foreign economies could fare more poorly than currently projected: the European economies may fall into recession; Japan's current recession may become more severe than expected; other Asian countries may suffer sharp recessions also, and major Latin American countries are already mired in or at risk of recession, particularly Argentina. In short, much of the world may well be in recession or near-recessionary conditions at the same time. In that case, export demand would suffer more than currently forecasted.

The DOB forecast presumes that the Federal government's fiscal policy actions to-date will result in more funds being spent on goods and services and on projects that enhance economic growth in the short run. If a significant portion of recently enacted tax cuts is saved rather than spent, or if increased government spending simply crowds out private sector spending, then the stimulus may be significantly less effective than expected. It is possible that the Federal government will authorize additional revenue and spending initiatives, beyond those already in place. The DOB forecast presumes that the impact of such measures would likely be offset by higher interest rates.

The large and quite rapid decline in the federal funds rate indicates that a powerful monetary stimulus is in place. However, the effectiveness of monetary actions depends on the desire by consumers and businesses to borrow money, as well as on the willingness of banks to lend. Therefore, monetary policy could have a smaller impact than projected.

The forecast is always at the mercy of surprise shocks. While there exist beneficial as well as detrimental shocks, the most plausible ones at the current time would have strong negative effects on the economy. A major sabotage of the oil producing or delivery process would send oil prices soaring. Further terrorist attacks could severely weaken consumer interest in continuing normal shopping behavior. Financial defaults in Japan, Argentina or elsewhere in the developing world could lead to financial shocks that would be very detrimental to an economy already in recession.

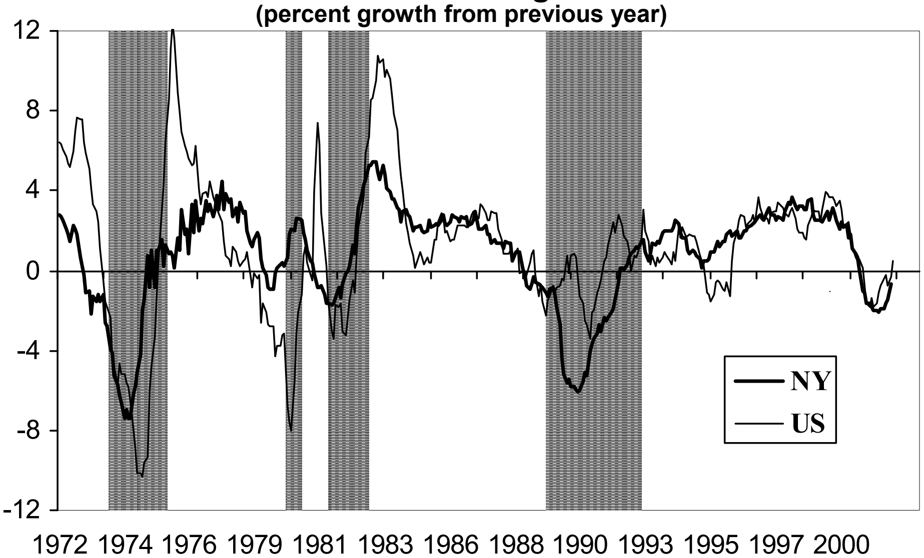
On the other hand, the economy may be stronger than expected. Many of the downside risks enumerated above may fail to materialize. The stock market may do much better than expected, so that the wealth effect may be more supportive of continued consumer spending. Oil prices could continue to drop dramatically, providing further relief to consumers. Finally, monetary and fiscal policy may be more stimulative than expected.

THE NEW YORK ECONOMY

With New York City at the epicenter of the September 11 disaster, the New York State economy is bearing the brunt of the consequent decline in economic activity and employment losses. Thousands of workers have been relocated out-of-state, at least temporarily. Moreover, workers continue to lose their jobs consistent with the contraction in business activity resulting directly or indirectly from the disaster. Given the paramount importance of the financial services, media, and tourism industries to the State economy, it is clear that economic and revenue costs of the World Trade Center disaster will be much more pronounced in New York than in other states.

Prior to September 11, the State economy's rate of growth had been slowing in line with the nation (see Figure 20). Last year's environment of high interest rates and plunging stock prices led to the demise of many "New Economy" firms in the telecommunications, internet and other high-technology industries. Employment growth slowed upstate, with some areas experiencing job declines relative to the same period in 2000. The weakness within the nation's manufacturing sector was paralleled upstate, where manufacturing remains an important component of the economic base. As established corporations faced declining profits, they began to reduce costs by laying off workers. Similarly, those firms tied to the fortunes of the manufacturing sector, particularly in the business service sector, also reduced their workforces.

Figure 20
New York and U.S. Leading Indicator Index
(percent growth from previous year)



Note: Shaded areas represent NY recessions.
Source: DRI-WEFA; The Conference Board; and DOB staff estimates.

Wage growth for the first quarter of 2001 appeared to be accelerating, even as employment growth was slowing down. However, much of the State's first quarter wage growth of 9.6 percent for 2001 is believed to have occurred downstate, due primarily to large bonus payments, particularly within the finance and insurance sector.[8] Finance and insurance sector wages comprised 30.7 percent of total State wages during the first quarter of 2001, a share that is even higher for the downstate region. These earnings are an important growth engine for other downstate activities, such as real estate transactions, retail sales, eating and drinking at restaurants and bars, and entertainment. Those large bonus payments were in turn related to the extremely high level of securities industry profits for the first half of 2000. However, even before September 11, private sector employment growth in the downstate region had fallen sharply from a strong 2.8 percent for all of 2000, to 1.8 percent through the first nine months of 2001 (see Table 4).

[8] The Division of the Budget staff estimate of State wages for first quarter 2001 is based on ES202 data at the firm level.

TABLE 4
NEW YORK STATE EMPLOYMENT GROWTH BY REGION
(percent growth)

	2000		January-September 2001		October and November 2001	
	Total	**Private**	**Total**	**Private**	**Total**	**Private**
Statewide	2.1	2.3	1.2	1.4	(0.7)	(1.0)
Downstate	2.5	2.8	1.5	1.8	(1.1)	(1.2)
New York City	2.8	3.3	1.4	1.8	(1.9)	(2.6)
Upstate	1.3	1.1	0.6	0.7	0.1	(0.5)

Source: New York State Department of Labor, CES.

The events of September 11 dramatically changed the outlook for downstate New York. It is estimated that more than 25 million square feet of office space was either destroyed or damaged on September 11. In the immediate aftermath, economic activity was severely restricted in the area of Manhattan below 14th Street, where over 710,000 people were employed, according to New York State Department of Labor estimates. Many firms were unable to conduct business. The financial markets remained closed for an unprecedented four days, and a large number of high-paying jobs have been relocated out of New York, at least temporarily. Transportation and communications continue to be disrupted. Much of the financial district in southern Manhattan remains closed to normal traffic flow and vital transportation infrastructure has been destroyed. In October, State employment fell for the first time since January 1996. Declines in employment over the next several months are inevitable as firms continue to suffer both the direct and indirect economic impacts of the September 11 disaster.

NEW YORK STATE BUSINESS CYCLES

The Division of the Budget believes that the State economy is in recession. However, there is no official mechanism for dating business cycles at the sub-national level. Recognizing that each state's economy follows its own unique path, DOB staff constructs an index measuring overall economic conditions for New York.[9] The index combines four State data series, including private sector employment, hours worked in the manufacturing sector, the unemployment rate, and sales tax receipts (as a proxy for retail sales). Based on the New York State Index of Coincident Economic Indicators, four prior business cycles have been identified for New York since the early 1970's, as reported in Table 5. Recessions are judged to begin after four to five consecutive declines in the index and conversely are estimated to end after four to five consecutive increases in the index.

TABLE 5
NEW YORK STATE BUSINESS CYCLES

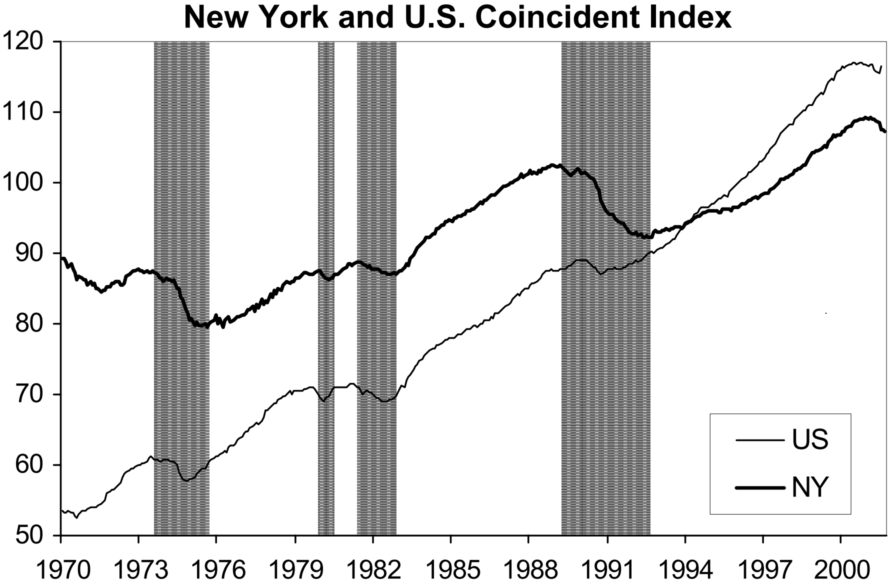
Peak Date	Trough Date	Length of Recession (months)	Private Sector Employment Loss
October 1973	November 1975	25	384,800
February 1980	September 1980	7	55,800
August 1981	February 1983	18	76,600
June 1989	November 1992	41	551,600

Source: DOB staff estimates.

[9] The methodology used to construct the DOB index is based on Stock, J.H, and M.W. Watson. (1991), A Probability Model of the Coincident Economic Indicators, in K. Lahiri and G. H. Moore (eds.), Leading Economic Indicators: New Approaches and Forecasting Records, New York: Cambridge University Press, pp. 63-85.

The Division of the Budget projects that the 2001-02 downturn will not be as deep as the recession which began in New York in the late 1980's and lasted more than three years. Figure 21 indicates that the State's last recession began in July 1989, a full year before the national recession, which began in August 1990. In addition, the State recession lasted 41 months until December 1992, well beyond the official trough of the national downturn. In fact, there are some similarities between current economic conditions and those of the early 1990's. For example, the stock market underwent a significant correction in October 1987, not long before the prolonged recession. Similarly, the stock market has undergone a protracted decline between April 2000 and October 2001. Then, as now, the finance sector is expected to experience significant job losses. In addition, the U.S. was engaged militarily during both recessions.

Figure 21
New York and U.S. Coincident Index



Note: Shaded areas represent NY recessions.
Source: DRI-WEFA; DOB staff estimates.

However, there are also significant differences between the early 1990's and the current economic situation. The initial impact of the September 11 disaster on employment was large and immediate. Not only did thousands of individuals lose their lives, but thousands of workers whose offices were either destroyed or became uninhabitable were transferred to temporary out-of-state office space. The State's travel and tourism industry came to a near standstill. The Division of the Budget estimates an employment decline for the State of over 100,000 for the fourth quarter of 2001, compared with the same period a year ago. This decline is much larger than the job loss experienced at the beginning of the last recession.

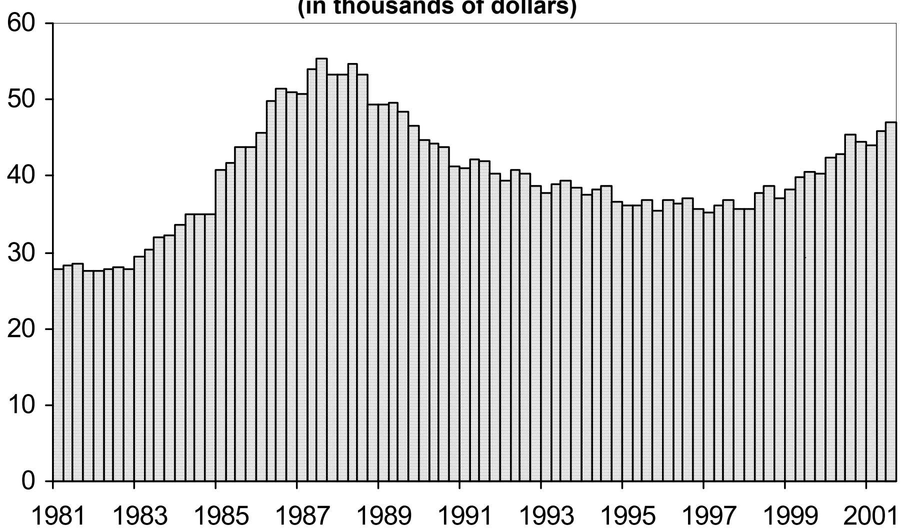
The estimated distribution of job losses across industries for the current recession also differs significantly from that of the early 1990's recession. The national slowdown originated in the manufacturing sector in the middle of 2000. For this reason, the State's economic slowdown first became evident in some of New York's upstate regions where manufacturing still represents almost 20 percent of regional employment. For the State economy as a whole, manufacturing represents a noticeably lower share of total employment than it did ten years ago. However, the slowdown in manufacturing precipitated a decline in the demand for business services, which has become even more important to the State economy since the early 1990's.

Even before September 11, the decline in business services had spread to the travel industry, as businesses looked for ways to cut back on expenses. However, that slowdown became a crisis in the wake of the World Trade Center disaster. Both the fear of further attacks and the delays and inconvenience associated with intensified security measures have decreased the demand for air travel services. Given the heavy dependence of the New York City and State economies on travel and tourism, these events have been particularly damaging to the State economy.

Although the cutbacks in service sector jobs are projected to be deep, they still do not approach the depth of the manufacturing job losses suffered during the last recession. During the last recession, the manufacturing sector suffered in two ways. Corporate restructuring, which had begun in the 1980's in the wake of intensified global competition, accelerated. Moreover, the downsizing of the U.S. Department of Defense following the end of the Cold War significantly reduced the number of defense contracts awarded to State firms. Consequently, New York State lost manufacturing jobs at extremely high rates, peaking at a 6.2 percent loss in 1991. Currently, the State's manufacturing sector is experiencing job losses, but at much lower rates than were experienced during the early 1990's.

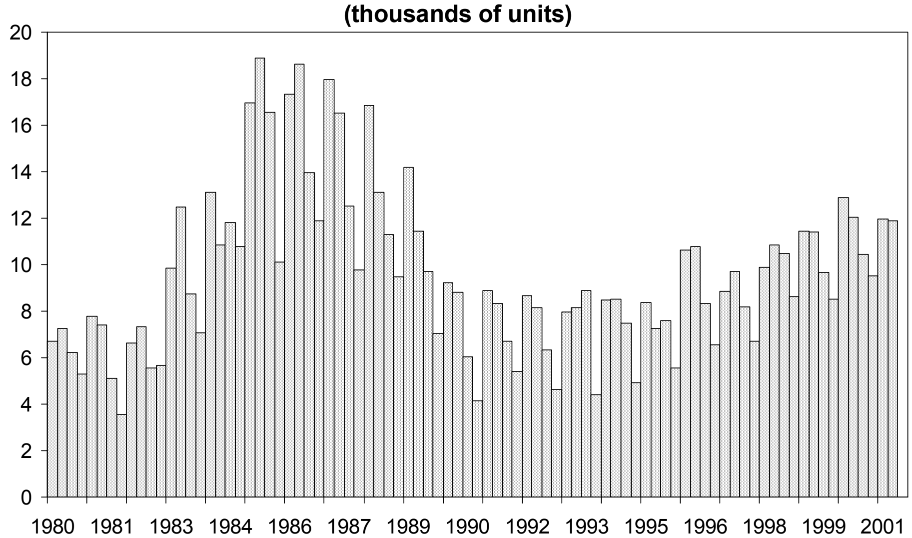
The last recession was also exacerbated by the collapse of the downstate real estate market that followed the employment cutbacks in the finance sector. Figure 22 indicates the extraordinary growth in home prices that occurred in the downstate metropolitan area, even after adjusting for inflation. The rise in home values contributed to the large increase in construction activity that occurred during much of the 1980's (see Figure 23). The decline in home values following the 1987 decline in the stock market precipitated five consecutive annual declines in construction employment from 1989 to 1993. Although home values have risen in recent years, Figure 23 indicates much less speculative building than occurred in the 1980's. Moreover, the effort to recover and rebuild following the destruction of the World Trade Center is expected to increase the demand for construction employment in the coming years.

Figure 22
New York Metro Area Median House Price
Adjusted for Inflation
(in thousands of dollars)



Note: Metro area also includes parts of New Jersey and Connecticut.
CPI for the metro area is used to adjust for inflation.
Source: DRI-WEFA.

Figure 23
New York State Housing Permits
(thousands of units)



Source: U.S. Dept. of Commerce, Bureau of Census.

With the State economy and the State's fiscal condition better positioned than before the previous recession, the current downturn may not be a long one. During the last recession, State employment underwent 15 consecutive quarters of decline, corresponding to a total loss of over 500,000 jobs. Moreover, the loss of manufacturing employment as a result of corporate restructuring and defense downsizing represented a permanent shift in the structure of the State economy. In contrast, the current loss of business service and tourism jobs is expected to be temporary.

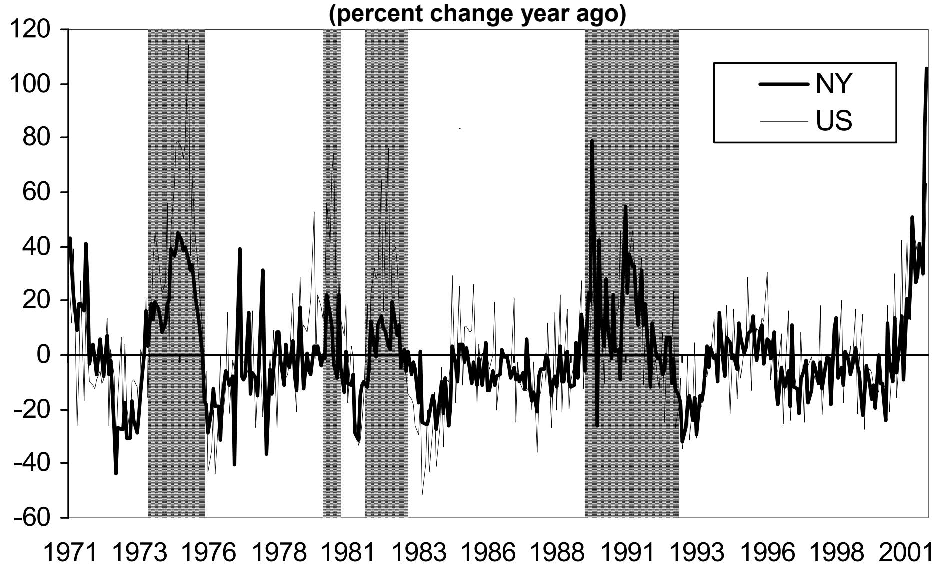
In addition, the loss of government jobs is expected to be much more moderate compared to the significant downsizing that occurred during the last recession.[10] Indeed, after adjusting for the employment surge associated with the conducting of the 2000 Census, government employment is expected to rise during the current slowdown.

EMPLOYMENT OUTLOOK

The national recession, combined with the aftermath of the events of September 11, has brought nine years of State employment growth to an end. Before September 11, initial unemployment insurance benefit claims for the nation as a whole had been rising faster than for New York (see Figure 24). However, the job losses stemming from the World Trade Center disaster raised the number of initial claims for New York by 80 percent in September compared with the same month a year ago. Data for October shows initial claims rising by over 100 percent above the same month in 2000.

[10] The revenue impact of September 11 notwithstanding, the State's fiscal condition going into this recession should lessen the need for significant workforce reductions during the forecast period. Indeed, upon raising the State's bond rating earlier this year, Fitch, Inc. noted that, "Surpluses are now routinely achieved as a result of conservative budgeting practices and a favorable economy." (Fitch, Inc. Press release, February 20, 2001.) Standard & Poor's noted that, "Unlike previous periods, the State has retained an appropriate level of reserves…." (Standard & Poor's, *Public Finance*, December 20, 2000.)

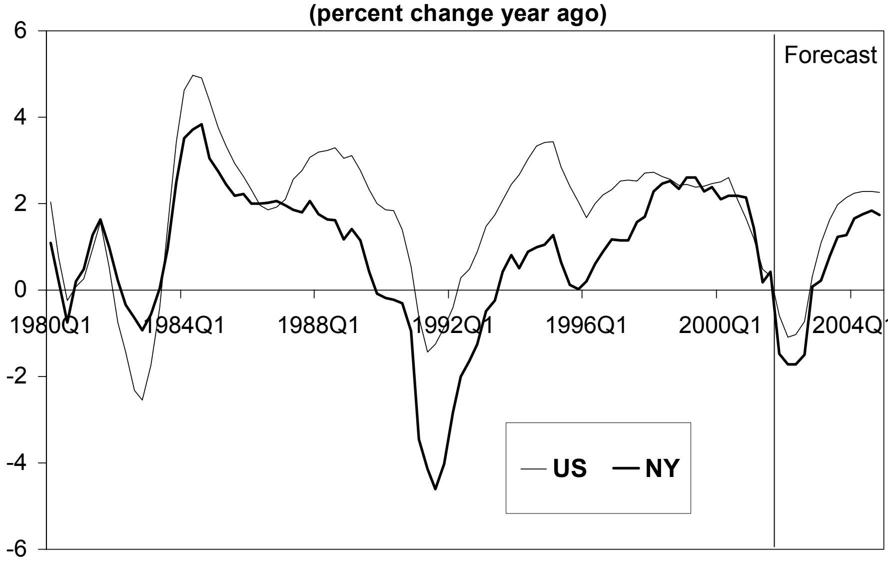
Figure 24
Initial Claims -- New York vs. U.S.
(percent change year ago)



Note: Shaded areas represent NY recessions.
Source: DRI-WEFA.

Total State nonagricultural employment is projected to fall 1.2 percent in 2002, following a 0.1 percent growth in 2001 (see Table 6). The rate of decline projected for the State for 2002 is significantly greater than the 0.6 percent decline forecast for the nation as a whole (see Figure 25). Private sector employment is projected to decline 1.5 percent in 2002, representing a loss of approximately 103,000 jobs, following a 0.1 percent increase for 2001. This represents a significant shift from the 2.3 percent increase for 2000. Table 7 reports projected changes in employment for selected major NAICS sectors (see Box 6). Employment in all of the State's major economic sectors are projected to decline, except for construction, education, health and social services, and public administration. The greatest rates of job loss will be experienced in the manufacturing, finance and insurance, and transportation and warehousing sectors. The State's average annual unemployment rate is expected to rise significantly to 6.5 percent next year from 4.8 percent in 2001. However, this compares favorably with the last three recessions. The State's unemployment rate peaked at 10.2 percent in 1976, 8.6 percent in 1982 and 1983, and again at 8.6 percent in 1992.

Figure 25
Employment Growth -- New York vs U.S.
(percent change year ago)



Source: NYS Department of Labor; DOB staff estimates.

TABLE 6
EMPLOYMENT GROWTH BY MAJOR NAICS SECTORS
(percent change)

	1999	2000	2001	2002	2003
Utilities	(3.6)	0.2	3.1	(0.7)	0.2
Construction	9.5	5.7	3.4	4.8	1.8
Mining and Manufacturing	(2.5)	(1.9)	(3.7)	(4.5)	(0.9)
Wholesale Trade	2.0	0.8	(2.3)	(2.6)	(0.6)
Retail Trade	3.0	2.4	(0.1)	(1.8)	0.5
Transportation and Warehousing	3.0	2.2	(1.0)	(4.8)	0.6
Information	2.5	4.7	1.9	(1.7)	0.2
Finance and Insurance	0.9	0.0	(1.7)	(4.3)	0.6
Real Estate and Rental and Leasing	3.1	1.5	0.3	(0.1)	1.5
Professional, Scientific and Technical Services	6.1	6.0	0.9	(1.5)	1.4
Management of Companies and Enterprises; Administrative and Support and Waste Management, and Remediation Services	7.0	6.4	(0.1)	(2.0)	1.5
Educational Services	0.7	3.1	3.6	1.8	2.5
Health Care and Social Assistance	2.8	1.7	1.3	2.0	2.9
Arts, Entertainment, and Recreation Accommodation, and Food Services; Other Services (except Public Administration)	4.4	2.1	0.8	(2.1)	1.4
Public Administration	1.4	1.5	0.1	0.1	(0.1)
Statewide	2.6	2.2	0.1	(1.2)	0.9

Source: New York State Department of Labor, ES202; DOB staff estimates.

BOX 6
THE TRANSITION FROM SIC TO NAICS: A SNAPSHOT OF THE STATE ECONOMY IN 2000

Beginning in March 2003, employment and wage data for New York State and sub-state regions will be published according to the North American Industrial Classification System (NAICS) instead of the current Standard Industrial Classification (SIC) system (see Box 3). In anticipation of the conversion to the NAICS, DOB has constructed estimates of NAICS employment and wage data at the 20 group 2-digit level for current employment and wage data, going back to 1975. The basis for the data construction is the employment and wage data that is received by the New York State Department of Labor under the unemployment insurance program (ES202 data). Recently, each firm has been reporting their employment and wages under both a SIC and a NAICS code.

The overlap of the SIC and NAICS codes at the firm level permits a reliable methodology for constructing a historical time series back to 1975 for employment and wages. The firm level data is aggregated to the 2-digit level on both a SIC and a NAICS basis. Three regions are specified: upstate, downstate, and unclassified. The statewide numbers are the sum of the three regions. For each region, and for each 2-digit SIC industry, the percentage of the industry that is allocated to each of the 2-digit NAICS groups is calculated using the most recently available data. Then, to get the total for a specific NAICS group, the percentages relating to that NAICS group are applied to the data for all the SIC industries. These same percentages are applied to the SIC data for all prior time periods in order to create a NAICS-based historical time series at the 2-digit level for both employment and wages.

In the SIC system, industries are classified into ten major sectors. The three largest sectors are services, government, and retail, accounting for 34.2 percent, 16.5 percent, and 15.3 percent of total State employment, respectively. The two smallest sectors are agriculture, forestry, and fishing; and mining. Together, they account for less than 1 percent of total employment. Under NAICS, government becomes the largest sector, accounting for 16.6 percent of the total employment, followed by health care and social assistance (12.9 percent) and retail trade (10.7 percent). The smallest four sectors are mining; management of companies and enterprises; agriculture, forestry, fishing ,and hunting; and utilities. Together they account for less than one percent of total employment

Under NAICS, the manufacturing sector's share of total employment decreases from 10.3 percent to 9.5 percent. This is due, in part, to the shift of publishing from manufacturing to the newly created information sector. In addition, firms which specialize in research and development, now classified under manufacturing, will be classified professional, scientific, and technical services under NAICS. The retail trade sector's share is significantly reduced under the new system, from 15.3 percent to 10.7 percent, reflecting primarily the removal of eating and drinking industries from this sector into the new accommodation and food services sector. The finance, insurance, and real estate (FIRE) under SIC becomes the finance and insurance (FI) sector under NAICS, causing its share to be reduced from 8.8 percent to 6.8 percent. Real estate industries are joined by rental and leasing to form a new sector under NAICS.

The manufacturing sector's share of State employment has declined almost continually over the post-World War II period. This has been due to increasing global competition, rising productivity, and, most importantly, the profound change in the industrial structure of the State economy. The transition from a traditional manufacturing base to a more technology-intensive form of manufacturing is expected to continue. The events of September 11 will accelerate the decline in manufacturing employment. It is estimated that the State will lose 36,000 manufacturing jobs in the fourth quarter of 2001 (compared with the same period last year) as a result of the September 11 disaster and the national and global recession. Manufacturing employment is expected to fall 4.5 percent in 2002. The situation is expected to improve by the end of 2002, with the recovery of both the U.S. and global economies.

The destruction of the World Trade Center had a severe impact on the finance and insurance sector, particularly on the securities industry. It is estimated that this sector will lose 31,000 jobs by the end of 2001, compared with the fourth quarter of 2000. The finance and insurance sector has not been a significant contributor to employment growth over the last four decades, which saw a large degree of consolidation. The pace of consolidation accelerated over the past two years due to the repeal of the Glass-Steagal Act of 1933 which prohibited a single firm from offering banking, brokerage and underwriting, and insurance services. The fallout from the September 11 disaster, along with continued consolidation and the weak profit performance of the securities industry, is expected to result in this sector's largest employment decline in over 25 years during 2002.

The State's transportation and warehousing sector is also expected to suffer extensive job losses due to the impact of September 11. It is estimated that this sector will lose 12,800 jobs by the end of the fourth quarter compared with a year ago. Owing to the combined national and global recessions, and the continued terrorist threat, employment in this sector is expected to contract 4.8 percent for 2002 (see Table 7).

TABLE 7
CHANGE IN NEW YORK STATE EMPLOYMENT FOR 2002
SELECTED NAICS SECTORS

Manufacturing	(34,800)
Finance and Insurance	(24,400)
Arts, entertainment, accommodation and food, and other services	(20,100)
Retail trade	(16,000)
Management, administrative and support and waste management and remediation services	(9,100)
Transportation and Warehousing	(10,600)
Construction	16,100
Health and Social Assistance	21,800
All Other	(25,300)
Total	(102,400)

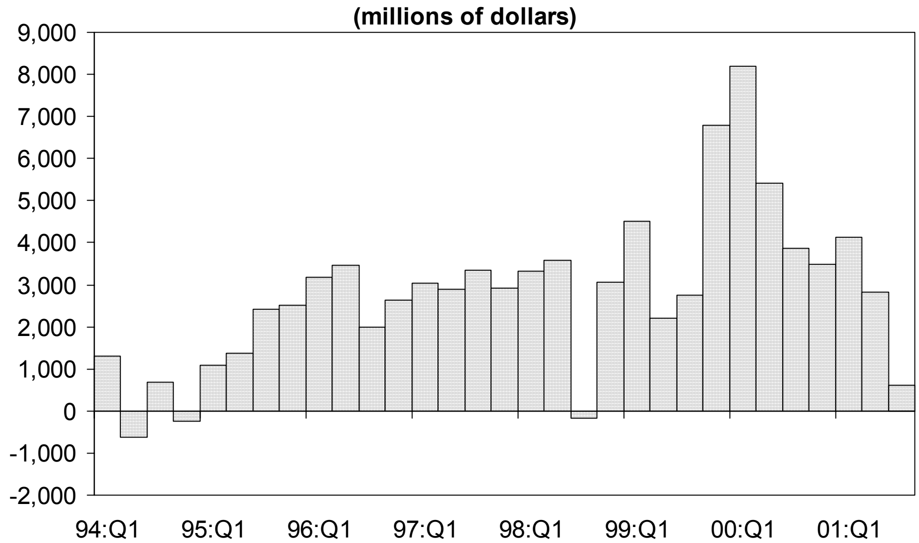
Source: New York State Department of Labor, ES202; DOB staff estimates.

Construction has been a leading growth sector in recent years, due to rising home prices, relatively low interest rates, and the strength of the economic expansion. Employment growth in this sector is expected to remain strong due mainly to the recovery and reconstruction efforts following the September 11 disaster, as well as to low interest rates. Construction employment is expected to grow 4.8 percent for 2002, following growth of 3.1 percent for 2001.

FINANCIAL MARKET ACTIVITY ON THE DECLINE

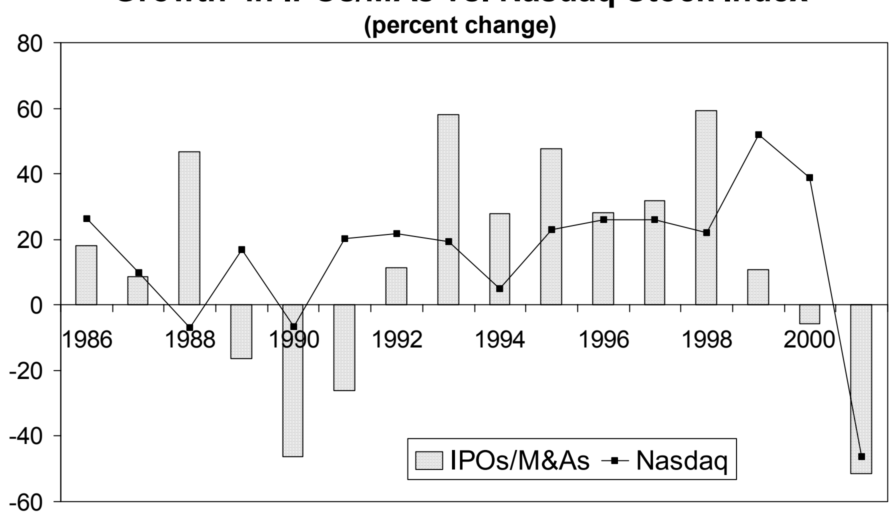
Prior to September 11, securities industry profit growth had slowed relative to the previous year (see Figure 26). The decline in equity prices and the downturn in U.S. corporate profits had resulted in a sharp reduction in the number and dollar value of IPO's and mergers and acquisitions value, two important revenue sources for the industry. Through November 2001, the dollar amount of IPO's is down 38.7 percent from the same period in 2000 (see Figure 27). Revenue earned from merger and acquisition activity is down 51.5 percent for the first three quarters of this year. In contrast, debt underwriting has achieved record levels due to falling interest rates. Based on data through November, the value of total debt underwriting is up 37.3 percent thus far this year. Nevertheless, the extremely high level of profits earned in 2000, particularly in the first half of the year, proved unsustainable.

Figure 26
Securities Industry Pre-Tax Profits



Source: Securities Industry Association.

Figure 27
Growth in IPOs/MAs vs. Nasdaq Stock Index



Note: Growth rates for 2001 are based on three quarters of data for IPOs/MAs.
Source: DRI-WEFA; Thomson Financial Services.

Revenue earned in the securities industry has been on a steady decline since its peak in the first quarter of 2000. Nearly all of the industry's important revenue sources — commissions, market-making gains, underwriting, margin interest income, and mutual fund sales — are contributing to the decline. Most noticeable is the revenue from the tech-stock heavy over-the-counter market, which has plunged by more than 50 percent since its peak in the first quarter of 2000. The bright spot is the revenue from fixed income and derivatives market activity. Due to both the Federal Reserve's interest rate cuts and a flight to quality on the part of investors, revenue from bond trading activity for the first three quarters of 2001 rose 27.8 percent over the same period in 2000. In addition, the volatility of the financial market has caused many investors to be active in the derivatives market in order to hedge their market risk. However, it is unlikely that the increased revenue from these two areas would be sufficient to offset the declines from other sources, given that these two sectors only comprise about 10 percent of total industry revenue in a typical year.

An empirical analysis, based on data for the 20 year period from the first quarter of 1980 through the second quarter of 2001, indicates a significant positive correlation between commission revenue in the current quarter and the rate of return on financial assets over the previous four quarters. As the four quarter rate of return on assets becomes positive, traders enter the market hoping to capitalize on the market's upward momentum. The entry of these "momentum traders" increases transactions volume and thereby commission revenues. Correspondingly, a negative return would result in significantly less trading in the current quarter because few momentum traders would enter the market. Those who have been in the market would hold on to their positions, resulting in less commission revenue. Macroeconomic conditions also have an impact on commission revenue. Prior quarter GDP growth and consumer price inflation tend to be associated with rising commission revenues, while an increase in the federal funds rate tends to be associated with a decline in revenues. These factors suggest little growth in commission revenues over the forecast period.

Impact of World Trade Center Disaster

The Division of the Budget estimates that the events of September 11 will add to the negative impact of the national recession on the profits of the securities industry. The loss in human capital is inestimable. Additionally, the industry incurred losses due to the destruction of physical capital and the cost of relocating operations. The industry's estimated third quarter profits of $0.6 billion were the lowest since the industry incurred net losses during the third quarter of 1998 as a consequence of the Asian financial crisis. For the first three quarters of 2001, securities industry profits are down about 57 percent from the same period in 2000. The fall in profits is contributing to mounting layoffs within the industry. In addition, the sharp decline in profits is expected to result in a severe decline in finance and insurance industry cash bonuses of 43.7 percent for the 2001-02 State fiscal year. This decline is expected to be exacerbated by firms weighting their bonus payouts more heavily in favor of stock options, as well as by the transfer of dislocated workers out-of-State.

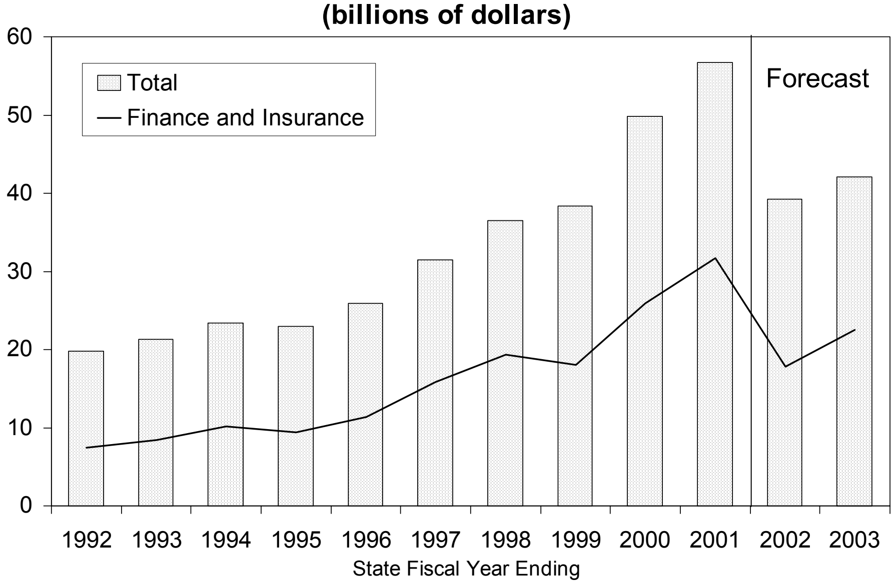
OUTLOOK FOR INCOME

Variable Income Growth

Variable income is defined as that portion of wages derived from bonus payments, stock incentive income, and other one time payments (see Box 7). As a performance incentive for a given calendar year, firms tend to pay employee bonuses during either the fourth quarter of that year or the first quarter of the following year. Although stock options tend to be granted during the same quarters, often as part of a bonus package, an employee may exercise that option, thus transforming it into income, at any time of the year. However, the concentration of variable income payments in the fourth and first quarters makes the State fiscal year a logical period of analysis for discussing the determinants of variable income growth.

As already noted, securities industry profits are estimated to deteriorate significantly during 2001, due to the decline in revenues from financial market activities, such as IPO's and mergers and acquisitions. Moreover, tens of thousands of positions have been lost due to the events of September 11. Therefore, the Division of the Budget projects that variable income for the finance and insurance sector will fall 43.7 percent during the 2001-02 State fiscal year (see Figure 28). Variable income for that sector is expected to rise 26.1 percent during 2002-03, bringing variable income for the finance and insurance sector back to its 1997-98 level.

Figure 28
New York State Bonus Income
(billions of dollars)



Source: NYS Department of Labor; DOB staff estimates.

Although the decline will be most dramatic for finance and insurance firms, the New York economy will see a drop in bonus income across all industries. The largest decline outside of finance and insurance will be in the information sector, due in large part to the collapse of the telecommunications sector. The next largest decline will be seen in the State's manufacturing sector. Overall, bonus income outside of the finance and insurance sector is expected to decline 14.6 percent during 2001-02 and decline 8.7 percent for 2002-03. Total State bonus income is projected to fall 30.9 percent for 2001-02, followed by growth of 7.1 percent for 2002-03. On a calendar year basis, total State bonus income is expected to increase 2.0 percent for 2001, followed by a decline of 24.0 percent for 2002.

BOX 7
THE CONSTRUCTION OF NEW YORK STATE WAGES
AND THE ESTIMATION OF VARIABLE INCOME

Trends in State wages are critical to an accurate analysis and forecast of personal income tax liability and collections. To improve the link between the economic and tax variables on a quarterly basis, the Division of the Budget (DOB) constructs its own wage series from the available primary data sources. This series differs from the data published by the U.S. Bureau of Economic Analysis (BEA).

The Division of the Budget uses only New York data to construct its State wage series. The primary source is data collected under the Federal Unemployment Insurance Program, known as the ES 202 data file. In contrast, the BEA uses national information to adjust the quarterly values for seasonal variation, as well as to ensure that state-level wages add up to national estimates. The consequence is often a significant difference between the two series in both the quarterly pattern and the annualized growth rates. For example, according to staff estimates based on the ES 202, wage growth for the first and second quarters of 2000, on a percent-change-year-ago basis, was 18.3 percent and 8.5 percent, respectively. The comparable growth rates originally published by the BEA were 2.4 percent and 5.4 percent. These estimates have since been revised up to 6.0 percent and 9.1 percent, respectively. However, the lack of timeliness in the revision process limits the usefulness of BEA for State forecasting purposes.

A comparison with yet another source of wage data also demonstrates the greater accuracy of the ES 202. Since the amount of wages withheld for personal income tax purposes varies systematically with wages itself, withholding data provide a useful guide for estimating State wage growth. For example, wages withheld during the first quarter of 2000 were 18.6 percent above withholding for the same quarter of the previous year. This estimate is much more consistent with the growth rate derived from the ES 202 than with the BEA's estimate of 2.4 percent.

Once an entire year of ES 202 data becomes available, the BEA revises its state-level wage data to be more consistent with that data source. For this reason, the Division of the Budget's method performs well in anticipating the BEA's revised estimates of annual growth in New York wages. To make the actual magnitudes of the Division of the Budget's wage series more strictly comparable to the BEA wage series, noncovered and unreported legal wages must be added to wages taken directly from the ES 202. The addition of these components typically changes the annual growth rate for State wages by no more than two-tenths of one percentage point.

An increasing portion of New York State wages are paid on a variable basis, in the form of either bonus payments or proceeds derived from the exercise of stock options. No government agency collects data on variable income as distinct from ordinary wages; therefore, it must be estimated. The Division of the Budget derives its estimate of bonuses from firm level data as collected under the Unemployment Insurance program. This method allows a large degree of flexibility as to when individual firms actually make variable income payments. However, as with any estimation method, some simplifying restrictions are necessary. DOB's method incorporates the assumption that each establishment makes variable income payments during at most two quarters of the year. However, the determination as to which quarters contain these payments is made at the firm level.

Firms report their wages to the Unemployment Insurance program on a quarterly basis. The firm's average wage per employee is calculated for each quarter. The average over the two quarters with the lowest average wages are assumed to reflect the firm's base pay, that is, wages excluding variable pay. If the average wage for either of the remaining quarters is significantly above the base wage, then that quarter is assumed to contain variable income.[1] The average variable payment is then defined as total average wage minus the base average wage, after allowing for an inflation adjustment to base wages. Total variable pay is then calculated by multiplying the average bonus payment by the total number of firm employees. It is assumed that only private sector employees earn variable pay.

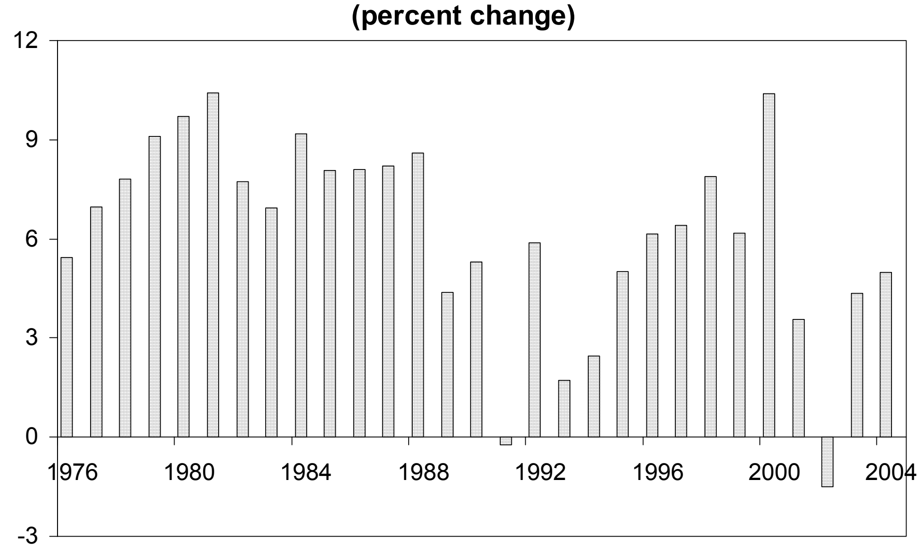
[1] The threshold adopted for this purpose was 25 percent. However, the variable income estimates are fairly robust to even a five percentage point swing in this criterion.

Total State Wages

Unlike the variable component of income, nonbonus wages are driven largely by changes in employment and the nonbonus average wage, and are therefore relatively more stable. After adjusting for inflation, the State's nonbonus average wage is believed to have a stable long-run relationship with the real U.S. average wage. However, State real average wages can deviate from their long-run trend due to short-term fluctuations related to the business cycle or shocks to the regional economy. Non-bonus average wage growth is estimated to increase by 3.1 percent in 2002, following projected growth of 3.7 percent for 2001. Total non-bonus wages are projected to grow only 1.9 percent for 2002, following 3.8 percent growth for 2001.

The decline in bonuses, lower inflation, reduced employment, and slower growth in non-bonus average wages are all expected to contribute to a decline in the State's overall average wage of 0.3 percent for 2002. This would be the first decline in the State's average wage since the ES202 data was first reported in 1975. The combined impact of the decline in average wages and the decline in employment is expected to reduce total wages by 1.5 percent for 2002, following growth of 3.6 percent for 2001 (see Figure 29).

Figure 29
New York State Wage Growth
(percent change)



Source: NYS Department of Labor; DOB staff estimates.

Total State Personal Income

In October 2001, the Bureau of Economic Analysis released revised estimates of State personal income for the years1998 through 2000[11]. New York State's personal income was revised up by $4.6 billion for 1998 (see Table 8). The largest revisions were to wages and property income — $2.7 billion and $1.3 billion, respectively. Property income for 1999 was revised down by $2.8 billion, resulting in a downward revision of $2.3 billion for personal income for that year. For 2000, the upward revision to wages was cancelled out by negative revisions to other income components, producing almost no change in personal income. The

[11] See Jeffrey L. Newman, "State Personal Income, Revised Estimates for 1998-2000," *Survey of Current Business* (October 2001): 99-115.

net impact of these revisions resulted in an increase in personal income growth for 1998 and 2000 by 0.8 percentage points and 0.4 percentage points, respectively; while for 1999, growth was revised down by 1.2 percentage points.

TABLE 8
NEW YORK STATE PERSONAL INCOME REVISIONS

	1998	1999	2000
Level			
(billions of dollars)			
Current	590.4	614.6	655.6
Previously published	585.8	616.9	655.6
Revision	4.6	(2.3)	0.0
Percent Growth			
Current	6.7	4.1	6.7
Previously published	5.8	5.3	6.3
Revision	0.8	(1.2)	0.4

Source: Bureau of Economic Analysis, U.S. Department of Commerce.

The Division of the Budget projects a 1.0 percent increase in the nonwage components of State and personal income for 2001, followed by a growth of 5.0 percent in 2002. The slow growth in 2001 is caused by the 2.6 percent decline in property income. The decline in interest rates and profits, along with the property damage and loss of business that occurred as a result of the September 11 disaster, are expected to result in weak growth. The Division of the Budget projects that weakness in both the wage and nonwage components of income will result in growth of only 2.6 percent in total personal income for 2001 (see Table 9). The decline in wages caused by reductions in both bonus income and employment will produce 1.1 percent growth in total personal income for 2002.

TABLE 9
NEW YORK STATE SELECTED ECONOMIC INDICATORS
CALENDAR YEAR
(percent change)

	2000 (actual)	2001 (preliminary)	2002 (forecast)	2003 (forecast)	2004 (forecast)	2005 (forecast)
Personal Income[2]	7.4	2.6	1.1	3.8	4.3	4.5
Wages and Salaries[2]						
Total	10.4	3.6	(1.5)	4.4	5.0	4.7
Without Bonus[1]	9.0	3.8	1.9	3.8	4.9	4.6
Bonus[1]	20.4	2.0	(24.0)	9.6	5.5	5.3
Wage Per Employee	8.1	3.4	(0.3)	3.5	3.2	3.2
Property Income	4.1	(0.5)	3.4	1.5	2.4	2.8
Proprietors' Income	4.9	1.6	4.9	5.1	5.3	5.1
Transfer Income	3.8	6.1	7.5	6.1	5.3	6.9
Nonfarm Employment[2]						
Total	2.2[3]	0.1[3]	(1.2)	0.9	1.7	1.5
Private	2.3	0.1	(1.5)	1.1	2.0	1.7
Unemployment Rate (percent)	4.6	4.8	6.5	6.4	6.1	5.9
Composite CPI of New York[1]	3.2	2.9	2.4	2.5	2.4	2.4

[1] Series created by the Division of the Budget.

[2] Nonagricultural employment, wage, and personal income numbers are based on the data provided by the Unemployment Insurance Program (202 data).

[3] The currently published total employment for 2000 produces a growth rate of 2.1 percent. However, DOB anticipates an upward revision of 0.1 percentage point when the data become final. For 2001, the current estimate of the growth rate is 0.7 percent and DOB expects the rate to be revised downward.

Source: U.S. Department of Commerce, Bureau of Economic Analysis; New York State Department of Labor; DOB staff estimates.

BOX 8
THE NEW YORK STATE DIVISION OF THE BUDGET'S
NEW YORK MACROECONOMIC MODEL

DOB'S New York Macroeconomic model (DOB/N.Y.) attempts to capture the fundamental linkages between the New York and the national economies. Clearly, New York's economy depends on economic developments in the U.S. economy, usually expanding when the national economy is growing and contracting when the nation is in recession. However, this relationship is neither simple nor static. The growth rate of the State's economy can vary substantially in comparison to the nation. For example, during the last national recession, the State's recession began noticeably earlier and ended significantly later than for the nation as a whole. Alternatively, during the early 1980's recession, the State's economy fared better than the nation.

The objective of DOB/N.Y. is to quantify the linkages between the United States' economy and New York's economy in an econometric modeling framework — one that specifically identifies the economic conditions in New York. DOB/N.Y. is a structural time series model with most of the exogenous variables derived from DOB/U.S. In general, the long-run equilibrium relationships between State and national economic variables are captured by a cointegration/error correction specification, while the State's specific dynamics are modeled using a restricted vector autoregressive (RVAR) framework. DOB/N.Y. has four major components: a nonfarm payroll employment segment, a real nonbonus average wage segment, a bonus payment segment, and a nonwage income segment.

Employment

The national economy affects New York employment through two channels. First, if State employment growth for a specific sector is related to the growth of the U.S. employment in the same sector, U.S. employment for that sector is specified as an exogenous variable in the equation. Second, overall U.S. economic conditions, as measured by the growth of real U.S. GDP, is included either directly in the employment equations for some sectors or indirectly through the VAR relationships.

Intra-sectoral relationships for New York employment can be different from those for the nation as a whole. These relationships are captured in a restricted VAR model where the impact of one sector on other sectors is explicitly specified.

Average Real Nonbonus Wages

Our analysis suggests the existence of a long-run equilibrium relationship between real nonbonus average wage for most New York sectors and the national real average wage. Thus, the State average real nonbonus wage by sector is modeled in a cointegration/error correction framework. This modeling approach is based on the belief that, in the long run, since both labor and capital are free to move in a market economy, regional differences in labor costs tend to disappear (this process may take quite a long time). This formulation allows for short-run adjustments towards equilibrium, which describe the short-run dynamics of State-specific economic conditions.

Bonus Income

The DOB model for finance and insurance bonus income incorporates those factors which drive Wall Street profits — merger and acquisition activity, IPO's, and the volume of debt underwriting. Our analysis shows that bonuses paid in the State's other economic sectors tend to have long-term equilibrium relationships with those paid in the finance and insurance sectors; more technically — bonus payments in the financial services sector are cointegrated with bonuses paid in most other sectors. Consequently, the results from the finance and insurance sector bonus model are used to estimate bonuses paid in other sectors.

Nonwage Incomes and Other Variables

The New York nonwage components, except for the residence adjustment, are all driven by their national counterparts. The relationship is modeled as a change in the New York variable as a function of a change in the U.S. nonwage counterpart along with lags of the independent and dependent variables as appropriate to account for short-term fluctuations.

Risks to the New York Forecast

In addition to the uncertainties described earlier for the U.S. economy, the forecast contains risks specific to New York. The most significant risks to the New York economic forecast pertain to the pace of layoffs related to the events of September 11, and the impact of both the disaster itself and deteriorating economic conditions on employee wages. Fewer layoffs, stronger financial markets, and higher employee bonuses than projected imply a brighter picture of the State economy than reflected in the current forecast. Similarly, greater job losses, weaker financial markets, and smaller bonus payments than expected imply a dimmer picture.

The extensive job losses projected for the finance and insurance sector may result in a small spike in wage income in the form of severance pay. This represents an upside risk to the New York wage forecast for 2002.

SOURCES OF VOLATILITY IN THE INCOME TAX BASE — A RISK ASSESSMENT

Historically, the uncertainty surrounding such volatile income components as capital gains, bonuses, and stock incentive payouts, and the small number of taxpayers who account for the majority of this income, has posed significant risks to the Division of the Budget's personal income tax forecast. This is especially true in light of the turbulent conditions recently observed in the financial markets. The volatility in these components produces a wide range in potential income growth (see Figure 33 and Figures 36 through 39, below). Although the Division of the Budget's projection approaches the middle of that range, the cost to the State of inaccurately forecasting revenues is not symmetric about the midpoint. Given the real possibility of significant declines in taxable income, the cost of moving above the forecast could be much higher than the cost of moving below. A potential shortfall in receipts that results in a mid-year budgetary deficit could have severe consequences, possibly requiring spending cuts, revenue increases, or the issuance of deficit notes. Therefore, a conservative approach to projecting these components is warranted.

In recent years, personal income tax revenues in New York State have increased considerably despite several major tax cuts. In the 1980-81 State fiscal year, personal income tax receipts represented 50 percent of State General Fund total tax receipts. However, by the 2000-01 State fiscal year, that ratio was 65 percent. While this increase is certainly due, in part, to the improvement in the State economy, the magnitude of the growth in receipts has far exceeded that which can be easily measured using conventional economic indicators. For example, in 1999, the most recent year for which complete State income tax liability data are available, State personal income grew 4.0 percent, while New York State adjusted gross income (NYSAGI) grew 8.4 percent, and total personal income tax liability grew 10.5 percent.

These large differentials can be attributed to several factors. The gap between personal income growth and NYSAGI growth is primarily related to measurement issues. Personal income is a National Income and Product Accounts (NIPA) definition, and therefore comprises income derived from value added to current production. Adjusted gross income measures the taxable components of income and, as such, includes components which are taxable but not counted in personal income, such as capital gains realizations. Since the gain earned from the sale of a financial asset excluding transaction costs is not related to current production, it is not included in the NIPA concept of personal income. With the dramatic run-up in equity prices in 1999, capital gains realizations rose accordingly.

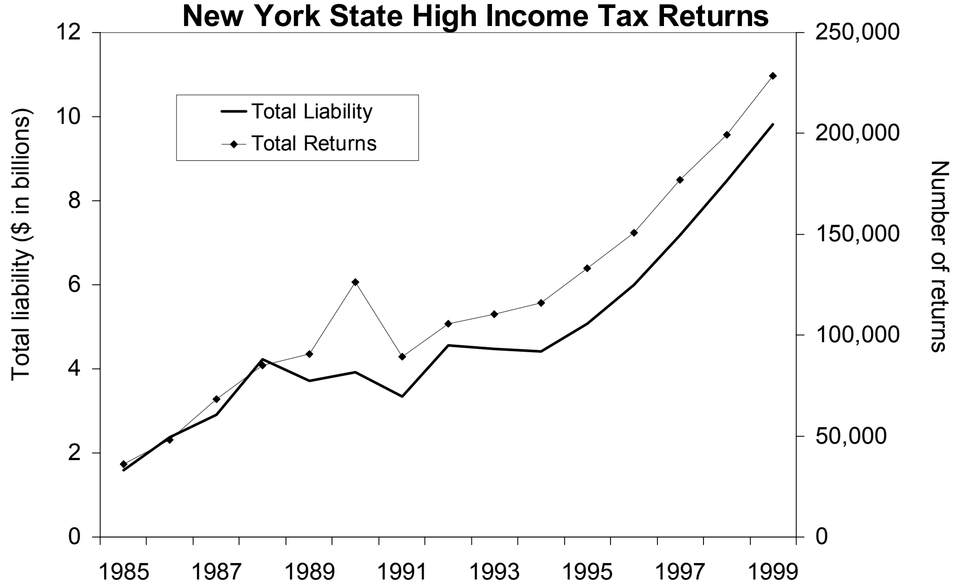
The gap between growth in NYSAGI and personal income tax liability is, in part, related to the progressiveness of the State tax system. Taxpayers move into higher tax brackets as their incomes rise. For instance, between 1998 and 1999, the latest year for which detailed income tax data are available, the average effective tax rate, as measured by the ratio between personal income tax liability and NYSAGI, increased from 4.54 percent to 4.63 percent, without any significant changes in tax law.

It is estimated that the volatility in State personal income tax receipts extended into 2000 and 2001. Based on Division of the Budget staff estimates, personal income tax liability grew 17.6 percent in 2000, but is projected to decline 5.4 percent for the current year. These fluctuations in liability are related to estimated growth in adjusted gross income of 12.7 percent for 2000 and an estimated decline of 3.6 percent for 2001. This compares to personal income growth of 7.4 percent for 2000 and estimated growth of 2.6 percent for 2001. The most critical factors explaining the estimated dramatic changes in New York income tax receipts include changes in the State's income distribution, and the variable nature of specific components of taxable income, such as bonus wages and capital gains realizations.

CHANGES IN THE STATE DISTRIBUTION OF INCOME

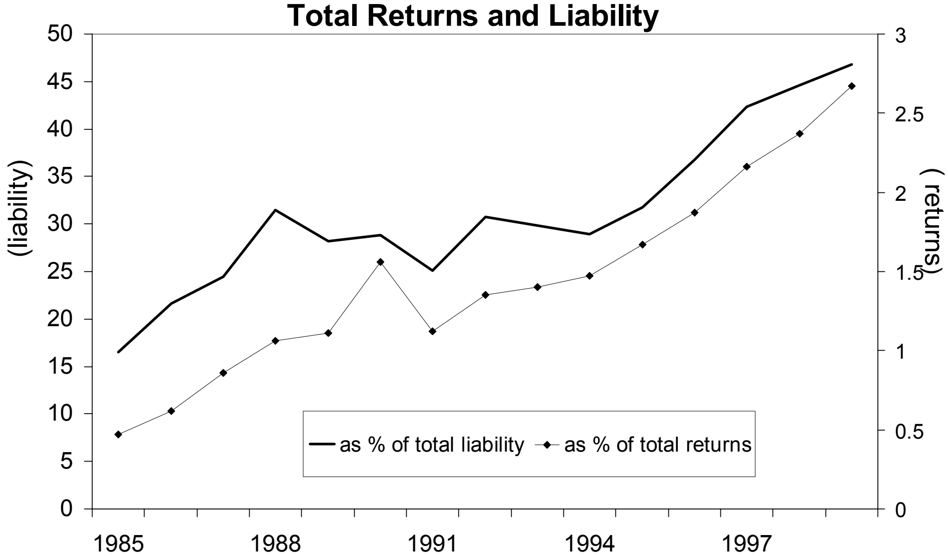
About 8.5 million tax returns were filed in New York State in 1999, representing growth of about 1.7 percent per year since 1995. However, the number of taxpayers reporting NYSAGI above $200,000 has seen annual increases of close to 15 percent (see Figure 30). In 1999, the most recent year for which detailed tax return data are available, these high-income taxpayers represented 2.7 percent of all taxpayers. However, they accounted for 34.8 percent of NYSAGI and fully $9.8 billion of personal income tax liability, or 46.8 percent of the total (see Figure 31). While the rapid growth in income among the State's high-income citizens has produced unprecedented growth in State tax receipts, reliance upon this growth as a source of future revenues continues to pose a substantial risk to the financial plan. This is because the incomes of high-income taxpayers tend to be more heavily weighted toward the more volatile components of adjusted gross income, such as bonus wages and capital gains realizations.

Figure 30
New York State High Income Tax Returns



Source: NYS Department of Taxation and Finance; DOB staff estimates.

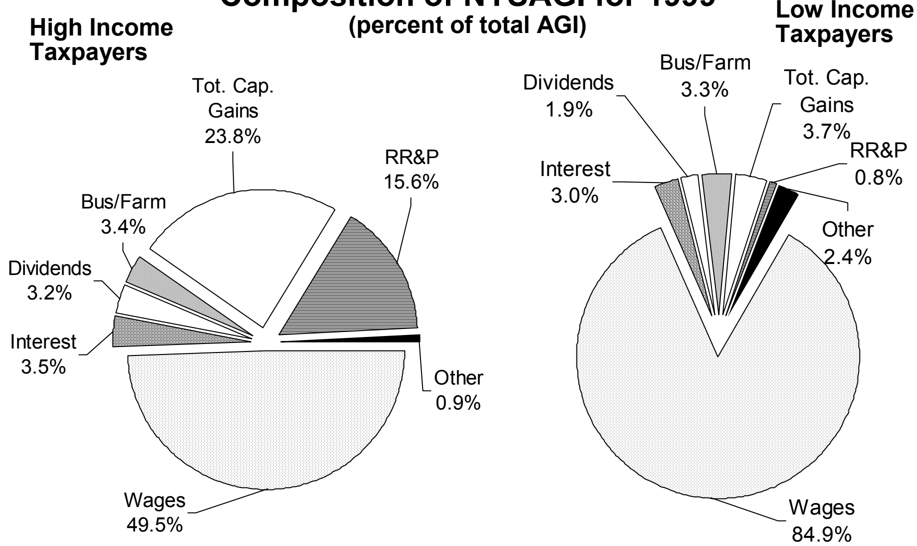
Figure 31
High Income Taxpayers as Percent of Total Returns and Liability



Source: NYS Department of Taxation and Finance; DOB staff estimates.

Given the progressive nature of the State's tax system, forecasting total income tax liability entails not only forecasting total income, but the distribution of income as well. Out-year estimation of income distribution is especially risky when the economy is at or near a business cycle turning point, as it is today, since the share of income earned within the highest income brackets can fluctuate dramatically with the business cycle. Clearly, the most volatile components of AGI comprise a much larger share of total AGI for the State's high-income taxpayers than for others, and for high-income taxpayers, those shares can change radically over time. For example, capital gains realizations for taxpayers with AGI less than $100,000 grew from 1.1 percent of AGI to 3.1 percent between 1991 and 1999. For high-income taxpayers with AGI above $200,000, the comparable shift was from 12 percent to 24 percent.

Figure 32
Composition of NYSAGI for 1999
(percent of total AGI)



Note: High income taxpayers are defined are those reporting NYSAGI of more than $200,000.
Source: NYS Dept. of Taxation and Finance.

BOX 9
ESTIMATING FORECAST RISK USING MONTE CARLO SIMULATION

The Division of the Budget uses forecasting models to project future values for the components of New York State adjusted gross income. These models presume that the historical relationships between the components of income and a number of key economic indicators are useful for projecting their future behavior. They also presume that these relationships are stable and can be estimated using standard statistical methods. Since all statistical models are simplifications of complex relationships, they are subject to model misspecification error. In addition, there is risk associated with the forecasts for the exogenous economic indicators. However, even if a model is well specified and the future values of the exogenous inputs can be predicted with certainty, a statistical forecast remains subject to risk. There is always a component that cannot be captured by the model, which is simply ascribed to random variation. Moreover, the estimated parameters of the model are themselves random variables and, as such, are subject to estimation error.

For a given model specification and a given set of exogenous inputs, one can evaluate the risk to the forecast due to the random variation in the variable one is trying to forecast, as well as the random variation in the model parameters. The tool used most commonly in econometric research for evaluating this risk is the Monte Carlo simulation study. For each simulation, a random number generator is used to generate sequences of values from a probability distribution. The random variation in the forecast variable and in the parameter estimates is typically assumed to be governed by normal and multivariate normal distributions, respectively. Each individual simulation is comprised of a random draw from the distribution of the model errors, as well as random draws from the multivariate distribution of the parameter estimates. Then the model is solved for the endogenous variable, given a fixed input data set. This “experiment” is typically repeated thousands of times, yielding thousands of predicted values for the endogenous variable. After all the simulations are performed, a mean and standard deviation of the predictions can be calculated. Thousands of replications of the simulation permit the estimation of a confidence interval around the forecast. That interval can, in turn be used to assess the risk associated with the forecast.

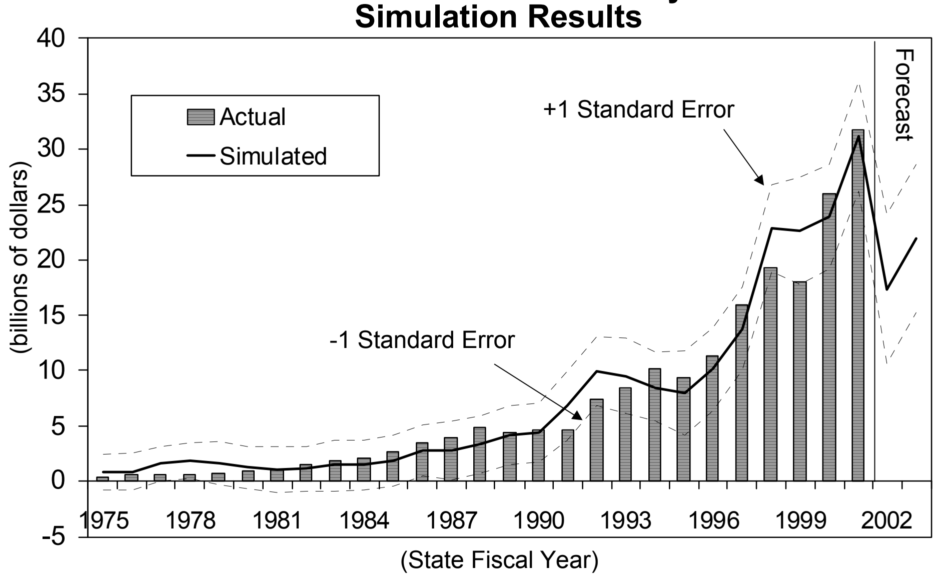
VOLATILITY IN THE MAJOR COMPONENTS OF NYSAGI

The Bonus Component of Wages

Total State wages grew by $34.4 billion in 2000, a 10.4 percent increase.[12] Total bonus payments are estimated to have grown by $8.6 billion, representing about 23.6 percent of the total increase in wages. In fact, the share of total wages paid out in bonuses has been increasing steadily. While growth in this component of wages is, in part, the result of a strong economy, the exceptional performance of the financial sector has been equally important. DOB's forecast for finance and insurance sector bonuses is driven largely by the performance of the major sources of income for financial sector firms, such as underwriting activity related to IPO's, mergers and acquisitions, and debt. Therefore, it is not surprising that bonus income exhibits much more volatility than the nonvariable component of State wages and salaries. As a result of the current economic downturn and its disproportionate reverberation within the financial sector, it is expected that financial and insurance sector bonuses paid out during the 2001-02 State fiscal year will decline by 43.7 percent.

Figure 33 presents the results of a simulation of the DOB bonus income model for the finance and insurance sector (see Box 9). A 66 percent confidence band is constructed by adding and subtracting one standard deviation to and from the mean of the simulated values at each point in time. DOB expects finance and insurance sector bonuses to reach $22.5 billion for the 2002-03 State fiscal year. However, the simulation results indicate that, with a 66 percent probability, bonuses will range from $15.8 billion to $28.7 billion — a $13 billion range (see Table 10).

Figure 33
Finance and Insurance Industry Bonus Simulation Results



Note: Shocks to both model errors and parameters are simulated.
Source: NYS Dept. of Labor; staff estimates.

[12] DOB bases its estimates of total State wages and bonus income on ES 202 data (see Box 7). Taxable wages, the largest component of NYSAGI, are assumed to grow at the same rate as total State wages but are typically smaller in magnitude.

TABLE 10

FORECAST OF SELECTED NYSAGI COMPONENTS FOR 2002 — MONTE CARLO SIMULATION RESULTS

	Level (billions of dollars)			Growth Rate (percent)		
	Forecast	**Low[1]**	**High[1]**	**Forecast**	**Low**	**High**
Finance and Insurance Bonuses[2]	22.5	15.8	28.7	26.1	(11.1)	60.3
Positive Capital Gains	47.5	41.1	54.7	15.0	(0.3)	32.6
Positive Rent/Royalty & Partnership	40.8	38.0	43.8	(0.3)	(7.2)	7.2
Dividend Income	10.1	9.4	10.9	0.0	(6.8)	7.2
Interest	12.1	11.4	12.8	(3.1)	(8.6)	2.7

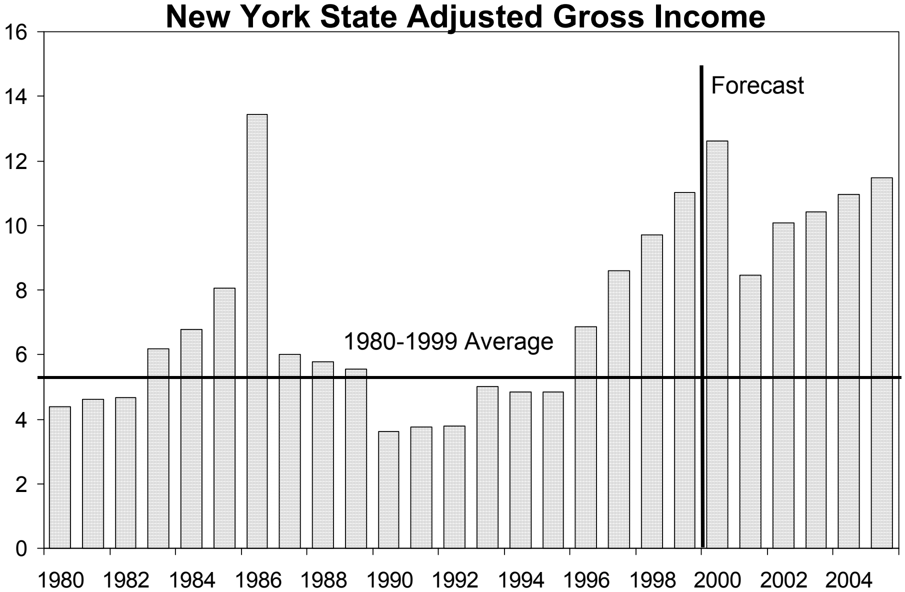
[1]High and low values are calculated by adding and subtracting one standard deviation to and from the point forecast.
[2]Pertains to 2002-03 State fiscal year.

Capital Gains Realizations

The growing share of capital gains as a percentage of total NYSAGI has made more urgent the need to reliably project this source of income (see Figure 34). To that end, the Division of the Budget has constructed a forecasting model that attempts to capture some of the inherent volatility of capital gains realization behavior.[13] The Division of the Budget's model incorporates those factors that are most likely to influence realization behavior, such as: expected and actual tax law changes and stock market activity (see Figure 35). Some of these elements are highly volatile themselves, making capital gains very difficult to forecast with a large degree of precision (see Figure 36). There is little doubt that the growth in realizations from 1995 to 1999 is directly related to the dramatic growth in equity prices observed during those years. Therefore, the significant drop in stock prices observed in 2000, and which continued in 2001, poses significant risks to the financial plan in the current State fiscal year and will continue to do so for the next year as well. For 2002, positive capital gains realizations are estimated to rise 15 percent above their 2001 level, but with a 66 percent confidence band of plus or minus 18 percentage points (see Table 10).

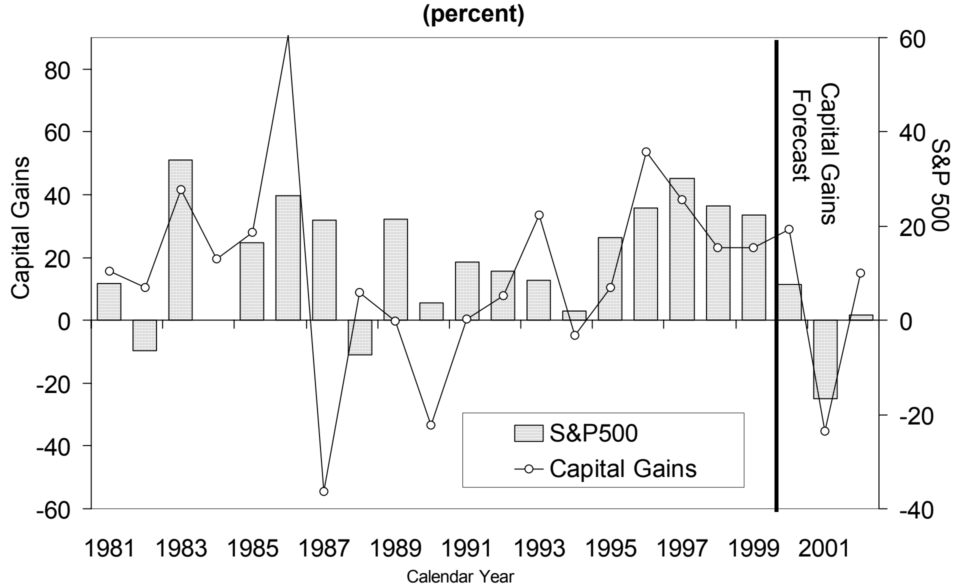
[13] The Division of the Budget capital gains model draws heavily from Preston Miller and Larry Ozanne "Forecasting Capital Gains Realizations," Congressional Budget Office, August 2000.

Figure 34
Capital Gains Realizations as Percent of Total New York State Adjusted Gross Income



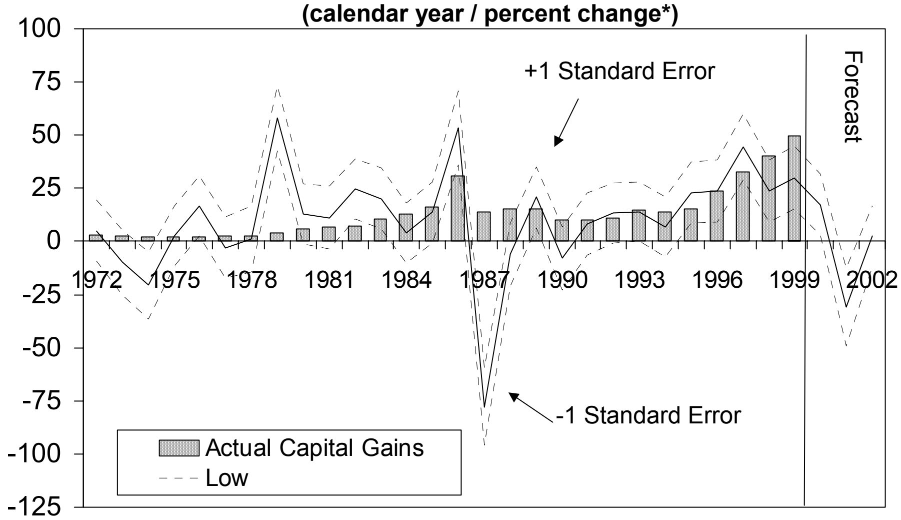
Source: NYS Department of Taxation and Finance, DOB staff estimates.

Figure 35
Capital Gains Realizations and the S&P 500
(percent)



Source: DRI-WEFA; NYS Dept. of Taxation and Finance; DOB staff estimates.

Figure 36
Capital Gains Realizations Simulation Results
(calendar year / percent change*)

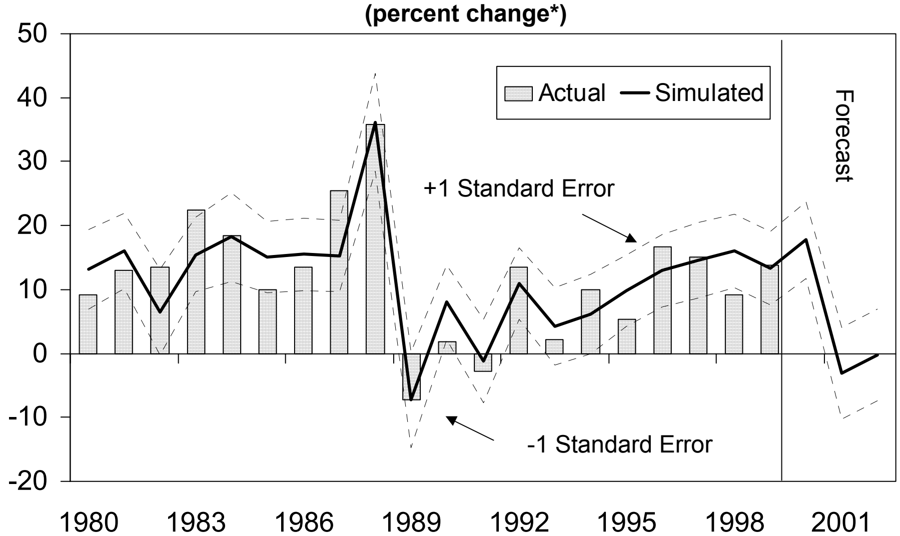


* Dependent variable is an approximation to percent change.
Note: Shocks to both model errors and parameters are simulated.
Source: NYS Dept. of Taxation and Finance; DOB staff estimates.

Rent, Royalty, Partnership, and S-Corporation Income

New York rent, royalty, partnership and S-corporation income is believed to be closely related to overall State economic conditions. The biggest component is partnership income, which has historically been correlated with changes in total State wages. However, the variability in partnership income is much greater than that of wages. For example, from 1980 to 1999, average annual growth in this component of NYSAGI was about 13 percent, with a standard deviation of 7 percentage points. In contrast, wages grew at an average rate of 6.6 percent during the same period, with a standard deviation of 2 percentage points. Hence, an effort was made to capture this additional variation by including additional indicators, such as equity market growth. Even with these adjustments, the forecasting range remains large (see Table 10), as the results of our simulation studies suggest (see Figure 37).

Figure 37
Partnership Income Simulation Results
(percent change*)

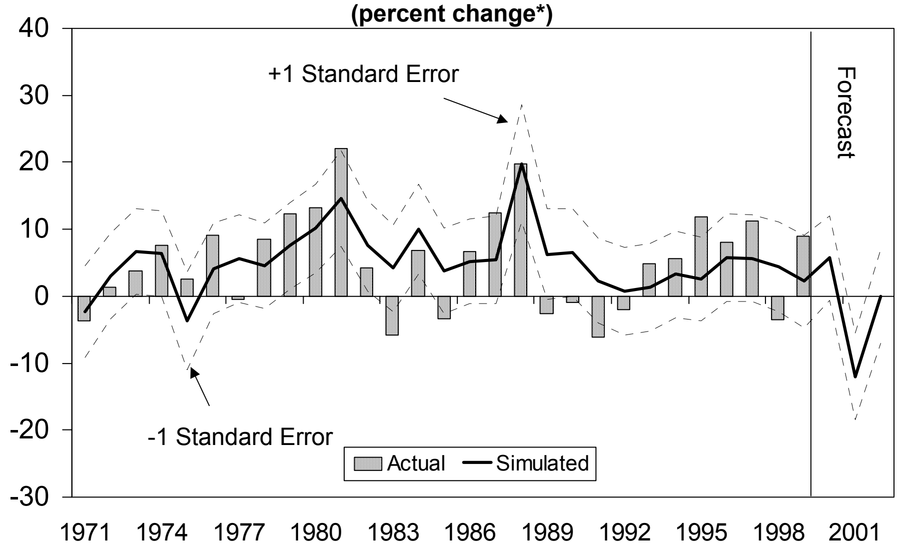


* Dependent variable is an approximation to percent change.
Note: Shocks to both model errors and parameters are simulated.
Source: NYS Dept. of Taxation and Finance; DOB staff estimates.

Dividend Income

Historically, the range of variation for dividend income has been very wide, ranging from a decline of 6 percent in 1991 to an increase of 22 percent in 1981. Much of this variation is assumed to be related to the business cycle. For example, during the State's last recession, dividend income declined for four consecutive years from 1989 to 1992. Dividend income fell again in 1998 when the Asian financial crisis produced a sharp, albeit short-lived, downturn in equity prices. Firm behavior may be another source of volatility in dividend income. For example, anecdotal evidence suggests that, during the stock market boom of the late 1990's, many companies were buying back their own stock as a way of substituting price appreciation for dividend payments. This allowed shareholders to take advantage of the lower capital gains tax rate, since dividends are taxed at the higher, ordinary income tax rate. A large portion of the variation in taxable dividend income cannot be explained by DOB's forecasting model, as indicated in Table 10 and in Figure 38.

Figure 38
Dividend Income Simulation Results
(percent change*)

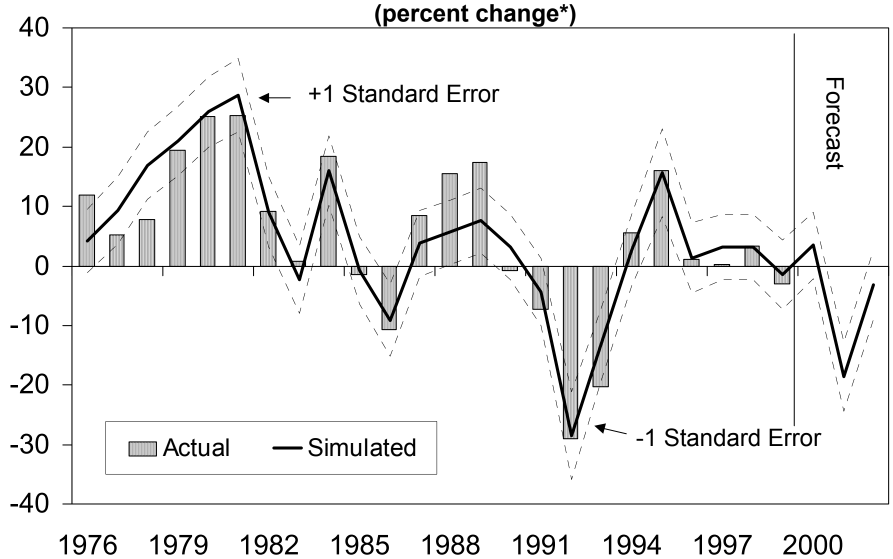


* Dependent variable is an approximation to percent change.
Note: Shocks to both model errors and parameters are simulated.
Source: NYS Dept. of Taxation and Finance; DOB staff estimates.

Interest Income

For a given amount of assets, an increase in the interest rate will increase interest income. DOB's interest income forecasting model is based on this simple concept. In addition, the overall trend in taxable interest income for New York is found to closely track that of U.S. interest income, a NIPA component of personal income. However, taxable interest income for New York is much more volatile. For the period from 1976 to 1999, the average growth rate for the New York series was 5.9 percent, with a standard deviation of over 13 percentage points. In contrast, U.S. interest income growth over the same period averaged 9.0 percent, with a standard deviation of 7.0 percentage points. The additional volatility in the New York series could be related to the behavioral response of State taxpayers to past changes in the tax law related to interest income. The simulation results indicate again that the forecasting range is still quite large (see Table 10 and Figure 39).

Figure 39
Interest Income Simulation Results
(percent change*)



* Dependent variable is an approximation to percent change.
Note: Shocks to both model errors and parameters are simulated.
Source: NYS Dept. of Taxation and Finance; DOB staff estimates.

In summary, given the uncertainty surrounding such volatile components as capital gains realizations and bonus and stock incentive income, and given the small number of taxpayers who account for the majority of this income, there exists significant risk to the Division of the Budget's personal income tax forecast. A source of this risk stems from the connection between revenues and the stock market, which is extraordinarily difficult to forecast. This risk is further compounded by the uncertainty at a business cycle turning point. As a result, for the upcoming years, forecasts for income tax receipts should be viewed with caution, consistent with the volatile movements in the major components of New York State adjusted gross income.

RECENT TRENDS IN ALL FUNDS TAX RECEIPTS

Growth in All Funds tax receipts has been very volatile over the past three decades, reflecting both underlying economic conditions and significant changes in tax policy. The relatively small annual average growth in receipts during the 1990's was largely due to three factors: the severe economic downturn experienced in New York during the early 1990's, reduced inflation rates, and the significant tax reductions enacted over the 1995-2000 period. The projected decline in tax receipts for 2001-02 and the flat receipt growth in 2002-03 is directly related to the adverse effects the of national economic recession and the negative impact on receipts caused by the World Trade Center disaster.

The share of total tax receipts derived from the personal income tax has increased to historically high values in recent years, reaching 60 percent for the first time in 2000-01. It is estimated that the income tax will remain at 60 percent of All Fund tax receipts in 2001-02 and 2002-03.

By definition, the personal income tax is sensitive to changes in the income of State residents and non-residents who earn taxable income in New York. In recent years, growth in employment and rapid increases in the income of high-income individuals have driven the income tax share upward, while the share of most other taxes has declined. (See Economic Backdrop section.)

The user taxes and fees share of total taxes has declined since the early 1970's, reflecting, in part, that such taxes tend to be less sensitive to changes in the income of State residents than does the personal income tax. In addition, user taxes such as the taxes on cigarettes, motor fuel and alcoholic beverages are taxed at rates fixed in statute per quantity of the product consumed. These taxes are not very sensitive to price changes and, as a result, tend to grow more slowly than other tax sources which include price increases in their base.

The business tax share of total taxes is very volatile, as a result of the significant variability of taxable business profits, but has declined in recent years due partially to reductions in tax rates and the base subject to tax. However, the volatility inherent in business taxes means that its share of total taxes can grow (decrease) above (below) average growth in an unpredictable manner.

The share of other taxes have been dominated by the repeal of the real property gains tax and the gift tax, and the reduction in the pari-mutuel tax and the estate tax.

ALL FUNDS TAX RECEIPTS
(millions of dollars)

			Percent of All State Funds Tax Receipts Accounted for By:			
Fiscal Year	All Funds Tax Receipts[1]	Percent Change	Personal Income Tax[1]	User Taxes and Fees	Business Taxes	Other Taxes
1972-73	7,807		41.1	38.2	16.4	4.3
1973-74	8,187	4.9	41.9	38.3	15.8	3.9
1974-75	8,663	5.8	41.4	37.9	16.8	3.8
1975-76	9,422	8.8	41.9	36.5	18.0	3.6
1976-77	10,348	9.8	43.7	34.1	18.4	3.7
1977-78	10,505	1.5	42.9	35.3	19.0	2.8
1978-79	11,154	6.2	45.3	35.0	17.1	2.6
1979-80	12,138	8.8	47.6	34.0	16.3	2.1
1980-81	13,496	11.2	49.0	31.4	17.4	2.2
1981-82	15,143	12.2	53.1	29.3	15.8	1.9
1982-83	16,025	5.8	51.6	29.8	16.0	2.6
1983-84	18,644	16.3	50.3	29.4	17.2	3.2
1984-85	20,392	9.4	51.0	28.1	16.7	4.2
1985-86	22,572	10.7	51.3	28.0	16.0	4.7
1986-87	24,358	7.9	51.2	27.1	15.7	6.0
1987-88	25,859	6.2	52.5	27.3	15.2	5.0
1988-89	26,262	1.6	52.7	27.7	14.5	5.1
1989-90	28,050	6.8	54.5	28.0	13.3	4.2
1990-91	27,818	(0.8)	52.0	27.6	16.1	4.3
1991-92	29,847	7.3	50.1	27.1	19.1	3.7
1992-93	31,661	6.1	50.4	26.3	19.7	3.6
1993-94	33,026	4.3	50.0	26.0	20.6	3.4
1994-95	33,050	0.1	50.6	27.4	18.6	3.4
1995-96	33,927	2.7	51.3	27.0	18.4	3.3
1996-97	34,620	2.0	50.7	27.1	18.8	3.4
1997-98	35,921	3.8	50.9	27.1	18.3	3.7
1998-99	38,495	7.2	53.5	26.2	16.6	3.8
1999-2000	41,389	7.5	56.0	25.6	14.8	3.5
2000-01	44,658	7.9	60.3	23.9	13.1	2.7
2001-02*	42,797	(4.2)	59.9	24.7	12.7	2.7
2002-03**	43,311	1.2	60.0	24.9	12.5	2.6

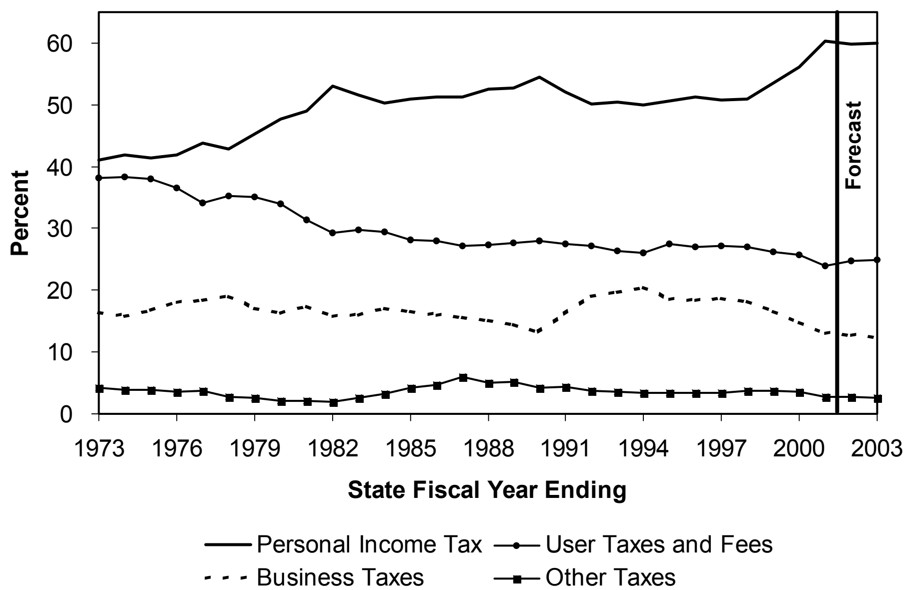
[1] Personal Income Tax defined as gross receipts less refunds — 2000-01 receipts reflect an adjustment for the timely payment of refunds.

* Estimated.

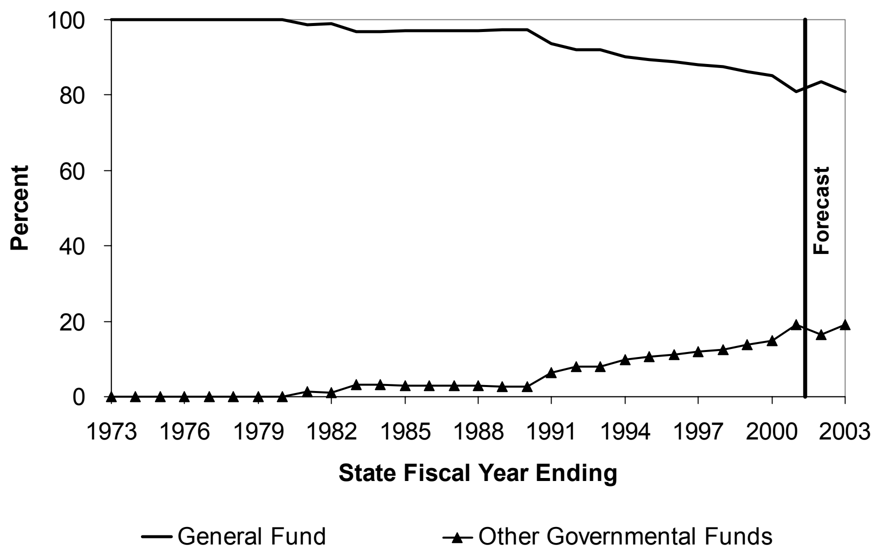
** Projected.

Note: For law changes affecting amounts flowing into various funds, see individual revenue stories.

Tax Share of State Funds by Major Tax Categories



Share of Tax Receipts by Major Fund Type



DEDICATED FUND TAX RECEIPTS

Several tax sources are dedicated in whole or part to State Funds which are earmarked for specific purposes. The following table reports tax receipts by fund for the dedicated tax sources.

DEDICATED FUND TAX RECEIPTS
(millions of dollars)

	2000-01 Actual	2001-02 Estimate	2002-03 Recommended
SPECIAL REVENUE FUNDS			
School Tax Relief Fund (STAR)			
Personal income tax	3,076.5	1,310.0	2,630.0
Dedicated Mass Transportation Trust Fund	345.5	422.6	474.1
Petroleum business tax	287.4	327.4	331.9
Motor fuel tax	58.1	64.8	64.5
Motor vehicle fees	0.0	30.4	77.7
Mass Trans. Operating Assistance Fund	1,109.7	1,081.9	1,094.8
Corporate Surcharges			
Corporation franchise tax	295.1	243.0	251.0
Corporation and utilities tax	121.9	134.0	122.0
Insurance tax	60.4	64.0	54.5
Bank tax	85.8	86.3	97.0
Other			
Sales and use tax	368.2	367.4	370.4
Petroleum business tax	108.2	117.2	118.9
Corporation and utilities — sections 183 & 184	70.1	70.0	81.0
Total Tax Receipts: Special Revenue Funds	4,531.7	2,814.5	4,198.9
DEBT SERVICE FUNDS			
Debt Reduction Reserve Fund			
Personal income tax	250.0	250.0	0.0
Emergency Highway Reconditioning and Preservation Fund			
Motor fuel tax	55.8	57.4	57.1
Emergency Highway Construction and Reconstruction Fund			
Motor fuel tax	55.8	57.4	57.0
Clean Water/Clean Air Fund			
Real estate transfer tax	292.7	263.0	246.6
Local Government Assistance Tax Fund			
Sales and use tax	2,091.9	2,038.6	2,094.4
Total Tax Receipts – Debt Service Funds	2,746.2	2,666.4	2,455.1
CAPITAL PROJECTS FUNDS			
Dedicated Highway and Bridge Trust Funds	1,125.0	1,442.0	1,561.4
Petroleum business taxes	489.3	557.4	565.2
Motor fuel tax	323.3	345.3	343.1
Motor vehicle fees	157.3	388.3	464.0
Highway use tax	155.1	151.0	155.3
Auto rental tax	0.0	0.0	33.8
Environmental Protection Fund			
Real estate transfer tax	112.0	112.0	112.0
Total Tax Receipts – Capital Projects Funds	1,237.0	1,554.0	1,673.4
Total Tax Receipts – Other Funds	**8,514.9**	**7,034.9**	**8,327.4**

*Reflects use of STAR reserve of $1.2 billion in 2001-02.

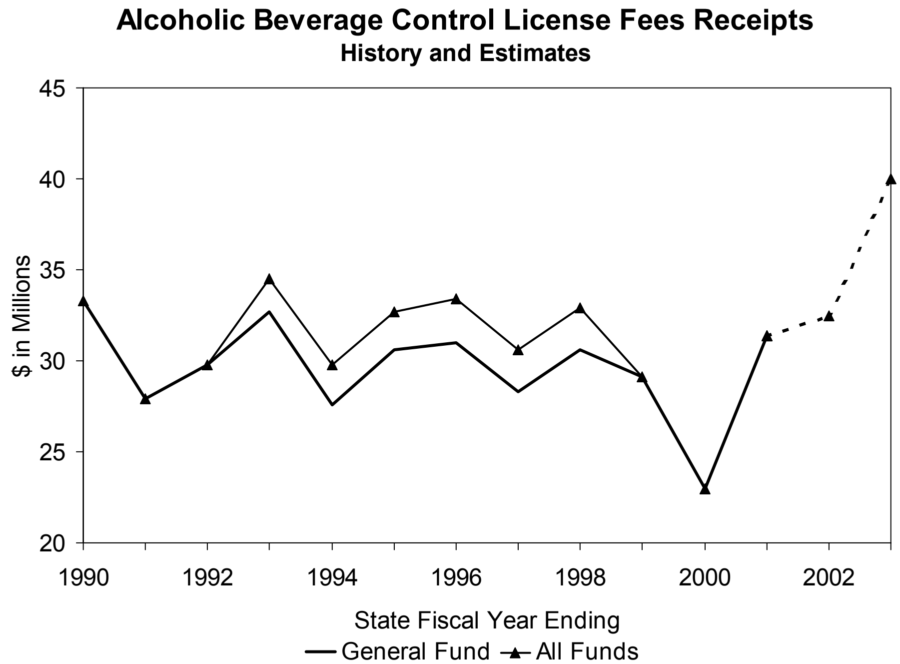
GOVERNMENTAL TAX RECEIPTS

The following table reports tax receipts for all Governmental Funds.

GOVERNMENTAL TAX RECEIPTS
(millions of dollars)

	2000-01 Actual	2001-02 Estimate	2002-03 Recommended
Personal Income Tax	26,892.1	28,537.0	25,922.0
User Taxes and Fees	10,669.7	10,582.5	10,786.1
Sales and use tax	8,731.7	8,526.4	8,749.9
Cigarette and tobacco tax	528.3	514.3	500.6
Motor fuel tax	510.3	524.9	521.7
Motor vehicle fees	494.7	620.2	606.6
Highway use tax	155.1	151.0	155.3
Alcoholic beverage tax	179.3	177.1	178.2
ABC license fees	31.4	32.5	40.0
Auto rental tax	38.9	36.1	33.8
Business Taxes	5,846.4	5,428.3	5,396.5
Corporation franchise tax	2,630.6	1,998.0	2,012.0
Corporation and utilities tax	1,009.4	1,191.0	1,198.0
Insurance tax	644.0	694.0	570.5
Bank tax	591.3	543.3	600.0
Petroleum business tax	971.1	1,002.0	1,016.0
Other Taxes	1,199.5	1,154.6	1,141.5
Estate tax	717.1	740.0	751.2
Gift tax	41.4	4.5	0.0
Real property gains tax	6.2	5.5	2.1
Real estate transfer tax	404.7	375.0	358.6
Pari-mutuel tax	29.4	29.0	28.9
Other taxes	0.7	0.6	0.7
Total Taxes	44,607.7	45,702.4	43,246.1

ALCOHOLIC BEVERAGE CONTROL LICENSE FEES



DESCRIPTION

New York State distillers, brewers, wholesalers, retailers, and others who sell alcoholic beverages are required by law to be licensed by the State Liquor Authority. License fees vary, depending upon the type and location of the establishment or premises operated, as well as the class of beverage for which the license is issued. The most significant source of revenue in this category is the licensing of about 2,500 retail liquor outlets, including package stores engaged in carry-out sales, and about 26,300 bars and restaurants that offer on-premises consumption. The majority of State-licensed bars and restaurants (20,694 in 2000) are authorized to sell beer, wine, and liquor. Approximately 3,750 licensees are permitted to sell only beer and wine. The remaining 1,877 licensees in 2000 sold only beer.

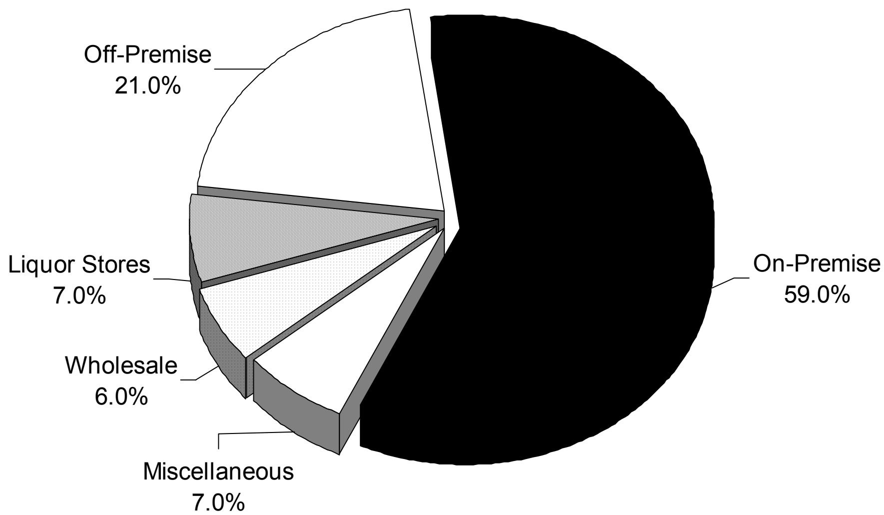
NUMBER OF LICENSES BY CATEGORY
(calendar year)

		Bars and Restaurants						
	Liquor Stores	Beer, Wine and Liquor	Beer and Wine	Beer Only	Subtotal	Grocery Stores	Wholesale	Total
1993	2,906	20,312	3,134	1,845	25,291	19,778	1,041	49,016
1994	2,836	20,030	3,177	1,796	25,003	19,656	1,048	48,543
1995	2,753	19,831	3,372	1,763	24,966	19,768	1,057	48,544
1996	2,673	19,782	3,497	1,838	25,117	19,743	1,074	48,607
1997	2,621	19,708	3,490	1,843	25,041	19,462	1,125	48,249
1998	2,596	19,853	3,712	1,950	25,515	19,417	1,142	48,670
1999	2,560	20,325	3,640	1,883	25,848	19,202	1,031	48,587
2000	2,491	20,694	3,748	1,877	26,319	19,167	1,201	49,178

SIGNIFICANT LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1997		
License Renewal	The required purchase of a triennial license was changed to allow licensees to continue to purchase a triennial license or optionally purchase an annual or biennial license at a prorated cost.	December 1, 1998

Alcoholic Beverage Control License Fees
Share of 2000 Receipts by Licensee Category



2001-02 RECEIPTS

Compared to 2000-01, gross alcoholic beverage control license fee receipts are estimated to increase by more than 3 percent.

Alcoholic beverage control license fee receipts to date are $26.3 million after refunds, 19.7 percent greater than receipts for the comparable period in 2000-01. Collections appear to have returned to pre-1998 patterns when, typically, more than 50 percent of annual receipts were collected during the first 6 months of the fiscal year. 2001-02 is the first year with no downward pressure on receipts resulting from 1997 licensing legislation. As a result, 2001-02 gross receipts are projected at $34 million and refunds at $1.5 million, resulting in estimated net receipts of $32.5 million.

2002-03 PROJECTIONS

Gross alcoholic beverage control license fee receipts under proposed law are projected to be $42 million. Refunds will be approximately $2 million, bringing estimated 2002-03 net receipts to $40 million.

Legislation submitted with this Budget will, for most licensees, increase alcoholic beverage control license fees based on the increase in the alcoholic beverage producer price index since 1976. A smaller group of licensees, made up primarily of grocery stores, will see their fees increase based on the increase in the index since 1992. This increase will be phased in over a three-year period, beginning April 1, 2002, and is expected to increase collections by $8 million in 2002-03

OTHER FUNDS

For the period from 1992-93 through 1997-98, a portion of license fee receipts was deposited in the Alcoholic Beverage Control Enhancement Account. Revenues deposited into the Account were used to support efforts to improve compliance with licensing regulations and expedite license processing. Beginning in 1998-99, this special revenue fund was eliminated, and since that time all licensing fees have been deposited in the General Fund.

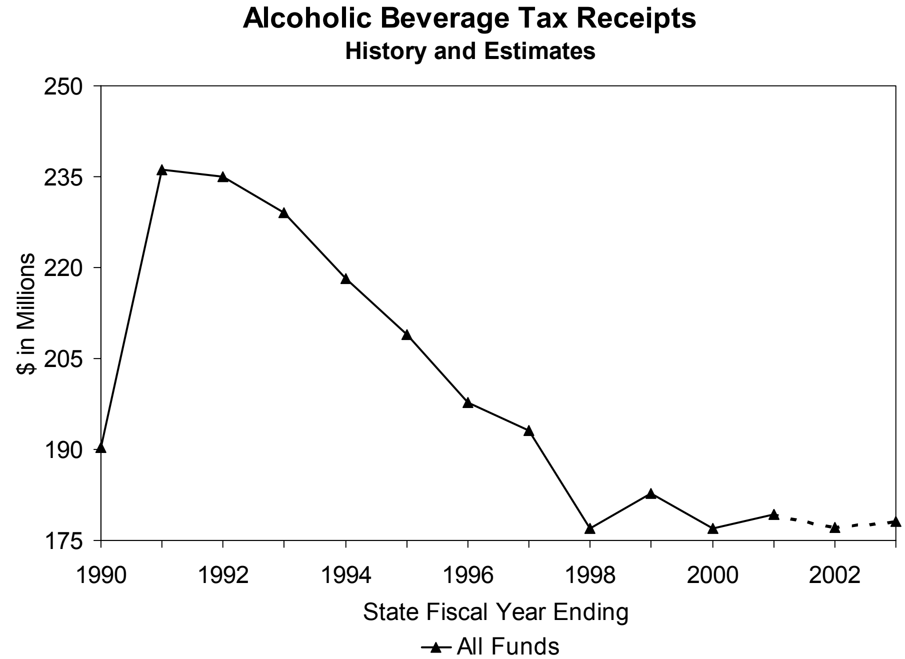
GENERAL FUND

General Fund receipts for 2001-02 are estimated to be $32.5 million. In 2002-03, General Fund receipts are projected to reach $40 million, assuming enactment of legislation proposed with this Budget.

ALCOHOLIC BEVERAGE CONTROL LICENSE FEES RECEIPTS (thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual						
1993-94	29,852	2,237	27,615	2,155	0	0	29,770
1994-95	33,864	3,283	30,581	2,100	0	0	32,681
1995-96	33,956	2,981	30,975	2,400	0	0	33,375
1996-97	31,748	3,417	28,331	2,300	0	0	30,631
1997-98	33,162	2,629	30,533	2,387	0	0	32,920
1998-99	32,282	3,190	29,092	0	0	0	29,092
1999-2000	25,566	2,615	22,951	0	0	0	22,951
2000-01	33,140	1,787	31,353	0	0	0	31,353
	Estimated						
2001-02	34,000	1,500	32,500	0	0	0	32,500
2002-03							
Current Law	33,500	1,500	32,000	0	0	0	32,000
Proposed Law	42,000	2,000	40,000	0	0	0	40,000

ALCOHOLIC BEVERAGE TAXES



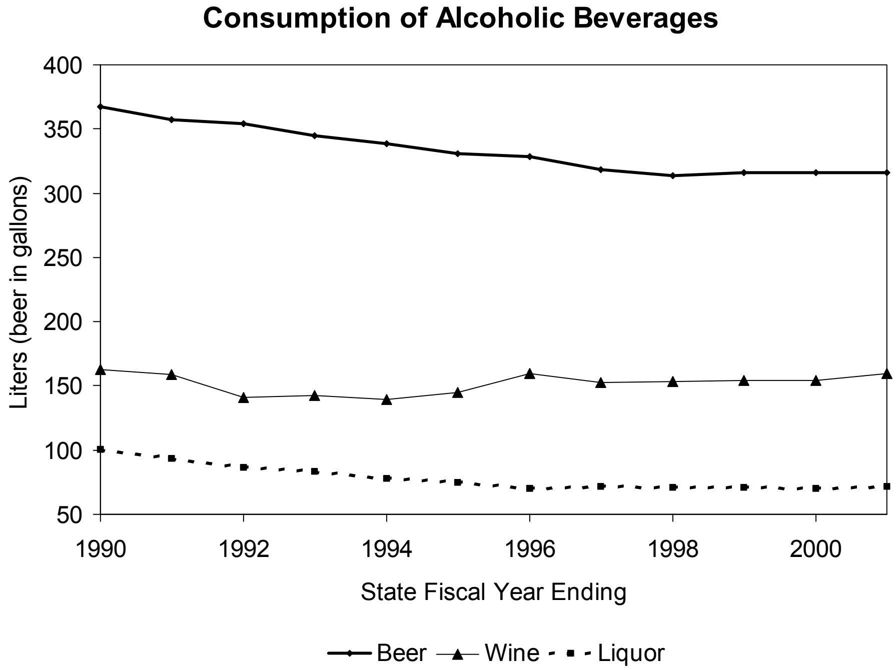
DESCRIPTION

New York State imposes excises at various rates on liquor, beer, wine and specialty beverages. These taxes are remitted by licensed distributors and noncommercial importers of such beverages in the month following the month of delivery.

State tax rates for 2001-02 are as follows (dollars per unit of measure):

Liquor over 24 percent alcohol	1.70	per liter
All other liquor with more than 2 percent alcohol	0.67	per liter
Natural sparkling wine	0.05	per liter
Artificially carbonated sparkling wine	0.05	per liter
Still wine	0.05	per liter
Beer with 0.5 percent or more alcohol	0.125	per gallon
Liquor with not more than 2 percent alcohol	0.01	per liter
Cider with more than 3.2 percent alcohol	0.01	per liter

Overall, per capita consumption of taxed beverages has remained fairly constant in recent years. However, there have been shifts in consumer preferences. For example, wine consumption has recently increased relative to liquor and beer consumption. In addition, the movement of alcohol beverage demand towards less expensive beverages with lower alcoholic content is attributed, in part, to the impact of rising prices on beverages with higher alcohol content.



SIGNIFICANT LEGISLATION

A significant number of statutory changes have been made to the alcoholic beverage tax since its inception. The following table summarizes the major tax legislation enacted since 1994.

SIGNIFICANT ALCOHOLIC BEVERAGE TAX LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1995		
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 21 cents to 16 cents per gallon.	January 1, 1996
Legislation Enacted in 1998		
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 16 cents to 13.5 cents per gallon.	January 1, 1999
Legislation Enacted in 1999		
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 13.5 cents to 12.5 cents per gallon.	April 1, 2001
Exemption	Increased the small brewers exemption for the first 100,000 barrels of domestically brewed beer to 200,000 barrels.	April 1, 2001
Legislation Enacted in 2000		
Exemption	Accelerated the small brewers exemption increase by moving the effective date from April 1, 2001, to January 1, 2000.	January 1, 2000
Beer Tax Cut	Reduced the State excise tax rate on beer with at least 0.5 percent alcohol from 12.5 cents to 11 cents per gallon.	September 1, 2003

The State continues to suffer tax evasion due to the bootlegging of alcoholic beverages from other states. Enforcement legislation enacted in 1993 added registration, invoice and manifest requirements, as well as seizure and forfeiture provisions. Additionally, the legislation provided higher fines for the bootlegging of varying volumes of liquor. These alcoholic beverage enforcement provisions have provided some protection to the State's liquor industry and the tax base, thereby moderating year-over-year declines in State alcoholic beverage tax receipts. Legislation enacted in 1997 extended these enforcement provisions from October 31, 1997, to October 31, 2002. Legislation submitted with this Budget proposes to extend these provisions permanently.

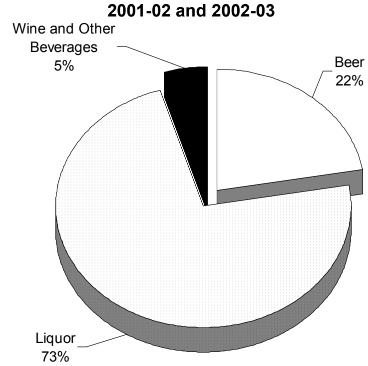
ALCOHOLIC BEVERAGE TAX ENFORCEMENT PROVISIONS

Violations	Volume	Penalties
Import liquor without registration		Class A misdemeanor
Produce, distill, manufacture, compound, mix or ferment liquors without registration or tax payments		Class A misdemeanor
Cause liquor covered by a warehouse receipt to be removed from a warehouse		Class A misdemeanor
Three or more above violations in a five-year period		Class E felony
Import liquor without registration	More than 360 liters within one year	Class E felony
Produce, distill, manufacture, compound, mix or ferment liquors without registration or tax payments	More than 360 liters within one year	Class E felony
Cause liquor covered by a warehouse receipt to be removed from a warehouse	More than 360 liters within one year	Class E felony
Custody, possession or control of liquor without registration or tax payments		Class B misdemeanor
Custody, possession or control of liquor without registration or tax payments	Exceeds 360 liters	Class E felony
Import liquor without registration	More than 90 liters	Seize transportation vehicles and liquor.
Distribute or hold liquor for sale without paying alcoholic beverage taxes	More than 90 liters	Seize transportation vehicles and liquor.
A distributor fails to pay the tax		10 percent of the tax amount to be due, plus 1 percent each month after the expiration. The penalty shall not be less than $100 but not exceeding 30 percent in aggregate.
Any other person fails to pay the tax		50 percent of the tax amount to be due, plus 1 percent each month after the expiration. The penalty shall not be less than $100.

2001-02 RECEIPTS

Net receipts of $137.0 million to date in the current fiscal year represent a decrease of 2.4 percent from the comparable period in 2000-01. The decline is due primarily to the one cent beer tax rate cut effective April 1, 2001. Accordingly, alcoholic beverage tax receipts for 2001-02 are estimated at $177.1 million. The bulk of estimated receipts, $128.9 million, are derived from the tax on liquor. The 1997 enforcement provisions will preserve an estimated $3 million in liquor tax revenues that otherwise would have been lost due to evasion and avoidance.

Alcoholic Beverage Tax Receipts 2001-02 and 2002-03



The April 1, 2001, excise tax reduction on beer is expected to reduce beer tax collections by $3.1 million. Total beer tax receipts are estimated to be $39.6 million. Revenues from wine and other specialty beverages are estimated to reach $8.6 million in 2001-02.

COMPONENTS OF ALCOHOLIC BEVERAGE TAX RECEIPTS
(millions of dollars)

	1996-97	1997-98	1998-99	1999-2000	2000-01	2001-02	2002-03
	Actual					--Estimated--	--Projected--
Beer	50.6	50.2	47.8	42.7	42.8	39.6	39.3
Liquor	126.2	125.4	125.7	125.2	128.0	128.9	130.2
Wine and Other	8.3	8.5	8.5	8.3	8.5	8.6	8.7
Subtotal	185.1	184.1	182.0	177.0	179.3	177.1	178.2
Reconciliation	8.0	(7.1)	0.8	0.8	0.0	0.0	0.0
Net Total	193.1	177.0	182.8	177.0	179.3	177.1	178.2

2002-03 PROJECTIONS

In the coming fiscal year, the consumption of liquor and wine is expected to grow while beer consumption is expected to decline modestly. Taken together, estimated consumption and tax rate changes are projected to result in a minor increase in receipts. Total alcoholic beverage tax receipts are projected to be $178.2 million. This includes $130.2 million from liquor. Projected beer excise tax receipts of $39.3 million include a reduction of $3.1 million due to the 2001 one cent per gallon beer excise tax reduction. Revenues from wine and other specialty beverages are projected to total $8.7 million.

Legislative enactment of the proposed enforcement provisions would protect $1 million in liquor tax receipts in 2002-03, and about $3 million in subsequent years.

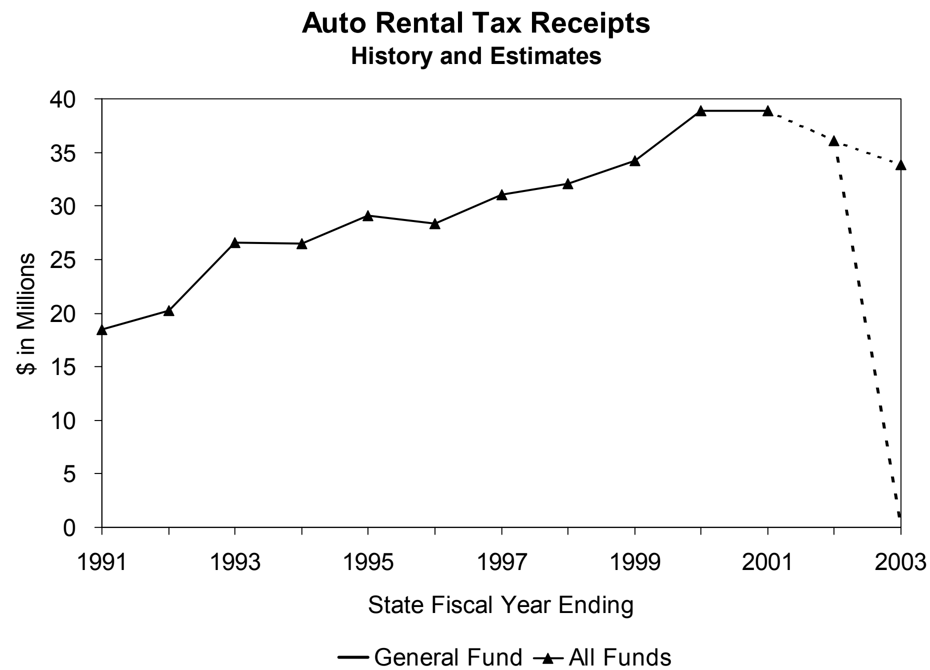
GENERAL FUND

All receipts from the alcoholic beverage tax are deposited in the General Fund.

ALCOHOLIC BEVERAGE TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual						
1993-94	218,341	99	218,242	0	0	0	218,242
1994-95	209,134	98	209,036	0	0	0	209,036
1995-96	198,280	492	197,788	0	0	0	197,788
1996-97	192,960	(123)	193,083	0	0	0	193,083
1997-98	177,124	115	177,009	0	0	0	177,009
1998-99	183,087	316	182,771	0	0	0	182,771
1999-2000	177,093	55	177,038	0	0	0	177,038
2000-01	179,407	67	179,340	0	0	0	179,340
	Estimated						
2001-02	177,200	100	177,100	0	0	0	177,100
2002-03							
(current law)	177,300	100	177,200	0	0	0	177,200
(proposed law)	178,300	100	178,200	0	0	0	178,200

AUTO RENTAL TAXES



DESCRIPTION

Since June 1, 1990, the State has imposed a 5 percent tax on charges for any rental or use in New York State of a passenger car with gross vehicle weight of 9,000 pounds or less that has seating capacity for nine or fewer passengers. The tax applies to a vehicle rented by a resident or a nonresident, regardless of where the vehicle is registered. The tax does not apply to a car lease covering a period of a year or more.

2001-02 Receipts

Receipts from the auto rental tax are influenced by the overall health of the economy, including consumer and business spending, and by the strength of the State's tourism industry. Collections to date are $30.6 million, down 8.1 percent, or $2.7 million from the comparable period of the prior fiscal year. Based on collections to date and the impact of the World Trade Center (WTC) disaster on air travel, General Fund auto rental tax receipts for 2001-02 are estimated at $36.1 million, down $2.8 million, or more than 7 percent from 2000-01.

2002-03 Projections

The full-year impact of reduced air travel resulting from the WTC disaster and the recession is projected to decrease 2002-03 receipts to $33.8 million, or $2.3 million below 2001-02.

OTHER FUNDS

Legislation submitted with this Budget proposes to dedicate all receipts from the auto rental tax to the Dedicated Highway and Bridge Trust Fund, effective April 1, 2002.

GENERAL FUND

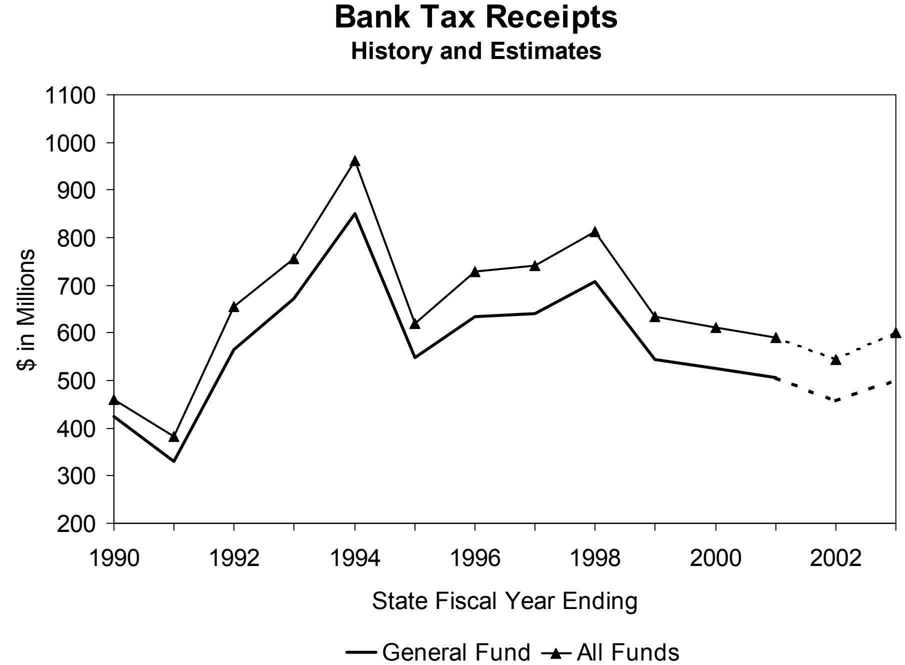
Under the proposed legislation, effective April 1, 2002, no auto rental tax receipts will be deposited in the General Fund.

AUTO RENTAL TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Gross Capital Projects Funds	Refunds	Net Capital Projects Funds[1/]	Debt Service Funds	All Funds Net Collections
	Actual								
1993-94	26,473	0	26,473	0	0	0	0	0	26,473
1994-95	29,069	0	29,069	0	0	0	0	0	29,069
1995-96	28,344	0	28,344	0	0	0	0	0	28,344
1996-97	31,056	0	31,056	0	0	0	0	0	31,056
1997-98	32,039	0	32,039	0	0	0	0	0	32,039
1998-99	34,241	0	34,241	0	0	0	0	0	34,241
1999-2000	38,843	0	38,843	0	0	0	0	0	38,843
2000-01	38,916	0	38,916	0	0	0	0	0	38,916
	Estimated								
2001-02	36,100	0	36,100	0	0	0	0	0	36,100
2002-03									
(current law)	33,800	0	33,800	0	0	0	0	0	33,800
(proposed law)	0	0	0	0	33,800	0	33,800	0	33,800

[1/] Dedicated Highway and Bridge Trust Fund

BANK TAX



DESCRIPTION

The bank tax is levied by Article 32 of the Tax Law on banking corporations conducting business in New York State. As the graph above shows, Article 32 receipts have been volatile, reflecting statutory and regulatory changes and the variable profit performance of the banking sector.

Tax Rate

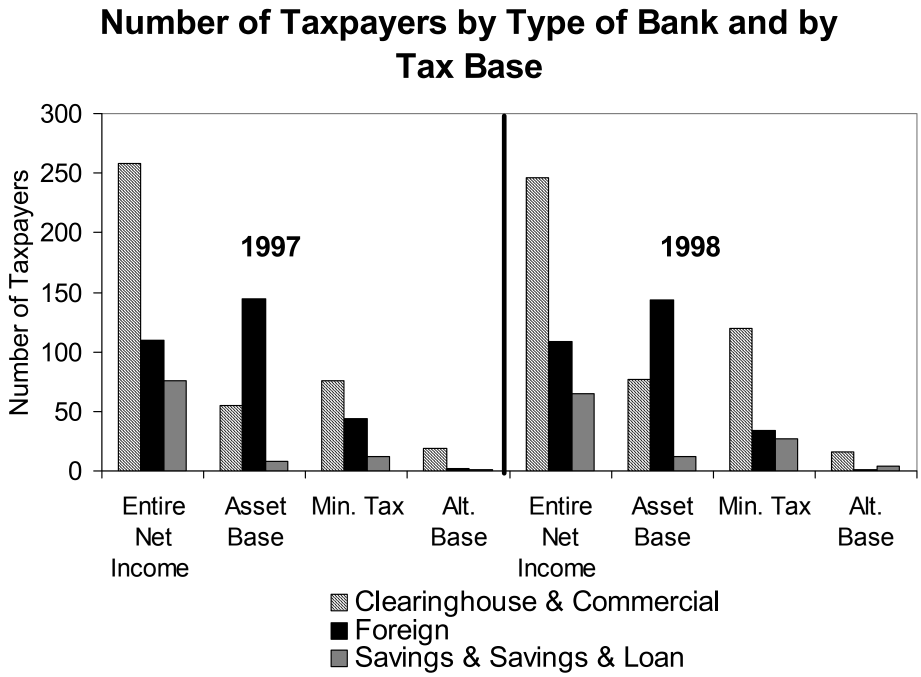
Article 32 bank tax liability is the highest of the following four computations:

1. 8 percent of allocated entire net income (ENI), reduced to 7.5 percent for taxable years beginning on or after July 1, 2002;
2. 10 percent of allocated alternative entire net income (ENI without regard to specified exclusions);
3. 1/10, 1/25, or 1/50 of a mill of allocated taxable assets; or
4. a minimum tax of $250.

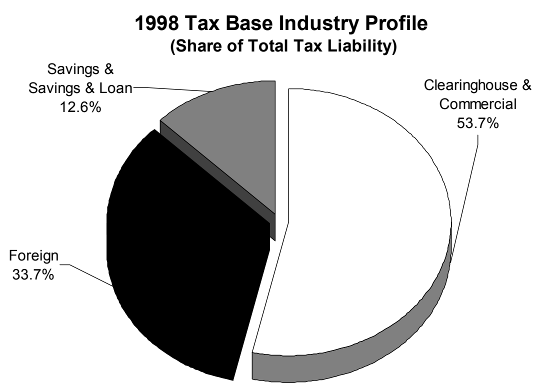
Additionally, a temporary surcharge is imposed on taxpayers within the Metropolitan Commuter Transportation District (MCTD), with a rate of 17 percent of the portion of tax allocable to such district.

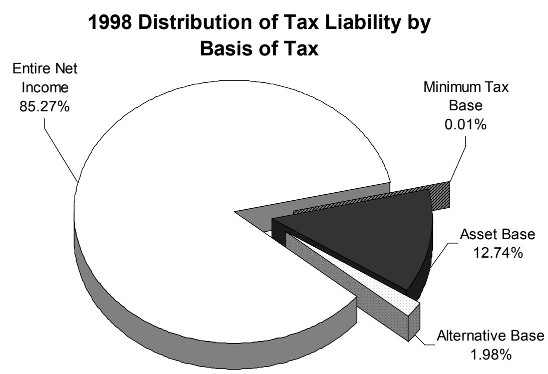
Tax Base

The primary source of data on bank tax liability is the Bank Tax Study File, which is compiled by the Department of Taxation and Finance's Office of Tax Policy Analysis (OTPA). The study file includes tax data on all banks filing under Article 32. Between 1997 and 1998 (1998 representing the most recent information available), total tax liability decreased by roughly 17 percent, from $643 million to $533 million, while the number of taxpayers increased by 6 percent, with the majority of the increase in clearinghouse and commercial banking institutions. The following graph illustrates that, between 1997 and 1998, the number of clearinghouse and commercial taxpayers paying under the minimum tax base increased by roughly 58 percent. The increase in the number of filers under the minimum tax base resulted, in part, from the increased use of tax credits against ENI. In addition, tax liability under the asset base was significantly higher in 1998 than in 1997, further reducing the number of filers under the ENI base.



The following pie charts illustrate that clearinghouse and commercial banking institutions paid roughly 54 percent of total tax liability in 1998, while foreign banking institutions and savings and savings and loan institutions accounted for 33.7 percent and 12.6 percent of liability respectively. Additionally, payments under the ENI base comprised roughly 85 percent of total tax liability under Article 32 in 1998.





SIGNIFICANT LEGISLATION

The bank tax structure includes various exclusions, exemptions, tax credits, and other statutory devices designed to reduce State tax liability. The primary objective of these incentives is to provide economic incentives to stimulate the New York economy.

SIGNIFICANT BANK TAX LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1994		
Subsidiary Capital	Subsidiary capital taxation rules allow deduction of 60 percent of the amount by which gains exceed losses from such capital, to the extent such gains and losses were taken into account in determining taxable income.	January 1, 1994
Legislation Enacted in 1997		
Credit for Employing Individuals with Disabilities	Employers who employ individuals with disabilities may claim a credit for a portion of wages paid to such individuals.	January 1, 1998
Net Operating Loss	Allows banks to claim a net operating loss deduction (NOLD) for losses incurred on or after January 1, 2001.	January 1, 2001
Legislation Enacted in 1998		
Investment Tax Credit	Bank taxpayers that are brokers/dealers in securities may claim a credit for equipment used in broker/dealer activities and in activities connected with broker/dealer operations.	October 1, 1998
Legislation Enacted in 1999		
Rate Reduction — ENI	Reduced the ENI tax rate from 9 percent to 7.5 percent in phases over three years.	June 30, 2000

2001-02 RECEIPTS

Based on collections to date, net collections for the year are estimated to be $543 million, representing a $48 million decrease from the 2000-2001 level. The decrease of approximately 8 percent is the result of several factors. The most significant factor is the impact of the World Trade Center (WTC) disaster of September 11. Several taxpayers under this article had substantial office space located in and around the World Trade Center that was destroyed or damaged. These taxpayers are expected to have significant uninsured losses in both property and lost business activity which will likely lower their tax liability to New York State.

In addition, the economy has entered a recession. (See Economic Backdrop section.) Weakness in the economy has led to an increase in the bad debt carried by banks resulting in a deterioration in the financial condition of many banks.

Following the passage of the Federal Gramm-Leach Bliley Act, some large banks engaged in the acquisition of financial service firms. As the economic climate has worsened, these banks are now looking to restructure to eliminate affiliates with disappointing earnings. This restructuring may lower earnings and associated liability throughout the current State fiscal year, but should result in improved performance in future years.

Finally, bank tax receipts have been adjusted to reflect an expected decline in audit receipts during the second half of the current State fiscal year. Audit collections are expected to be lower due to the disruption of the audit process caused by the WTC tragedy.

2002-03 PROJECTIONS

Net bank tax collections are expected to be $600 million in 2002-03, which is $57 million above the amount estimated to be received in 2001-02.

The bank tax projection is based, in part, on the underlying relationship between tax liability and bank profitability. Corporate profits, which have declined significantly over the course of the 2001-02 State fiscal year, are expected to improve during 2002-03. It is expected that corporate profitability will see improvement and growth throughout the 2002-03 State fiscal year.

Already scheduled tax reductions are expected to reduce bank tax receipts in both the 2001-02 and 2002-03 State fiscal years. Specifically, receipts will decline by an additional $45 million in 2001-02, and $38 million in 2002-03 due to previously enacted legislation, including the reduction of the entire net income tax rate, the prospective net operating loss deduction, and the expansion of the ITC credit.

OTHER FUNDS

Under current law, a surcharge is imposed at a rate of 17 percent of the portion of the statewide tax liability of the business that is allocated to the MCTD, and is the principal revenue source of the Mass Transportation Operating Assistance Fund (MTOA). Based on collections to date, the bank tax contribution to MTOA for 2001-02 is projected to reach approximately $86 million. MTOA receipts are affected by the same factors impacting overall bank tax receipts, and are expected to increase by 13 percent to $97 million in 2002-03.

GENERAL FUND

Based on collections to date, General Fund net collections for 2001-02 are projected to decrease by $48 million, a 9.5 percent decrease from State fiscal year 2000-2001, primarily driven by large decreases on 2001 liability and reductions in audit receipts.

It is expected that the poor performance of the industry stemming from the WTC attack will be primarily limited to the 2001-02 State fiscal year, and that significant charges against earnings taken by banks during the 2001-02 State fiscal year will set the stage for higher earnings in 2002-03. Bank tax receipts for State fiscal year 2002-03 are expected to increase by 10 percent, primarily driven by the recovery in the banking sector, and the receding impact of the WTC disaster on audit collections.

GENERAL FUND RECEIPTS BY TYPE OF BANK
(thousands of dollars)

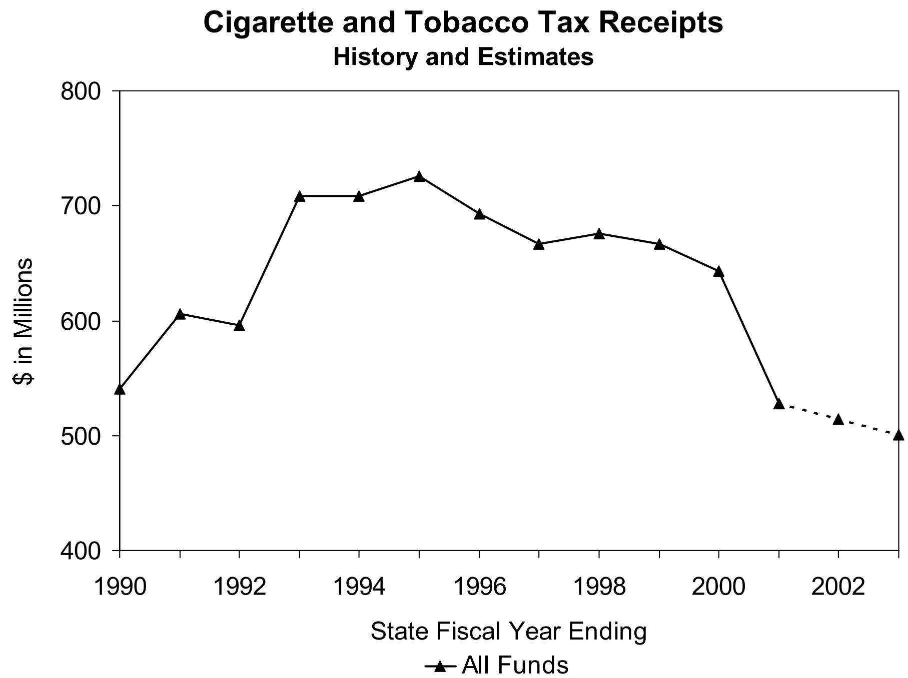
	State Banks, Trust Companies and National Banks	Savings Banks	Savings and Loan Associations	Total
	Actual			
1993-94	784,033	45,861	20,840	850,734
1994-95	486,102	50,965	10,885	547,952
1995-96	611,513	24,455	(1,305)	634,663
1996-97	637,448	(3,003)	5,492	639,937
1997-98	700,344	1,183	5,796	707,323
1998-99	527,485	11,706	4,866	544,058
1999-2000	515,528	5,186	4,795	525,509
2000-01	495,896	5,188	4,392	505,476
	Estimated			
2001-02	449,490	3,531	3,979	457,000
2002-03	494,734	3,886	4,379	503,000

BANK TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual								
1993-94	905	55	851	115	4	112	0	0	962
1994-95	615	67	548	78	8	71	0	0	619
1995-96	702	68	635	99	5	94	0	0	729
1996-97	724	84	640	110	9	101	0	0	741
1997-98	766	58	707	114	8	105	0	0	812
1998-99	624	80	544	102	11	91	0	0	635
1999-2000	598	72	526	94	9	85	0	0	611
2000-01	598	92	505	97	11	86	0	0	591
	Estimated								
2001-02	509	52	457	97	11	86	0	0	543
2002-03	557	54	503	109	12	97	0	0	600

[1] MCTD 17 percent surcharge deposited in the Mass Transportation Operating Assistance Fund.

CIGARETTE AND TOBACCO TAXES



DESCRIPTION

Tax Rate and Base

The New York State cigarette excise tax is imposed by Article 20 of the Tax Law on the sale or use of cigarettes within the State. The current tax rate is $1.11 per package of 20 cigarettes.

The Federal government imposes a cigarette excise tax on manufacturers and first importers of cigarettes. The Federal tax rate was increased from 24 to 34 cents per pack on January 1, 2000, and again to 39 cents per pack on January 1, 2002. New York City also levies a separate cigarette excise tax of 8 cents per pack. Historical changes in State, City and Federal tax rates are shown in the following table.

STATE, FEDERAL AND NEW YORK CITY CIGARETTE EXCISE TAX RATES (since 1950)

State		Federal		New York City	
	Rate (cents)		***Rate*** (cents)		***Rate*** (cents)
Before April 1, 1959	2	Before November 1, 1951	7	Before May 1, 1959	1
April 1, 1959	5	November 1, 1951	8	May 1, 1959	2
April 1, 1965	10	January 1, 1983	16	June 1, 1963	4
June 1, 1968	12	January 1, 1991	20	January 1, 1976	8
February 1, 1972	15	January 1, 1993	24		
April 1, 1983	21	January 1, 2000	34		
May 1, 1989	33	January 1, 2002	39		
June 1, 1990	39				
June 1, 1993	56				
March 1, 2000	111				
April 3, 2002	150				

The State also imposes a tax on other tobacco products, such as chewing tobacco and cigar tobacco, at a rate of 20 percent of their wholesale price. The Federal government also imposes an excise tax on manufacturers and importers of tobacco products at various rates, depending on the type of product.

Administration

State registered stamping agents, most of whom are wholesalers, purchase tax stamps from the State and affix the stamps to cigarette packages to be sold by New York State registered retailers. Purchasers of non-State stamped cigarettes, such as cigarettes sold out-of-State or on Indian reservations, must remit the cigarette excise tax on purchases in excess of two cartons directly to the Department of Taxation and Finance.

Tax Evasion

Cigarette tax evasion is a serious problem in New York and throughout the Northeast. Widespread evasion not only reduces State and local revenues, but also has an adverse impact on legitimate wholesalers and retailers. The Department of Taxation and Finance has acted vigorously to curb cigarette bootlegging through investigatory and enforcement efforts. Legislation, enacted in 1996, substantially increased penalties for retailers and wholesalers who sell unstamped or illegally stamped packages of cigarettes.

The positive effects of this enforcement legislation were realized in 1999, with an increase in the number of new retailer license applications. This increase, as well as an enhanced State enforcement presence, may have led to less severe declines in taxable cigarette consumption than would otherwise have been realized.

CIGARETTE TAX RATES IN NEW YORK AND BORDERING STATES*
(cents per pack)

	2001	2000	1999	1998	1997	1996
Connecticut	50	50	50	50	50	50
Massachusetts	76	76	76	76	76	76
New Jersey	80	80	80	80	40	40
New York	111	111	56	56	56	56
Pennsylvania	31	31	31	31	31	31
Vermont	44	44	44	44	44	44

* Highest rate in effect during calendar year.

Effective March 1, 2000, New York raised its tax by 55 cents to $1.11 per pack. Also in 2000, the Governor signed comprehensive legislation targeted at combating cigarette bootlegging and reducing youth and adult smoking by banning Internet sales. This legislation was ruled unconstitutional by the U.S. District Court of the Southern District of New York and enjoined from going into effect. The State has filed an appeal which has yet to be heard. Significant statutory changes, since 1996 are shown below.

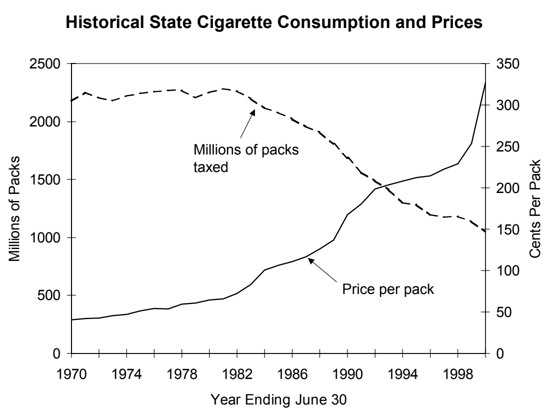
SIGNIFICANT LEGISLATION

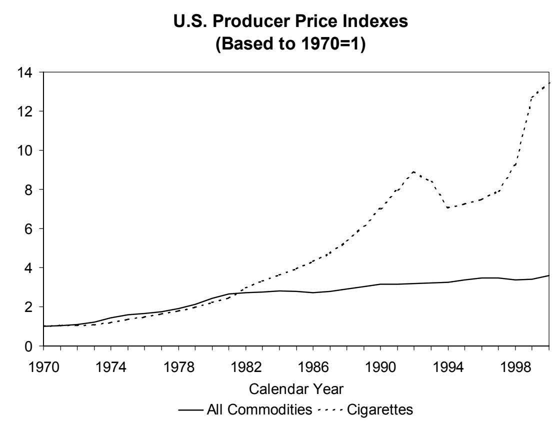
Subject	Description	Effective Date
Legislation Enacted in 1996		
Enforcement Provisions	Increased penalties and fines for selling unstamped cigarettes, violation of retail dealer and vending machine registration provisions, and providing inaccurate registration information.	December 3, 1996

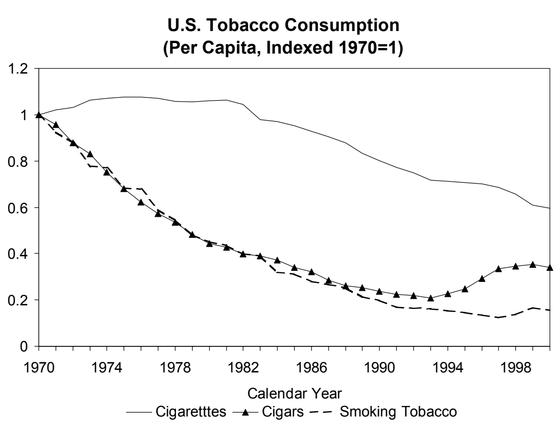
Subject	Description	Effective Date
Legislation Enacted in 1999		
Cigarette Tax Increase	Increased the cigarette excise tax from 56 cents to $1.11 per pack, as part of the Health Care Reform Act (HCRA) of 2000.	March 1, 2000
Legislation Enacted in 2000		
Underage Smoking	Increased penalties for illegal sales of tobacco products to minors.	September 1, 2000
Enforcement Provisions	Created civil and criminal penalties for persons who sell and ship cigarettes to persons who are not licensed or registered cigarette dealers or agents.	November 16, 2000
Enforcement Provisions	Created civil and criminal penalties for carriers who transport cigarettes to persons who are not licensed or registered cigarette dealers or agents.	January 1, 2001
Safe Cigarettes	Required the promulgation and imposition of fire-safety standards for cigarettes and rolled tobacco products sold in New York.	January 1, 2003
Legislation Enacted In 2002		
Cigarette Tax Increase	Increased the cigarette excise tax from $1.11 per pack to $1.50 per pack.	April 3, 2002

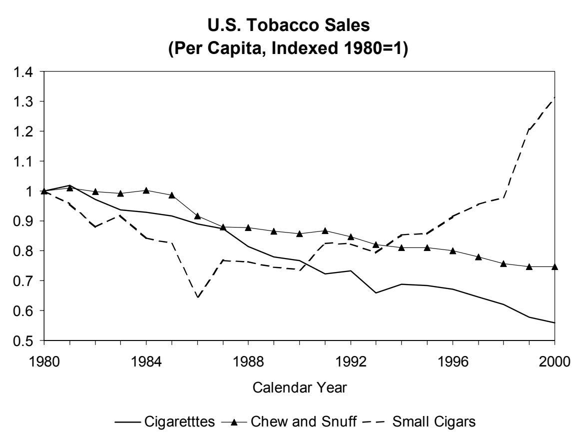
BRIEF REVIEW OF RECEIPTS HISTORY

Taxable cigarette consumption in New York has declined by more than 50 percent since 1970 due to price increases, growing public awareness of the adverse health effects of smoking, smoking restrictions imposed by governments, anti-smoking education programs, and changes in consumer preferences toward other types of tobacco. The following graphs summarize some of these trends.









Total cigarette and tobacco receipts are estimated at $1,012.2 million, a decrease of $11.6 million, or 1.1 percent from 2000-01. The 2001-02 annual rate of decline is understated. To date, total cigarette and tobacco tax receipts are $779.9 million, a decrease of $23.6 million, or 2.9 percent below comparable receipts in 2000-01. However, in anticipation of the April 3, 2002 tax increase, consumers are expected to move some cigarette purchases from 2002-03 into 2001-02. In addition, receipts in April 2000 were artificially low due to consumer pre-buying in anticipation of the March 1, 2000 tax increase. These two behavioral changes serve to lower the estimated annual rate of decline to only 1.1 percent.

Underlying taxable cigarette consumption continued its secular decline in 2001-02. The decline in consumption is partially attributable to an estimated price increase of 7.3 percent. Since the Tobacco Settlement was signed in November 1998, the producer price index (which does not include taxes) for cigarettes has increased 65 percent (see graph above), as tobacco companies have attempted to recoup normal increases in operating costs and the cost of the settlement through price increases. Also, restrictions on cigarette advertising and a general increase in the awareness of the health consequences of smoking have contributed to long-term declining trends in cigarette consumption.

2002-03 PROJECTIONS

Legislation enacted in January 2002 raises the cigarette tax from the current $1.11 per pack to $1.50 per pack, effective April 3, 2002. Accordingly, total cigarette and tobacco tax revenue is projected to be $1,249.2 million, an increase of $237 million, or 23.4 percent from State fiscal year 2001-02. Legislation proposed in the Executive Budget will establish the percentage distributions of cigarette tax revenue shown in the following table.

Cigarette Tax Distribution* (percent)
Current Law

General Fund	50.45
HCRA**	49.55

Cigarette Tax Distribution (percent)
Proposed Law

February 1, 2002 to March 31, 2002	
General Fund	44.60
HCRA	55.40
Beginning April 1, 2002	
General Fund	38.78
HCRA	61.22

* Excludes tobacco tax
** Tobacco Control and Insurance Initiatives Pool

The long-term factors reducing cigarette consumption will continue to exert negative pressure on receipts. Price increases will continue to have a significant effect on taxable cigarette consumption in 2002-03. Wholesale prices are expected to rise 9.2 percent, and overall prices are expected to rise 17 percent (including the enacted tax increase). As cigarette prices are high in New York relative to the surrounding states, there is an added incentive for smokers to purchase cigarettes in surrounding states, bootlegged cigarettes, or cigarettes sold through mail order or on the Internet and evade or avoid paying the tax.

OTHER FUNDS

The bulk of the amount generated by the increase of the cigarette tax to $1.50 will be deposited in the Tobacco Control and Insurance Initiatives Pool established in the Health Care Reform Act of 2000 (HCRA). Based on the percentage distribution of cigarette tax receipts in effect between February 1, 2002 and March 31, 2002 (see table above), the pool will receive an additional $17.5 million in 2001-02 when compared with current law estimates. An estimated $497.9 million (including current law receipts) will be deposited in the pool in 2001-02. Based on the percentage distribution in effect beginning April 1, 2002 (see above table), receipts deposited in the pool in 2002-03 will total a projected $748.6 million.

GENERAL FUND

The proposed law is designed to hold estimated General Fund receipts harmless when compared with current law. General Fund cigarette and tobacco tax receipts for 2001-02 are estimated at $514.3 million, a decline of $14 million, or 2.6 percent, from 2000-01. To date, General Fund cigarette and tobacco tax receipts are an estimated $402.9 million, a decline of $12.1 million, or 2.9 percent.

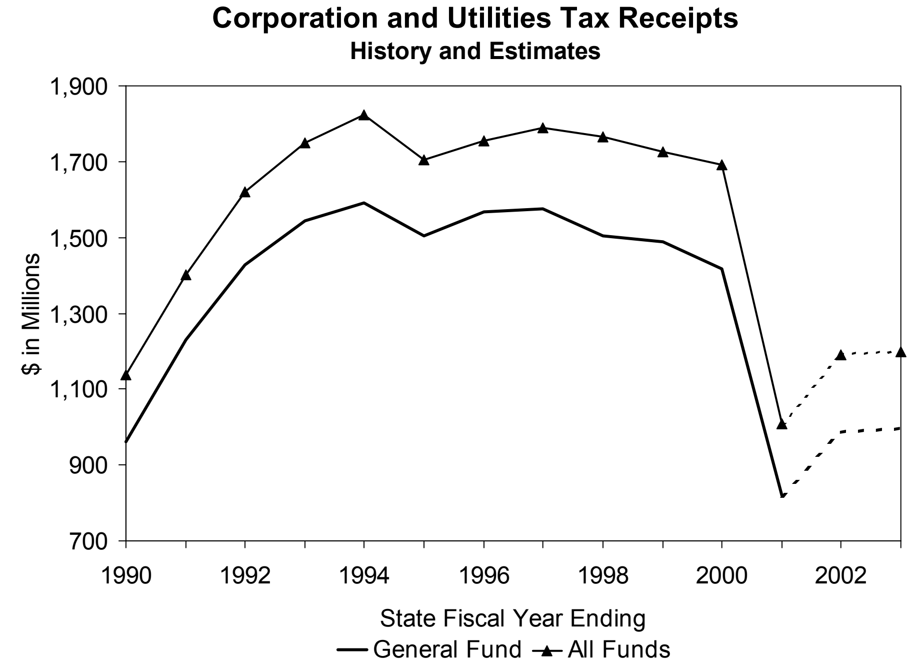
For 2002-03, General Fund cigarette tax receipts are projected to be $474.3 million. The tax on tobacco products and license fees is expected to total $26.3 million, an increase of $1.1 million from 2001-02. This increase is largely due to a continuation of the consumption trends and an expected shift of cigarette smokers to tobacco products, including roll-your-own tobacco, as a result of the significant price increases for cigarettes.

CIGARETTE AND TOBACCO TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual						
1993-94	716,103	8,485	707,618	0	0	0	707,618
1994-95	734,134	7,638	726,496	0	0	0	726,496
1995-96	700,691	7,275	693,416	0	0	0	693,416
1996-97	675,756	8,724	667,032	0	0	0	667,032
1997-98	680,950	5,447	675,503	0	0	0	675,503
1998-99	671,699	5,118	666,581	0	0	0	666,581
1999-2000	648,609	5,451	643,158	0	0	0	643,159
2000-01	532,662	4,371	528,291	0	0	0	528,291
	Estimated						
2001-02*	518,300	4,000	514,300	0	0	0	514,300
2002-03*	504,600	4,000	500,600	0	0	0	500,600

* Note: in 2001-02 an estimated $497.9 million will be deposited in the Tobacco Control and Insurance Initiatives Pool, and in 2002-03 projected $748.6 million (or $282.8 million above current law projections) will be deposited.

CORPORATION AND UTILITIES TAXES



DESCRIPTION

Article 9 of the Tax Law imposes taxes and fees on a number of specialized industries, including public utilities, newly organized or reorganized corporations, out-of-State corporations doing business in New York State, transportation and transmission companies, and agricultural cooperatives. Article 9 receipts come primarily from the public utility, telecommunications, and transportation industries. Most Article 9 taxpayers that conduct business in the Metropolitan Commuter Transportation District (MCTD) are subject to a 17 percent surcharge on their liability attributable to the MCTD. Surcharge receipts plus portions of other Article 9 taxes are deposited in the Mass Transportation Operating Assistance Fund (MTOAF). Recent statutory and regulatory changes have significantly diminished the role of traditional energy utilities as the primary source of Article 9 receipts.

Tax Rates and Base

The pie chart in the Receipts History section depicts the share of total 2000-01 Article 9 General Fund collections accounted for by each section of the Article.

Section 180 assesses an organization tax upon newly incorporated or reincorporated domestic (in-State) corporations. The tax is imposed at a rate of 1/20 of 1 percent of the total amount of the par value (the nominal or face value of a security) of the stock that the corporation is authorized to issue; for shares of "no-par" value, the rate is five cents per share. The tax also applies to any subsequent change in the capital structure on stocks (adjustment to the par value, a change in the number of "no-par" value stocks, etc.), or newly authorized stock.

Section 181 imposes a license fee on out-of-State corporations for the privilege of exercising a corporation franchise or conducting business in a corporate or organized capacity in New York State at a rate equivalent to the organization tax imposed by section 180. An annual maintenance fee of $300 is also imposed.

Section 183 provides for a franchise tax on transportation and transmission companies including telecommunications, trucking, railroad, and other transportation companies. The tax is imposed using the highest of the following three alternatives: a rate of 1.5 mills on each dollar of the net value of capital stock allocated to New York State; a tax rate of 3/8 of a mill per dollar of par value for each 1 percent of dividends paid on capital stock if dividends amount to 6 percent or more; or a minimum tax of $75.

Section 184 is imposed on gross earnings of transportation and local telecommunications corporations from all sources in the State, including an allocated portion of receipts from interstate transportation-related transactions. The tax rate on telephone companies subject to section 184 of Article 9 is 0.375 percent, as of July 1, 2000. All toll revenues from international, interstate, and inter-Local Access Transport Areas (LATAs) services and 30 percent of intra-LATA toll revenues are excluded from the tax base. Under this section, railroad and trucking companies that elect to remain subject to Article 9 taxes pay the tax at a rate of 0.375 percent for periods beginning in July 2000 and thereafter.

Section 185 imposes a franchise tax on agricultural cooperatives at the rate of 1 mill per dollar of the net value of the corporation's issued capital stock allocated to New York State.

Legislation enacted with the 2000-01 Budget repealed section 186 retroactive to January 1, 2000. This section had imposed a franchise tax on public utilities including waterworks, gas, electric, steam heating, lighting and power companies. These companies are now taxed under Article 9-A of the Tax Law (corporate franchise tax).

Section 186-a imposes a tax on the furnishing of utility services (including both energy and lighting public utilities). This includes the 186-A commodity tax imposed on the gross operating income of utilities, corporations, and other entities not subject to the supervision of the Department of Public Service. It also includes the 186-P transmission and distribution tax imposed on the gross income of utilities and other entities that are supervised by the Department of Public Service, and that sell or furnish fuel, such as gas or electricity, through pipes or mains. Recent statutory changes reduced the tax rates under section 186-a. Further, the 2000-01 legislation established a separate tax rate imposed on commodity sales and on the sale of transmission/distribution services used to transport and deliver utility services to homes and businesses. The commodity portion of the section 186-a tax will be eliminated January 1, 2005. The tax rate schedule for the commodity and transmission/distribution portions of the current tax is reported in the table below.

TAX RATES CONTAINED IN SECTION 186-A

Effective Date	Type	Rate (percentage)
Prior to January 1, 2000	Commodity	3.25
	Transmission/Distribution	3.25
January 1, 2000	Commodity	2.10
	Transmission/Distribution	2.50
January 1, 2001	Commodity	2.00
	Transmission/Distribution	2.45
January 1, 2002	Commodity	1.90
	Transmission/Distribution	2.40
January 1, 2003	Commodity	0.85
	Transmission/Distribution	2.25
January 1, 2004	Commodity	0.40
	Transmission/Distribution	2.125
January 1, 2005	Commodity	0.00
	Transmission/Distribution	2.00

That part of the section 186-a tax imposed on the transmission/distribution of electric and gas utility services for nonresidential customers will be eliminated through a phased-in exclusion of gross receipts according to the following schedule. When fully phased in on January 1, 2005, only the residential portion of transmission/distribution services will remain taxable under section 186-a, at a rate of 2.0 percent.

PHASE-IN SCHEDULE FOR EXCLUSION OF T&D NONRESIDENTIAL CUSTOMERS

Effective Date	Rate (percentage)
Calendar Year 2000	0
Calendar Year 2001	0
Calendar Year 2002	25
Calendar Year 2003	50
Calendar Year 2004	75
Calendar Year 2005	100

Section 186-e imposes a tax on the gross receipts generated from telecommunications services. This rate was reduced to 2.5 percent on January 1, 2000.

Section 189, effective August 1, 1991, imposes a tax on the importation of natural gas for use by the importer. The cost used in the calculation of the tax is the wellhead cost of natural gas. Recent reforms will phase down the rate over a five-year period and eliminate the tax effective January 1, 2005. Taxpayers producing or extracting natural gas from their own wells for their own use are exempt from this tax, as is natural gas used by cogenerators for host site energy production.

On May 1, 2001, the New York State Court of Appeals ruled that section 189 violated the Commerce Clause insofar as it failed to avoid theoretical double taxation by failing to provide a valid credit against this section for certain taxes that may have been paid to other states. In October 2001, legislation was enacted that provides a credit for taxes paid to another state, thus eliminating the double taxation issue and the Commerce Clause violation. The phase-out of the tax will continue, as scheduled.

TAX RATES CONTAINED IN SECTION 189

Effective Date	Rate (percentage)
Prior to January 1, 2000	4.25
January 1, 2000	2.10
January 1, 2001	2.00
January 1, 2002	1.90
January 1, 2003	0.85
January 1, 2004	0.40
January 1, 2005	0.00

Payment of the Tax

The first payments of the year's liability, under the franchise taxes imposed by Article 9 (corporation tax), Article 9-A (general business tax), or Article 32 (bank tax), are considered payments of section 180 or 181 liability. In 1996, the New York State Department of Taxation and Finance determined that maintenance fee receipts paid by corporations, together with their other franchise tax remittances, should be reflected in the Department's accounts as section 181 liabilities. As a result, the appropriate amount of liability from 1993, 1994 and

1995 was adjusted in 1996-97 and 1997-98. Such adjustments are not a net cash gain to the Financial Plan. The roughly $21 million increase in 1999-2000 in section 181 receipts was fully offset by reductions in other tax articles, primarily the corporation franchise tax.

Taxpayers subject to sections 184, 186, 186-a and 186-e make tax payments on an estimated basis in March, June, September and December. A final payment is made in March. These payment schedules are comparable to those required for corporations taxable under other articles of the Tax Law. Furthermore, for taxable years beginning in 1994, State estimated tax rules for large businesses conform to Federal rules. This requires affected firms to pay 100 percent of their tax liability by the twelfth month of their fiscal year.

SIGNIFICANT LEGISLATION

The following list highlights significant legislation enacted since 1994 affecting Article 9 taxes:

Subject	Description	Effective Date
Legislation Enacted in 1994		
Temporary Business Tax Surcharge	Eliminated the 15 percent surcharge for sections 183, 184, 186, and 186-a over three years.	January 1, 1994
Legislation Enacted in 1995		
Telecommunications Act of 1995	Restructured the transmission portion of section 184 to apply to only local telecommunication services. Also, all toll revenues from interstate, and inter-LATAs services were exempted.	January 1, 1995
	Enacted section 186-e, which imposed a 3.5 percent excise tax on receipts from telecommunications services.	
	Replaced the property factor with a new allocation mechanism. Under the “Goldberg” allocation method, receipts are allocated to New York if the call originates or terminates in this State and is charged to a services address in this State, regardless of where the charges for such services are billed or ultimately paid.	
	Shifted the access deduction from inter-exchange carriers and local carriers who are ultimate sellers to initial sellers.	
Section 184	Exempted 30 percent of intra-LATA toll receipts.	January 1, 1996
Legislation Enacted in 1996		
Trucking and Railroad Companies	Allowed these companies the option of being taxed under the general corporate franchise tax (Article 9-A).	January 1, 1997
	Reduced the tax rate on section 184 for these companies from 0.75 percent to 0.6 percent.	
Legislation Enacted in 1997		
Power for Jobs Program	Created a tax credit against section 186-a, to compensate utilities for revenue losses associated with participation in the program. The program makes low-cost power available to businesses, small businesses and not-for-profit corporations for job retention and creation. The credit is allowed to the utility providing low cost power to retail customers selected by the Power Allocation Board.	1997
Alternative Fuels Vehicle Credit	Created a tax credit equaling 50 percent of the incremental costs (capped at $5,000 per vehicle); 60 percent of the cost of clean-fuel components (capped at $5,000 or $10,000 per vehicle depending on weight); and 50 percent of the cost of new clean-fuel refueling property.	January 1, 1998
Rate Reductions	Reduced the section 184 tax rate from 0.75 percent to 0.375 percent.	January 1, 1998
	Reduced section 186-a and section 186-e tax rates from 3.5 percent to 3.25 percent as of October 1, 1998, and to 2.5 percent on January 1, 2000.	
Credit for Employers Who Hire Persons With Disabilities	Created a tax credit equaling 35 percent of the first $6,000 of qualified wages (maximum of $2,100 per employee).	January 1, 1998

Subject	Description	Effective Date
Legislation Enacted in 1999		
MTOA Fund	Increased the percent of collections from section 183 and section 184 to be distributed to the MTOA Fund from 54 percent to 64 percent on January 1, 2000, and to 80 percent on January 1, 2001.	January 1, 2000 January 1, 2001
Section 189	Exempted generation plants that import natural gas for the production of electricity.	January 1, 2001
Section 183	Eliminated the excess dividends base for those local telecommunications companies with fewer than one million access lines.	January 1, 2002
Legislation Enacted in 2000		
Utility Tax Reform	Repealed the section 186 tax. Section 186-a and section 189 tax are phased-out over a five-year period. Elimination of the gross receipts tax for manufacturers and industrial energy customers retroactive to January 1, 2000; elimination of the tax for all other business customers over a five-year period. For residential consumers, the commodity tax is eliminated and the transmission/distribution rate of the 186-a tax is reduced from 2.5 percent to 2.0 percent.	January 1, 2000
Power for Jobs	Provided an additional 300 megawatts of low-cost power to businesses across New York through the Power for Jobs program.	January 1, 2001
Legislation Enacted in 2001		
Section 189	Created a prospective and retroactive credit for taxes paid to other states where natural gas was purchased.	Retroactive to August 1, 1991

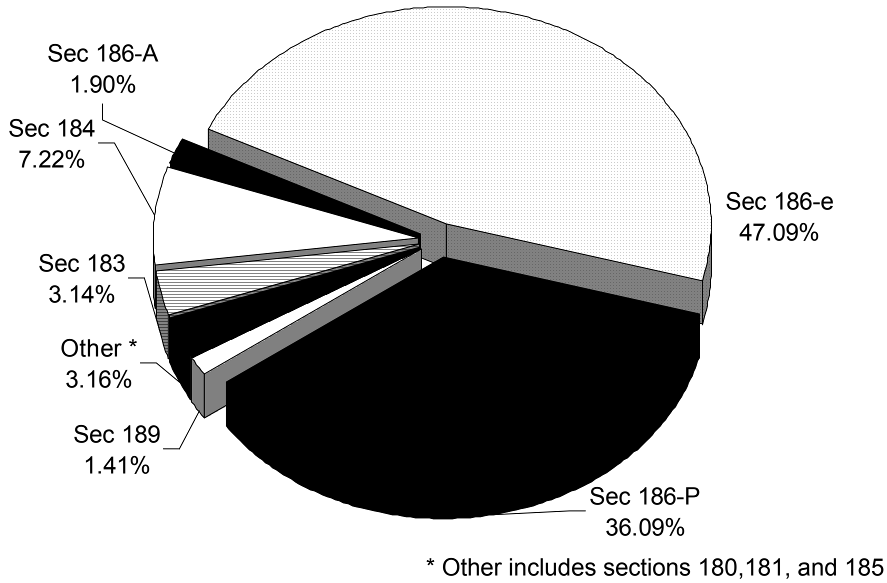
BRIEF REVIEW OF RECEIPTS HISTORY

For State fiscal years 1990-91 through 2000-01, Article 9 receipts have been highly variable. To a great extent, this volatility is the product of the numerous statutory changes elaborated on in the prior section. The volatility is also associated with fluctuations in energy prices and telecommunications demand.

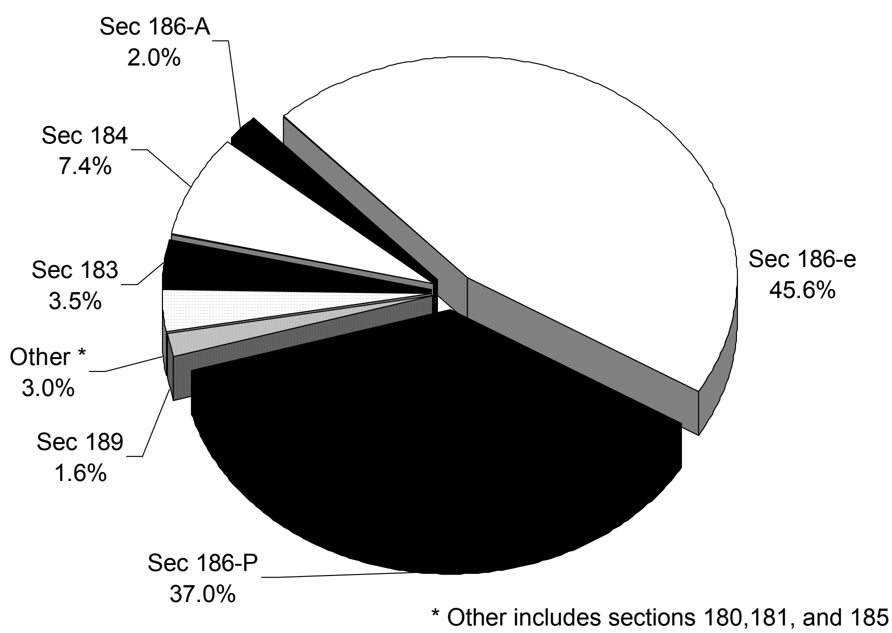
History of General Fund

The pie charts below show the breakdown of collections, by section of law, for All Funds and the General Fund. For State fiscal years 1990-91 through 2000-01, the General Fund averaged 86.8 percent of All Funds. However, this percentage is expected to change to 82.8 percent in 2001-02 and 82.7 percent in 2002-03, due to the increased percentage of collections from sections 183 and 184 that have been earmarked to the MTOAF, sections 186-a and 186-e rate reductions, and other statutory changes enacted in 2000.

All Funds Percent Distribution by Section
2000-01 State Fiscal Year



General Fund Percent Distribution by Section
2000-01 State Fiscal Year



History of Other Funds

SECTIONS 183 AND 184 DISTRIBUTION TO FUNDS SINCE 1982 (percentage)

Effective Date	General Fund	MTOAF
July 1, 1982	60.0	40.0
April 1, 1996	52.0	48.0
January 1, 1997	50.5	49.5
January 1, 1998	46.0	54.0
January 1, 2000	36.0	64.0
January 1, 2001	20.0	80.0

Special Revenue Funds (SRFs) are dedicated funds used to support activities that are outside the scope of the General Fund. For Article 9, there are two such revenue streams.

Section 205 of the Tax Law requires that portions of the taxes imposed under sections 183 and 184 to be deposited in the Metropolitan Mass Transportation Operating Assistance Account of the MTOAF. The table above reports the statutory allocation of tax receipts by fund.

As stated earlier, the MCTD business tax surcharge applies to Article 9. Taxpayers that do business within the MCTD (which includes the counties of New York, Bronx, Kings, Queens, Richmond, Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk and Westchester) are subject to a 17 percent surcharge on their liability attributable to the MCTD area.

2001-02 RECEIPTS

Corporations and utilities taxes for 2001-02 are expected to yield total All Funds receipts of $1,191 million. This is an increase of 18 percent compared with 2000-01.

Total All Funds receipts for 2001-02 include an estimated $22 million in audit collections. After adjusting for refunds, year-to-year cash collections are expected to increase by approximately $190 million.

The World Trade Center disaster is expected to have a modest negative impact on the utilities and telecommunications sectors. Uncertainties remain regarding the amount of damage to underground infrastructure, such as service lines for telephones, electricity, and steam near and around the disaster site. The loss of customers is expected to reduce receipts for transmission and distribution companies.

Receipts for 2001-02 have also been adjusted to reflect legislation enacted in 2001 which reinstated the section 189 Gas Import Tax, which was ruled unconstitutional by the New York State Court of Appeals in the Tennessee Gas Pipeline Company case. This resulted in preserving $114 million in both refunds and ongoing receipts.

The primary factors examined when estimating corporation and utilities tax collections include the consumption of electricity and natural gas, and the associated price of each commodity. Although wholesale prices for natural gas were at record levels from last November through April, some of New York's utilities were not subject to the fluctuation in market prices due to fixed price contracts. If the utility had a market price pass-through clause, there would be an automatic adjustment made for a rate increase or decrease. These automatic adjustments had an initial positive effect on receipts beginning in late November and early December of State fiscal year 2000-01 and the first quarter of State fiscal year 2001-02, as natural gas prices increased dramatically. Similarly, utilities with automatic adjustments reflected the decreasing price of natural gas beginning in the spring. Natural gas prices have dropped significantly from last year's levels and are expected to remain stable due to increased supply and less demand. Receipts will reflect this more normal level of natural gas prices in the following months.

The tables below report annual consumption and prices of electricity and natural gas. The information shown for the years 1991 to 2000 is based on published reports of the Public Service Commission. The quantities in the table reflect sales to ultimate consumers and includes sales for resale.

CALENDAR YEAR HISTORY OF ELECTRICITY AND NATURAL GAS SALES
1991 TO 2000
(quantity in millions)

	Electricity Sales (kilowatt hours)	Percent Change	Gas Sales (M cubic feet)	Percent Change
1991	134,176	1.2	430.2	3.9
1992	124,926	(6.9)	497.6	15.7
1993	136,236	9.0	506.0	1.7
1994	133,531	(2.0)	530.0	4.7
1995	134,609	0.8	622.9	17.5
1996	135,256	0.5	603.6	(3.1)
1997	135,605	0.3	638.2	5.7
1998	116,305	(14.2)	482.5	(24.4)
1999	115,059	(1.1)	531.4	10.1
2000	105,637	(8.2)	636.1	19.7

CALENDAR YEAR HISTORY OF ELECTRICITY AND NATURAL GAS PRICES
1991 TO 2000

	Electricity Price (kilowatt hours)	Percent Change	Gas Price (M cubic feet)	Percent Change
1991	10.98	4.6	6.45	(0.3)
1992	11.39	3.7	6.51	1.0
1993	12.00	5.4	7.14	9.7
1994	12.23	1.9	7.55	5.7
1995	10.95	(10.5)	7.21	(4.5)
1996	11.09	1.3	8.03	11.4
1997	11.08	(0.0)	7.22	(10.1)
1998	10.50	(5.2)	8.25	14.3
1999	10.26	(2.3)	7.73	(6.3)
2000	11.21	9.3	8.40	8.7

All of section 186-e receipts and three-quarters of section 184 receipts in recent years have come from telecommunications companies. New services and the explosion in data communications have increased call and message volume, while competition and deregulation have held down prices.

Legislation enacted in 1996 to lower section 184 taxes on rail and trucking companies is estimated to reduce collections by $12 million in 2001-02. The sections 184, 186-a and 186-e rate reductions enacted in 1997 are estimated to reduce collections in 2001-02 by $387.5 million. The Power for Jobs tax credit program, first enacted in 1997, accelerated in 1998, and expanded in 2000 and 2001 legislation, will reduce receipts by an estimated $100 million. Legislation enacted in 2000 is estimated to reduce collections in 2001-02 by $211 million.

2002-03 PROJECTIONS

Corporation and utilities taxes for 2002-03 are expected to yield total All Fund receipts of $1,198 million. This is an increase of 1 percent compared with 2001-02.

For 2002, the consumption of electricity is projected to grow 1.4 percent, while natural gas consumption is expected to increase by nearly 1.4 percent. At the same time, the price of electricity is projected to decline by less than 1 percent and the price of natural gas is estimated to decrease by nearly 9 percent. Factors such as the substitution of cheaper fuel types, the severity of the weather, and the availability of oil or natural gas all influence energy consumption and energy prices. Telecommunications companies' receipts are expected to grow approximately 5 percent.

Apart from underlying economic activity and related changes in the price and quantity of utility services consumed, collections will continue to be affected by scheduled tax rate reductions. The rail and trucking legislation enacted in 1996, pertaining to section 184, is estimated to reduce collections by $13 million in 2002-03. The rate reductions enacted in 1997 and 2000 are estimated to reduce collections in 2002-03 by almost $700 million. Collections of prior-year liabilities, after audit, are projected at $20 million in 2002-03.

OTHER FUNDS

As mentioned previously, a portion of Article 9 receipts are deposited into two special revenue funds. The section 183 and 184 collections deposited in the MTOAF will total an estimated $70 million for 2001-02 and $81 million for 2002-03.

The MTCD business tax surcharge will result in deposits of an estimated $134 million for 2001-02 and $122 million for 2002-03 into the MTOAF.

GENERAL FUND

General Fund collections for 2001-02 are estimated to be $987 million, an increase of $170 million over last year. These receipts include an estimated $22 million in audit collections.

For 2002-03, the General Fund collections are estimated at $995 million. This includes an estimated $22 million in audit receipts, offset by $30 million in refunds.

Risks

At this time, it is too soon to anticipate all of the economic changes that may result from the World Trade Center attacks. Any major effects of the attacks on the utility industry or long-term delays in the recovery effort could potentially have a larger impact on tax liability than we are currently anticipating.

The forecast assumes average temperature ranges during 2001 and 2002. Continued milder-than-average weather could reduce heating or cooling energy demand and lower consumption below the current forecast. Prices are sensitive to supply and demand conditions in the commodity markets, as well as to general inflation. Ongoing changes in the regulation of electric services and natural gas distribution and sale have the potential to interact with our tax structure in unpredictable ways.

The telecommunications forecast assumes the continuation of steady growth, especially within the information technology, wireless, and Internet markets. However, if market saturation begins to occur in any sector, demand could fall, resulting in a level of consumption below the current forecast. Furthermore, prices are sensitive to changes in supply and demand, disposable income, business market conditions, changes in technology, and general inflation.

CORPORATION AND UTILITIES TAX RECEIPTS BY SECTION
(millions of dollars)

Section of Law	Type of Companies	Collections[1] 2000-01 Actual	2001-02 Estimated	2002-03 Projected
180	Organizations and reorganizations	5.8	4.4	4.4
181	Foreign corporations and maintenance fees	27.8	26.2	26.2
183	Transportation and transmission companies	32.6	35.9	39.4
184	Additional tax on transportation and transmission companies	68.8	51.5	61.6
185	Agricultural cooperatives	0.2	0.2	0.2
186	Water, steam, gas, electric, light and power companies	(49.8)	0.0	0.0
186a & e	Public utilities/telecommunication	787.6	939.5	930.8
189	Natural gas importers	14.5	14.0	13.1
	Subtotal	887.5	1,067.7	1,075.7
		Special Revenue Funds		
	Less Other Funds			
	MTOAF[2]	70.1	70.0	81.0
	Net General Fund	817.4	987.0*	995.0

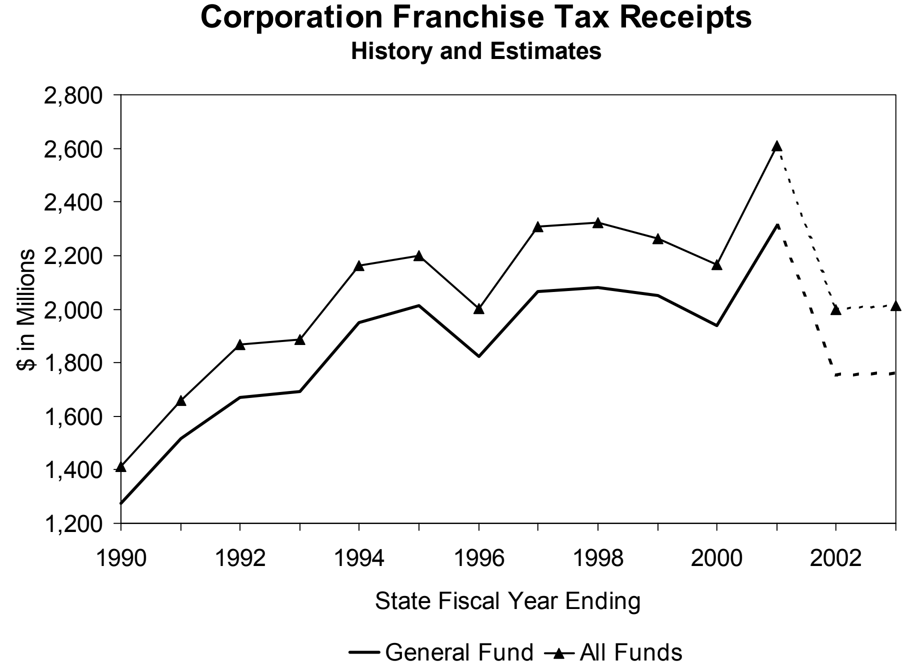
[1] Receipts from the regional business tax surcharge are excluded.
[2] Per statute, 54 percent of sections 183 and 184 receipts in 1998 and 1999, 64 percent in 2000, and 80 percent in 2001 and thereafter, are dedicated to the MTOAF.
* Reflects adjustments made for Tennessee Pipeline case and World Trade Center attacks.

CORPORATION AND UTILITIES TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Gross Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	Capital Projects Funds	Gross Debt Service	All Funds Net Collections
	Actual								
1993-94	1,604	12	1,592	233	1	232	0	0	1,824
1994-95	1,574	69	1,505	203	3	200	0	0	1,705
1995-96	1,581	14	1,567	190	1	189	0	0	1,756
1996-97	1,616	39	1,577	214	2	212	0	0	1,789
1997-98	1,517	13	1,504	243	2	241	0	0	1,745
1998-99	1,509	20	1,489	242	2	240	0	0	1,729
1999-2000	1,450	32	1,418	276	2	274	0	0	1,692
2000-01	847	30	817	193	1	192	0	0	1,009
	Estimated								
2001-02	1,017	30	987	205	1	204	0	0	1,191
2002-03	1,025	30	995	205	2	203	0	0	1,198

[1] Receipts from the MTA business tax surcharge and funds dedicated to MTOAF sections 183 and 184.

CORPORATION FRANCHISE TAX



DESCRIPTION

The corporation franchise tax is levied by Article 9-A of the Tax Law on domestic and foreign corporations for the privilege of exercising their corporate franchise or of doing business, employing capital, owning or leasing property, or maintaining an office in New York.

Corporate franchise tax receipts have historically been characterized by significant volatility. These fluctuations can be attributed to several factors, such as variations in the rate of corporate profit growth; changes in the profit performance of important New York industries, such as financial service companies; and tax law and administrative changes, such as rate reductions, allowing railroad and trucking companies to elect to be taxed under Article 9-A, and the deregulation and change in the tax treatment of electric utility companies.

Tax Rate

The Article 9-A corporation franchise tax requires a taxpayer to compute tax liability under four alternative bases and pay under the base that results in the largest tax. The four bases apply to:

1. An allocated entire net income base, which begins with Federal taxable income before net operating loss deductions and special deductions. A rate of 7.5 percent is applied to this base after the exclusion, deduction, or addition of certain items and the base is allocated to New York. Tax credits will further reduce tax otherwise due.
2. An alternative minimum tax base, which equals entire net income adjusted to reflect certain Federal tax preference items and adjustments and State-specific net operating loss (NOL) modifications, at a current rate of 2.5 percent.
3. A capital base at a rate of 0.178 percent. Allocated business and investment capital form the capital base with a maximum annual tax of $350,000.
4. A fixed dollar minimum, which ranges from $100 to $1,500, depending on the size of the corporation's gross payroll, including general executive officers, during the applicable tax period.

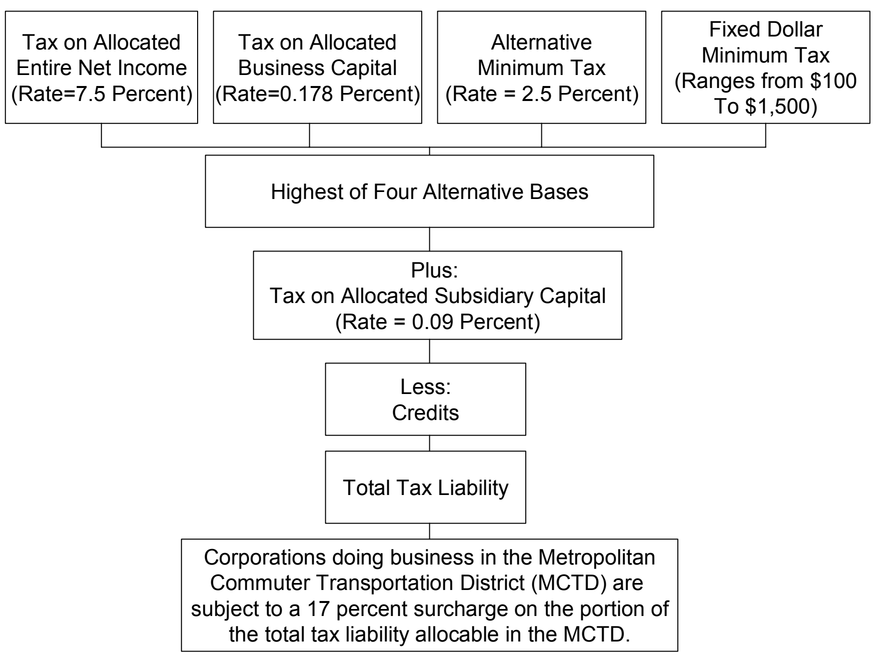
For tax years ending after June 1990 and before July 1994, a temporary State business surcharge of 15 percent of tax due after the application of any credits was in effect. The surcharge fell to 12.5 percent during 1994, to 7.5 percent during 1995, to 2.5 percent during 1996, and was eliminated during 1997. Since 1990, S corporations have also been required to pay tax based on a differential rate, computed as the difference between the Article 9-A rate and the Article 22 rate.

Article 13 of the Tax Law levies a tax of 9 percent on the unrelated business income of otherwise tax-exempt organizations operating in the State.

Additionally, legislation first enacted in December 1982, and subsequently extended, imposes a temporary surcharge on business taxes to support mass transportation in the Metropolitan Commuter Transportation District (MCTD). The MCTD comprises New York City, Long Island, and the counties of Dutchess, Orange, Putnam, Rockland and Westchester. The surcharge rate is 17 percent of tax otherwise due, allocable to the district, after deduction of allowable credits.

The following flow chart shows how alternative tax bases are used to compute Article 9-A tax liability.

Article 9-A Flowchart



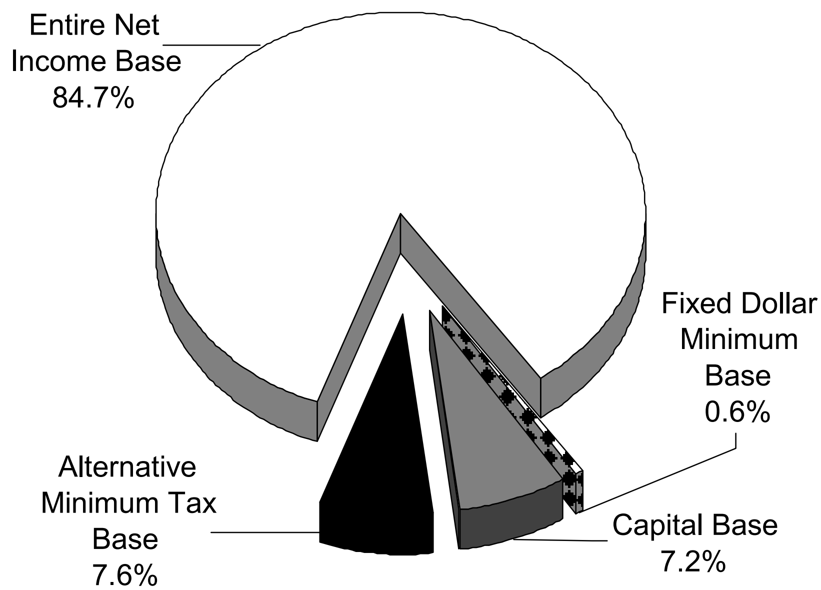
TAX BASE

The corporation franchise tax is made up of business entities classified as either C corporations or S corporations. The New York State Department of Taxation and Finance's Office of Tax Policy Analysis (OTPA) compiles corporate tax return data relating to the total number of C and S corporations and tax liability for these entities. The most recent data, from the *1996 New York State Corporation Tax Statistical Report*, indicates that 259,285 taxpayers filed as C corporations, while 254,236 taxpayers filed as S corporations. The number of C corporations and S corporations did not change significantly from the prior year.

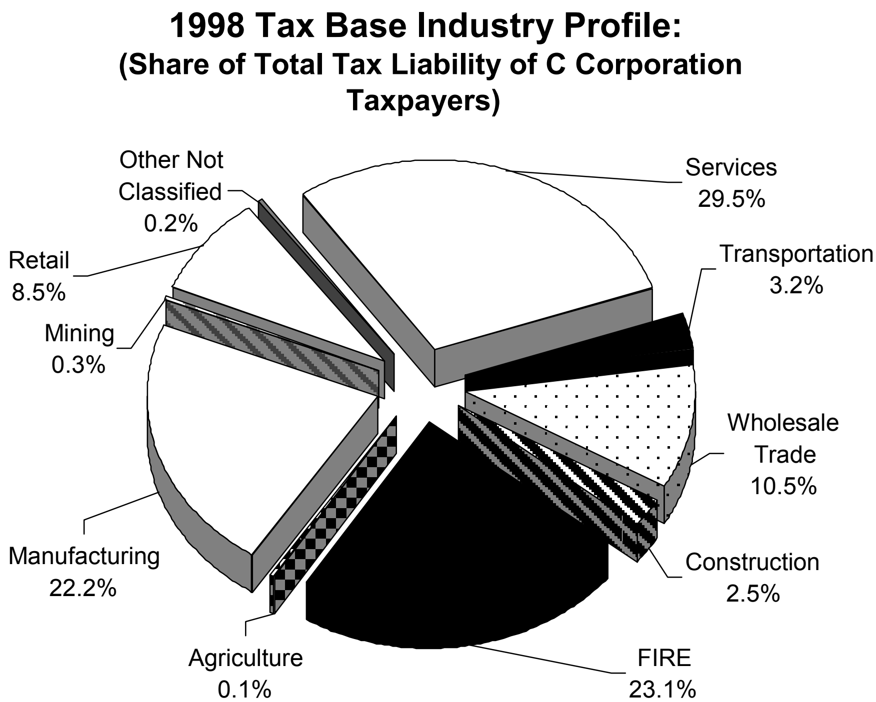
The OTPA's Corporate Franchise Tax Study File contains the most recent data available on Article 9-A liability. It includes all corporations filing under Article 9-A, except fixed dollar minimum tax filers and S corporations. The most current liability information is for the 1998 tax year.

Several characteristics of C corporations are noteworthy. In 1998, nearly 85 percent of liability was paid under the entire net income base. The alternative minimum tax is the second largest base, at 7.6 percent of liability. (See chart below.)

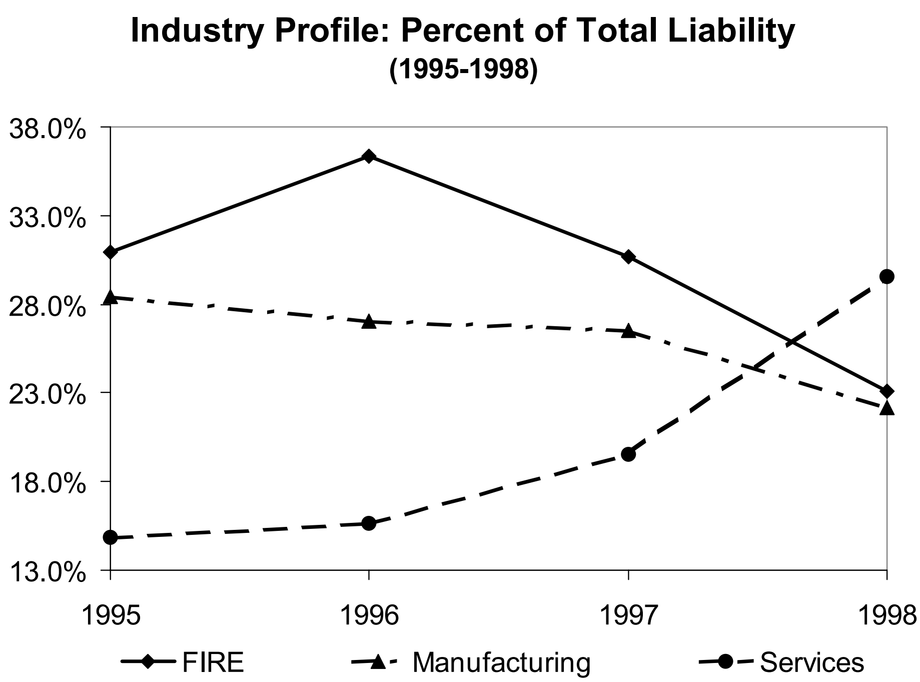
1998 Distribution of Tax Liability by Basis of Tax



The next chart shows the distribution of tax liability by major industry sector. Liability paid by the finance, insurance, and real estate sector (FIRE) made up approximately 23 percent of total tax liability paid by C corporation taxpayers in 1998, with the manufacturing sector accounting for 22 percent of liability. The service industry has grown quite significantly and, in 1998, represented almost 30 percent of total liability.



The following chart illustrates the fluctuation in the percentage of liability paid by the three industries that typically make up the largest share of liability: FIRE, manufacturing and services. The FIRE industry is historically one of the largest sources of tax receipts for Article 9-A. Liability for this industry, however, tends to be very volatile over time, rising, for example, to 36 percent in 1996 and then dropping to 23 percent in 1998. In comparison, the service industry has exhibited uninterrupted growth in recent years. Finally, the manufacturing industry's share of total liability has declined steadily over the same period.



SIGNIFICANT LEGISLATION

The corporate franchise tax structure includes various exclusions, exemptions, tax credits, and other statutory devices designed to adjust State tax liability. The distribution of these benefits varies widely among firms. The primary objective of these provisions is to provide economic incentives to stimulate the New York economy and to eliminate tax inequities across firms. The following table summarizes the major corporation franchise tax legislation enacted since 1994.

SIGNIFICANT CORPORATION FRANCHISE TAX LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1994		
Exclusion of Income for Foreign Airlines	Allowed foreign airlines to exclude the following items from entire net income: all income from international operations of aircraft effectively connected to the United States; foreign passive income, and income earned overseas from overseas operations of aircraft.	Retroactive to January 1, 1989
Temporary Business Tax Surcharge	Eliminated the temporary 15 percent surcharge over a four year period.	January 1, 1994
Special Additional Mortgage Recording Tax (SAMRT)	Provided for refundability of the unused portion of the SAMRT credit to both regular and S corporation nonbank mortgage lenders.	January 1, 1994
Depreciation	Changed the Modified Accelerated Cost Recovery System (MACRS) depreciation rule for non-New York property to conform to provisions of the Federal Tax Reform Act of 1986.	January 1, 1994
Limited Liability Companies (LLC) and Limited Liability Partnerships (LLP)	Provided New York State authority for formation of LLCs and LLPs, which are business organizations that provide many of the tax benefits associated with partnerships and the liability protection afforded to corporations.	October 24, 1994
Investment Tax Credit/ Employment Incentive Credit (EIC)	Extended carryover period for this credit from 7 to 10 years.	January 1, 1994
Rate Reduction – Alternative Minimum Tax (AMT)	Reduced rate from 5.0 percent to 3.5 percent.	January 1, 1995
Legislation Enacted in 1996		
Rehabilitation Credit for Historic Barns	Allowed taxpayers to claim corporate franchise tax credit for the rehabilitation of historic barns in New York State.	January 1, 1997
Agricultural Property Tax Credit	Allowed eligible farmers to claim a real property tax credit against the corporate franchise tax.	January 1, 1997
Legislation Enacted in 1997		
Investment Tax Credit Carryforward	Allowed any unused pre-1987 investment tax credit to remain available until 2002. Post-1986 investment tax credit extended to 15-year carry forward.	January 1, 1998
Alternative Fuel Vehicle Credit	Provided corporations and individuals with a tax credit for a portion of the cost of purchasing or converting a vehicle to operate on alternative fuels.	January 1, 1998
Credit for Employing Individuals with Disabilities	Allowed employers who employ individuals with disabilities to claim a credit for a portion of wages paid to such individuals.	January 1, 1998
Legislation Enacted in 1998		
Rate Reduction – AMT	Reduced rate from 3.5 percent to 3.0 percent phased in over 2 years.	June 30, 1998
Investment Tax Credit	Brokers/dealers in securities may claim a credit for equipment or buildings used in broker/dealer activity and in activities connected with broker/dealer operations.	October 1, 1998
Emerging Technology Companies Credit	Provided, under the New York State Emerging Industry Jobs Act, corporate franchise tax credits for qualified emerging technology companies that create new jobs, or for certain corporate taxpayers that invest in emerging technology companies located in New York State.	January 1, 1999
Rate Reduction – ENI	Reduced the tax rate from 9 percent to 7.5 percent over a three-year period beginning after 6/30/99.	June 30, 1999

Subject	Description	Effective Date
Legislation Enacted in 1999		
Rate Reduction – AMT	Reduced rate from 3.0 percent to 2.5 percent.	June 30, 2000
Mergers and Acquisitions	Repealed the provisions relating to mergers, acquisitions and consolidations.	January 1, 2000
Alternative Fuel Vehicle Credit	Expanded the alternative fuel credits to electric and clean fuel vehicles sold or leased to governmental entities, provided that the companies manufacture the vehicles in New York and create at least 25 full-time jobs.	January 1, 2000
Airline Apportionment	Reduced the percentage of income apportioned to New York by 40 percent by changing the allocation formula to multiply the New York Factor in the numerator of each component in the formula.	January 1, 2001
EDZ/ZEA Wage Tax Credit	Doubled the existing Economic Development Zone (EDZ) and Zone Equivalent Area (ZEA) wage tax credits.	January 1, 2001
Defibrillator Credit	Granted a new credit of $500 per automated external defibrillator.	January 1, 2001
Legislation Enacted in 2000		
Energy Reform and Reduction	Energy companies, previously taxed under section 186 of Article 9, will now be subject to the Article 9-A corporate franchise tax.	January 1, 2000
Industrial or Manufacturing Business Credit (IMB)	A refundable credit provided for any of the gross receipts taxes and the section 189 gas import tax on manufacturing uses of energy.	January 1, 2000
Securities and Commodities Brokers or Dealers Customer Sourcing	Allows securities broker/dealers to allocate receipts, which constitute commissions, margin interest or account maintenance fees, as a service performed at the customer's mailing address.	January 1, 2001
Empire Zones (EZ)	Economic Development Zones (EDZ) are transformed to Empire Zones, effectively providing for virtual "tax free" zones for certain businesses. The enhanced benefits include a tax credit for real property taxes, a tax reduction credit, and sales and use tax exemption. The tax reduction credit may be applied against the fixed dollar minimum tax, which may reduce the taxpayer's liability to zero.	January 1, 2001
Rate Reduction – S Corporations	Reduced the differential tax rate imposed on S corporations by 45 percent.	June 20, 2003
Rate Reduction – Small Businesses	Small businesses with entire net income of $200,000 or less pay a reduced tax rate of 6.85 percent.	June 30, 2003

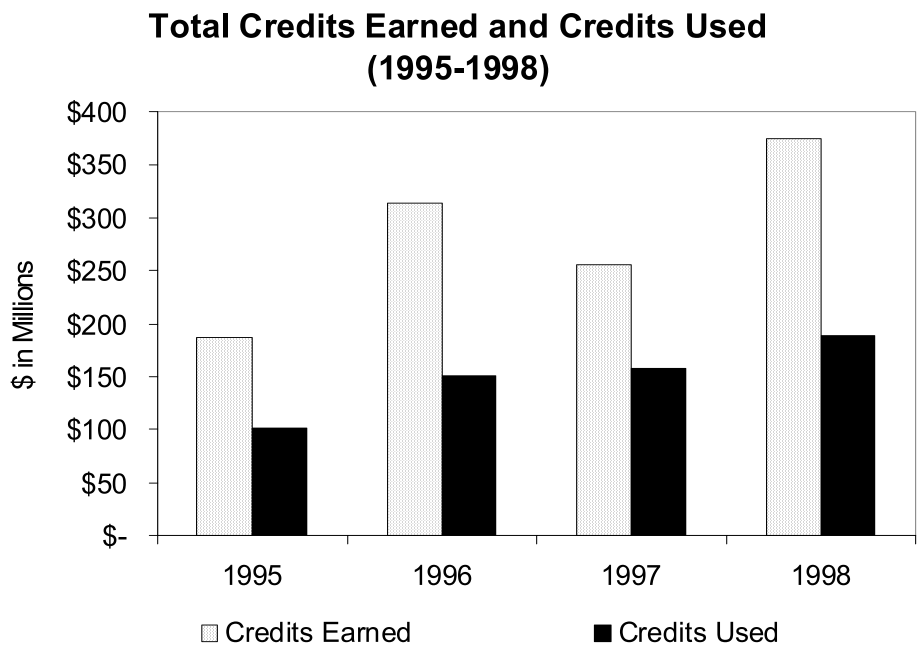
Proposed Legislation

This year the Governor has proposed two targeted tax incentives designed to spur economic development throughout the State.

- **Tax Incentives for Brownfield Redevelopment:** As part of the proposed Superfund program, these tax incentives will encourage the remediation and redevelopment of brownfields to productive use. Brownfields are abandoned or underutilized properties found in many areas that require environmental remediation. The incentives include tax credits for the costs associated with the site remediation of brownfields and the purchase of property used on a brownfield site. In addition, the program also includes property tax benefits for brownfields of at least ten acres and no more than 100 acres in upstate cities, as well as an enhanced property tax credit for upstate mega-brownfields — those of more than 100 acres. The credits apply to tax years beginning on or after January 1, 2003, for site costs incurred and property placed in service on or after January 1, 2002. These credits are available to regular corporations, personal income taxpayers, utilities, banks and insurance companies.
- **Enhancements to the New York State Low-Income Housing Tax Credit Program:** Beginning in 2002, an additional $2 million will be available to enhance the provisions of the Low-Income Housing Tax Credit Program, included in the 2000-01 Enacted Budget. This will allow even more participants to become involved in this

important program, which is designed to encourage investments in low-income housing. Eligible taxpayers include regular corporations, personal income taxpayers, banks and insurance companies.

Credits



The graph shows major credits earned and used by Article 9-A taxpayers, and illustrates that the amount of credits earned greatly exceeds the amount of credits used. These credits include the investment tax credit (ITC), Empire Zone credits, the alternative minimum tax (AMT) credit, the farmer's school credit, and a special additional mortgage recording credit. Credits earned is the amount of credit earned by a taxpayer in the current tax year. This is prior to any credit recapture, and does not include credits from any prior years. From 1995 to 1998, the number of credits earned increased by nearly 98 percent. This trend is expected to continue as more targeted tax credits have been enacted and are being utilized by businesses in the State. For example, the ITC for the financial services industry, which was enacted in 1998, accounted for an additional $108 million in credits earned during 1998. The total ITC accounts for the majority of the tax credit base. In 1998, the ITC accounted for about 86 percent of all tax credits earned and about 70 percent of all tax credits used. It is anticipated that the amount of ITC used will increase due to tax law changes reducing the AMT rate to 3.0 percent in 1998 and to 2.5 percent in 2000. This is because the AMT effectively limits the amount of credits a taxpayer can use to reduce tax liability.

Historically, Tax Law provisions prevented taxpayers from using tax credits to reduce final tax liability below the fixed dollar minimum tax, or the AMT. This resulted in taxpayers carrying forward a significant amount of tax credits into subsequent tax years. In 1998, nearly $1.7 billion worth of tax credits were carried forward. Legislation enacted in 2000, however, made it possible to apply the employment incentive credit and the newly created tax reduction credit against the AMT if taxpayers are within an Empire Zone. Additionally, the tax reduction credit for qualified Empire Zone enterprises may be applied against the fixed dollar minimum tax, which may reduce the taxpayer's corporate franchise tax liability to zero. It is expected that these tax relief measures will result in fewer tax credits being carried forward, because taxpayers will be able to use more credits against liability.

2001-02 RECEIPTS

Based on collections to date, total net collections for the entire State fiscal year are estimated to reach $1,998 million, a $632 million dollar decrease from the 2000-01 level. The decrease is the result of several factors. Perhaps the most important is the impact of the terrorist attacks on New York City on September 11. These attacks have had a significant short-term impact on the liability of taxpayers under this article. Several taxpayers had substantial office space located in and around the World Trade Center (WTC) that was destroyed or damaged. These taxpayers are expected to have significant losses in both property and business activity which should serve to lower their tax liability.

Also, payments on 2001 liability had already been broadly depressed prior to September 11. Payments by fiscal filers on 2001 liability, excluding the impact of the WTC, were down approximately 43 percent through September. Payments by calendar filers were down roughly 9 percent, before the impact of the WTC tragedy. Much of the decrease in 2001 liability payments can be attributed to an overall decline in business profitability.

Profits from financial services firms, which traditionally make up a substantial portion of Article 9-A receipts, suffered from declines in both stock values and trading activity.

Further, receipts were reduced due to the impact of roughly $290 million in already enacted tax reductions.

Finally, corporate tax receipts have been adjusted to reflect an expected decline in audit receipts during the second half of the current State fiscal year. Audit collections are expected to be lower due to the disruption of the audit process caused by the World Trade Center disaster.

The Executive Budget proposes two new targeted tax relief measures. These include enhancements to the Low-Income Housing Tax Credit Program and tax credits for brownfield redevelopment. The proposed increase in credit allocation for the Low-Income Housing Tax Credit Program will not affect receipts in 2001-02 but will reduce 2002-03 receipts by $2 million. The brownfield tax credits will not have an impact on receipts until 2003-04.

2002-03 PROJECTIONS

Corporate franchise tax receipts are expected to increase by 1 percent from estimated 2001-02 levels to $2,012 million. The projection is driven by several factors. The decline in corporate profitability, at the national and State level, is expected to be largely limited to the 2001-02 State fiscal year. In addition, the direct impact of the events of September 11 should have a less significant impact on receipts than during the 2001-02 State fiscal year. In contrast, the impact of an additional $116.8 million in already enacted tax reductions will reduce receipts.

The corporate franchise tax projection is based, in part, on the underlying relationship between liability and overall corporate profitability. Corporate profits, which have declined significantly over the course of the 2001-02 State fiscal year, are expected to improve during 2002-03. It is expected that corporate profitability will see improvement and growth over the 2002-03 State fiscal year.

Executive Budget proposals will reduce receipts. The Low-Income Housing Tax Credit will reduce receipts by $2 million in 2002-03. The brownfield tax credits will not affect receipts until 2003-04.

OTHER FUNDS

Under current law, a surcharge is imposed at a rate of 17 percent of the portion of the statewide tax liability of the business that is allocated to the MCTD and is the principal revenue source of the Mass Transportation Operating Assistance Fund (MTOA). In addition, the MTOA fund was held harmless from the ENI rate reduction, which began in 1999. As a result MTOA collections will not be diminished by the corresponding reduction in General Fund receipts. Based on collections to date, the Article 9-A MTOA contribution for 2001-02 is projected to reach approximately $243 million, a 17.6 percent decrease from 2000-01. As with General Fund receipts, surcharge collections are affected by the volatility of the financial services sector and general growth in business activity for the current tax year. Consistent with overall estimates, and the fact that the MTOA is protected from the corporate franchise tax reduction, 2002-03 State fiscal year collections are expected to increase by roughly 3.3 percent.

GENERAL FUND

Based on collections to date, General Fund net collections for 2001-02 are projected to decrease by $580 million, a 24.8 percent decrease from State fiscal year 2000-2001, primarily driven by large decreases on 2001 liability, reductions in audit receipts, and the continued impact of previously enacted tax reductions.

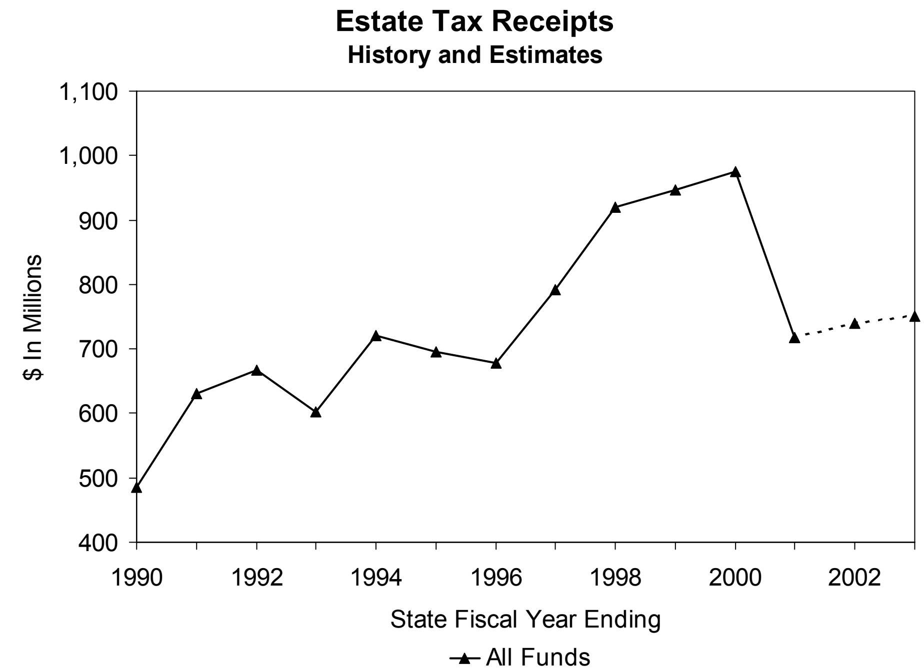
General Fund receipts for State fiscal year 2002-03 are expected to increase slightly over 2001-02 levels. This slight increase is the product of increasing corporate profitability, offset by the impact of previously enacted tax cuts, as well as the continued disruption of the audit process.

CORPORATATION FRANCHISE TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual								
1993-94	2,217	268	1,948	232	18	214	0	0	2,162
1994-95	2,289	278	2,012	207	20	187	0	0	2,199
1995-96	2,217	396	1,821	217	36	182	0	0	2,002
1996-97	2,414	348	2,067	274	36	239	0	0	2,306
1997-98	2,381	300	2,081	289	27	262	0	0	2,343
1998-99	2,479	429	2,050	243	30	213	0	0	2,262
1999-2000	2,422	483	1,939	272	43	229	0	0	2,168
2000-01	2,817	482	2,335	316	21	295	0	0	2,630
	Estimated								
2001-02	2,115	360	1,755	274	31	243	0	0	1,998
2002-03 (proposed law)	2,122	361	1,761	283	32	251	0	0	2,012

[1] MCTD 17 percent surcharge deposited in Mass Transportation Operating Assistance Fund.

ESTATE TAXES



DESCRIPTION

New York imposes a tax on the estates of deceased State residents, and on that part of a nonresident's estate made up of real and tangible personal property located within New York State.

Current Law

Legislation enacted in 1997 significantly reduced State estate tax collections and changed the way the New York State estate tax was imposed. The State's estate tax rate structure, credits and exemptions were eliminated in two phases, and State liability was set to equal to the maximum Federal credit for state death taxes.

The first phase of the estate tax legislation, for those dying on or after October 1, 1998, and before February 1, 2000, increased the unified credit (the credit that can be used to reduce liability of either the estate or gift tax under the unified imposition of these taxes) from $2,950 to $10,000, thereby increasing the value of transfers exempt from taxation to $300,000. In addition, the requirement for 90 percent of the estate tax to be paid within six months of death to avoid underpayment interest was changed to seven months.

The second phase for decedents dying on or after February 1, 2000, eliminated New York's estate tax rate schedule and provided that New York State's estate tax would be equal to the Federal credit for state death taxes paid. New York also automatically conformed State law to the unified credit provisions specified in Federal law. In February 2000, Federal law set the unified credit at $675,000 and contained a schedule that increased the credit to $1 million by 2006. (See table below.) In addition, consistent with Federal law, 100 percent of tax liability is due within nine months of the decedent's death.

New Federal Legislation

Congress recently enacted the Economic Growth and Tax Relief Reconciliation Act of 2001. The new Federal law converted the unified credit to an exemption and accelerated the phase-in schedule (see table below) to effectively exempt the first $1 million of the value of an estate in 2002. Because New York conforms to the unified credit portion of Federal law, there is an acceleration of the $1 million exemption in New York law, from 2006 to 2002.

State unified credit/exemption under the prior and current Federal law:

State Unified Credit/Exemption Amounts

Year	Prior to 2001 Federal Tax Reduction Program	After 2001 Federal Tax Reduction Program
2000, 2001	$ 675,000	$ 675,000
2002, 2003	700,000	1,000,000
2004	850,000	1,000,000*
2005	950,000	1,000,000*
2006 and thereafter	1,000,000	1,000,000*

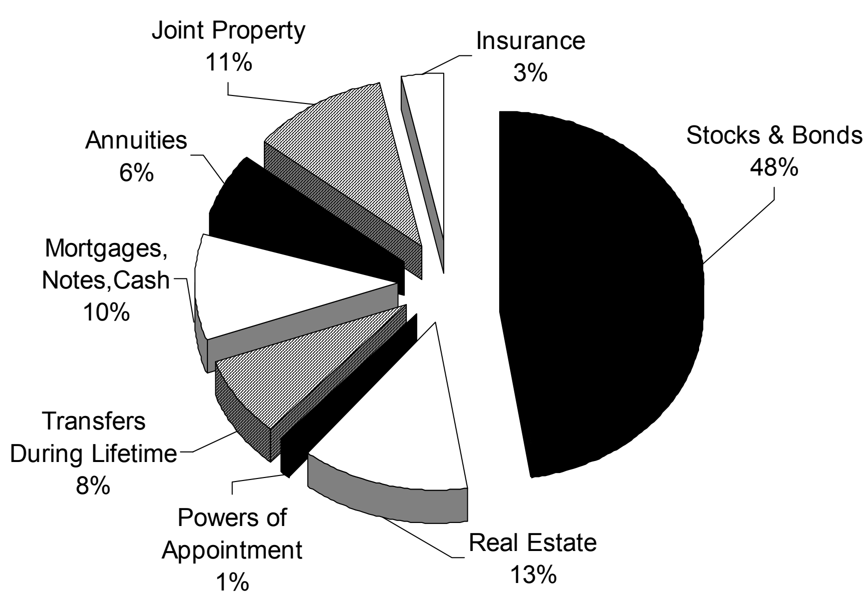
* New York State law caps the Unified Exemption at $1 million. The Federal law increases the amount to $1.5 million in 2004 and 2005, $2 million in 2006, 2007, and 2008, and $3.5 million in 2009.

In addition, the new Federal law phases out the Federal credit for state death taxes over four years, by 25 percent per year. The provisions of New York's law setting the estate tax liability equal to the Federal credit for state death taxes conforms to the Federal law as it existed on July 22, 1998. As a result, New York estate tax liability will be unaffected by the phase-out of the Federal credit for state death taxes.

Factors Affecting Yield

The recent yield of this tax has been heavily influenced by three factors: tax law changes, variations in the relatively small number of large estates, and the value of the equity market, given the large component of corporate stock in large taxable estates. Recent tax law changes have reduced estate tax collections from the smallest estates. As a result, volatility in receipts is expected to increase due to the more random nature of collections from large estates.

Components of Taxable Gross Estates
State Fiscal Year 1999-2000



SIGNIFICANT LEGISLATION

The major statutory changes since 1994 are reported below.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Unified Credit for Estate and Gift Taxes	Increased credit from $2,750 to $2,950, thereby eliminating the tax on taxable gifts/estates of $115,000 or below, up from $108,600.	June 9, 1994
Legislation Enacted in 1995		
Deduction	Authorized a principal residence deduction of $250,000 (maximum).	June 7, 1995
Legislation Enacted in 1997		
Unified Credit for Estate and Gift Taxes	Conforms New York State law to Federal law as of July 22, 1998, except for the unified credit provisions.	July 22, 1998
	Increased credit from $2,950 to $10,000, thereby eliminating the tax on taxable estates and gifts of $300,000 or below.	October 1, 1998
	Increased credit to eliminate tax on taxable estates of $675,000 or below.	February 1, 2000
	Increased credit to eliminate tax on taxable estates of $700,000 or below.	January 1, 2002
	Increased credit to eliminate tax on taxable estates of $850,000 or below.	January 1, 2004
	Increased credit to eliminate tax on taxable estates of $950,000 or below.	January 1, 2005
	Increased credit to eliminate tax on taxable estates of $1,000,000 or below.	January 1, 2006
Estate Tax Rate	Set the New York estate tax rates equal to the Federal credit for State estate taxes paid.	February 1, 2000
Gift Tax	Repealed.	January 1, 2000
Tax Liability Due Date	Increased from six to seven months.	October 1, 1998
	Increased from seven to nine months (same as Federal).	February 1, 2000
Legislation Enacted in 1998		
Closely-Held Business	Interest on deferred payments of estate tax where estate consists largely of a closely-held business reduced from 4 percent to 2 percent.	January 1, 1998
Legislation Enacted in 1999		
Family-Owned Business Deduction	Family-owned business exclusion repealed and replaced with family-owned business deduction, conforming to Federal changes.	December 31, 1997
Penalty and Interest	Penalty and interest waived on estate tax associated with a cause of action that was pending on the date of death, or which was associated with the decedent's death. The waiver is applicable from the date the return disclosing the cause of action if filed.	July 13, 1999

2001-02 RECEIPTS

For the 2001-02 fiscal year, estate tax receipts are estimated at $740.0 million, after subtracting estimated refunds of $40 million. This is composed of $253.4 million from extra large estates with payments of $4 million or more, $280.0 million from large estates with payments between $500,000 and $4 million, and $246.6 million from small estates with payments of less than $500,000. These receipts include Case and Resource Tracking System (CARTS) collections estimated at $40 million. This represents an increase of 3.2 percent from the $717.1 million collected in 2000-01. It is estimated that the first full year effects of the tax reductions enacted in 1997 have reduced total receipts by $392.5 million, or 36.5 percent from the 1993-94 base.

In developing projections for estate tax receipts, the value of household net worth is used to forecast receipts from estates that make payments of less than $4 million. A distributional analysis is utilized to estimate receipts and the number of estates where payments exceed $4 million.

Year-to-date net estate tax collections of $552.6 million for 2001-02 are 3.9 percent lower than collections during the comparable period in 2000-01. Receipts are expected to decline over the rest of the fiscal year, reflecting estimated declines in the value of household net worth of 7.7 percent in 2001-02.

Year-to-date collections from extra large estates are $169.3 million, a 27.6 percent increase over the comparable period in 2000-01. Collections from large estates decreased by $31.2 million, or 17.8 percent, to $143.6 million. Similarly, small estate payments also experienced a decrease of $28.3 million, down 10.6 percent, to $239.7 million from the similar period of 2000-01. These declines largely reflect both the recent weakness in the equity markets and the impact of previously enacted tax reductions.

CARTS collections through seven months of 2001-02 were $27.6 million, an increase of about 109 percent from the same period of 2000-01, reflecting a large audit payment in the first half of the fiscal year. Year-to-date refunds for 2001-02 were $24.2 million, 52 percent below the same period of 2000-01.

2002-03 PROJECTIONS

The combination of increasing the Federal unified credit from $675,000 to $1 million, and moving to a pick-up tax will partially offset an estimated 4.8 percent increase in the base of the tax. Including estimated CARTS collections of $25 million and refunds of $40 million, net estate tax receipts are projected to be $751.2 million in 2002-03.

ESTATE TAX RECEIPTS BY SIZE OF ESTATE
(millions of dollars)

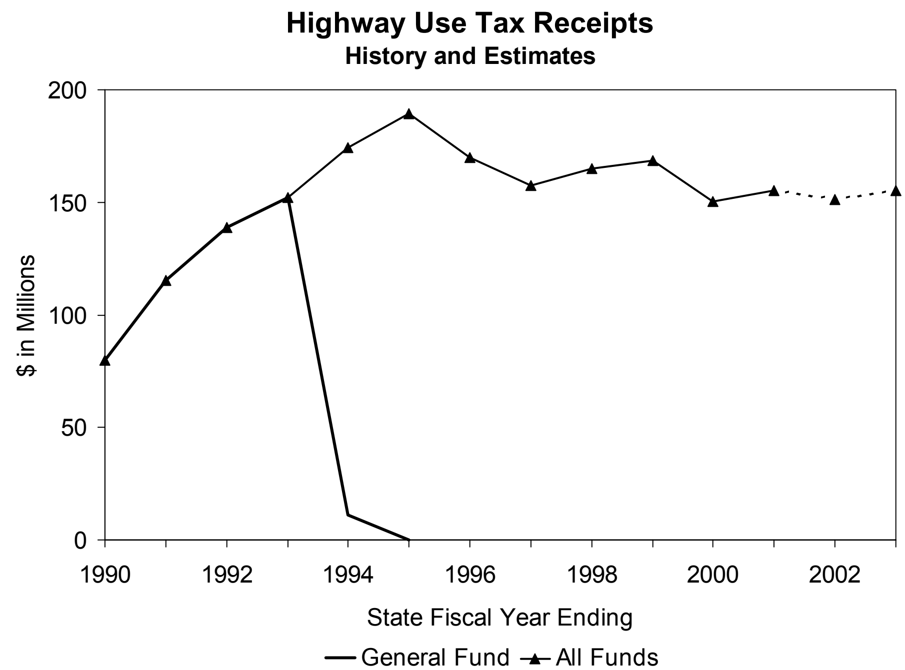
	Extra Large Estates[1]		Large Estates[2]		All Large Estates		Small Estates[3]	Grand Total
	Number	Taxes	Number	Taxes	Number	Taxes	Taxes	Taxes
1991-92	11	158.7	111	149.9	122	308.6	398.5	707.1
1992-93	9	78.8	125	135.9	134	214.7	410.7	625.4
1993-94	15	163.3	127	163.5	142	326.8	434.1	760.9
1994-95	13	141.4	140	152.8	153	294.2	460.6	754.8
1995-96	9	105.1	132	158.2	141	263.3	459.8	723.1
1996-97	24	243.0	123	151.3	147	394.3	447.7	842.0
1997-98	23	317.4	160	195.6	183	513.0	454.8	967.8
1998-99	19	221.8	215	259.5	234	481.3	511.7	993.0
1999-2000	14	176.8	188	229.6	204	514.1	460.9	975.0
2000-01	20	210.5	199	277.0	215	541.7	175.4	717.1
Estimated								
2001-02	18	253.4	173	280.0	190	533.4	206.6	740.0
2002-03	18	220.6	180	289.0	197	509.6	241.6	751.2

[1] Liability of at least $4.0 million.
[2] Liability of at least $0.5 million but less than $4.0 million.
[3] Liability less than $0.5 million. (All refunds are subtracted from small estates.)

ESTATE TAX RECEIPTS
(thousands of dollars)

	General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
				Actual			
1993-94	760,901	40,660	720,241	0	0	0	720,241
1994-95	754,844	59,250	695,594	0	0	0	695,594
1995-96	723,097	44,399	678,698	0	0	0	678,698
1996-97	842,015	50,457	791,558	0	0	0	791,558
1997-98	967,785	48,424	919,361	0	0	0	919,361
1998-99	993,086	46,641	946,445	0	0	0	946,445
1999-2000	1,028,698	53,526	975,172	0	0	0	975,172
2000-01	777,100	60,000	717,100	0	0	0	717,100
				Estimated			
2001-02	780,000	40,000	740,000	0	0	0	740,000
2002-03	791,200	40,000	751,200	0	0	0	751,200

HIGHWAY USE TAX



DESCRIPTION

Highway use tax revenues are derived from three sources: the truck mileage tax, highway use permit fees, and the fuel use tax.

Truck Mileage Tax

The truck mileage tax is levied on commercial vehicles having a loaded gross weight of more than 18,000 pounds, or an unloaded weight in excess of 8,000 pounds for trucks and 4,000 pounds for tractors. The tax is imposed at rates graduated according to the gross vehicle weight. The tax is calculated by multiplying the number of "laden" or "unladen" miles traveled on public highways of the State by the appropriate tax rate.

In addition, a supplemental tax equal to the base truck mileage tax was imposed prior to January 1, 1999. Effective January 1, 1999, the supplemental tax was reduced by 50 percent, and effective April 1, 2001, the supplemental tax was reduced by an additional 20 percent of the remaining tax.

BASE TRUCK MILEAGE TAX RATES

Gross Weight Method

Laden Miles Gross Weight of Vehicle	Mills Per Mile
18,001 to 20,000	6.0
20,001 to 22,000	7.0
(increased gradually to)	
74,001 to 76,000	35.0
76,001 and over	add 2 mills per ton and fraction thereof
Unladen Miles Unloaded Weight of Truck	
18,001 to 20,000	6.0
20,001 to 22,000	7.0
(increased gradually to)	
28,001 to 30,000	10.0
30,001 and over	add 5/10 of a mill per ton and fraction thereof
Unloaded Weight of Tractor	
7,001 to 8,500	6.0
8,501 to 10,000	7.0
(increased gradually to)	
16,001 to 18,000	10.0
18,001 and over	add 5/10 of a mill per ton and fraction thereof

Unloaded Weight Method

Unloaded Weight of Truck	Mills Per Mile
8,001 to 9,000	4.0
9,001 to 10,000	5.0
(increased gradually to)	
22,501 to 25,000	22.0
25,001 and over	27.0
Unloaded Weight of Tractor	
4,001 to 5,500	6.0
5,501 to 7,000	10.0
(increased gradually to)	
10,001 to 12,000	25.0
12,001 and over	33.0

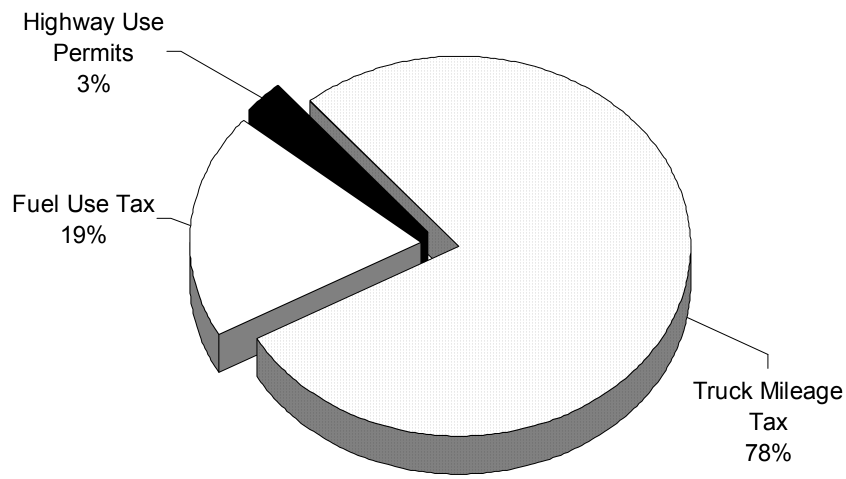
Highway Use Permits

Highway use permits are used to denote those vehicles subject to the highway use tax. The permits are issued triennially at a cost of $15 for an initial permit and $4 for a permit renewal. Additionally, special permits are issued for the transportation of motor vehicles, for automotive fuel carriers, and for trips into New York State not to exceed 72 hours.

Fuel Use Tax

The fuel use tax is a complement to the motor fuel tax and the sales tax, and is levied on commercial vehicles: (1) having two axles and a gross vehicle weight of more than 26,000 pounds; (2) with three or more axles, regardless of weight; or (3) used in combination when the gross vehicle weight exceeds 26,000 pounds. In contrast to the motor fuel tax, which is imposed upon the amount of fuel purchased within the State, the fuel use tax is imposed on fuel purchased outside but used within New York. This tax is levied on the basis of the number of miles traveled on the public highways of the State. The aggregate fuel use tax rate is the sum of the appropriate motor fuel tax rate and the sales tax rate. The statewide rate for the sales tax component is 7 percent of the average price of fuel — a cents-per-gallon equivalent is set quarterly. A credit or refund is allowed for motor fuel tax or sales tax paid on fuels purchased but not used within the State.

Components of Highway Use Tax Receipts
Estimated State Fiscal Year 2001-02



SIGNIFICANT LEGISLATION

A significant number of statutory changes have been made to the highway use tax since its inception. The following table summarizes the major highway use tax legislation enacted since 1994.

SIGNIFICANT HIGHWAY USE TAX LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1994		
Thruway Mileage	Reduced the truck mileage tax rates imposed on New York State Thruway mileage by one-half and eliminated such rates on and after January 1, 1996	January 1, 1995
Refunds	Permitted taxpayers who purchase more fuel in New York State than they consume in the State to claim refunds or credits for all excess payments of State fuel use taxes (prior to January 1, 1995, taxpayers could only obtain a refund or credit for the motor fuel tax portion of the fuel use tax).	January 1, 1995
International Fuel Tax Agreement	Authorized the State to join the federally mandated International Fuel Tax Agreement (IFTA) on January 1, 1996. This agreement provides for the uniform reporting and collection of fuel-use-related taxes among IFTA jurisdictions. Under IFTA, jurisdictions may only impose a fuel use tax on vehicles with loaded gross weights of more than 26,000 pounds or with three or more axles. Therefore, since January 1, 1996, vehicles with loaded gross weights between 18,000 pounds and 26,000 pounds and with fewer than three axles, that had been taxed in New York, were excluded from the fuel use tax.	
Legislation Enacted in 1995		
Fuel Use Tax Rate Cut	Reduced the diesel fuel excise tax rate from ten cents per gallon to eight cents per gallon. As a result, the diesel fuel tax component of the fuel use tax was also reduced to eight cents per gallon.	January 1,1996
Legislation Enacted in 1998		
Supplemental Tax	Reduced the truck mileage supplemental tax by 50 percent.	January 1, 1999
Legislation Enacted in 2000		
Supplemental Tax	Reduced the truck mileage supplemental tax by 20 percent.	April 1, 2001

2001-02 RECEIPTS

Net highway use tax receipts for 2000-01 were $155.1 million, including truck mileage tax receipts of $122.3 million, fuel use tax receipts of $28.1 million, and highway use permit fees of $4.7 million.

In the current fiscal year, slow economic growth contributed to only a moderate increase in trucking demand. In fact, truck mileage tax receipts to date in 2001-02 are 3.7 percent below the comparable 2000-01 period. This decline was partly due to the cut in the supplemental tax rate. Fuel use tax receipts to date in 2001-02 are 2.9 percent greater than the comparable 2000-01 period due primarily to higher fuel prices.

Based on collection experience to date, and the weak economic outlook (see Economic Backdrop section), highway use taxes will continue to grow slowly. Net truck mileage tax receipts are projected at $118 million, including a $7.7 million reduction due to the supplemental tax rate cut, fuel use tax receipts at $28.7 million, and permit fees at $4.3 million, bringing total estimated highway use tax receipts for 2001-02 to $151.0 million.

2002-03 PROJECTIONS

Total highway use tax receipts for 2002-03 are projected at $155.3 million. The base of the truck mileage tax (demand for trucking) is expected to increase by only 1.8 percent as a result of the weak economy. Tax Law changes enacted in 2000, which reduced the truck mileage supplemental tax by 20 percent, will reduce truck mileage tax receipts by approximately $7.9 million. Net truck mileage tax receipts are estimated at $120.1 million. Due to the effect of decreased fuel prices, the sales tax component of the fuel use tax is estimated to decrease by about 7 percent. As a result, fuel use tax receipts are expected to decline to $28.2 million. Permit fees of $7.0 million reflect a peak triennial renewal year.

OTHER FUNDS

The Dedicated Highway and Bridge Trust Fund receives all highway use tax receipts.

GENERAL FUNDS

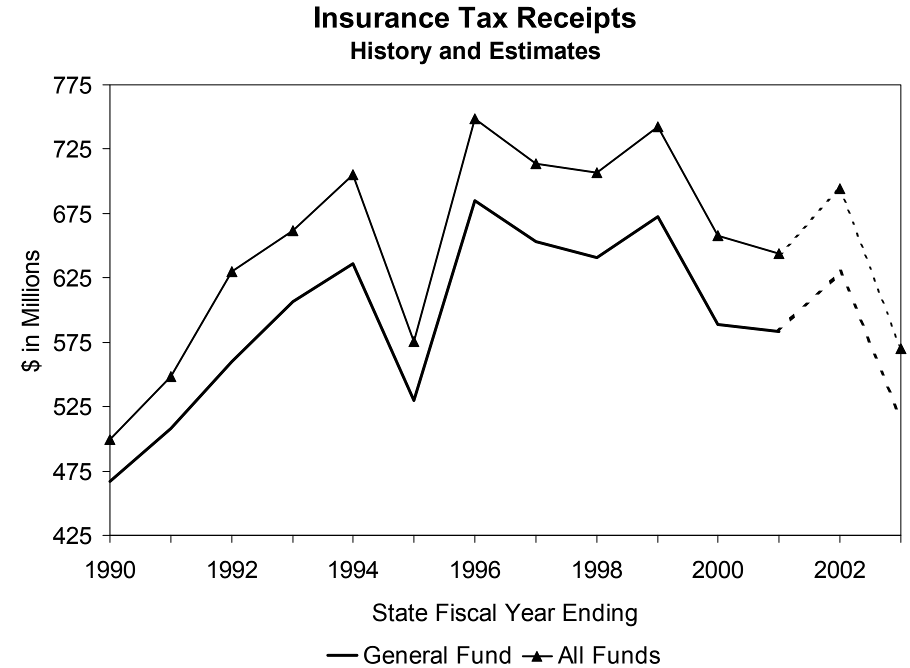
Since 1994-95, no highway use tax receipts have been deposited in the General Fund.

HIGHWAY USE TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Gross Capital Projects Funds[1]	Refunds	Net Capital Projects Funds[1]	Debt Service Funds	All Funds Net Collections
	Actual								
1993-94	10,897	0	10,897	0	166,071	2,723	163,348	0	174,245
1994-95	0	0	0	0	191,738	2,577	189,161	0	189,161
1995-96	0	0	0	0	174,377	4,373	170,004	0	170,004
1996-97	0	0	0	0	164,226	6,912	157,314	0	157,314
1997-98	0	0	0	0	167,644	2,834	164,810	0	164,810
1998-99	0	0	0	0	171,525	2,858	168,667	0	168,667
1999-2000	0	0	0	0	151,994	1,769	150,225	0	150,225
2000-01	0	0	0	0	157,180	2,105	155,075	0	155,075
	Estimated								
2001-02	0	0	0	0	153,000	2,000	151,000	0	151,000
2002-03	0	0	0	0	157,300	2,000	155,300	0	155,300

[1] Dedicated Highway and Bridge Trust Fund

INSURANCE TAXES

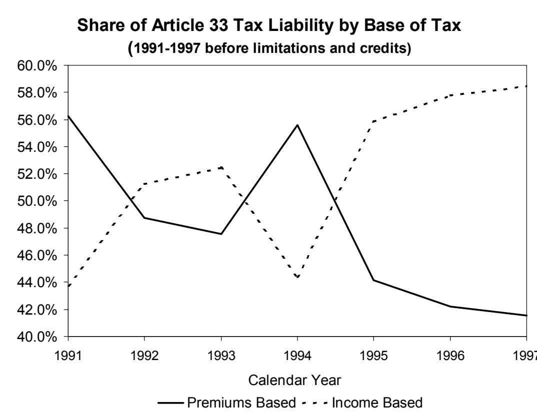


DESCRIPTION

The State collects taxes from insurance corporations, insurance brokers and certain insureds under Article 33 of the Tax Law and the Insurance Law. In addition, those Article 33 taxpayers doing business in the Metropolitan Commuter Transportation District (MCTD), which includes the counties of New York, Bronx, Kings, Queens, Richmond, Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk and Westchester, are subject to a 17 percent surcharge on their tax liability attributable to the MCTD area.

Article 33 of the Tax Law

Article 33 of the Tax Law imposes a franchise tax on insurance corporations for the privilege of doing business or otherwise exercising a corporate franchise in New York. The insurance tax has two components.



The franchise tax component of the insurance tax is computed under four alternative bases, with tax due based on the alternative base generating the maximum tax. In addition, there is a 0.08 percent tax rate applied to subsidiary capital allocated to New York. The four alternative bases and rates are described in Table 1.

TABLE 1
RATES FOR THE NET INCOME COMPONENT OF THE FRANCHISE TAX
BY TYPE OF BASE

Base	Rate
Allocated entire net income	8.50 percent for taxable years beginning after June 30, 2000 and before July 1, 2001. 8.00 percent for taxable years beginning after June 30, 2001 and before July 1, 2002. 7.50 percent for taxable years beginning on or after July 1, 2002.
Allocated business and investment capital	1.6 mills for each dollar
Allocated income and officers' salaries	9.00 percent
Minimum tax	$250

Tax is allocated to New York under the entire net income base by a formula, which apportions entire net income based on weighted ratios of premiums (with a weight of nine) and wages (with a weight of one), earned or paid in New York, to total premiums and total wages for the tax year for all employees.

The second component of the franchise tax is the additional franchise tax on gross premiums, less refunded premiums written on risks located or resident in New York. This tax is added to the highest of the alternatives from the net income base. The rate of the premiums tax is determined by the type of insurance covered and the type of insurer. Table 2 reports the appropriate rates.

TABLE 2
PREMIUM TAX RATES
BY TYPE OF INSURER

Type of Premium	Type of Insurer	Rate
Life, accident and health	Life and health	0.7 percent
Accident and health	Property and casualty	1.0 percent
Property and casualty	Property and casualty	1.3 percent

A maximum tax is computed based on net premiums. This limitation, or cap, differs according to the type of insurer. Currently, life insurers determine their limitation by multiplying net premiums by 2.0 percent. Nonlife insurers multiply net premiums by 2.4 percent. Table 3 shows the limitation percentages by insurer.

TABLE 3
LIMITATION ON TAX
BY TYPE OF INSURER

Type of Insurer	Cap Level
Life insurers	2.0 percent of taxable premiums.
All others	2.4 percent of taxable premiums for taxable years beginning after June 30, 2000 and before July 1, 2001. 2.2 percent of taxable premiums for taxable years beginning after June 30, 2001 and before July 1, 2002. 2.0 percent of taxable premiums for taxable years beginning on or after July 1, 2002.

Generally, taxpayers with tax liability that exceeds the limitation may not reduce their liability with tax credits to a level below the limitation. However, special treatment is allowed for Empire Zone and Zone Equivalent Area tax credits. Taxpayers may use these credits to reduce their tax liability below the limitation.

Article 33-A of the Tax Law

Chapter 190 of the Laws of 1990 established a tax of 3.6 percent of premiums on independently procured insurance under Article 33-A of the Tax Law. This tax is imposed on any individual, corporation or other entity purchasing or renewing an insurance contract covering certain property and casualty risks located in New York from an insurer not authorized to transact business in New York under a certificate of authority from the Superintendent of the Insurance Department.

Insurance Law

The Insurance Law authorizes the Superintendent of Insurance to assess and collect retaliatory taxes from a foreign insurance corporation, when the overall tax rate imposed by its home jurisdiction on New York companies exceeds the comparable tax rate imposed by New York on such foreign insurance companies.

Retaliatory taxes have been utilized by the states since the nineteenth century to ensure a measure of fairness in the interstate taxation of insurance corporations. Retaliatory taxes deter other states from discriminating against foreign corporations and effectively require states with a domestic insurance industry to maintain an overall tax rate on insurance corporations that is generally consistent with other states.

Nevertheless, there are a variety of mechanisms for taxing insurance corporations throughout the states, and differences in overall tax rates among the states are inevitable. New York provides an additional measure of protection for its domestic insurance industry by allowing domestic corporations to claim a credit under Article 33 of the Tax Law for 90 percent of the retaliatory taxes legally required to be paid to other states.

The Insurance Law also imposes a premiums tax on a licensed excess lines insurance broker when a policy covering a New York risk is procured through such broker from an unauthorized insurer (an unauthorized insurer is an insurer not authorized to do business in New York). Transactions involving a licensed excess lines broker and an insurer not authorized to do business in New York are permissible under limited circumstances delineated in Article 21 of the Insurance Law. The tax is imposed at a rate of 3.6 percent of premiums covering risks located in New York.

Metropolitan Commuter Transportation District Business Tax Surcharge

Insurance corporations and other corporations doing business in the New York metropolitan region are subject to a 17 percent temporary business tax surcharge on tax liability within the MCTD region. Receipts from this tax surcharge are deposited in a special revenue fund, the Mass Transportation Operating Assistance Fund, dedicated to mass transit assistance in the New York metropolitan region.

SIGNIFICANT LEGISLATION

Credits

In recent years, targeted tax credits have been extended to Article 33 taxpayers, including certified capital companies (CAPCOs), investment tax credit (ITC), long term care insurance, low-income housing and Empire Zones. The table below lists the major tax credits available under Article 33.

DESCRIPTION OF MAJOR TAX CREDITS

Subject	Description
Retaliatory Tax Credit	Allows a credit up to 90 percent of retaliatory taxes paid to other states by New York domiciled or organized insurers.
Fire Insurance Tax Credit	Allows a credit for taxes paid on certain fire insurance premiums.
Investment in Certified Capital Companies Tax Credit	Equals 100 percent of the amount invested in CAPCOs for taxable years beginning after 1998. The credit is claimed at 10 percent per year for ten years. There is a dollar cap on the investment proceeds eligible for the credit. The original statewide cap was $100 million set in 1998. It was increased to $130 million in 1999 and to $280 million in 2000.
Special Additional Mortgage Recording Tax (SAMRT)	Provides up to 100 percent of SAMRT paid. A carry forward is allowed.
Investment Tax Credit	Allows insurance taxpayers that are brokers/dealers in securities to claim a credit for equipment or buildings used in broker/dealer activity and in activities connected with broker/dealer operations.
Long-Term Care Insurance Credit	Creates a 10 percent credit for the cost of purchasing long-term care insurance as defined in the Insurance Law.
Low-Income Housing Tax Credit	Mirrors the structure of the existing Federal low-income housing tax credit. In addition, the State program expands the Federal program to include more moderate-income households. Generally, the amount of the credit is the applicable percentage, depending on whether a building is new, existing, or federally subsidized, of the qualified basis of each eligible low-income building.
Empire Zones Program	Provides various tax incentives for insurers certified in Empire Zones. The enhanced benefits of this program include a tax credit on real property taxes paid, a tax reduction credit, and a sales and use tax exemption.

Furthermore, there are also several types of insurance contracts which are exempt from the franchise tax. These include, but are not limited to, annuity contracts and certain health insurance contracts for insureds aged 65 years and older as provided under section 4236 of the Insurance Law.

Certain corporations and other entities which provide insurance are exempt from State franchise taxes and the regional business surcharge. Non-profit medical expense indemnity corporations and other health service corporations, organized under Article 43 of the Insurance Law, are exempt from these State taxes. Health maintenance organizations (HMOs) and Blue Cross/Blue Shield corporations are examples of such exempt entities.

Recent Legislative Changes

The table below highlights significant legislation enacted since 1994 affecting insurance taxes:

INSURANCE TAX LEGISLATION

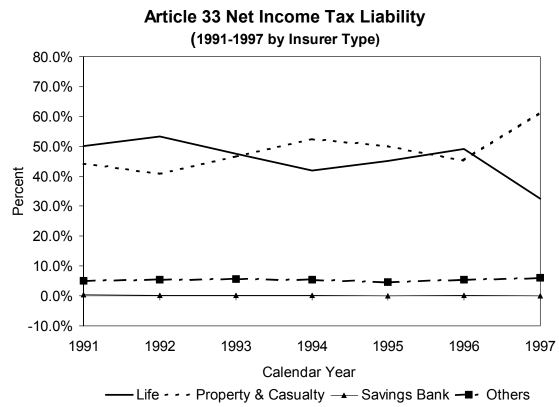
Subject	Description	Effective Date
Legislation Enacted in 1994		
Temporary Business Tax Surcharge	Reduces the surcharge from 15 percent to 10 percent, 5 percent, and 0 percent over three years.	January 1, 1994
Legislation Enacted in 1997		
Premium Tax Rate for Life Insurers	Reduces the premium tax rate from 0.8 percent to 0.7 percent.	January 1, 1998
Cap on Tax Liability	Reduces the limitation on tax liability for life insurers from 2.6 percent to 2.0 percent.	January 1, 1998
Credit for Investment in Certified Capital Companies	Credit equals 100 percent of amount invested in CAPCO's for taxable years beginning after 1998. The rate equals 10 percent per year for ten years. The statewide cap was set at $100 million.	January 1, 1999
Captive Insurance Companies	Allows the formation of captive insurance companies. Subject to a special premiums tax with a top rate of 0.4 percent or $5,000. This is in lieu of the premiums and income-based tax.	January 1, 1998

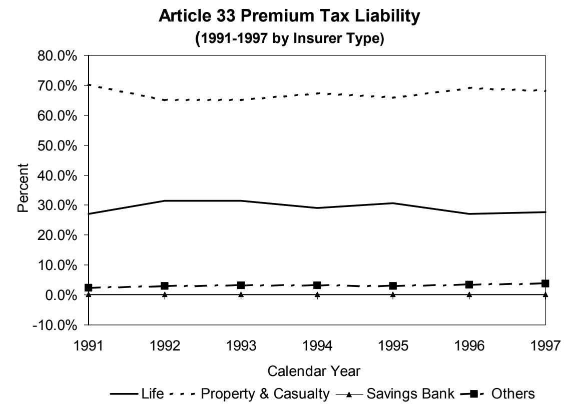
Subject	Description	Effective Date
Legislation Enacted in 1999		
CAPCOs	The statewide cap is increased from $100 million to $130 million.	January 1, 2001
State Insurance Fund	Conforms the State Insurance Fund tax treatment to the regular insurance tax.	January 1, 2001
Entire Net Income (ENI) Tax Rate	Reduces ENI tax rate over a three-year period: • 8.5 percent for taxable years beginning after June 30, 2000 and before July 1, 2001. • 8.0 percent for taxable years beginning after June 30, 2001 and before July 1, 2002. • 7.5 percent for taxable years beginning on or after July 1, 2002.	June 30, 2000
Cap on Tax Liability	Reduces the limitation on tax liability for non-life insurers over a three-year period: • 2.4 percent for taxable years beginning after June 30, 2000 and before July 1, 2001. • 2.2 percent for taxable years beginning after June 30, 2001 and before July 1, 2002. • 2.0 percent for taxable years beginning on or after July 1, 2002.	June 30, 2000
Legislation Enacted in 2000		
CAPCOs	The statewide cap was increased from $130 million to $280 million.	January 1, 2002
Investment Tax Credit	Insurance taxpayers that are brokers/dealers in securities may claim a credit for equipment or buildings used in broker/dealer activity and in activities connected with broker/dealer operations.	Available for property placed in service between January 1, 2002 and October 1, 2003.
Long-Term Care Insurance Credit	Creates a 10 percent credit for cost of purchasing long-term care insurance as defined in the Insurance Law.	January 1, 2002
Low-Income Housing Tax Credit	Based on the structure of the Federal low-income housing tax credit. In addition, the credit is expanded to include housing constructed for moderate-income households. The amount of the credit depends on whether a building is new, existing, or federally subsidized.	January 1, 2000
Empire Zones Program	Provides Qualified Empire Zone Enterprises (QEZE) tax incentives in Empire Zones. Transforms the current Economic Development Zones into virtual "tax-free" zones for certain businesses. The enhanced benefits of this program include a tax credit on real property taxes paid, tax reduction credit, and sales and use tax exemption.	January 1, 2001

2001-02 RECEIPTS

The estimate of All Funds receipts for State fiscal year 2001-02 is $694 million, an increase of 7.8 percent over the prior year. This primarily reflects an increase in premiums written in the 2001 calendar year. The World Trade Center (WTC) disaster is expected to negatively affect net income, but the bulk of the impact is estimated to depress 2002-03 receipts.

The following graphs illustrate, for the 1991-1997 period, that the Property/Casualty and Life/Health sectors combined have historically accounted for over 90 percent of tax liability.





State Insurance Fund

In New York State, the State Insurance Fund, which has a large volume of workers' compensation claims related to the WTC tragedy, may also experience a large increase in claims. The estimate assumes State fiscal year 2001-02 losses of approximately $12 million in tax liability for the State Insurance Fund.

Property and Casualty Companies

The property and casualty sector is the largest sector of the industry, and represents over half of the State's insurance tax collections. Many property and casualty companies will be adversely affected by the WTC disaster. Recent industry estimates of direct industry losses are in the $30 billion to $60 billion range. The disaster will affect all lines of insurance, including workers' compensation, property, casualty, and reinsurance. Industry experts have reported that primary insurers will have losses in excess of their reinsurance coverage.

The property and casualty sector typically accounts for over 60 percent of premium tax liability and 45 percent of net income tax liability. The five largest lines of business under property and casualty lines of business are automobile, workers' compensation, commercial multi-peril, general liability, and homeowners multi-peril. They account for approximately 80 percent of premiums. Table 4 reports actual property and casualty premiums from 1994 through 2000 and estimates for 2001 and 2002 for New York State.

TABLE 4
PROPERTY AND CASUALTY INSURANCE
NEW YORK CALENDAR YEAR PREMIUMS
(millions of dollars/percent)

Lines of Insurance	1994	1995	1996	1997	1998	1999	2000	2001 (est.)	2002 (est.)
Automobile	8,572	8,913	9,466	9,490	9,631	9,594	9,664	10,109	10,338
percent change	*5.50*	*3.98*	*6.20*	*0.26*	*1.49*	*(0.38)*	*.70*	*4.60*	*2.27*
Workers' Compensation	3,769	3,650	3,121	2,725	2,686	2,725	3,154	3,223	3,437
percent change	*6.02*	*(3.15)*	*(14.49)*	*(12.70)*	*(1.41)*	*1.44*	*15.8*	*2.18*	*6.64*
Commercial Multi-Peril	2,043	2,139	2,097	2,031	2,071	2,002	2,085	2,178	2,229
percent change	*1.84*	*4.70*	*(1.96)*	*(3.15)*	*1.99*	*(3.33)*	*4.16*	*4.47*	*2.33*
General Liability	1,981	1,853	1,851	2,091	2,734	1,825	2,148	2,262	2,296
percent change	*2.17*	*(6.45)*	*(0.11)*	*12.99*	*30.90*	*(33.25)*	*17.71*	*5.29*	*1.53*
Homeowners' Multi-Peril	1,868	1,966	2,053	2,133	2,181	2,230	2,326	2,447	2,553
percent change	*6.05*	*5.27*	*4.43*	*3.91*	*2.33*	*2.25*	*4.32*	*5.17*	*4.37*
Other	3,689	3,567	3,574	3,620	3,641	3,635	3,720	3,835	3,959
percent change	*12.03*	*(3.31)*	*0.20*	*1.29*	*0.61*	*(1.53)*	*(5.13)*	*3.11*	*3.22*
TOTAL P/C PREMIUMS	21,922	22,088	22,162	22,090	22,945	22,011	23,098	24,053	24,813
Annual Increase/Decrease *percent change*	*4.85*	*0.75*	*0.34*	*(0.32)*	*3.87*	*(4.07)*	*4.94*	*4.14*	*3.16*

The WTC disaster is not expected to materially affect premiums in the short run. In the long run, the premiums tax could increase as rates for commercial insurers rise. Net premiums for property and casualty companies overall grew by 4.9 percent in 2000 and are expected to grow at a slightly slower pace in 2001 and 2002.

Property and casualty net income tax liability is estimated to grow by 4.1 percent in 2001. This estimate reflects the higher stock trading levels for many property and casualty insurers for most of the year as a result of a shift in investor emphasis from technology to the insurance industry. Higher stock values for insurers increase profits, resulting in higher incomes.

Also affecting net income tax liability are payouts of claims. The industry is required to honor claims from catastrophes that occurred this year, as well as to continue paying claims for prior year catastrophic events. Over the next two years, property and casualty net income tax liability will be significantly affected by the payouts of claims due to the WTC disaster.

Life and Health Companies

Life and health insurance is the second largest sector of the industry and represents approximately a third of the State's insurance tax collections. Premiums for life and health companies are expected to grow by only 2.5 percent on a year-over-year basis. In general, the life insurance industry is not expected to be adversely affected by the WTC disaster. Overall, the estimate reflects continued growth at historical averages for this industry.

2002-03 PROJECTIONS

All Funds collections for 2002-03 are projected at $570.5 million, a decrease of approximately 18 percent. The State fiscal year 2002-03 receipt losses are concentrated in the property and casualty sector, where receipts are expected to decline by approximately $100 million due to the WTC disaster. In addition, collections will be lower due to statutory tax reductions which reduce the ENI rate to 8.0 percent and the premiums cap on non-life insurers to 2.2 percent.

The forecast of receipts from property and casualty insurers is based on an increase in premium liability of 4.6 percent, primarily resulting from modest growth in the automobile and homeowners sectors. The estimated premium growth is more than offset by the impact of the WTC disaster on net franchise tax liability. Operating losses may result as companies draw down on existing reserves or investment portfolios.

Beyond unanticipated costs arising from the WTC disaster, additional risks to the forecast include a continued slowdown in the economy, which could affect certain lines of insurances, such as nonstandard automobile insurance. Given industry and economic conditions, some companies are withdrawing from certain lines of business, such as homeowners and private passenger automobile. Consolidations in this industry are expected to occur as weaker companies join with larger insurers. It is expected that, overall, increased premium prices will be easier to implement because risk profiles will now be reclassified to take into consideration the WTC attack.

The forecast assumes that the life and health sector will grow modestly through the 2002 tax year. The New York share of premiums written will remain approximately 8 percent of the national market, and premiums written are expected to grow 2.5 percent per year. Net income tax liability for this sector is projected to grow by 4.0 percent. Sales of variable annuities have fallen with the stock market in recent quarters. A major risk to the forecast will be the continued softening of the economy, which will affect investment portfolios and annuity sales. Recent Federal tax law changes appear to have had little effect on the industry. The Federal Tax Act of 2001, which contained a repeal of estate taxes, is expected to have little effect on the industry. The Gramm-Leach-Bliley Act of 1999, which permits insurance companies, banks and brokerages to form consolidated companies offering a full range of financial services, appears to be having little impact in the short run. Beyond unanticipated costs arising from the WTC disaster, additional risks to the forecast include Securities Exchange Commission and National Association of Securities Dealers investigations into alleged abuses in variable benefit insurance and annuities.

OTHER FUNDS

There is a surcharge of 17 percent upon companies tax liability attributed to the MCTD region and is deposited in the Mass Transportation Operating Assistance Fund. For 2001-02, the deposit is estimated at $64 million. The estimate is $54.5 million for 2002-03.

GENERAL FUND

Based on collections to date, net collections for the year are estimated to be $630 million. This represents an increase of approximately $46 million from the prior year. The receipts estimate for 2001-02 includes an estimated $40 million in audit collections.

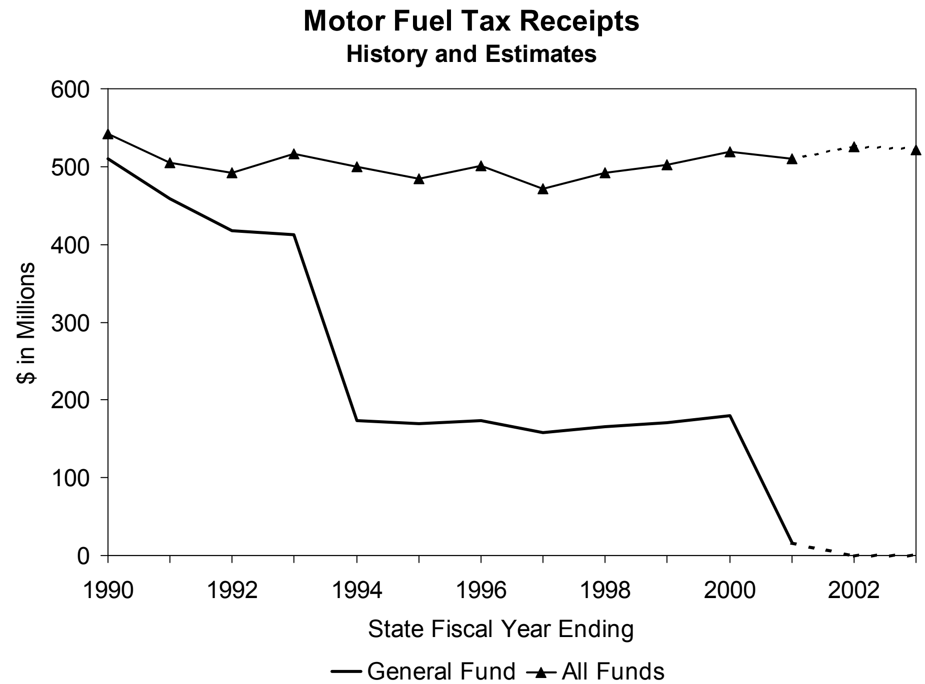
For 2002-03, General Fund collections are estimated at $516 million. The large decline is attributable to the WTC disaster. This includes an estimated $40 million in audits, offset by $40 million in refunds. The following table provides the receipts estimate for 2001-02 and the forecast for 2002-03, as well as a history of receipts for 1993-94 through 2000-01.

TABLE 5
INSURANCE TAX RECEIPTS
(millions of dollars)

	Tax Law		Insurance Law							
	Gross General Fund	Refunds	Net	Net General Fund	Gross Special Revenue Funds	Refunds	Net Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
	Actual									
1993-94	678	25	17	636	73	4	69	0	0	705
1994-95	593	36	27	530	50	4	46	0	0	576
1995-96	728	29	14	685	68	4	64	0	0	749
1996-97	715	29	33	653	68	8	60	0	0	713
1997-98	699	32	26	641	69	3	66	0	0	707
1998-99	744	45	26	673	76	6	70	0	0	743
1999-2000	633	45	(1)	589	79	10	69	0	0	658
2000-01	659	42	33	584	65	5	60	0	0	644
	Estimated									
2001-02	710	40	40	630	72	8	64	0	0	694
2002-03	596	40	40	516	62	7	55	0	0	571

[1] Mass Transportation Operating Assistance Fund

MOTOR FUEL TAX



DESCRIPTION

Motor fuel and diesel motor fuel taxes are levied by Article 12-A of the Tax Law upon the sale, generally for highway use, of gasoline and diesel fuel, respectively. The rate of tax imposed on each gallon of gasoline and diesel fuel is eight cents.

The motor fuel tax is levied primarily on fuel used in motor vehicles operating on the public highways of the State or in recreational motor boats operating on the State's waterways. Exemptions, credits and refunds are allowed for certain other uses of gasoline and diesel motor fuel.

Exemptions from the motor fuel tax include:
- kerosene and crude oil;
- fuel not used in motor vehicles. "Motor vehicle" is defined as any vehicle propelled by power, except muscular power. However, vehicles such as boats (other than pleasure craft), road building machinery and tractors used exclusively for agricultural purposes are excluded from the definition of motor vehicles;
- fuel used in tanks of vehicles entering New York State;
- sales to state, local and Federal governments, the United Nations and qualifying Indian nations; and
- certain hospitals that qualify as exempt organizations under section 1116(a)(4) of the Tax Law.

Other exemptions apply only to the diesel motor fuel tax, including certain sales for heating purposes and sales of kero-jet fuel for use in airplanes.

Full and partial refunds and credits of tax paid are available for fuel used by:
- omnibus carriers or taxicabs;
- nonpublic school vehicle operators, exclusively for education-related purposes; and
- volunteer ambulance services.

Administration

Although the motor fuel tax is imposed on the ultimate consumer of the fuel, the tax is remitted upon importation into New York. This tax-on-first-import system is designed to reduce gasoline tax evasion, which has involved bootlegging from other states and successions of tax-free sales among "dummy" corporations masked by erroneous record keeping and reporting.

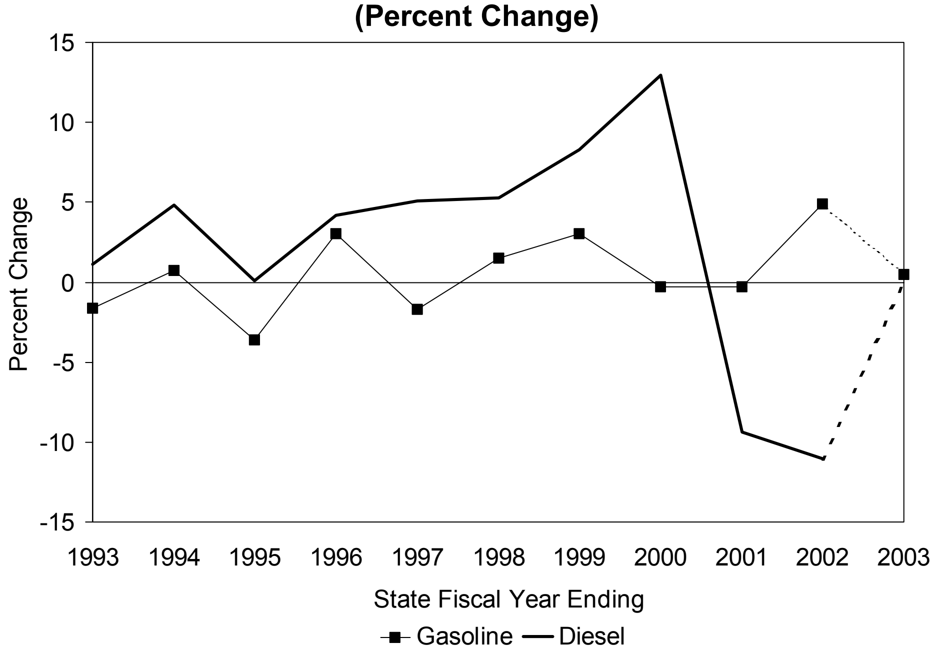
Since 1988, taxes on diesel motor fuel have been collected upon the first non-exempt sale in the State. Prior to that time, the diesel motor fuel tax was collected at the time of retail sale or use by a bulk user.

Chapter 55 of the Laws of 1992 requires accelerated remittance of the tax by taxpayers with annual liability of more than $5 million for motor fuel and petroleum business taxes combined. The taxes for the first 22 days of each month must be remitted electronically or by certified check by the third business day following that period. Taxpayers can choose to make either a minimum payment of three-fourths of the comparable month's tax liability for the preceding year, or 90 percent of actual liability for the 22 days. Taxes for the balance of the month are remitted on the twentieth of the following month.

Consumption History

As the following graph illustrates, diesel consumption was quite strong between 1994-95 and 1999-2000, reflecting robust demand for diesel fuel resulting from strong economic growth. The sharp decline in 2000-01 diesel gallonage reflects, in part, higher prices for diesel fuel. Gasoline consumption has grown more slowly, but increased sharply in 1998-99 partially due to low gasoline prices during that period. Gasoline consumption declined slightly in 1999-2000 and 2000-01 due to higher prices.

Gasoline and Diesel Reported Gallons
(Percent Change)



SIGNIFICANT LEGISLATION

Statutory changes since 1994 are reported below.

Subject	Description	Effective Date
Legislation Enacted in 1995		
Tax Liability	Reduced the diesel motor fuel tax from 10 cents to 8 cents per gallon.	January 1, 1996
Exemption	Provided an up-front exemption from the motor fuel excise tax for retail sales of aviation gasoline.	September 1, 1995
Legislation Enacted in 2000		
Distribution	Increased the percentage of motor fuel receipts dedicated to highway construction and transit.	April 1, 2000

2001-02 RECEIPTS

All Funds receipts to date are $412.9 million, $21.2 million, or 5.4 percent, above the comparable period in 2000-01. Gasoline receipts increased by $26.8 million (7.8 percent) as lower gasoline prices prompted distributors to increase inventories. Diesel receipts decreased by $5.6 million (11.4 percent).

For the remainder of the year, the demand for diesel fuel is expected to fall as the State's economy continues to weaken. Due to the large increase in gasoline inventories earlier in the year, gasoline receipts for the remainder of the year are expected to be below 2000-01 receipts for the same period. For the fiscal year as a whole, diesel consumption is expected to drop 11.0 percent from 2000-01 levels. Gasoline consumption is expected to increase by 4.9 percent from 2000-01 levels.

Total motor fuel tax receipts are estimated at $524.9 million, an increase of $14.6 million, or 2.9 percent, from 2000-01. Gasoline receipts are estimated to increase by $21.1 million (4.7 percent) and diesel receipts to decrease by $6.5 million (10.5 percent). Due to the World Trade Center disaster, fewer tax enforcement personnel will be available in the short-term to deter the illegal importation of fuel into the State. This could result in a small loss of receipts during the remaining months of 2001-02.

2002-03 PROJECTIONS

The gasoline and diesel consumption projections for 2002-03 reflect a slow recovery from recession and estimated fuel prices that begin increasing early in 2002. All Funds receipts are projected to be $521.7 million, a decrease of $3.2 million (0.6 percent). Gasoline receipts are projected to decrease by $3.2 million. Diesel receipts are projected to remain at $55.1 million.

OTHER FUNDS

Motor fuel tax revenues are by law distributed to four funds: the Dedicated Highway and Bridge Trust Fund, the Dedicated Mass Transportation Trust Fund, the Emergency Highway Reconditioning and Preservation Fund, and the Emergency Highway Construction and Reconstruction Fund. The fund distribution is shown in the following table.

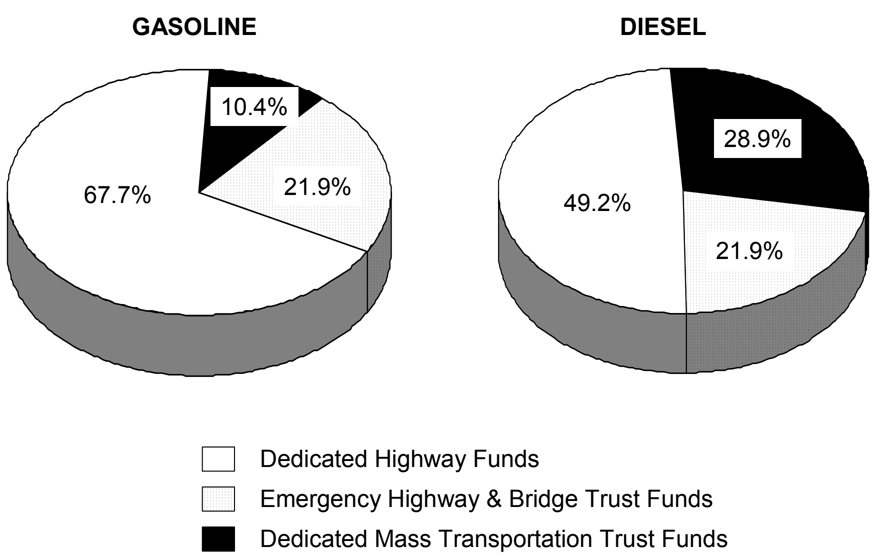
MOTOR FUEL TAX FUND DISTRIBUTION
(percent)

Effective Date	General Fund	DHBTF[1]	EHF[2]	DMTTF[3]
Prior to April 1, 1993				
Gasoline	78.1	0.0	21.9	0.0
Diesel	78.1	0.0	21.9	0.0
Prior to April 1, 2000				
Gasoline	28.1	50.0	21.9	0.0
Diesel	78.1	0.0	21.9	0.0
Prior to April 1, 2001				
Gasoline	0.0	67.7	21.9	10.4
Diesel	28.1	31.5	21.9	18.5
After April 1, 2001				
Gasoline	0.0	67.7	21.9	10.4
Diesel	0.0	49.2	21.9	28.9
After April 1, 2003				
Gasoline	0.0	81.5	0.0	18.5
Diesel	0.0	63.0	0.0	37.0

[1] Dedicated Highway and Bridge Trust Fund.
[2] Emergency Highway Reconditioning and Preservation Fund and the Emergency Highway Construction and Reconstruction Fund.
[3] Dedicated Mass Transportation Trust Fund.

The percentage distribution of motor fuel tax revenue by fund and fuel type is the same for State fiscal years 2001-02 and 2002-03, and is displayed in the following pie chart.

Motor Fuel Tax Deposits by Fund
State Fiscal Year 2001-02 and 2002-03



GENERAL FUND

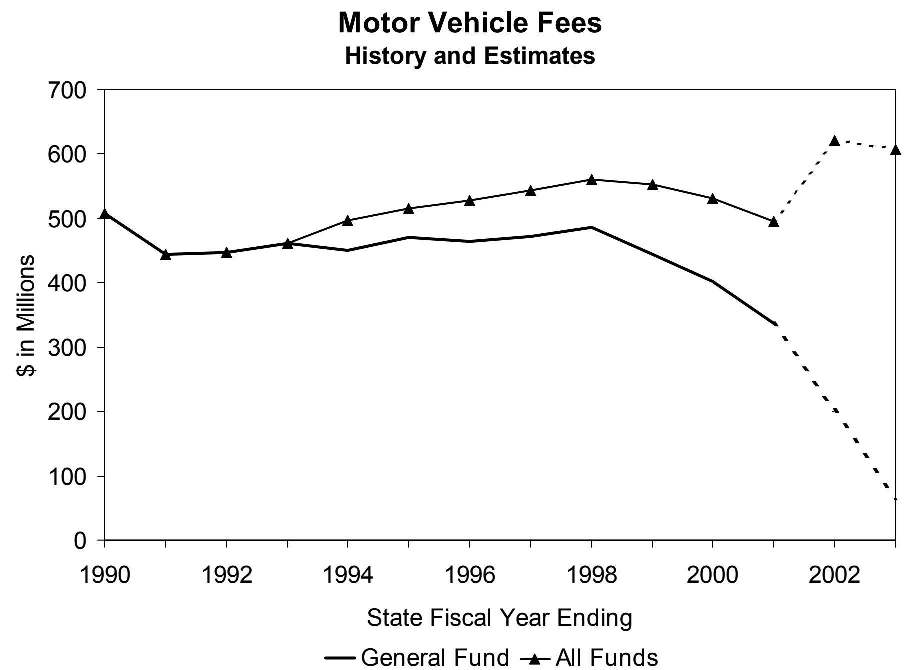
In 2001-02 and 2002-03, no motor fuel tax receipts will be deposited in the General Fund.

MOTOR FUEL TAX RECEIPTS
(thousands of dollars)

	All Funds Gross Collections	Net General Fund	Net Special Revenue Funds[1]	Net Capital Projects Funds[2]	Net Debt Service Funds[3]	All Funds Refunds	All Funds Net Collections
	Actual						
1993-94	514,489	173,634	0	212,211	113,806	14,838	499,651
1994-95	500,728	168,968	0	212,514	103,480	15,766	484,962
1995-96	515,775	173,597	0	220,460	107,425	14,293	501,482
1996-97	484,324	157,531	0	210,835	103,143	12,815	471,509
1997-98	503,666	165,255	0	218,897	107,562	11,953	491,713
1998-99	512,075	171,148	0	221,288	109,882	9,757	502,318
1999-2000	533,633	179,933	0	225,358	113,482	14,860	518,773
2000-01	524,251	17,312	58,088	323,291	111,633	13,926	510,325
	Estimated						
2001-02	537,900	0	64,800	345,300	114,800	13,000	524,900
2002-03	534,700	0	64,500	343,100	114,100	13,000	521,700

[1] Dedicated Mass Transportation Trust Fund.
[2] Dedicated Highway and Bridge Trust Fund.
[3] Emergency Highway Reconditioning and Preservation Fund and Emergency Highway Construction and Reconstruction Fund.

MOTOR VEHICLE FEES



DESCRIPTION

Motor vehicle fees are derived from a variety of sources, but consist mainly of vehicle registration and driver licensing fees.

Registration Requirements and Exemptions

In general, motor vehicles, motorcycles, trailers, semitrailers, buses, and other types of vehicles operating in New York are required to be registered with the Department of Motor Vehicles. Vehicles owned by nonresidents and registered with a political jurisdiction outside the State are not usually required to be registered in New York.

Certain vehicles registered in New York are exempt from registration fees. The exemptions include: vehicles owned by the State or municipalities; passenger vehicles owned by consular offices, provided reciprocity is granted; and vehicles owned and used for the transportation of animals by a society for the prevention of cruelty to animals.

Fee Schedules

Most vehicle registration fees in New York are based on weight. Two important exceptions are buses, which are charged according to seating capacity, and semitrailers, which are registered for a flat fee. The main registration fees are as follows:

MAIN REGISTRATION FEES

Type of Vehicle	Weight of Vehicle	Annual Fee (dollars)
Passenger vehicle	Each 100 lbs. or major fraction thereof up to 3,500 lbs.	0.645
	Plus: for each 100 lbs or major fraction thereof above 3,500 lbs.	0.97
Passenger vehicle – minimum fee		10.35
Passenger vehicle – maximum fee		56.06
Passenger vehicle propelled by electricity		12.94
Auto truck and light delivery vehicle	Each 500 lbs. maximum gross weight or fraction thereof	2.88
Tractors (registered separately from semitrailers)	Each 100 lbs. maximum gross weight or fraction thereof	1.21
Trailers	Each 500 lbs. maximum gross weight or fraction thereof	4.31
Semitrailers – pre-1989 model year		23.00 per year
Semitrailers – model year 1989 or later		69.00 for period of 5.5 years to 6.5 years
Bus – seating capacity 15 to 20 passengers		59.80

The other main source of motor vehicle fees are driver licensing fees. The main categories of license fees are listed below.

MAIN LICENSING FEE CATEGORIES

Type of License	Fee (dollars)
Initial application	10.00
Learner's permit	2.50 – for each six months
Learner's permit – commercial driver's license	7.50 – for each six months
License renewal	2.50 – for each six months
License renewal – commercial driver's license	7.50 – for each six months

In summary, the largest sources of revenue are fees from vehicle registration and drivers' licenses. Other fees, relating to the operation of motor vehicles in the State, yield relatively minor amounts of revenue.

Administration

Traditionally, registration and licensing occur at the central and district offices of the Department of Motor Vehicles, by mail, and at county clerk's offices in most counties. The county clerks were historically compensated with a fixed portion of each fee, but more recently, they receive a percentage of gross receipts.

COUNTY CLERKS' RETENTION SCHEDULE

Type of Retention	Period
Fixed portion of each fee.	Until December 31, 1996
8.1 percent of gross receipts.	From January 1, 1997
9.3 percent of gross receipts.	From July 1, 1998
12.7 percent of gross receipts.	From April 1, 1999

SIGNIFICANT LEGISLATION

Below is a summary of significant statutory or administrative changes in recent years affecting revenues from motor vehicle fees.

Subject	Description	Effective Date
Administrative Changes 1996		
Licenses	License renewal period extended to five years.	April 1, 1996
Legislation Enacted in 1997		
Licenses	Original license period extended to five years.	September 1, 1997
Motorcycles	Add $2.50 to annual fee for registration and $0.50 for each six months to license or permit and earmark both to Motorcycle Safety Fund.	January 1, 1998
Administrative Changes 1997		
Photo image fee	Photo image fee raised to $3.00.	April 1, 1997
Legislation Enacted in 1998		
Registration fees	Fees on passenger vehicle registration reduced 25 percent.	July 1, 1998
Administrative Changes in 2000		
License plates	Reissuance (January 2001-January 2003)	January 1, 2001
Licenses	License renewal period extended to eight years.	April 1, 2000

2001-02 RECEIPTS

Gross receipts for 2001-02 are estimated at $666 million. The estimate for receipts from registrations is $420 million, and the estimate for receipts from licenses and other fees is $246 million. An estimated $46 million in refunds and county clerk retentions will result in estimated net receipts from motor vehicle fees of $620 million. The estimate reflects the continuing reissuance of new registration plates and the extension of a driver's license renewal to eight years.

2002-03 PROJECTIONS

Gross receipts for 2002-03 are estimated at $647 million. The estimate for receipts from registrations is $403 million and $244 million for receipts from licenses and other fees. An estimated $40 million in refunds and county clerk retentions will result in estimated net receipts from motor vehicle fees of $607 million.

OTHER FUNDS

The Dedicated Highway and Bridge Trust Fund and the Dedicated Mass Transportation Trust Fund

A portion of motor vehicle fee receipts is distributed to the Dedicated Highway and Bridge Trust Fund, a capital fund. Since April 1, 1993, a percentage of registration fees has been earmarked to this fund. The percentage dedicated to the fund has been adjusted several times.

Pursuant to Chapter 63, Laws of 2000, in 2001-02 an additional 23.5 percent of registration fees is earmarked to (1) the Dedicated Highway and Bridge Trust Fund and (2) the Dedicated Mass Transportation Trust Fund; of this additional dedication, 63 percent is allocated to highways and 37 percent to mass transportation. Other moneys from non-registration fees are shared in the same proportion.

Again pursuant to Chapter 63, Laws of 2000, beginning in 2002-03 an additional 31 percent of registration fees will be earmarked to the same funds and in the same proportion as stated above. Thus, the total percentage of additional registration fees dedicated pursuant to Chapter 63, Laws of 2000, will amount to 54.5 percent. Since previous legislation had already earmarked 45.5 percent, all registration fees are earmarked to the two Trust Funds.

In fiscal year 2001-02, the Dedicated Highway and Bridge Trust Fund will receive an estimated $388 million and the Dedicated Mass Transportation Trust Fund will receive an estimated $30 million.

In fiscal year 2002-03, under current law, the Dedicated Highway and Bridge Trust Fund will receive a projected $292 million and the Dedicated Mass Transportation Trust Fund will receive a projected $78 million.

PROPOSED LEGISLATION

Legislation submitted with the Budget proposes (1) to double current boat registration fees, effective October 1, 2002, and valued at $1.3 million in 2002-03; and (2) to earmark additional moneys ($171.6 million in 2002-03) to the Dedicated Highway and Bridge Trust Fund from non-registration fees now deposited in the General Fund.

A summary of recent and projected dedication amounts are set out in the table below.

DISTRIBUTION FROM REGISTRATION FEES
(percent)

Effective Date	General Fund	Dedicated Highway and Bridge Trust Fund	Dedicated Mass Transportation Trust Fund
Prior to April 1, 1993	100.0	0.0	0.0
April 1, 1993	87.0	13.0	0.0
April 1, 1994	83.0	17.0	0.0
January 1, 1995	80.0	20.0	0.0
April 1, 1998	72.0	28.0	0.0
July 1, 1998	66.0	34.0	0.0
March 1, 1999	54.5	45.5	0.0
April 1, 2001	31.0	60.3	8.7
April 1, 2002	0.0	79.8	20.2

GENERAL FUND

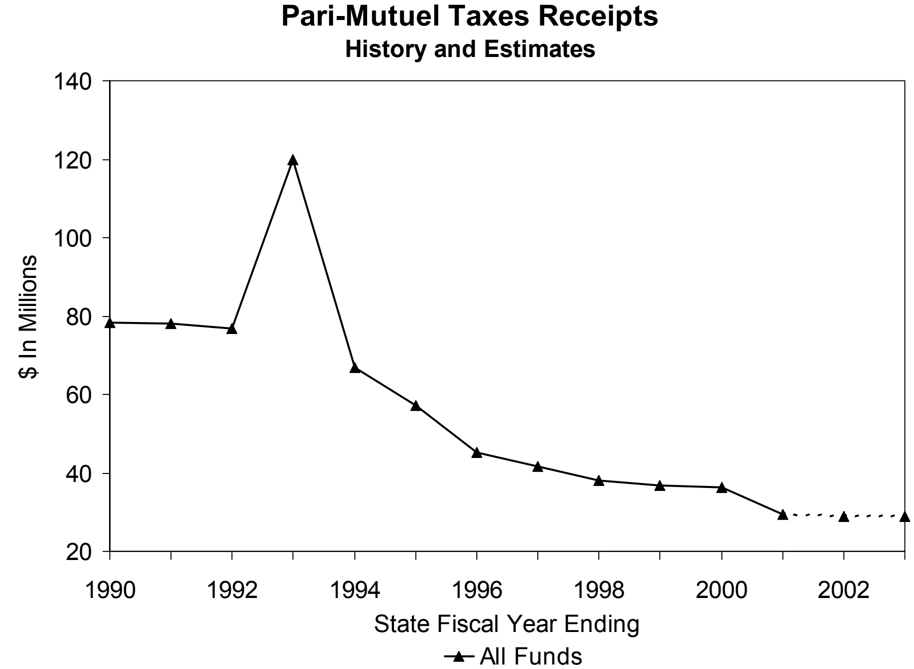
In Fiscal Year 2001-02, the General Fund will receive an estimated $201 million in motor vehicle fees. In Fiscal Year 2002-03, the General Fund will receive a projected $64.9 million based on proposed law.

MOTOR VEHICLE FEES
(thousands of dollars)

	Gross General Fund	Refunds	Less: County Clerks' Retention	Net General Fund	Special Revenue Funds[1]	Capital Projects Funds[2]	Debt Service Funds	All Funds Net Collections
	Actual							
1992-93	493,837	18,422	15,113	460,302	0	0	0	460,302
1993-94	482,312	16,570	15,748	449,994	0	46,655	0	496,649
1994-95	502,802	16,258	16,678	409,866	0	45,128	0	514,994
1995-96	500,181	18,958	16,663	464,560	0	62,390	0	526,950
1996-97	511,195	21,596	17,206	472,033	0	71,442	0	543,475
1997-98	517,178	11,436	19,324	486,418	0	73,096	0	559,514
1998-99	478,085	13,795	20,135	444,155	0	108,174	0	552,329
1999-2000	436,571	17,924	17,176	401,471	0	129,899	0	531,370
2000-01	372,554	18,712	16,425	337,417	0	157,309	0	494,726
	Estimated							
2001-02	247,500	24,000	22,000	201,500	30,400	388,300	0	620,200
2002-03								
(current law)	275,200	20,000	20,000	235,200	77,700	292,400	0	605,300
(proposed law)	104,900	20,000	20,000	64,900	77,700	464,000	0	606,600

[1] Dedicated Mass Transportation Transit Fund
[2] Dedicated Highway and Bridge Trust Fund

PARI-MUTUEL TAXES

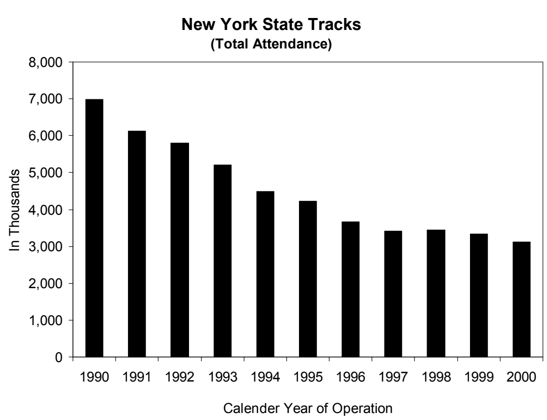


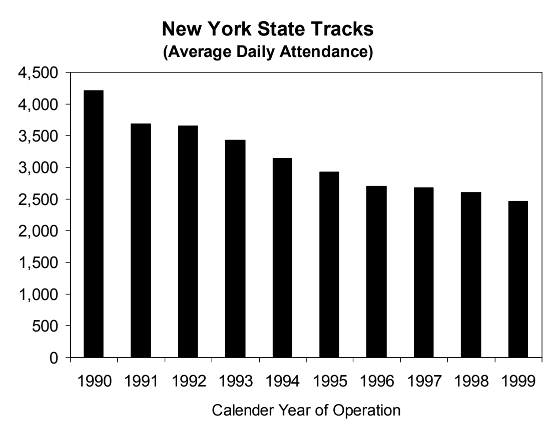
DESCRIPTION

Since 1940, taxes have been levied on pari-mutuel wagering activity conducted first at horse racetracks and, more recently, at off-track betting (OTB) parlors and simulcast theaters throughout the State. Each racing association or corporation pays the State a portion of the commission (the "takeout") withheld from wagering pools (the "handle") as a tax for the privilege of conducting pari-mutuel wagering on horse races.

To foster the New York agriculture and breeding industries, a portion of the takeout is allocated to the State's thoroughbred and standardbred (harness) horse breeding and development funds. During fiscal year 2000-01, $13 million and $7 million were allocated to the thoroughbred and harness funds, respectively.

Over the last two decades, the rise in OTB activity and simulcasting, which now accounts for 80 percent of the statewide handle, has been accompanied by corresponding declines in handle and attendance at racetracks.





To encourage the continuing viability of the industry, the State authorized higher takeouts to support capital improvements at non-New York Racing Association (NYRA) tracks and, more importantly, reduced its on-track tax rates by as much as 90 percent at thoroughbred and harness tracks. The State also assumed the costs for regulation and drug testing and increased the takeout on NYRA wagers involving two horses, while lowering the takeout on NYRA wagers involving one horse.

More recently, the State authorized telephone betting, in-home simulcasting experiments, expansion of simulcasting at both race tracks and OTB facilities, lowered the tax rates on simulcast wagering, eliminated the State franchise fee on nonprofit racing associations, and reduced tax rates.

SIGNIFICANT LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1994		
Tax Rates	Lowered rates on all wagers at harness tracks and at the Finger Lakes Race Association to 0.5 percent and provided credits up to 0.4 percent based on OTB simulcast handle of respective track.	September 1, 1994
Expanded Betting	Authorized widespread in-home simulcasting experiments, simulcasts of flat racing bridging the time gap between the end of New York flat racing and the beginning of harness racing, and tripled the number of out-of-State harness track simulcasts.	July 6, 1994
Breakage	Allotted the State's share of all OTB breakage to horse breeding funds.	July 6, 1994
Legislation Enacted in 1995		
Tax Rates	Lowered rate on regular bets (involving one horse) at NYRA from 5 percent to 4 percent and reduced the tax on NYRA wagers at OTB in half: from 1.1 percent to 0.5 percent on regular and multiple (involving two horses) bets, and from 3.1 percent to 1.5 percent on exotic (involving three or more) bets.	June 1, 1995
Takeout	Increased the takeout on NYRA wagers involving two horses (multiple bet) from 17 percent to 20 percent, while lowering the takeout on NYRA wagers involving one horse (regular bet) from 17 percent to 15 percent.	June 1, 1995
Legislation Enacted in 1998		
Tax Rates	Established the tax rate on all simulcast races at 1.5 percent for the initial race of the day and at 1.0 percent for later races, if NYRA is running. If NYRA is not racing, the tax rate on these races are 1.0 percent and 0.5 percent, respectively. Extended authorizations for lower tax rates for on-track and off-track bets on NYRA through June 30, 2002.	January 1, 1998
Franchise Fee	Eliminated NYRA franchise fee.	January 1, 1998
Legislation Enacted in 1999		
Tax Rates	Cut the tax rate on all NYRA bets to 2.6 percent.	September 10, 1999
	Cut the tax rate on all NYRA bets to 1.6 percent.	April 1, 2001
Legislation Enacted in 2001		
Expanded Simulcasting	Lowered the takeout on NYRA races, decreased the percentage of takeout going to purses, allowed a "pick six" wager provided two contemporaneous out-of-State simulcast signals during the Saratoga meeting and provided a third out-of-State contemporaneous simulcast signal during the winter months and provided lower State tax rates for the additional simulcast racing.	June 12, 2001

2001-02 RECEIPTS

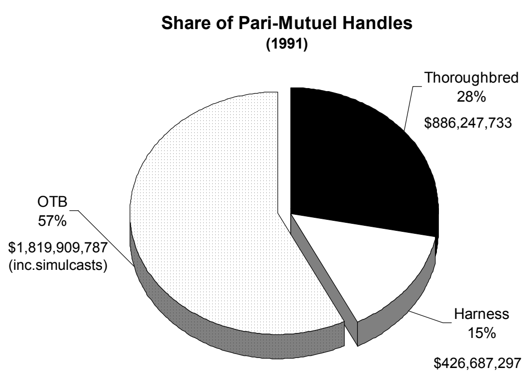
Increases in simulcast handle, especially from out-of-State races, is expected to be offset by a continued decline in on-track handle. As a result, the total 2001-02 statewide betting handle (both on- and off-track) is expected to remain largely unchanged at approximately $2.7 billion.

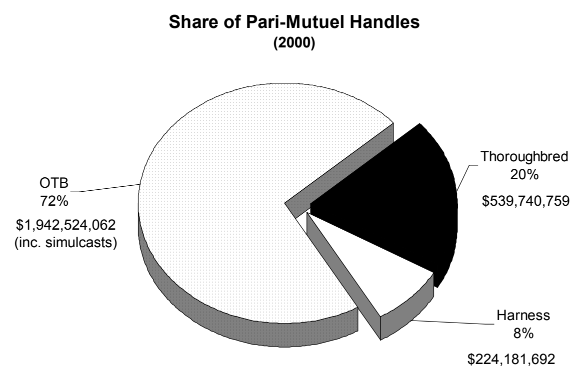
Total thoroughbred on-track handle, including simulcasts, is estimated at $578 million, down slightly from the prior year. The continuing decline in wagering on live harness races is being offset, in part, by increased simulcasting, with lower tax rates. Total harness handle is estimated at $203 million. Handle at off-track betting corporations is estimated to increase to $1.97 billion, up 1.5 percent.

Thoroughbred revenues, including simulcast receipts, are expected to decline by 32 percent to $9.6 million, largely the result of reduced tax rates. In addition, the Breeders Cup held on October 27, 2001, was a State tax exempt event that had an estimated revenue loss of $351,000 for State fiscal year 2002-03. OTB receipts are estimated to increase by 27.6 percent to $18.5 million, the increase largely reflecting the one-time loss of $3.8 million in 2000-01 receipts due to a court decision. Receipts from harness tracks are expected to increase 30 percent from $0.7 million to $0.9 million, resulting in total pari-mutuel tax receipts of $29 million.

2002-03 PROJECTIONS

The pari-mutuel projections for 2002-03 assume a full racing season. In total, State pari-mutuel tax receipts are projected at $28.9 million for 2002-03.





Total on-track thoroughbred receipts are projected to decline by 4 percent as a result of diminishing handle and attendance. A projected thoroughbred handle of $554.4 million, including betting on out-of-State races, will produce $9.2 million in tax receipts.

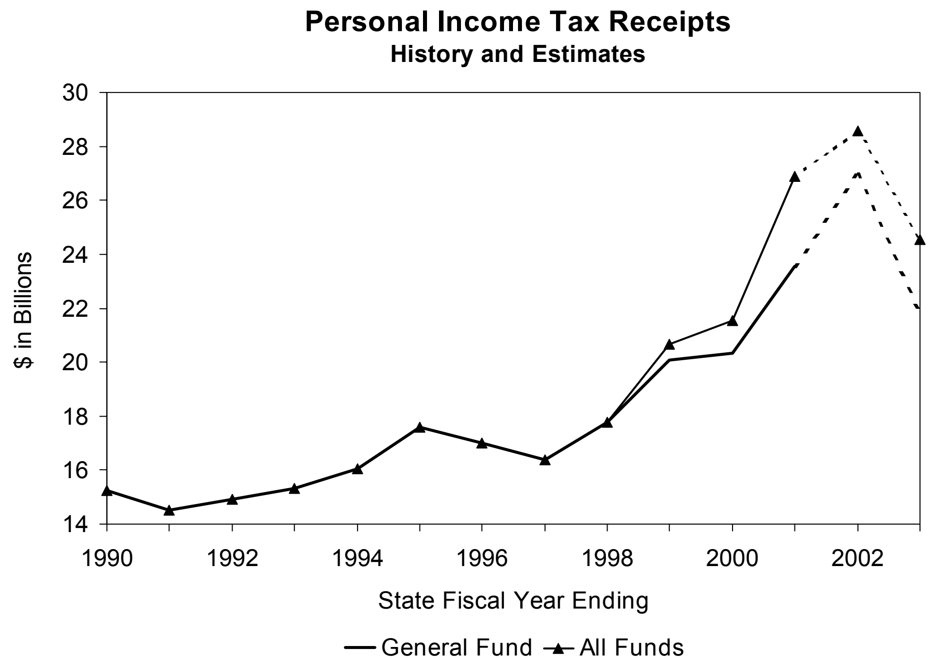
Harness racing handle is projected to decrease to $198.7 million, generating tax receipts of $0.9 million, including $0.6 million in revenue from on-track wagers and $0.3 million from simulcasting.

OTB handle is projected at $1.96 billion, producing tax receipts of $18.8 million.

PARI-MUTUEL TAXES RECEIPTS
(thousands of dollars)

	General Fund			Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Collections
	Flat	Harness	OTB				
	Actual						
1993-94	37,984	3,630	25,455	0	0	0	67,069
1994-95	34,306	2,817	20,189	0	0	0	57,312
1995-96	23,976	1,216	19,906	0	0	0	45,098
1996-97	20,417	1,075	20,124	0	0	0	41,616
1997-98	19,329	1,013	18,022	0	0	0	38,364
1998-99	18,643	923	17,355	0	0	0	36,921
1999-2000	17,218	795	18,356	0	0	0	36,369
2000-01	14,152	750	14,444	0	0	0	29,346
	Estimated						
2001-02	9,600	900	18,500	0	0	0	29,000
2002-03	9,200	900	18,800	0	0	0	28,900

PERSONAL INCOME TAX

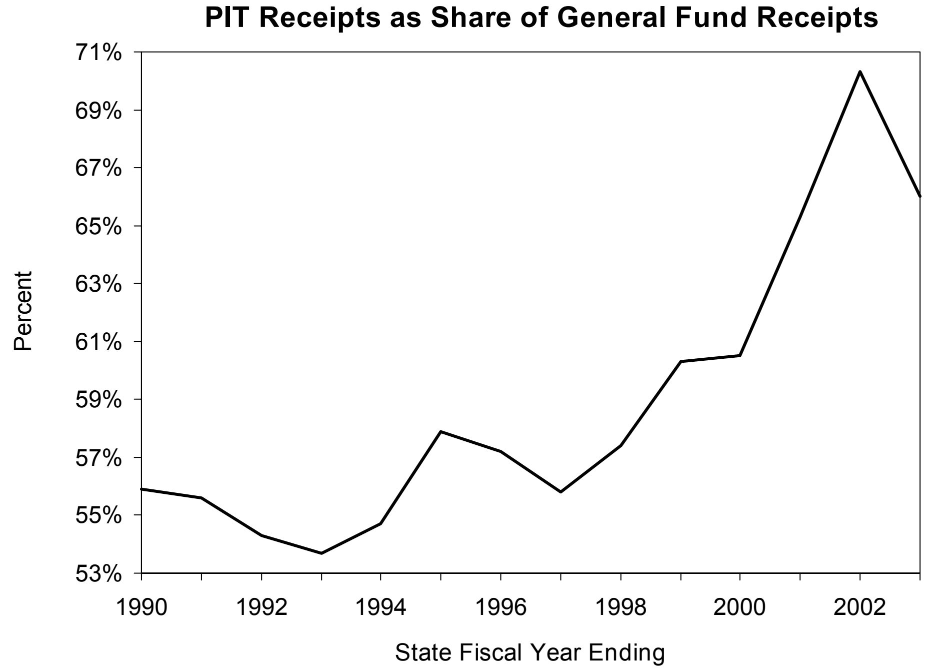


DESCRIPTION

The personal income tax is New York State's largest source of tax revenue. It is estimated that, during State fiscal years 2001-02 and 2002-03, the personal income tax will account for more than one-half of total General Fund receipts.

Over the last decade, New York has greatly simplified its tax structure by reducing the rates applied to income and increasing standard deductions. Since 1995, the overall income tax burden has been reduced by about 20 percent.

Tax Base



The State's tax structure adheres closely to the definitions of adjusted gross income and itemized deductions used for Federal personal income tax purposes, with certain modifications, such as: (1) the inclusion of investment income from debt instruments issued by other states and municipalities and the exclusion of income on certain Federal obligations; and (2) the exclusion of pension income received by Federal, New York State and local government employees, private pension and annuity income up to $20,000 ($40,000 for married couples filing jointly), and any Social Security income and refunds otherwise included in Federal adjusted gross income.

Beginning in 1991, the Federal limit on itemized deductions for taxpayers with Federal adjusted gross income (AGI) above a certain threshold is applied for State personal income tax purposes. This threshold amount, set at $100,000 ($50,000 for married couples filing separately) in 1991, was indexed for subsequent inflation. For 2001, the threshold is $132,950 ($66,475 for married couples filing separately). Allowable itemized deductions, except for medical expenses, casualty and theft losses, and interest payments, are reduced by the lower of either 3 percent of Federal adjusted gross income in excess of the threshold amount or 80 percent of allowable itemized deductions.

The Federal Economic Growth and Tax Relief Reconciliation Act of 2001 phases out the limitation on itemized deductions over four years beginning in 2006. The limitation is eliminated for 2010 and after.

Basic Tax Structure

For the 1989 through 1994 tax years, the tax was imposed at rates ranging from 4 percent to 7.875 percent on the taxable income of individuals, estates and trusts. For taxpayers with $100,000 or more of AGI, the benefit of the marginal tax rates in the lower brackets was recaptured through a supplementary mechanism in effect since 1991. In 1995, the State embarked on a major personal income tax cut program which was phased in over three years as shown below:

TABLE 1
PERSONAL INCOME TAX
TOP RATE, STANDARD DEDUCTIONS AND DEPENDENT EXEMPTIONS
1994 - 1997
(dollars)

	1994	1995	1996	1997
Top Rate	7.875%	7.59375%	7.125%	6.85%
Thresholds				
Married Filing Jointly	26,000	25,000	26,000	40,000
Single	13,000	12,500	13,000	20,000
Head of Household	17,000	19,000	17,000	30,000
Standard Deduction				
Married Filing Jointly	9,500	10,800	12,350	13,000*
Single	6,000	6,600	7,400	7,500
Head of Household	7,000	8,150	10,000	10,500
Dependent Exemption	1,000	1,000	1,000	1,000

* Legislation passed in 2000 increased the standard deduction for married couples filing jointly to $13,400 for 2001, $14,200 for 2002, and $14,600 for 2003 and after.

TABLE 2
CURRENT TAX SCHEDULES
(dollars)

Married - Filing Jointly			Single			Head of Household		
Taxable Income	Tax	of Amt. Over	Taxable Income	Tax	of Amt. Over	Taxable Income	Tax	of Amt. Over
0 to 16,000	0 +4.00%	0	0 to 8,000	0 +4.00%	0	0 to 11,000	0 +4.00%	0
16,000 to 22,000	640 +4.50%	16,000	8,000 to 11,000	320 +4.50%	8,000	11,000 to 15,000	440 +4.50%	11,000
22,000 to 26,000	910 +5.25%	22,000	11,000 to 13,000	455 +5.25%	11,000	15,000 to 17,000	620 +5.25%	15,000
26,000 to 40,000	1,120 +5.90%	26,000	13,000 to 20,000	560 +5.90%	13,000	17,000 to 30,000	725 +5.90%	17,000
40,000 and over	1,946 +6.85%	40,000	20,000 and over	973 +6.85%	20,000	30,000 and over	1,492 +6.85%	30,000

SIGNIFICANT LEGISLATION

Credits

Current law authorizes a wide variety of credits against personal income tax liability. The major credits are:

Credit	Description
Earned Income Tax Credit (EITC)	Allowed at a rate of 7.5 percent of the Federal credit in 1994, 10 percent in 1995, and 20 percent in 1996 and later. Starting in 1996, the EITC is offset by the amount of the household credit. The EITC was raised to 22.5 percent of the Federal credit in 2000, and 25 percent in 2001. It is scheduled to increase to 27.5 percent of the Federal credit for 2002, and to 30 percent of the Federal credit in 2003 and after. The credit is fully refundable for New York residents whose credit amount exceeds tax liability. The 2001 Federal Economic Growth and Tax Relief Reconciliation Act provided marriage penalty relief for married taxpayers filing jointly by increasing the phase-out range for the credit beginning in 2002.
Household Credit	Permitted for individuals in amounts declining from $75 to $20, as their household income rises to $28,000. For married couples and heads of households, in amounts declining from $90 to $20, as their household income rises to $32,000. This latter category is also eligible for additional amounts based on the number of eligible exemptions and income level. Legislation in 1995 continued the credit permanently.

Credit	Description
Child and Dependent Care Credit	Allowed at a rate of 20 percent or more of the comparable Federal credit. In 1997, the credit became refundable and equal to 60 percent of the Federal credit for those with incomes under $10,000, with a phase-down until it was 20 percent for incomes of $14,000 and above. In 1998, the percentage of the Federal credit increased to 100 percent for those with incomes less than $17,000, with this percentage gradually phasing down to 20 percent for those with incomes of $30,000 or more. For 1999, the phase-down from 100 percent to 20 percent began at incomes of $35,000 and ended at incomes of $50,000. For 2000 and later years, the credit as a share of the Federal credit equals 110 percent for incomes up to $25,000, phases down from 110 percent to 100 percent for incomes between $25,000 and $40,000, equals 100 percent for incomes between $40,000 and $50,000, phases down from 100 percent to 20 percent for incomes between $50,000 and $65,000, and equals 20 percent for incomes over $65,000. The credit is fully refundable for New York residents whose credit amount exceeds tax liability. Federal legislation passed in 2001 enriches the child and dependent care credit starting in 2003. This new legislation increases the maximum allowable expenses from $2,400 to $3,000 for one dependent ($4,800 to $6,000 for two or more dependents); the maximum credit rate from 30 percent to 35 percent; and the income at which the credit begins to phase down from $10,000 to $15,000.
Real Property Tax Circuit Breaker Credit	Based on a more inclusive definition of income than that used generally in the income tax. For eligible taxpayers over the age of 65, the credit ranges downward from $375 as income rises to $18,000; for other taxpayers, the credit can be as high as $75.
Agricultural Property Tax Credit	Permitted a credit for allowable school district property taxes paid by an eligible farmer on qualified agricultural property. A farmer must derive at least two-thirds of his or her Federal gross income from farming to be eligible. If a farmer's qualified acreage exceeds the base acreage stipulated for that tax year, the credit is reduced to less than the full amount of school property taxes paid. Base acreage is 100 acres for 1997, and 250 acres in 1998 and later tax years. Legislation in 1997, applying to 1998 and later years, extended the credit to additional farmers by: (1) altering the eligibility test to require that farm income be at least two-thirds of gross income less $30,000; (2) reducing adjusted gross income by farm debt principal payments when determining the credit phase-out; and (3) making the credit available based on sales from maple syrup, cider, and farm wineries. In 1998, the base acreage level was accelerated to 250 acres for the 1998 tax year; prior to this legislation, the 1998 base acreage level had been set at 175 acres. In 1999, legislation expanded the farmer's credit to include agricultural land set aside or retired under a Federal supply management or soil conservation program.
Rehabilitation Credit for Historic Barns	Effective for tax years starting in 1997 and after. This credit equals 25 percent of a taxpayer's qualified rehabilitation expenses incurred in restoring a pre-1936 agricultural barn.

In addition, credits are allowed for investment in certain productive facilities, for investment in economic development zones, and for personal income taxes paid to other states. Finally, the excess deduction credit was allowed in 1995 only to ease the transition to the new tax structure for taxpayers who itemized their deductions and whose taxable income was less than $24,500 ($49,000 for married couples).

Recent Statutory Changes

The following major tax law changes have had a significant impact on personal income tax receipts.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Tax Reform Deferral	Continued deferral of the remainder of the tax cut enacted in the Tax Reform and Reduction Act of 1987.	1994 tax year
Earned Income Tax Credit	Created a State credit as a percentage of the Federal amount. The rates were set at 7.5 percent of the Federal credit in 1994, 10 percent in 1995, 15 percent in 1996, and 20 percent for 1997 and after.	1994 and after
Legislation Enacted in 1995		
Standard Deduction	Increased the standard deduction over three years.	1995 and after
Tax Rate Schedule	Reduced the top tax rate from 7.875 percent to 6.85 percent and raised bracket thresholds over three years.	1995 and after
Earned Income Tax Credit	Accelerated into 1996 from 1997 the credit of 20 percent of the Federal amount, but offset it by the household credit.	1996

Subject	Description	Effective Date
Legislation Enacted in 1996		
Child and Dependent Care Credit	Increased the credit for taxpayers with adjusted gross incomes of less than $14,000 and made the credit refundable for residents beginning in 1996.	1996 and after
Agricultural Property Tax Credit	Created the credit.	1997 and after
Legislation Enacted in 1997		
Child and Dependent Care Credit	Increased credit to 100 percent of the Federal credit for incomes up to $17,000, phasing down to 20 percent for incomes of $30,000 or more.	1998 and after
Agricultural Property Tax Credit	Allowed $30,000 to be subtracted from income before calculating the percent of income from farming to qualify for the credit; subtracted principal payments on farm debt in calculation of the income to which the credit phase-out applies.	1998 and after
Solar Energy Credit	Created a credit for residential investment in solar electric generating equipment.	1998 and after
College Choice Tuition Savings Program	Created the New York State College Choice Tuition Savings Program.	1998 and after
Legislation Enacted in 1998		
Child and Dependent Care Credit	Increased the credit to 100 percent of the Federal credit for incomes up to $35,000, phasing down to 20 percent for incomes of $50,000 or more.	1999 and after
School Tax Relief Program (STAR)	Accelerated the fully effective senior citizens' school property tax exemption and began the deposit of a portion of personal income tax receipts into the STAR fund.	1998-99 school year
Legislation Enacted in 1999		
Earned Income Tax Credit	Increased the EITC to 22.5 percent of the Federal credit in 2000 and 25 percent of the Federal credit for subsequent tax years.	2000 and after
Agricultural Property Tax Credit	Expanded the credit to include land set aside or retired under a Federal supply management or soil conservation program. Also increased "base acreage" by acreage enrolled or participating in a Federal environmental conservation acreage reserve program.	2001 and after
Qualified Emerging Technology Credit (QETC)	Extended the credit to individual investors, including partners in partnerships and shareholders of subchapter S corporations.	2000 and after
Legislation Enacted in 2000		
Earned Income Tax Credit	Increased the State's EITC to 30 percent of the Federal credit over a two-year period, beginning in 2002. The expansion will first increase the EITC to 27.5 percent of the Federal credit in 2002 and then to 30 percent of the Federal credit in 2003 and after.	2002 and after
Child Care Credit	Increased the credit to 110 percent of the Federal credit for those with incomes up to $25,000, phased down from 110 percent to 100 percent for incomes between $25,000 and $40,000, equal to 100 percent for incomes between $40,000 and $50,000, phased down from 100 percent to 20 percent for incomes between $50,000 and $65,000, and equal to 20 percent for incomes greater than $65,000.	2000 and after
Long-Term Care Insurance Credit	Created a long-term care insurance credit equal to 10 percent of a taxpayer's long-term care insurance premium.	2002 and after
Marriage Penalty	Reduced the marriage penalty by increasing the standard deduction for taxpayers who are married filing jointly from $13,000 to $14,600 in three stages.	2001 and after
College Tuition Deduction/Credit	Created a deduction for the amount of tuition paid, up to $10,000, for attendance at a qualified institution of higher education. Also, the legislation provides the alternative of a refundable tax credit equal to 4 percent of such tuition. The credit will be at least the lesser of tuition paid or $200. The college tuition deduction will be implemented in four stages.	2001 and after
Petroleum Tank Credit	Created a two-year personal income tax credit of up to $500 for homeowners who remove and/or replace a residential fuel oil storage tank.	2001 and 2002

Subject	Description	Effective Date
Alternative Energy Fuel Cell Credit	Created an alternative energy fuel cell credit equal to 20 percent of the cost of purchasing and installing a fuel cell to supply power to the taxpayer's home.	2003 and after

PROPOSED LEGISLATION

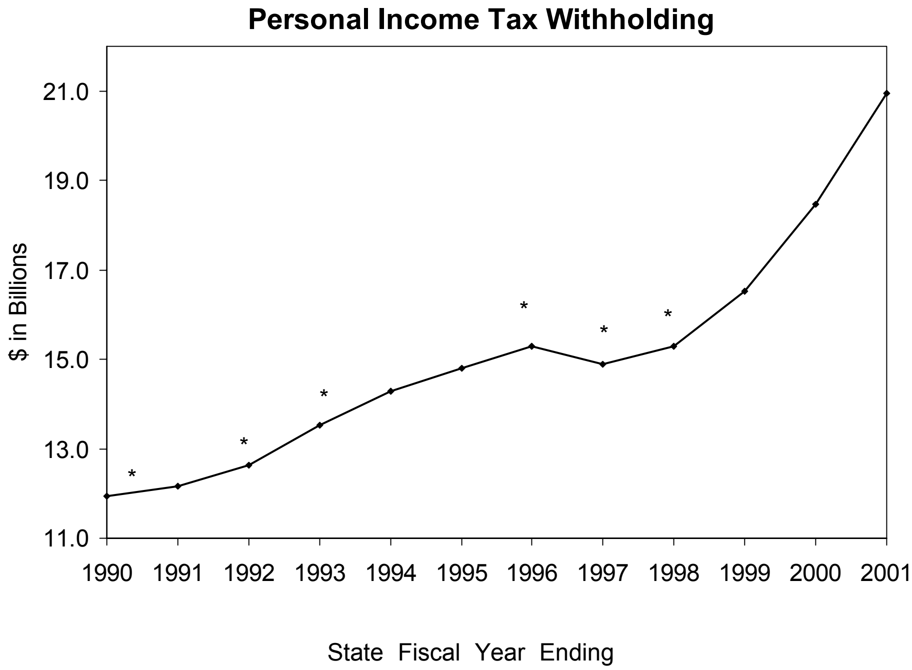
Legislation proposed with this Budget will amend withholding tax electronic funds transfer requirements, provide for a cost-of-living adjustment (COLA) for the income threshold for eligibility for enhanced STAR benefits for senior citizens, and provide technical corrections to the college tuition deduction/credit and petroleum tank credit.

In addition, new technology will allow the Department of Taxation and Finance to validate tax information more quickly, improve the selection process for identifying areas of noncompliance, and increase audit collections.

Withholding Changes

Various changes in tax rates, deductions and exemptions have been reflected in withholding tables as follows:

Effective Date	Feature	Changes
10/1/89	Deduction Allowance Rate Schedule	Increased to $5,000 for single taxpayers and to $5,500 for married taxpayers. Adopted 1989 rate schedule, with top rate at 7.875 percent.
10/1/91	Rate Schedule	Changed for taxpayers with taxable wages in excess of $90,000 annually to account for the Federal limitation on itemized deductions and for the State tax table benefit recapture.
7/1/92	Rate Schedule	Changed for taxpayers with taxable wages in excess of $150,000 annually to account for the State tax table benefit recapture.
7/1/95	Deduction Allowance Rate Schedule	Increased to $5,650 for single individuals, $6,150 for married couples. Lowered maximum rate to 7.59 percent and reduced the number of tax brackets.
4/1/96	Deduction Allowance Rate Schedule	Increased to $6,300 for single individuals, $6,800 for married couples. Lowered maximum rate to 7 percent and broadened the wage brackets to which the rates apply.
1/1/97	Deduction Allowance Rate Schedule	Increased to $6,975 for single individuals, $7,475 for married couples. Lowered maximum rate to 6.85 percent and broadened the wage brackets to which the rates apply.



The above graph shows the history of withholding collections since 1989-90. The symbol "*" indicated the timing of withholding table changes.

Refund Reserve Account Transactions

The personal income tax refund reserve account has been used to adjust fiscal-year collections for: (1) changes in withholding tables; (2) delays in implementation of withholding changes; and (3) accomplishing other State fiscal goals. The schedule shown in Table 3 traces the changes in the year-end balance of this account and the effect of those changes on reported fiscal-year collections. (Also see table 6 below for the effects of refund reserve transactions on the current and subsequent fiscal years.)

TABLE 3
MARCH 31 PERSONAL INCOME TAX REFUND RESERVE ACCOUNT BALANCES AND EFFECTS OF CHANGES ON REPORTED COLLECTIONS
(millions of dollars)

Year Ending March 31	Year End Balance	Change from Prior Year	Effect of Change in Year-End Balance on Reported General Fund Receipts
2001	3,517.4	(449.5)	Increased receipts by 449.5
2000	3,966.9	1,661.0	Decreased receipts by 1,661.0
1999	2,305.9	(86.3)	Increased receipts by 86.3
1998	2,392.2	530.4	Decreased receipts by 530.4
1997	1,861.8	1,183.5	Decreased receipts by 1,183.5
1996	678.4	400.4	Decreased receipts by 400.4
1995	278.0	(861.6)	Increased receipts by 861.6
1994	1,139.6	468.5	Decreased receipts by 468.5
1993	671.1	641.9	Decreased receipts by 641.9
1992	29.2	29.2	Decreased receipts by 29.2
1991	0.0	(48.6)	Increased receipts by 48.6
1990	48.6	48.6	Decreased receipts by 48.6

As part of the State's multi-year effort to end the Spring Borrowing through the Local Government Assistance Corporation (LGAC), State funds were deposited annually from 1993-94 through 1995-96 in the refund reserve account. The amounts deposited were $114 million in 1993-94, $136 million in 1994-95, and $271 million in 1995-96. LGAC funds in the refund reserve have totaled $521 million at the end of every year since 1995-96. At the end of 2001-02, these funds are available to finance refunds issued in the Spring of 2002, but must be restored to the reserve by March 31, 2003.

Since 1994-95, when the EITC was created, additional funds have been deposited in the refund reserve account at the end of each fiscal year to pay for a portion of the cost of new tax reductions. Typically, an amount equal to one-quarter of a tax reduction's cost for a specific tax year has been deposited in the account on the following March 31. This practice reflects the sound fiscal policy of paying for a tax reduction in a timely fashion and provides funds to pay additional refunds during April and May.

Table 4 shows the amount of reserves at the end of each fiscal year and the purposes for which the funds were reserved.

TABLE 4
PURPOSES OF MARCH 31 PERSONAL INCOME TAX REFUND RESERVE ACCOUNT BALANCES
(millions of dollars)

Date March 31 of	LGAC	Net Tax Reduction*	Reserves for Other Purposes	Total
1996	521	32	125	678
1997	521	73	1,268	1,862
1998	521	90	1,781	2,392
1999	521	7	1,778	2,306
2000	521	25	3,421	3,967
2001	521	41	2,955	3,517
2002 est.	521	91	1,133**	1,745**

* For EITC starting in 1995 (and subsequent increments), agricultural property tax credit starting in 1998, college choice tuition savings program starting in 1998, child care credit enhancements starting in 1999, marriage penalty relief, and college tuition deduction/credit starting in 2002.

** An estimated $1,133 million in 2001-02 reserves set aside for World Trade Center costs in the 2002-03 Financial Plan will be deposited to the refund reserve account on March 31, 2002. The $1,133 million is not included in personal income tax estimates for Financial Plan presentation purposes.

Timing of the Payment of Refunds

For many years, the payment of refunds during the final quarter of the State's fiscal year (i.e., the January-March period) had been explicitly modified to minimize potential year-end imbalances in the State's General Fund. This practice was made possible because the statute required merely that all refunds on timely filed claims (due no later than April 15, absent an approved request for an extension) be made by July 15 (i.e., within three months of the statutory due date) to avoid State liability for interest on late refunds. Effective since 1995, refunds must be paid within 45 days of the statutory due date to avoid State liability for interest.

Tax Tribunal Decision

In July 1997, the State's Tax Appeals Tribunal delivered a decision regarding the proper computation of State itemized deductions for certain high-income taxpayers. The new computation takes into consideration the interaction between State and Federal itemized deductions in determining State and local income taxes. The Tribunal's decision, which by law the State cannot appeal, reduces total personal income tax liability.

Components of Adjusted Gross Income and Estimated Tax Liability

Adjusted gross income (AGI), the income base used to determine personal income tax liability, includes the major components listed in Table 5.

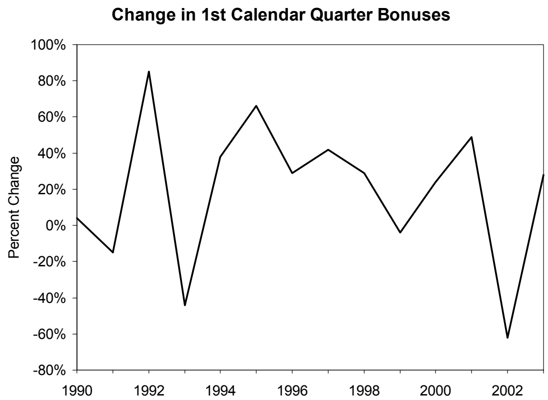
TABLE 5
DISTRIBUTION OF THE MAJOR COMPONENTS
OF NEW YORK ADJUSTED GROSS INCOME (AGI)
(millions of dollars)

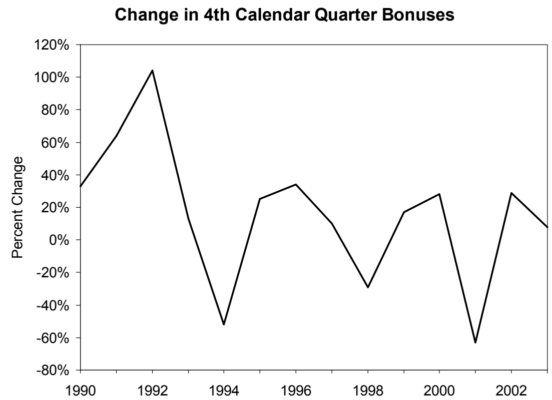
Component of Income	1994	1995	1996	1997	1998	1999	2000	2001	2002
	Actual						Estimated		
NYSAGI									
Amount	301,362	321,124	347,981	383,179	417,996	453,130	510,580	492,157	492,677
% Change	1.4	6.6	8.4	10.1	9.1	8.4	12.7	(3.6)	0.1
Wages									
Amount	242,771	253,551	266,334	285,919	309,614	328,851	363,212	376,226	370,428
% Change	2.0	4.4	5.0	7.4	8.3	6.2	10.4	3.6	(1.5)
Share of NYSAGI	80.6	79.0	76.5	74.6	74.1	72.6	71.1	76.4	75.2
Capital Gains									
Amount	12,032	14,086	22,441	31,563	38,929	48,330	62,584	39,852	45,892
% Change	(10.0)	17.1	59.3	40.7	23.3	24.1	29.5	(36.3)	15.2
Share of NYSAGI	4.0	4.4	6.4	8.2	9.3	10.7	12.3	8.1	9.3
Interest and Dividends									
Amount	19,630	22,680	23,534	24,652	24,807	25,299	26,440	22,603	22,211
% Change	5.7	15.5	3.8	4.8	0.6	2.0	4.5	(14.5)	(1.7)
Share of NYSAGI	6.5	7.1	6.8	6.4	5.9	5.6	5.2	4.6	4.5
Taxable Pension									
Amount	15,694	16,620	17,391	18,953	18,891	20,854	21,397	22,074	22,773
% Change	20.0	5.9	4.6	9.0	(0.3)	10.4	2.6	3.2	3.2
Share of NYSAGI	5.2	5.2	5.0	4.9	4.5	4.6	4.2	4.5	4.6
Business and Partnership Income									
Amount	19,666	25,868	31,425	35,288	37,142	42,035	48,559	43,562	44,402
% Change	(4.7)	31.5	21.5	12.3	5.3	13.2	15.5	(10.3)	1.9
Share of NYSAGI	6.5	8.1	9.0	9.2	8.9	9.3	9.5	8.9	9.0
All Other Incomes/ Adjustments*									
Amount	(8,430)	(11,680)	(13,142)	(13,195)	(11,387)	(12,239)	(11,612)	(12,160)	(13,029)
% Change	29.5	38.6	12.5	0.4	(13.7)	7.5	(5.1)	4.7	7.2

* Include alimony received, unemployment income, IRA income, and other incomes. This number is negative due to the Federal and New York adjustments to income, which together reduce final NYSAGI.

Strong performances in the financial sector in recent years caused a significant shift in the capital gains share of AGI. From 1994 to 2000, the share of capital gains in AGI is estimated to have more than tripled, from 4.0 percent to 12.3 percent. Over the same period, the share of wages in AGI is estimated to have decreased from 80.6 percent to 71.1 percent. Business and partnership income also shows strong growth between 1994 and 2000, although at roughly one half the rate of growth of capital gains, and accounts for an estimated 9.5 percent of AGI in 2000. The AGI data suggest that much of the rapid growth in liability in recent years can be attributed to the large increases in realized capital gains and business income.

Changes in timing of year-end bonus payments also affect the AGI growth rate. It is estimated that bonuses in the financial and insurance sector represent more than half of the total bonuses paid out each year. Under traditional patterns, about 40 percent of financial and insurance sector bonuses for a given year are paid in December, with the balance distributed in the beginning of the following year. In the 1992-93 cycle, however, a large share of the bonuses normally paid in January and February 1993 was accelerated into December 1992 to avoid potential Federal tax increases in 1993. It is estimated that as much as 75 percent of financial and insurance bonuses were paid that month. This unusual pattern recurred in the 1993-1994 period. Bonuses for 1994 through 2000, however, returned to a distribution closer to the pre-1992-93 pattern, where it is estimated that approximately 30 percent of financial and insurance bonuses were paid at the end of the calendar year, while 70 percent were paid early in the following year.





Prior to the World Trade Center disaster of September 11, 2001, an economic slowdown was already underway. The terrorist attacks shocked the struggling economy and pushed the nation into recession. (See Economic Backdrop section.) AGI grew at an average annual rate of more than 9 percent. It is expected that the poor economic performance will last into 2002 and that New York AGI will decline in 2001 and be unchanged in 2002, partially reversing the tremendous growth of AGI during the past six years.

1999 and 2000 Liability

Based on tax collections, total liability for 1999 was approximately $21.6 billion. Of this amount, $21 billion was accounted for by the 8.5 million returns covered in the annual study of personal income tax returns prepared by the New York State Department of Taxation and Finance. The balance reflects liability received from fiduciary returns, late filed returns and other transactions excluded from the annual study. The AGI amount in the tax study for 1999 was $453 billion, yielding an average effective tax rate of 4.6 percent.

As in 1997, 1998 and 1999, it is expected that the 2000 tax year saw a significant increase in income concentrated in the high income segment of taxpayers, as a result of a strong performance in the financial sector. AGI is estimated to have grown nearly 13 percent, to $511 billion, in 2000. Wages and salaries are estimated to have increased about 10.4 percent. Following 41 percent growth in 1997, 23 percent growth in 1998, and 24 percent in 1999, capital gains are estimated to have risen close to 30 percent in 2000. Interest and dividend income is estimated to have increased 4.5 percent, following growth of 2 percent in 1999. Business net income and income derived from partnerships and S corporations are expected to have risen 15.5 percent in 2000, following a 13.2 percent increase in 1999. The Economic Backdrop section provides more detail on the estimation of these AGI components.

The 1997 tax year saw the implementation of the final phase of the three-year personal income tax cut passed in June 1995. This enacted legislation raised the standard deduction and reduced the tax rate imposed on taxable income. Further legislation enacted since 1995 has increased the child and dependent care credit and the earned income tax credit. Other new credits and the New York State College Choice Tuition Savings Program were also created. These tax reductions have resulted in considerable savings for New York State taxpayers. The resulting 2000 liability, as extrapolated from the 1999 study file, is estimated to be more than $24.6 billion, yielding more than 17.5 percent growth compared to 1999. The effective tax rate is estimated to be 4.8 percent. Without the tax cuts enacted since 1995, it is estimated that liability would have been approximately $30 billion.

2001 AGI and Liability

Adjusted gross income is estimated to decrease 3.6 percent to $492 billion. Wages and salaries are estimated to increase a modest 3.6 percent. This increase reflects the healthy bonuses paid in early 2001 as a result of the strong equity market performance of the previous year. However, the employment situation deteriorated considerably during the second half of 2001. Indeed, it is estimated that the State lost about 130,000 jobs in the last quarter of 2001 as compared to the same quarter in 2000.

Interest and dividend income is estimated to have declined 14.5 percent, reflecting the several cuts in the federal funds rate by the Federal Reserve, and poor corporate earnings, after many years of extraordinary expansion. Capital gains realizations are projected to decline by approximately 36 percent in 2001 as a result of sharp declines in equity prices. Business net income and income derived from partnerships and S corporations are also estimated to have fallen 10 percent below 2000 levels.

As a result, estimated liability is projected to decrease 5.4 percent to $23.3 billion, an estimated loss of nearly $1.3 billion in revenues compared to 2000.

2002 AGI and Liability

In 2002, AGI is expected to remain flat, reflecting the continuing slowdown in the economy. Wages and salaries are projected to decrease 1.5 percent, a loss of $6 billion compared to the previous year. This decline includes the impact of job losses and an estimated reduction in financial sector bonuses of almost 50 percent.

Capital gains realizations are expected to grow 15 percent. Despite this increase, however, the amount of realizations still will be well below 1999 levels. The other components of income, in aggregate, are expected to remain essentially unchanged.

Under current law, estimated liability is projected to decline 0.6 percent to $23.2 billion, $100 million less than 2001. This decline is largely the result of the estimated decline in financial sector bonus payments paid in the first quarter of 2002.

Risks in Liability Estimates

The estimates are subject to significant risks. The national economy is in recession and vulnerable to any significant shock. The recession could be less severe or substantially more severe than expected. The stock market and financial services industry may do much better or worse than envisioned. In addition, capital gains, which represent a major component of AGI, exhibit a high degree of volatility. (See the section entitled Sources of Volatility in the Economic Backdrop section of this Appendix.)

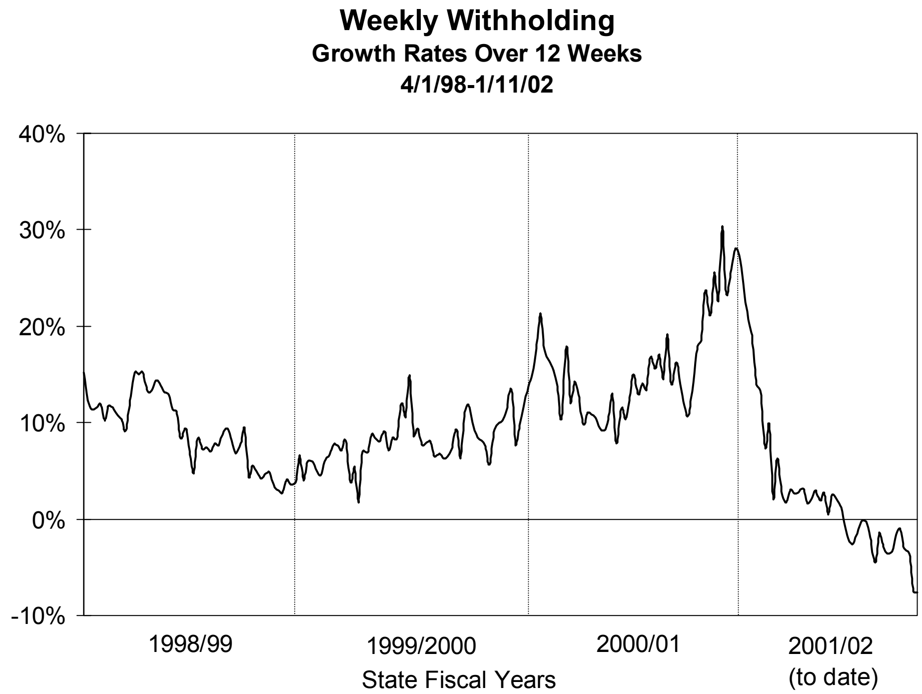
2001-02 RECEIPTS

Based on current economic conditions, net personal income tax receipts for the 2001-02 fiscal year are now estimated at $28,537 million.

Key risks for the remainder of the fiscal year include the amount of withholding tax collections to be received in the first quarter of 2002 and the balance of estimated payments to be received on 2001 liability.

The current forecast assumes that estimated payments on 2001 liability will be 15.9 percent lower than comparable payments on 2000 liability.

Withholding collections increased 0.5 percent through the first nine months of the fiscal year. As the following chart illustrates, there has been a sharp drop in withholding growth this fiscal year to date. It is expected that withholding collections will decrease 10.7 percent for the remainder of 2001-02, largely reflecting declines in bonus payments in the December to March period.



Without refund reserve transactions, net receipts are estimated at $25,632 million, a decrease of 3.1 percent from comparable 2000-01 receipts. The components of the estimate are detailed in Table 6, and are based on estimated collections of $18.9 billion through December.

TABLE 6
PROJECTED FISCAL-YEAR COLLECTION COMPONENTS
ALL FUNDS
(millions of dollars)

	2000-2001 (Actual)	2001-02 (Estimated)	2002-03 (Projected)
Receipts			
Withholdings	20,955	20,267	21,067
Estimated Payments	6,874	6,395	6,430
Current Year	5,621	4,725	5,020
Prior Year*	1,253	1,670	1,410
Final Returns	1,684	1,895	1,605
Current Year	118	120	125
Prior Year*	1,566	1,775	1,480
Delinquent Collections	558	600	720
Gross Receipts	30,071	29,157	29,822
Refunds			
Prior Year*	2,313	2,175	2,490
Previous Years	187	185	185
Current Year	960	960	960
State-City Offset*	169	205	200
Total Refunds	3,629	3,525	3,835
Reserve Transactions	450	2,905	(65)
Net Receipts	26,892	28,537	25,922

* These components, collectively, are known as the "settlement" on the prior year's tax liability.

The planned balance in the refund reserve account on March 31, 2002, is $612 million. Not included in this balance is the $1,133 million reserve for World Trade Center costs that also will be deposited in the refund reserve account on March 31, 2002. Of this amount, $521 million is attributable to Local Government Assistance Corporation (LGAC) transactions in 1993-94 ($114 million), 1994-95 ($136 million) and 1995-96 ($271 million). These transactions are part of the State's multi-year effort to end the Spring Borrowing and, while $521 million is available to finance refunds to be issued in the spring of 2002, it must be restored to the reserve by March 31, 2003. To continue the practice of depositing a portion of the cost of new personal income tax reductions in the reserve fund, $91 million in additional funds will be deposited in the reserve account on March 31.

An added risk to the estimate of 2001-02 receipts results from the timing of bonus payments paid by financial services companies. A large portion of these bonuses is paid in the first quarter of the calendar year. As a result, these results were not available when the 2001-02 estimates were constructed. An additional risk is the amount of withholding and other tax payments delayed by taxpayers affected by the WTC disaster. Although New York State allowed delays until December 10, 2001, results, to date, suggest only a small movement of cash resulting from delayed payments.

2002-03 PROJECTIONS

Based on current law, net personal income tax receipts would be expected to decrease by 9.7 percent, to $25,767 million, in 2002-03. Reported receipts include the net decrease to collections of $65 million from transactions in the refund reserve account. Not included in these receipts is the $1,133 million withdrawal from the refund reserve account that will be used for World Trade Center costs.

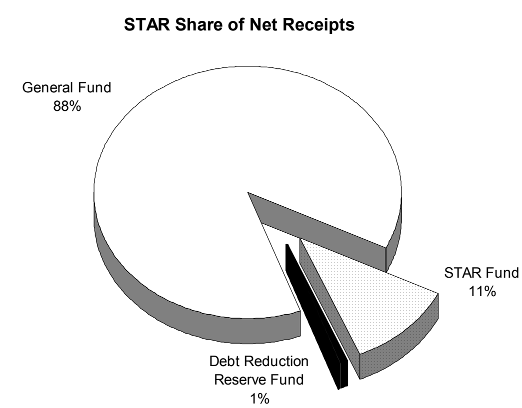
Under current law, withholding receipts would be projected to rise by 3.8 percent. Final payments related to 2001 returns are expected to decrease by $295 million from 2000 returns, reflecting the 2001 liability decrease.

The other major component of collections, estimated payments on 2002 income, will increase by 6.2 percent. This is consistent with expected non-wage income growth in 2002, the low base level of 2001 estimated tax payments, and lower growth in capital gains realizations following the high 1997 through 2000 growth rates that resulted, at least partially, from the 1997 Federal capital gains law changes.

Based on proposed law, withholding receipts are projected to rise 3.9 percent and assessment collections are projected to be $130 million higher than under current law. As a result, net personal income tax receipts are expected to decrease by 9.2 percent, to $25,922 million, in 2002-03.

OTHER FUNDS

Legislation enacted in 1998 created the School Tax Relief (STAR) Fund to help provide school tax reductions under the STAR program, accelerated the fully effective level of the enhanced senior citizens school property tax exemption into 1998-99, and accelerated the final level of the New York City personal income tax credit into the 1998 tax year for taxpayers age 65 or more. In 2001-02, dedicated personal income tax receipts of $1,310 million will be deposited into the School Tax Relief Fund. This amount is $50 million less than estimated at the time of the Mid-Year Update. In 2002-03, it is estimated that receipts of $2,630 million will be deposited into the Fund.



Personal income tax receipts of $250 million were deposited into the Debt Reduction Reserve Fund in each of the 2000-01 and 2001-02 fiscal years.

GENERAL FUND

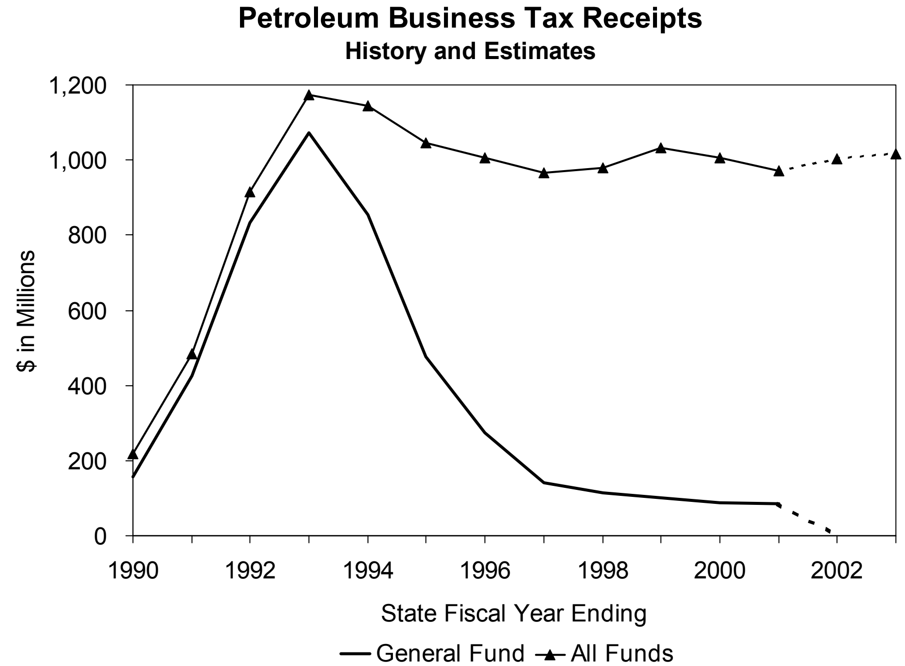
Under current law, General Fund net personal income tax receipts are estimated at $26,977 million in 2001-02 and would be estimated at $23,137 million in 2002-03. Under proposed law, General Fund net personal income tax receipts are projected at $23,292 million in 2002-03.

TABLE 7
PERSONAL INCOME TAX RECEIPTS
(millions of dollars)

	Gross General Fund	Refunds	Net General Fund Receipts	Refund Reserve Transactions	Net General Fund	Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds[2]	All Funds Net Collections
				Actual					
1993-94	18,727	2,225	16,502	468	16,034	0	0	0	16,034
1994-95	19,028	2,300	16,728	(862)	17,590	0	0	0	17,590
1995-96	19,857	2,459	17,398	400	16,998	0	0	0	16,998
1996-97	20,238	2,684	17,554	1,183	16,371	0	0	0	16,371
1997-98	21,088	2,799	18,289	530	17,759	0	0	0	17,759
1998-99	23,371	2,795	19,994	(86)	20,080	582	0	0	20,662
1999-2000	25,041	3,041	22,000	1,661	20,339	1,195	0	0	21,534
2000-01	26,744	3,629	23,115	(450)	23,565	3,077	0	250	26,892
				Estimated					
2001-02	27,597	3,525	24,072	(2,905)	26,977	1,310	0	250	28,537
2002-03									
(current law)	27,037	3,835	23,202	65	23,137	2,630	0	0	25,767
(proposed law)	27,192	3,835	23,357	65	23,292	2,630	0	0	25,922

[1] STAR Fund.
[2] Debt Reduction Reserve Fund.

PETROLEUM BUSINESS TAXES



DESCRIPTION

Article 13-A of the Tax Law imposes a privilege tax on petroleum businesses operating in the State, based upon the quantity of various petroleum products imported for sale or use in the State. The tax is collected monthly in conjunction with the State motor fuel taxes (Article 12-A). Article 13-A also imposes the petroleum business carrier tax on fuel purchased outside New York and consumed within the State. The carrier tax is collected quarterly along with the fuel use tax portion of the highway use tax. (See section titled Highway Use Tax.) Specifically exempted from Article 13-A taxes are fuel used for manufacturing, residential or not-for-profit organization heating purposes, fuel sold to governments, kerosene other than kero-jet fuel, crude oil, liquefied petroleum gas (LPG), and certain bunker fuel.

Tax Rates and Indexing

Petroleum business tax (PBT) rates have two components: the base tax, whose rates vary by product type; and the supplemental tax, which is imposed, in general, at a uniform rate. Both components are indexed to reflect petroleum price changes. (See Table 3.) Table 1 displays the per gallon PBT rates for 2001. Table 2 displays scheduled rates for 2002 and estimated rates for 2003, which reflect changes due to indexing.

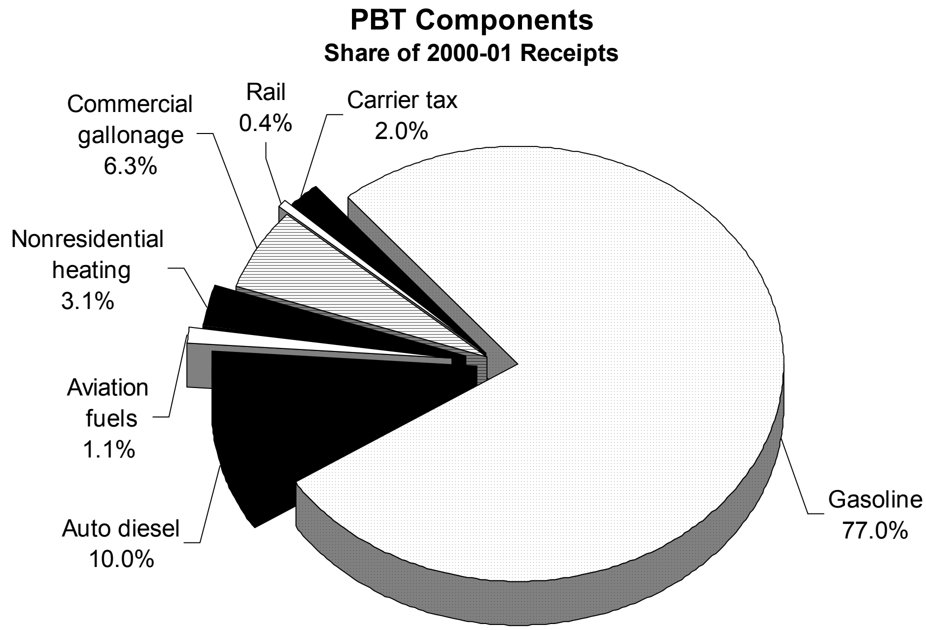
TABLE 1
PETROLEUM BUSINESS TAX RATES FOR 2001
(cents per gallon)

Petroleum Products	Jan.-Mar. 2001 Base	Supp	Total	Apr.-Dec. 2001 Base	Supp	Total
Automotive fuel						
Gasoline and other non-diesel	8.40	5.60	**14.00**	8.40	5.60	**14.00**
Diesel	8.40	3.85	**12.25**	8.40	3.85	**12.25**
Aviation gasoline	8.40	5.60	**14.00**	8.40	5.60	**14.00**
Net rate after credit	5.60	0.0	**5.60**	5.60	0.0	**5.60**
Kero-jet fuel	5.60	0.0	**5.60**	5.60	0.0	**5.60**
Non-automotive diesel fuels	7.60	5.60	**13.20**	7.60	5.60	**13.20**
Commercial gallonage after credit	7.60	0.0	**7.60**	7.60	0.0	**7.60**
Electric utility after credit	2.52	5.60	**8.12**	2.52	5.60	**8.12**
Nonresidential heating after credit	7.60	0.0	**7.60**	6.10	0.0	**6.10**
Residual petroleum products	5.90	5.60	**11.50**	5.90	5.60	**11.50**
Commercial gallonage after credit	5.90	0.0	**5.90**	5.90	0.0	**5.90**
Electric utility after credit	0.86	5.60	**6.46**	0.86	5.60	**6.46**
Nonresidential heating after credit	5.90	0.0	**5.90**	4.70	0.0	**4.70**
Railroad diesel fuel	8.40	3.85	**12.25**	8.40	3.85	**12.25**
Net rate after exemption/refund	7.10	0.0	**7.10**	7.10	0.0	**7.10**

TABLE 2
PETROLEUM BUSINESS TAX RATES FOR 2002 AND 2003
(cents per gallon)

Petroleum Products	Jan.-Aug. 2002 Base	Supp	Total	Sep.-Dec. 2002 Base	Supp	Total	2003* Base	Supp	Total
Automotive fuel									
Gasoline and other non-diesel	8.80	5.80	**14.60**	8.80	5.80	**14.60**	8.40	5.60	**14.00**
Diesel	8.80	4.05	**12.85**	8.80	4.05	**12.85**	8.40	3.85	**12.25**
Aviation gasoline	8.80	5.80	**14.60**	8.80	5.80	**14.60**	8.40	5.60	**14.00**
Net rate after credit	5.80	0.0	**5.80**	5.80	0.0	**5.80**	5.60	0.0	**5.60**
Kero-jet fuel	5.80	0.0	**5.80**	5.80	0.0	**5.80**	5.60	0.0	**5.60**
Non-automotive diesel fuels	7.90	5.80	**13.70**	7.90	5.80	**13.70**	7.60	5.60	**13.20**
Commercial gallonage after credit	7.90	0.0	**7.90**	7.90	0.0	**7.90**	7.60	0.0	**7.60**
Nonresidential heating after credit	6.30	0.0	**6.30**	4.30	0.0	**4.30**	4.10	0.0	**4.10**
Residual petroleum products	6.10	5.80	**11.90**	6.10	5.80	**11.90**	5.80	5.60	**11.40**
Commercial gallonage after credit	6.10	0.0	**6.10**	6.10	0.0	**6.10**	5.80	0.0	**5.80**
Nonresidential heating after credit	4.90	0.0	**4.90**	3.30	0.0	**3.30**	3.10	0.0	**3.10**
Railroad diesel fuel	8.80	4.05	**12.85**	8.80	4.05	**12.85**	8.40	3.85	**12.25**
Net rate after exemption/refund	7.50	0.0	**7.50**	7.50	0.0	**7.50**	7.10	0.0	**7.10**

*Projected – A fuel price decline of 12.5 percent in 2003 results in a 5 percent decline in the PBT index.



The basic and supplemental PBT tax rates are subject to separately computed annual adjustments, on January 1 of each year, to reflect the change in the producer price index for refined petroleum products for the 12 months ending August 31 of the immediately preceding year.

Early in the previous decade, PBT tax rates rose substantially due to indexing and sizable increases in the price of petroleum products. Tax rates rose about 20 percent on April 1, 1991, and by more than 16 percent on January 1, 1992. Annual legislation precluded the 1992 tax rates from being further indexed through 1995.

Legislation in 1994 provided that beginning January 1, 1996, and annually thereafter, tax rates would again be indexed, but tax rates could not increase or decrease by more than 5 percent per year. In addition to the 5 percent cap on tax rate changes, the statute required that the basic and supplemental tax rates be rounded to the nearest tenth of one cent. As a result, the percent change in tax rates usually does not exactly match the percent change in the index.

Based on the index, PBT rates for 2001 increased by 5 percent, and are scheduled to increase by another 5 percent for 2002. The index for January 1, 2003, is projected to decline by more than 5 percent, triggering a tax rate decrease of up to 5 percent for 2003. (See Tables 2 and 3.)

TABLE 3
FUEL PRICE AND PETROLEUM BUSINESS TAX INDEX
(percent change)

Year	Fuel Price	PBT Index
1992	16.47	16.47
1993	(14.40)	0.00
1994	(0.46)	0.00
1995	(8.72)	0.00
1996	4.41	4.41
1997	6.57	5.00
1998	7.96	5.00
1999	(18.60)	(5.00)
2000	(7.85)	(5.00)
2001	55.84	5.00
2002	13.54	5.00
2003*	(12.51)	(5.00)

* Estimated

Payments

Under 1992 legislation, businesses with yearly motor fuel and petroleum business tax liability of more than $5 million are required to remit, using electronic funds transfer, their total tax liability for the first 22 days of the month, within three business days after that date. Taxpayers can choose to make either a minimum payment of three-fourths of the comparable month's tax liability for the preceding year, or 90 percent of actual liability for the 22 days. The tax for the balance of the month is paid with the monthly returns filed by the twentieth of the following month.

SIGNIFICANT LEGISLATION

Numerous statutory changes have been made to the petroleum business tax during the last several years. The following is a list which summarizes the major legislation affecting petroleum business tax collections since 1994.

Subject	Description	Effective Date
Legislation Enacted in 1995		
Aviation Fuels	Effectively eliminated the supplemental tax imposed on aviation gasoline and kero-jet fuel and reduced the base tax rate for those products to a rate that is equivalent to the statutory supplemental tax rate. To maintain the first import system, which imposes the petroleum business tax on aviation gasoline upon importation, and still allow retail sellers of aviation gasoline to sell such product at a reduced rate, distributors of aviation gasoline must remit the full tax imposed on that product and may subsequently take a credit for the difference between the full rate and the reduced rate.	September 1, 1995
Not-for-profit Organizations	Provided full exemption for heating fuel that is for the exclusive use and consumption of certain not-for-profit organizations.	January 1, 1996
Legislation Enacted in 1996		
Railroads	Exempted diesel motor fuel used for railroads from the supplemental portion of the tax and reduced the base rate by 1.33 cents per gallon.	January 1, 1997
Commercial Heating	Provided full exemption from the supplemental tax imposed on distillate and residual fuels used by the commercial sector for heating.	March 1, 1997
Manufacturing	Expanded to a full exemption, the partial exemption provided for residual and distillate fuels used in manufacturing.	January 1, 1998
Diesel Supplemental Tax	Reduced by three-quarters of one cent per gallon the supplemental tax imposed on diesel motor fuel.	January 1, 1998
	Reduced by an additional one cent per gallon the supplemental tax imposed on diesel motor fuel.	April 1, 1999
Utilities	Increased by one-half cent per gallon the base tax credit for residual and distillate fuels used by utilities to generate electricity.	April 1, 1999

Subject	Description	Effective Date
Legislation Enacted in 1997		
Vessels	Created a credit or refund for fuel used in vessels that was purchased in the State and consumed outside the State; clarified that the export credit/refund applies to export for use, as well as sale; stated that the legal incidence of the tax is on consumers; and limited the judicial remedies available to taxpayers.	April 1, 1984
Legislation Enacted in 1999		
Commercial Heating	Reduced by 20 percent the petroleum business tax rates on commercial gallons for space heating.	April 1, 2001
Mining and Extraction	Provided for reimbursement of petroleum business tax imposed on fuels used for mining and extraction.	April 1, 2001
Legislation Enacted in 2000		
Minimum Tax	Eliminated the minimum taxes on petroleum businesses and aviation fuel businesses under the PBT.	March 1, 2001
Commercial Heating	Reduced by 33 percent the petroleum business tax rates on commercial gallons for space heating.	September 1, 2002

In past years, revenues from the petroleum business tax have been shared by the General Fund and the Mass Transportation Operating Assistance Fund (MTOAF). Prior to the 1990 revisions, the General Fund received 72.7 percent and MTOAF received 27.3 percent or a guaranteed amount. The 1990 statute converted the tax from a gross receipts tax to a cents-per-gallon tax, expanded the tax yield, and limited the MTOAF share to slightly more than 17.7 percent of the nonsurcharge revenues — the dollar equivalent of its share prior to the expansion. Carrier tax receipts were deposited in the General Fund until April 1, 2001.

Separate 1991 transportation legislation provided that on and after April 1, 1993, 100 percent of the supplemental tax and a portion of the base tax (see Table 4) would be split between the Dedicated Mass Transportation Trust Fund and the Dedicated Highway and Bridge Trust Fund.

Legislation enacted in 2000 redistributed PBT receipts. Effective April 1, 2001, all PBT General Fund receipts, including carrier tax receipts, were redistributed to the Dedicated Highway and Bridge Trust Fund and the Dedicated Mass Transportation Trust Fund.

Statutory changes to the allocation of the PBT by fund type are reported in Table 4.

TABLE 4
PBT BASE TAX FUND DISTRIBUTION
(percent)

Effective Date	General Fund	MTOAF[1]	Dedicated Funds Pool[2]
Prior to April 1, 1993	82.3	17.7	0.0
April 1, 1993	28.3	17.7	54.0
September 1, 1994	22.4	18.6	59.0
September 1, 1995	18.0	19.2	62.8
April 1, 1996	17.4	19.3	63.3
January 1, 1997	14.5	19.3	66.2
January 1, 1998	12.4	19.5	68.1
April 1, 1999	10.7	19.5	69.8
April 1, 2001	0.0	19.7	80.3

[1] This fund is split between the Public Transportation System Operating Assistance Account and the Metropolitan Mass Transportation Operating Assistance Account.
[2] This pool is split between the Dedicated Mass Transportation Trust Fund (37 percent) and the Dedicated Highway and Bridge Trust Fund (63 percent).

2001-02 RECEIPTS

Petroleum business tax receipts derived from motor fuel and diesel motor fuel are estimated to follow the same consumption trends as fuel subject to the motor fuel excise tax. (See section titled Motor Fuel Tax.) Residual fuels used by utilities are estimated to decrease due to the increase in the relative price of residual fuel oil compared to natural gas.

Collections to date, including audit receipts, surcharges and the carrier tax, are \$732.5 million, 0.6 percent above comparable receipts in 2000-01. Based on these collection trends, petroleum business tax receipts for the year are estimated at \$1,002 million. The estimate of receipts for 2001-02 reflects the 5 percent increase in PBT rates that took effect on January 1, 2001, and another scheduled 5 percent increase effective January 1, 2002. Due to the World Trade Center disaster, fewer tax enforcement resources will be available in the short-term to deter the illegal importation of fuel into the State. This could result in a small loss of receipts during the remaining months of 2001-02.

2002-03 PROJECTIONS

The forecast assumes a small increase in gasoline consumption and no growth in diesel consumption. The demand for residual fuels consumed by utilities is projected to decrease due to higher residual fuel prices relative to natural gas prices.

Projected 2002-03 receipts of \$1,016.0 million assume that fuel inventories will remain stable. The estimate also reflects 2000 legislation that reduced taxes on commercial heating by 33 percent and eliminated PBT minimum taxes. In addition, receipts for 2002-03 anticipate that the index used to set PBT tax rates in January 2003 will decline by 5 percent.

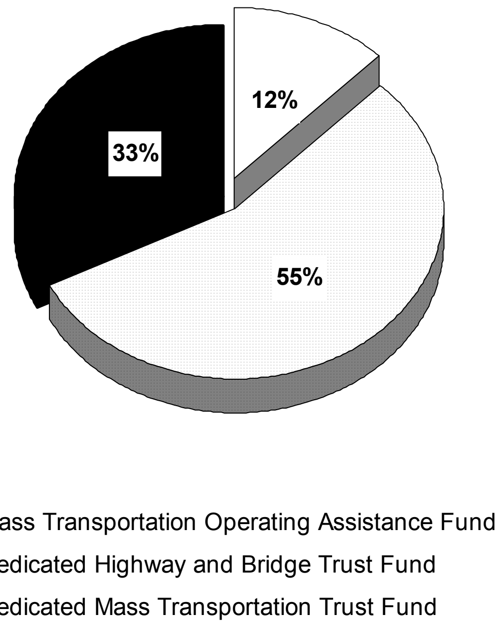
OTHER FUNDS

In 2000-01, the petroleum business tax provided MTOAF receipts of \$108.2 million, Dedicated Highway and Bridge Trust Fund receipts of \$489.3 million, and Dedicated Mass Transportation Trust Fund receipts of \$287.4 million.

Legislation enacted in 2000 significantly increased the flow of PBT funds to the Dedicated Funds Pool. Effective April 1, 2001, all PBT receipts previously deposited in the General Fund, including the balance of the basic tax and the carrier tax, are now deposited in the Dedicated Funds Pool. As a result, petroleum business tax receipts in 2001-02 are estimated to be \$117.2 million for MTOAF, \$557.4 million for the Dedicated Highway and Bridge Trust Fund, and \$327.4 million for the Dedicated Mass Transportation Trust Fund.

Petroleum business taxes in 2002-03 are projected to provide MTOAF receipts of \$118.9 million, Dedicated Highway and Bridge Trust Fund receipts of \$565.2 million, and Dedicated Mass Transportation Trust Fund receipts of \$331.9 million.

PBT Receipts 2001-02 and 2002-03



GENERAL FUND

In 2000-01, petroleum business tax receipts of $86.2 million were deposited in the General Fund.

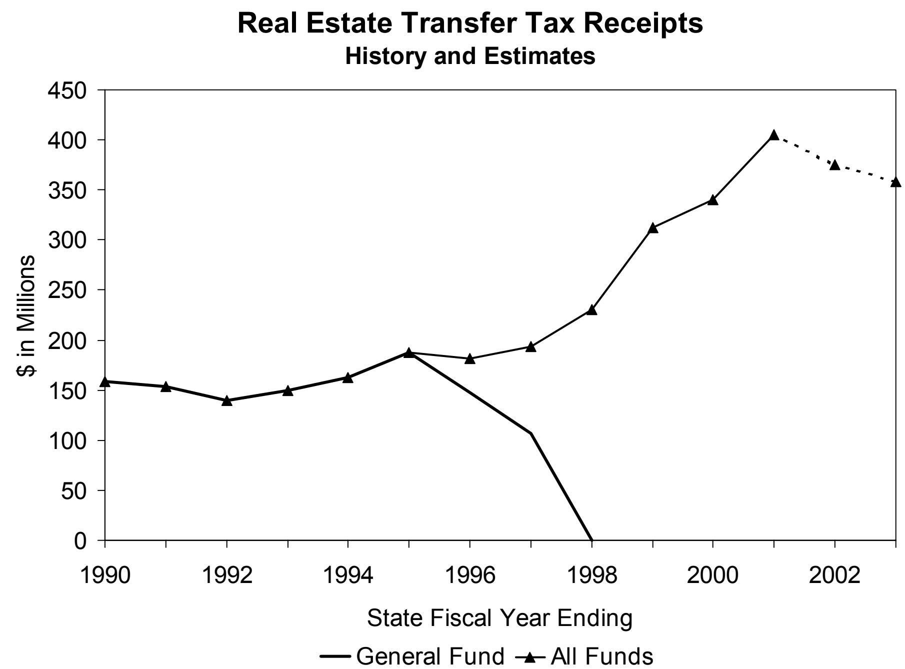
Legislation enacted in 2000 provided that all PBT receipts deposited in the General Fund be deposited in the Dedicated Funds Pool, effective April 1, 2001. As a result, no PBT receipts will be deposited in the General Fund in 2001-02 and 2002-03.

PETROLEUM BUSINESS TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Gross Special Revenue Funds[1]	Refunds	Net Special Revenue Funds[1]	Gross Capital Projects Funds[2]	Refunds	Net Capital Projects Funds[2]	All Funds Net Collections
	Actual									
1993-94	870,846	16,218	854,628	240,167	4,473	235,694	56,070	1,044	55,026	1,145,348
1994-95	482,522	7,558	474,964	347,434	5,442	341,992	232,626	3,644	228,982	1,045,938
1995-96	275,989	3,439	272,550	303,167	3,778	299,389	429,192	5,349	432,843	1,004,782
1996-97	143,469	2,570	140,899	379,155	6,791	372,364	462,341	8,281	454,060	967,323
1997-98	116,573	2,477	114,096	396,454	8,424	388,030	486,846	10,345	476,501	978,627
1998-99	103,247	1,218	102,029	422,123	4,742	417,381	519,132	5,829	513,303	1,032,713
1999-2000	90,297	1,146	89,151	414,867	4,810	410,057	511,595	5,932	505,663	1,004,871
2000-01	88,252	2,031	86,221	404,909	9,319	395,590	500,813	11,527	489,286	971,097
	Estimated									
2001-02	0	0	0	454,600	10,000	444,600	569,400	12,000	557,400	1,002,000
2002-03	0	0	0	456,600	5,800	450,800	572,400	7,200	565,200	1,016,000

[1] Dedicated Mass Transportation Trust Fund and Mass Transportation Operating Assistance Fund.
[2] Dedicated Highway and Bridge Trust Fund.

REAL ESTATE TRANSFER TAX



DESCRIPTION

The New York State real estate transfer tax is imposed by Article 31 of the Tax Law on each conveyance of real property or interest therein, when the consideration exceeds $500, at a rate of $4 per $1,000 of consideration. Prior to May 1983, the rate was $1.10 per $1,000 of consideration. The tax became effective August 1, 1968. An additional tax, effective July 1, 1989, is imposed on conveyances of residential real property for which the consideration is $1 million or more. The rate is 1 percent of the consideration attributable to residential property.

Typically, the party conveying the property (grantor) is responsible for payment of the tax, either through the purchase of adhesive documentary stamps, by the use of a metering machine or through other devices provided by the Commissioner of Taxation and Finance.

The tax rate imposed on conveyances into new or existing real estate investment trusts is $2 per $1,000 of consideration. New York State (including agencies, instrumentalities, subdivisions, and public corporations), the United States (including agencies and instrumentalities), and the United Nations are exempt. If an exempt entity is the grantor in a transfer, the tax burden falls upon the grantee. Significant exemptions from the tax are: conveyances to an exempt governmental agency, conveyances pursuant to the Federal bankruptcy act, and mere change of identity conveyances. A deduction from taxable consideration is allowed for any lien or encumbrance remaining at the time of sale involving a one-, two-, or three-family house or individual residential condominium unit.

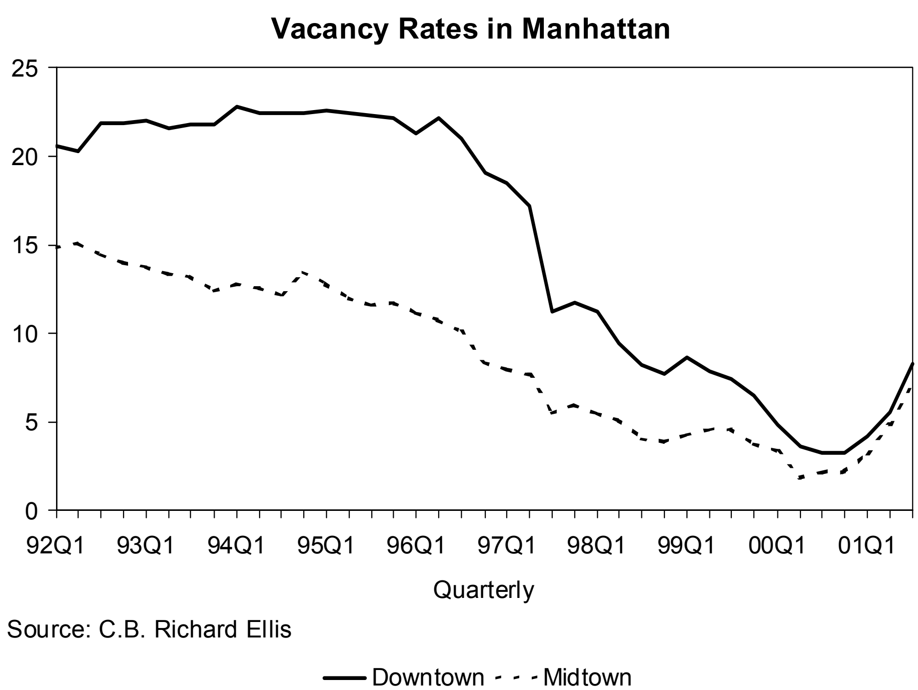
Administration

For deeded transfers, the tax is paid to a recording agent (generally, the county clerk). For non-deeded transactions, payments are made directly to the Commissioner of Taxation and Finance. All payments are due to the recording agent within 15 days of the transfer. For counties with more than $1.2 million in liability during the previous calendar year, payments received between the first and fifteenth day of the month are due to the Commissioner by the twenty-fifth day of the same month. Payments received in such counties between the sixteenth and the final day of the month are due to the Commissioner by the tenth day of the following month. Payments from all other counties are due to the Commissioner by the tenth day of the month following their receipt. Although the county payment schedule is statutory, it is not useful for predicting monthly cash flows due to the unpredictable payment behavior of some large counties.

2001-02 RECEIPTS

Reported collections to date are $296.6 million, an increase of 2 percent from 2000-01 collections for the comparable period. The increase is largely due to New York City remitting payments faster in 2001-02 than in 2000-01.

The sales of Rockefeller Center, the Lehman Brothers Building, and the payment associated with the July 2001 transfer of the World Trade Center are expected to boost 2001-02 receipts by approximately $21.3 million. These large transactions masked the relative weakness in the underlying fundamentals affecting receipts. During the first half of the fiscal year, the number of transfers were below year-ago levels and prices were virtually flat. For the remainder of the year, both the number of transfers and prices are expected to be below year-ago levels. The non-residential market, driven largely by the Manhattan commercial market, slowed in 2001-02. The decline in demand for office space was characterized by the exit of unprofitable companies from the commercial real estate market. The vacancy rate, which had declined steadily since 1994, began increasing early in 2001. Despite the loss of a significant amount of office space in downtown Manhattan due to the World Trade Center disaster, the downtown vacancy rate was actually higher in September 2001 (after the disaster) than in August 2001. The reasons for this phenomenon according to C.B. Richard Ellis, an international real estate company, were that: the market was already weak before the attack, firms are leasing space outside the City, firms are implementing pre-disaster plans to cut spending, and companies are using or renting “shadow space” that was vacant but rented before the disaster.



FISCAL YEAR LIABILITY THROUGH SEPTEMBER
(millions of dollars)

Region	2000-01 Liability	2001-02 Liability	Percent Change
Manhattan	37.5	38.1	1.5
Other Four Boroughs	27.7	25.5	(8.1)
Long Island	40.1	37.3	(7.0)
Rest of State	63.1	52.6	(16.6)
Central Office*	38.5	37.6	(2.3)

* Through October

Collections for the remainder of the fiscal year are expected to be $78.4 million, a decline of 31.2 percent from 2000-01 collections for the same period. The large decline is due largely to a payment error which caused $18.5 million in 2001-02 cash receipts to be reported as 2000-01 cash receipts. Net All Funds receipts are estimated at $375 million, down 7.3 percent from the prior fiscal year.

2002-03 PROJECTIONS

Mortgage rates are expected to rise somewhat in 2002-03. Accordingly, taxable residential transactions are expected to decline. Residential prices are expected to rise slightly. The factors which negatively affected nonresidential receipts during 2001-02 will continue to do so in 2002-03. Net All Funds receipts are expected to decrease $16.4 million or 4.4 percent, to $358.6 million.

OTHER FUNDS

During 2001-02 and 2002-03, the statutory amount of real estate transfer tax receipts diverted to the Environmental Protection Fund is $112 million. The remainder of real estate transfer tax receipts, estimated at $263 million in 2001-02 and $246.6 million in 2002-03, are to be deposited in the Clean Water/Clean Air Bond Debt Service Fund.

GENERAL FUND

The General Fund will receive no direct deposit of real estate transfer tax receipts in 2001-02 or 2002-03. However, the balance of the Clean Water/Clean Air Fund, not needed for debt service, is transferred to the General Fund.

REAL ESTATE TRANSFER TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds[1]	Gross Debt Service Funds[2]	Refunds	Debt Service Funds[2]	All Funds Net Collections
					Actual				
1993-94	163,174	618	162,556	0	0	0	0	0	162,556
1994-95	187,801	278	187,523	0	0	0	0	0	187,523
1995-96	148,505	307	148,198	0	33,500	0	0	0	181,698
1996-97	107,859	371	107,488	0	87,000	0	0	0	194,488
1997-98	0	0	0	0	87,000	142,747	115	142,632	229,632
1998-99	0	0	0	0	112,000	200,383	14	200,369	312,369
1999-2000	0	0	0	0	112,000	229,334	1,104	228,230	340,230
2000-01	0	0	0	0	112,000	293,181	436	292,745	404,745
					Estimated				
2001-02	0	0	0	0	112,000	263,500	500	263,000	375,000
2002-03	0	0	0	0	112,000	247,100	500	246,600	358,600

[1] Environmental Protection Fund.
[2] Clean Water/Clean Air Bond Debt Service Fund.

REPEALED TAXES

GIFT TAX

Until the gift tax repeal on January 1, 2000, New York was one of five states that imposed a gift tax as a complement to the transfer tax on estates to equalize the tax burden on lifetime transfers. Like the estate tax, the base of this levy was derived from the Federal tax base, with exclusions for transfers of property located outside the State. The tax was imposed on a lifetime basis — taxable gifts made during a taxpayer's lifetime, after allowable exclusions, were taxed in aggregate as one gift.

2001-02 Receipts and 2002-03 Projections

Net gift tax collections to date are $4.3 million. Net collections for 2001-02 are expected to be $4.5 million, consisting of $5.6 million in gross receipts and $1.1 million in refunds. No receipts are expected for 2002-03, or for any subsequent fiscal year.

CONTAINER TAX

From September 1, 1990, until November 30, 1995, New York State imposed a two-cent tax on all nonrefillable soda containers that are in the State's bottle and can recycling deposit system. The deposit system was created in 1983 by the New York State Returnable Container Law, which imposes a refundable five-cent deposit on bottles and cans of soda and beer, as well as wine cooler containers. Legislation enacted in 1995, effective December first of that year, cut the container tax to one cent per container. Legislation enacted in 1997 repealed the container tax effective October 1, 1998.

2001-02 Receipts and 2002-03 Projections

Container tax receipts for State fiscal year 2001-02 are negligible. This reflects the repeal of the tax effective October 1, 1998, and the net effect of audit collections and refunds. Receipts for 2002-03 are projected to be zero.

REAL PROPERTY GAINS TAX

The real property gains tax, enacted in 1983, was repealed on July 13, 1996. All property transferred after June 15, 1996, is exempt from the provisions of the real property gains tax. This tax was levied at a rate of 10 percent of the gain from sales of New York commercial property of $1 million or greater, including anything of value arising from land ownership, such as air rights or zoning credits. This tax was unique to New York State, and its elimination has made real property located in New York more appealing to investors.

2001-02 Receipts and 2002-03 Projections

Remaining collections stem primarily from deferred installment payments for tax liability arising from sales of condominium and cooperative housing for projects that were still being sold at the time of the gains tax repeal and collections from assessments processed through the Case and Resource Tracking System (CARTS). To date, these collections are $4.3 million, with an additional $1.2 million expected by the end of the State fiscal year. Total refunds for the year are estimated to be negligible. As a result, net real property gains tax collections for 2001-02 are estimated to be $5.5 million.

Collections from outstanding installments and CARTS will produce a projected $2.1 million in 2002-03. Refunds will be negligible.

HOTEL OCCUPANCY TAX

From June 1, 1990, through August 31, 1994, New York State imposed a special hotel and motel occupancy tax at the rate of 5 percent of the daily charge for hotel or motel rooms or suites. Exemptions were provided for permanent residents and for rooms where the daily rate was less than $100.

On September 1, 1994, the State repealed the State hotel and motel occupancy tax. State and, to a lesser extent, City hotel tax reductions have been credited with making New York City more attractive to tourists and convention planners.

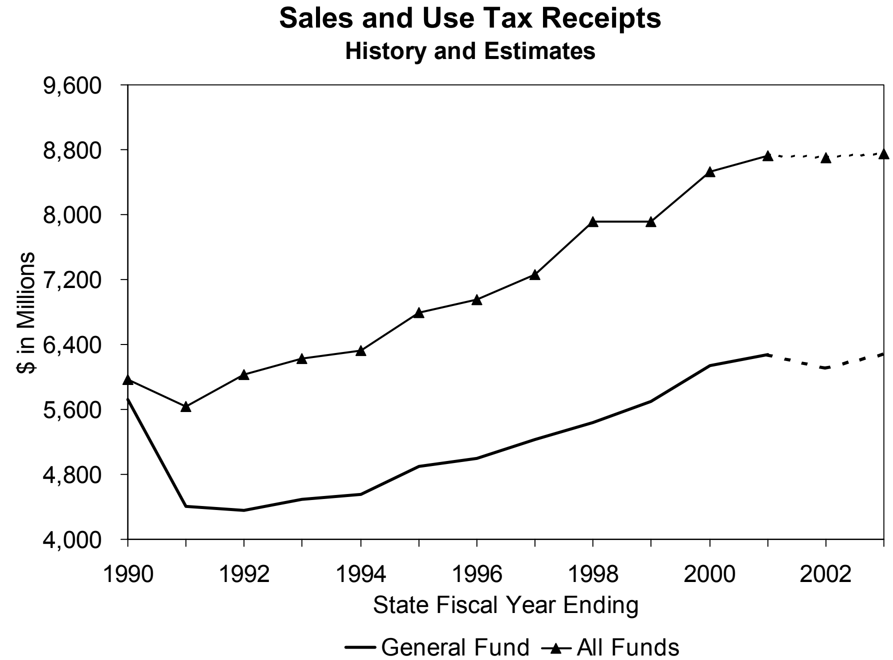
2001-02 Receipts and 2002-03 Projections

Hotel occupancy tax receipts for State fiscal year 2001-02 are expected to be negligible. Net residual payments for 2002-03 are projected to be zero.

REPEALED TAXES RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Net Collections
				Actual			
1993-94	323,505	30,035	241,853	0	0	0	241,853
1994-95	286,521	26,555	208,720	0	0	0	208,720
1995-96	320,930	47,010	228,319	0	0	0	228,319
1996-97	198,442	31,963	140,982	0	0	0	140,982
1997-98	201,143	38,572	135,532	0	0	0	135,532
1998-99	184,301	11,309	154,033	0	0	0	154,033
1999-2000	109,442	15,107	94,327	0	0	0	94,327
2000-01	53,183	5,548	47,628	0	0	0	47,628
				Estimated			
2001-02	11,120	1,120	10,000	0	0	0	10,000
2002-03	2,110	10	2,100	0	0	0	2,100

SALES AND USE TAX



DESCRIPTION

The sales and compensating use tax, which accounted for over 17.4 percent of 2000-01 General Fund revenues, not including transfers from other funds, is the second largest State tax revenue source (the personal income tax is the largest). The tax is levied on sales or uses within the State of most tangible personal property and on selected services.

Tax Rate

The tax, imposed by Article 28 of the Tax Law, was enacted in 1965 at the rate of 2 percent. The tax rate was increased to 3 percent in 1969 and to the current 4 percent rate in 1971.

Counties and cities are authorized to impose the tax at up to a combined 3 percent rate. However, 20 counties and 4 cities (including New York City) have sought and received temporary legislative authority to impose at a higher rate. Thus, the combined State-local sales and use tax rate exceeds 7 percent in many instances. More than 70 percent of the State's population resides in areas where the tax rate is 8 percent or higher. An additional 0.25 percent sales and use tax is imposed in the 12-county Metropolitan Commuter Transportation District (MCTD). The entire proceeds from the MCTD tax are earmarked for the Mass Transportation Operating Assistance Fund (MTOAF).

Base of Tax

In general, all retail sales of tangible personal property are taxed unless specifically exempt, but services are taxable only if they are enumerated in the Tax Law.

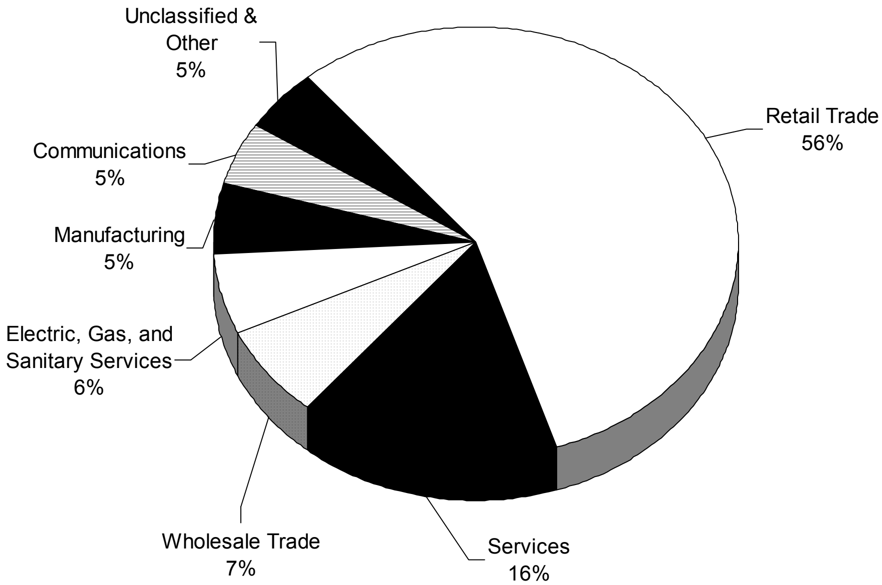
Specifically, the sales tax is applied to receipts from the retail sale of:

- tangible personal property (unless specifically exempt);
- certain gas, electricity, refrigeration and steam, and telephone service;
- selected services;

- food and beverages sold by restaurants, taverns and caterers;
- hotel occupancy; and
- certain admission charges and dues.

Examples of taxable services include hotel accommodations, installing or maintaining tangible personal property, and protective and detective services. An additional 5 percent sales tax is imposed on the receipts from the sale of telephone entertainment services that are exclusively delivered aurally.

Industry Shares of Taxable Sales and Purchases
March 1999 to August 1999



Although numerous exemptions of tangible personal property from tax have been enacted (see discussion below), 56 percent of total taxable sales and purchases subject to the use tax are accounted for by the retail trade industry. This includes, for example, automobile dealers, eating and drinking establishments, and general merchandise stores. The service industry, including hotels, automobile repair and business services, at 16 percent of the statewide total, accounts for the next largest share of taxable sales and purchases.

States are currently constrained by United States Supreme Court decisions limiting which out-of-state vendors can be required to collect the sales tax on a state's behalf. In general, a vendor must have some physical presence or nexus in a state to be required to collect that particular state's sales tax. Thus, a compensating use tax complements the sales tax, and is imposed on the use of taxable property or services in-state, if the transaction has not already been subject to tax. This would include, for example, taxable items purchased via mail order or over the Internet if the vendor has no taxable nexus with New York. The use tax also applies to certain uses of self-produced property or services. With some exceptions, the base of the use tax mirrors the base of the sales tax. The use tax is remitted by the purchaser directly to the New York State Department of Taxation and Finance, but low compliance for certain transactions is a continuing issue.

Exemptions

A myriad of exemptions from the sales tax have been enacted over the life of the tax. Broad exemptions have been provided for sales for resale and for machinery and equipment used in production or in research and development. These exemptions prevent multiple taxation of the same property or tax pyramiding. Additionally, items including food, medicines, medical supplies, residential energy, and clothing and shoes costing less than $110 have been excluded from the sales tax to reduce the regressivity of the tax.[1]

Other exemptions, such as sales to exempt organizations, certain vending machine sales and certain other coin-operated sales, are also provided. Legal, medical and other professional services, sales of real property, and rental payments are also beyond the scope of the sales tax.

Administration

Persons selling taxable property or services are required to register with the Department of Taxation and Finance as sales tax vendors. Vendors generally are required to remit the tax quarterly. However, vendors who collect more than $300,000 of tax in one of the immediately preceding four quarters must remit the tax monthly, by the twentieth of the month following the month of collection. Vendors collecting less than $3,000 yearly may elect to file annually, in June. Prior to June 1998, the threshold for opting to file annually was $250 in tax collected.

Vendors collecting more than $1 million annually in State and local tax are required to remit the tax by electronic funds transfer (EFT). Collections for the first 22 days of the month must be remitted electronically or by certified check within three business days thereafter. Legislation enacted in 1992 started the EFT program, originally with the threshold for mandatory participation at $5 million in annual tax liability. Legislation in 1994 and 1995 reduced the threshold to $4 million and to the current $1 million threshold, respectively. Approximately 34 percent of the tax is remitted via EFT. This Budget proposes to lower the EFT filing threshold to $500,000.

To reduce tax evasion, special provisions for remitting the sales tax on gasoline motor fuel and cigarettes have been enacted. Since 1985, the sales tax on gasoline has been remitted by the first importer of the fuel into New York. The tax is prepaid at a per gallon rate based on regional prices. Legislation, enacted in 1995, required prepayment of the sales tax on cigarettes. The tax is prepaid by cigarette agents at the same time as they pay for cigarette excise tax stamps.

Sales tax vendors are allowed to retain a portion of the sales tax that they have collected both as partial compensation for the administrative costs of collecting and remitting the tax and as an incentive for timely payment of the tax to the State. The vendor allowance, enacted in 1994, is currently 3.5 percent of tax liability up to a maximum of $150 per quarter for returns filed on time.

SIGNIFICANT LEGISLATION

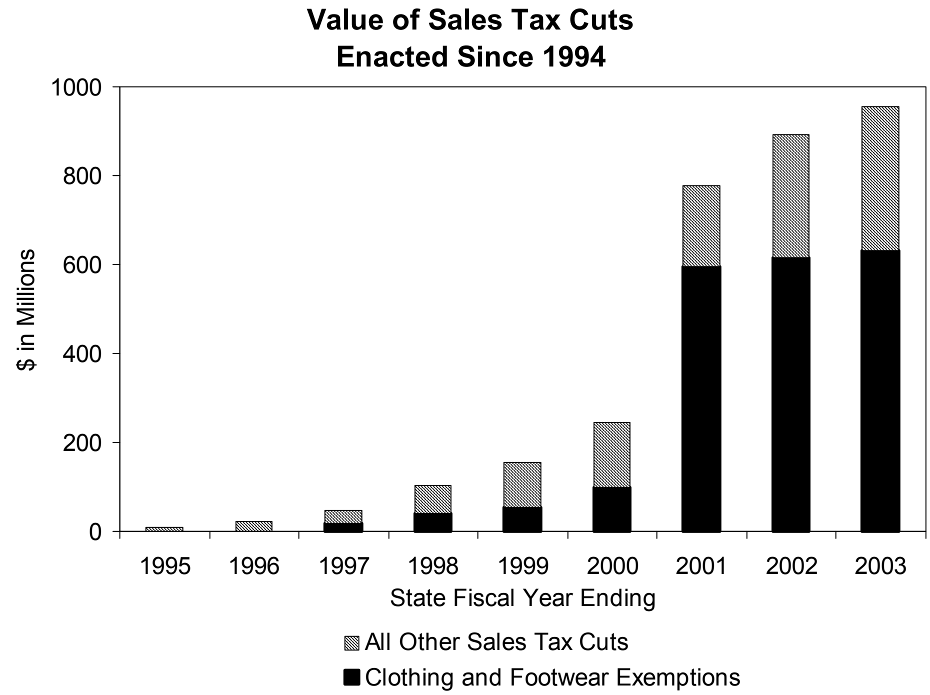
Numerous statutory changes have been made to the sales tax since its inception. The following table summarizes the major sales tax legislation enacted since 1994.

[1] Taxing a good or service is regressive if low-income persons pay a relatively greater share of their income on the taxed good or service than higher-income persons.

Subject	Description	Effective Date
Legislation Enacted in 1994		
Racehorses	Exempted certain registered racehorses used in authorized pari-mutuel events.	June 1, 1994
Vendor Allowance	Enacted the vendor allowance credit for timely filed quarterly or annual returns at the rate of 1.5 percent of State sales tax collected up to a maximum of $100 per return.	September 1, 1994
Legislation Enacted in 1995		
Homeowners' Associations	Exempted dues paid to homeowners' associations operating social or athletic facilities for their members.	September 1, 1995
Meteorological Services	Exempted the sale of meteorological information services.	September 1, 1995
Legislation Enacted in 1996		
Clothing and Footwear	Exempted clothing and footwear priced under $500 for the one-week period of January 18-24, 1997.	January 18-24, 1997
Promotional Materials	Expanded the exemption for certain printed promotional materials distributed by mail to customers in New York State.	March 1, 1997
Legislation Enacted in 1997		
Buses	Provided an exemption for buses used to transport persons for hire, and related parts and services.	December 1, 1997
Clothing and Footwear	Exempted clothing priced under $100 for the one-week periods of September 1-7, 1997 and September 1-7, 1998.	September 1-7, 1997, September 1-7, 1998
	Permanently exempted clothing priced under $100.	December 1, 1999
Homeowner Association Parking	Exempted parking services sold by a homeowners' association to its members.	December 1, 1997
Various Coin-Operated Devices	Raised the exemption threshold for bulk vending machine sales to 50 cents from 25 cents, exempted coin-operated car washes, exempted coin-operated photocopying costing under 50 cents, and exempted certain hot food and beverages sold through vending machines.	December 1, 1997
Vendor Allowance	Increased the sales tax vendor allowance from 1.5 percent to 3.5 percent of State tax collected capped at $150 per quarter.	March 1, 1999
Legislation Enacted in 1998		
Clothing and Footwear	Included footwear in the September 1-7, 1998, temporary clothing exemption and raised exemption threshold to $500 from $100.	September 1-7, 1998
	Exempted clothing and footwear priced under $500 during the January 17-24, 1999 period.	January 17-24, 1999
	Included footwear in the permanent clothing exemption beginning on December 1, 1999, and raised exemption threshold from $100 to $110.	December 1, 1999
Coin Telephones	Increased the exemption threshold for coin-operated telephone calls to 25 cents from 10 cents.	September 1, 1998
College Textbooks	Exempted textbooks purchased by college students which are required for their courses.	June 1, 1998
Computer Hardware	Exempted computer system hardware used to design and develop computer software for sale.	June 1, 1998
Internet Access Service	Codified State policy of exempting charges for Internet access services.	February 1, 1997
Materialmen	Allowed certain materialmen (i.e., building materials suppliers) to remit sales tax returns on either a cash or an accrual basis.	June 1, 1999
Telephone Central Office Equipment	Expanded existing exemption for telephone central office equipment to include such equipment or apparatus used in amplifying, receiving, processing, transmitting, and re-transmitting telephone signals.	September 1, 1998

Subject	Description	Effective Date
Legislation Enacted in 1999		
Clothing and Footwear	Changed the effective date of the permanent exemption for clothing and footwear priced under $110 from December 1, 1999, to March 1, 2000.	March 1, 2000
	Temporarily exempted clothing and footwear priced under $500 for the periods of September 1-7, 1999, and January 15-21, 2000.	September 1-7, 1999; January 15-21, 2000
Computer Hardware	Provided an exemption for computer system hardware used to design and develop Internet web sites for sale.	March 1, 2001
Farm Production	Expanded the farm production exemption to include fencing and certain building materials. Converted the refund for tax paid on motor vehicles to an exemption.	March 1, 2001
Telecommunications Equipment	Exempted machinery and equipment used to upgrade cable television systems to provide telecommunications services for sale and to provide Internet access service for sale.	March 1, 2001
Theater	Exempted certain tangible personal property and services used in the production of live dramatic or musical arts performances.	March 1, 2001
Legislation Enacted in 2000		
Farm Production	Exempted property, building materials and utility services used in farm production. Expanded definition of farms to include commercial horse boarding operations.	September 1, 2000
Internet Data Centers	Exempted computer hardware and software purchased by Internet Data Centers (web site hosting facilities) operating in New York. Included required equipment such as air conditioning systems, power systems, raised flooring, cabling, and the services related to the exempted property.	September 1, 2000
Vending Machines	Exempted food and drink sold through a vending machine that costs 75 cents or less.	September 1, 2000
Telecommunications Equipment and Communications Services	Exempted property used to provide telecommunications services, Internet access services, or a combination thereof. Also, exempted certain services to the exempted property, such as installation and maintenance. Provided a three-year exemption for machinery and equipment used to upgrade cable television systems to a digital-based technology.	September 1, 2000
Radio and Television Broadcasting	Exempts machinery and equipment (including parts, tools and supplies) and certain services used for production and transmission of live or recorded programs. A broadcaster includes Federal communications licensed radio and television stations, television networks, and cable television networks.	September 1, 2000
Pollution Abatement	Exempts manufacturing and industrial pollution control equipment and machinery.	March 1, 2001
Transmission and Distribution of Electricity and Gas	Phases out and eliminates over three years, the sales tax on the separately purchased transmission of electricity and gas.	September 1, 2000
Empire Zones	Exempts property and services used or consumed by qualified businesses within Empire Zones.	March 1, 2001
Purchase of Gas or Electricity from Outside of New York	Imposed a compensating use tax on purchases of gas or electricity from vendors located outside of New York	June 1, 2000
Legislation Enacted in 2001		
Empire Zones	Added eight new Empire Zones, for a total of 66 zones throughout the State. Four of the eight new Empire Zones will be effective immediately.	October 29, 2001

The tax cuts enacted since 1994-95 have had a substantial impact on sales tax receipts. The graph below depicts the estimated value of sales tax cuts enacted since 1994.



BRIEF REVIEW OF RECEIPTS HISTORY

The years since the 1980's exemplify the relationship between sales tax receipts and underlying economic factors. State fiscal years 1986-87 and 1987-88 were marked by growth in the continuing sales tax base of over 8 percent, which was clearly related to the strong employment and income growth in New York and the associated robust growth in the consumption of goods and services taxable in New York. Conversely, State fiscal years 1988-89 through 1991-92 were characterized by slower growth or actual declines in the sales tax base, and this parallels declines in New York employment, New York disposable income, and taxable consumption. For the State fiscal years 1992-93 through 1996-97, the State's economy came out of the recession more slowly and employment and personal income grew more modestly than the nation as a whole. This resulted in growth in the sales tax base that, although improved from the early 1990s, was moderate compared to the late 1980's. Since State fiscal year 1997-98, base sales tax receipts have grown over 5 percent per year, reflecting the robust economy and continued strength in taxable consumption, State employment, and disposable income.

2001-02 Receipts

State fiscal year 2001-02 receipts from the State's 4 percent sales tax are estimated at $8,159 million, a decrease of $204.5 million, or 2.4 percent, below 2000-01. The underlying sales tax base is estimated to decline 1.9 percent. Year-to-date sales and use tax receipts are $6,121.2 million, 3 percent or $191.2 million below the comparable period in 2000-01.

The decline in receipts can be partially attributed to an economy that was already slowing prior to September 11, 2001. Although the attack on the World Trade Center (WTC) worsened the slowdown in income, employment, and consumer spending in New York, it also had a direct negative impact on sales tax receipts. The Department of Taxation and Finance enforcement staff was adversely impacted by the attack. This will likely reduce non-voluntary collections. Also, tax-paying businesses were destroyed or temporarily shut down, and tourism spending declined sharply. The attack did cause business equipment purchases to rise after the attack, which will offset some of the negative impact of the attack on receipts.

Already enacted tax reductions have also served to reduce estimated 2001-02 sales tax receipts. The second phase of the exemption for the transmission and distribution of gas and electricity will reduce receipts by an estimated $17.5 million. Exemptions for theater equipment, hardware used for website development, pollution abatement equipment, and telecommunications equipment will reduce receipts by an estimated $33 million.

2002-03 PROJECTIONS

Cash receipts from the State's 4 percent sales tax in 2002-03 are projected to be $8,379.5 million or $220.5 million (2.7 percent) above 2001-02 levels.

The year-to-year change is the result of DOB's forecast of continuing growth in disposable income and taxable consumption, as well as previously enacted and proposed tax law changes. As in 2001-02, the WTC disaster will continue to affect economic growth and receipts. The next phase of the transmission and distribution exemption, effective September 1, 2002, is expected to reduce receipts by $22.9 million in 2002-03. Legislation included in this Budget proposes to lower the EFT filing threshold to $500,000, which will generate an estimated $32.5 million in additional receipts in 2002-03. Additional legislation proposes to use a suitable price index to calculate the pre-paid sales paid by cigarette distributors at the time they purchase cigarette tax stamps. The Federal government no longer publishes the index required by current law, which has resulted in the pre-paid sales tax on cigarettes remaining constant since 1997. This proposal will generate an estimated $5.8 million in receipts in 2002-03. Legislation enacted in January 2002 will increase the cigarette tax from $1.11 to $1.50 per pack. This proposal will generate an estimated $11.3 million in sales tax receipts in 2002-03. It should be noted that hold-harmless provisions in the Tax Law prevent the clothing exemption from reducing receipts that would have otherwise been available from the 0.25 percent Metropolitan Commuter Transportation District (MCTD) tax deposited in the Mass Transportation Operating Assistance Fund.

The primary risk factor for the sales and use tax estimate is the economic forecast, which provides the basis for the projection of growth in the taxable sales base. Unexpected slowdowns in income or employment would affect consumption and, therefore, impact the level of taxable sales.

OTHER FUNDS

The Local Government Assistance Corporation (LGAC) was created in 1990 to help the State eliminate its annual spring borrowing. To pay the debt service on the bonds issued by LGAC, the State has diverted the yield of one-fourth of net sales and use tax collections from the 4 percent statewide sales tax to the Local Government Assistance Tax Fund (LGATF). Sales tax deposits to LGATF were $2,092 million in 2000-01 and are estimated at $2,038.6 million in 2001-02 and $2,094.4 million in 2002-03. LGATF receipts in excess of debt service requirements on LGAC bonds are transferred to the General Fund.

The Mass Transportation Operating Assistance Fund was created in 1981 to finance State public transportation needs. MTOAF derives part of its revenues from the 0.25 percent sales and compensating use tax imposed in the Metropolitan Commuter Transportation District. MTOAF, which received $368.2 million in sales and use tax receipts in 2000-01, will receive an estimated $367.4 million in 2001-02 and $370.4 million in 2002-03.

GENERAL FUND

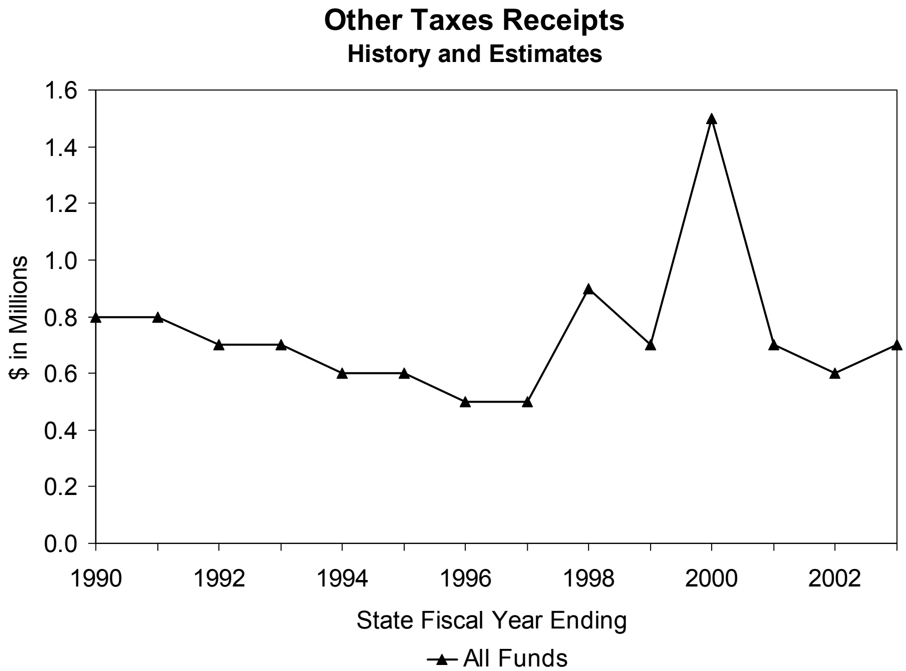
Direct deposits to the General Fund for 2001-02 are estimated to be $6,120.4 million, a decrease of $151.2 million, or 2.4 percent, from 2000-01 receipts. General Fund receipts in 2002-03 are projected to be $6,285.1 million, a 2.7 percent increase from the current year.

SALES AND USE TAX RECEIPTS
(thousands of dollars)

	Gross General Fund	Refunds	Net General Fund	Special Revenue Funds[1]	Capital Projects Funds	Debt Service Funds[2]	All Funds Net Collections
	Actual						
1993-94	4,578,362	18,785	4,559,577	248,163	0	1,514,826	6,322,566
1994-95	4,918,969	21,151	4,897,818	263,607	0	1,627,246	6,788,671
1995-96	5,036,299	41,451	4,994,848	292,199	0	1,665,744	6,953,791
1996-97	5,265,260	40,212	5,225,048	289,129	0	1,746,575	7,260,752
1997-98	5,466,602	24,254	5,442,348	305,949	0	1,813,532	7,561,829
1998-99	5,728,834	32,136	5,696,698	321,405	0	1,893,821	7,911,924
1999-2000	6,182,347	41,388	6,140,959	345,646	0	2,045,844	8,532,449
2000-01	6,310,956	39,391	6,271,565	368,226	0	2,091,901	8,731,692
	Estimated						
2001-02	6,159,400	39,000	6,120,400	367,400	0	2,038,600	8,526,400
2002-03							
(current law)	6,288,700	40,000	6,247,600	368,400	0	2,081,900	8,697,900
(proposed law)	6,325,100	40,000	6,285,100	370,400	0	2,094,400	8,749,900

[1] Mass Transportation Operating Assistance Fund
[2] Local Government Assistance Tax Fund

OTHER TAXES



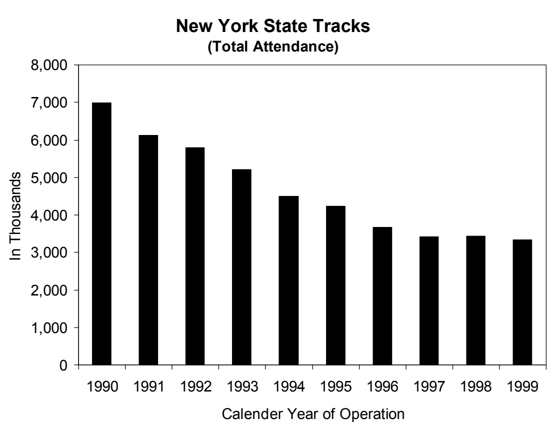
RACING ADMISSIONS TAX

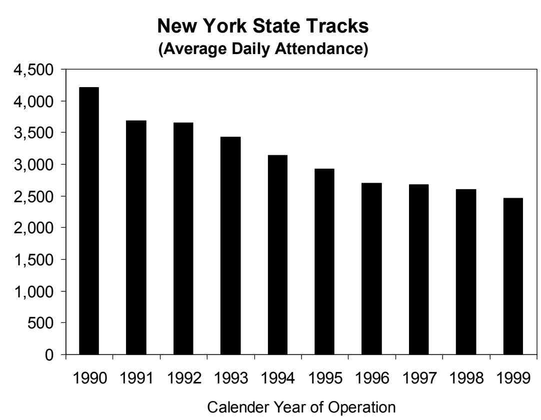
A 4 percent tax is levied on the charge for admissions to racetracks and simulcast theaters throughout the State. Expanded interstate competition and growth in off-track betting activity within New York, as well as the proliferation of casinos in close proximity to New York residents has led to declines in total paid attendance at tracks (see charts below) and in receipts from this source.

2001-02 Receipts and 2002-03 Projections

Given the successful extended racing season at Saratoga Race Course during the summer of 2001, 2001-02 receipts are estimated at $300,000.

Receipts for 2002-03 are projected to remain constant at $300,000. It is estimated that increased attendance at simulcast facilities and the Saratoga meet will be offset by continued modest admissions declines at other New York racetracks.





BOXING AND WRESTLING EXHIBITIONS TAX

A 3 percent tax is levied on gross receipts from boxing and wrestling exhibitions, including receipts from broadcast and motion picture rights. Single events of high spectator interest, such as a heavyweight championship fight, can influence the yield of the tax substantially, causing receipts to vary considerably from year to year.

2001-02 Receipts and 2002-03 Projections

Based on year-to-date collections of the current fiscal year, receipts are expected to reach $300,000. The World Trade Center terrorist attack on September 11, 2001, is expected to result in a marginal revenue reduction for this tax in State fiscal year 2001-02, due to cancellations and postponements of boxing and wrestling exhibitions in New York and to a drop in average attendance.

Receipts for the boxing and wrestling exhibitions tax are expected to marginally increase to $400,000 for State fiscal year 2002-03. The expected increase is the result of continued growth of on-site wrestling and boxing events.

OTHER TAXES RECEIPTS
(thousands of dollars)

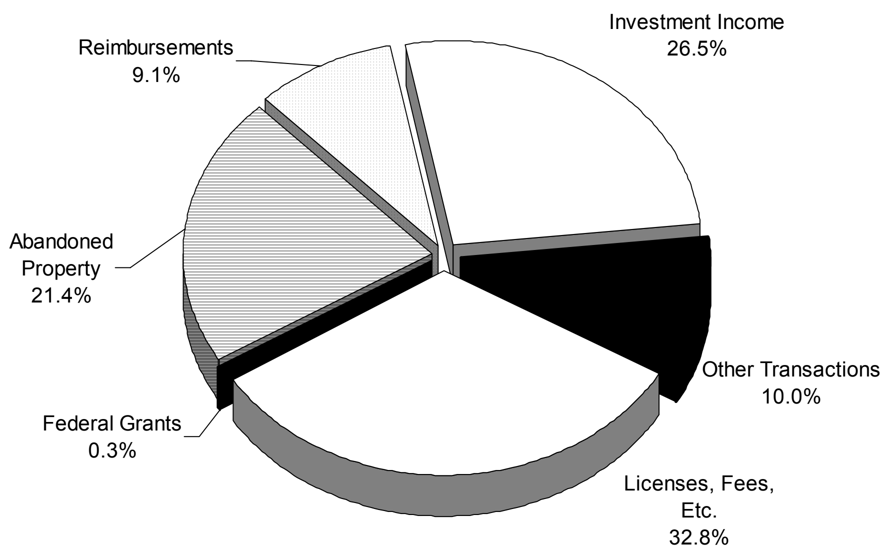
	General Fund		Special Revenue Funds	Capital Projects Funds	Debt Service Funds	All Funds Collections
	Admissions	Exhibitions				
	Actual					
1993-94	399	262	0	0	0	661
1994-95	357	277	0	0	0	634
1995-96	310	182	0	0	0	492
1996-97	272	232	0	0	0	504
1997-98	310	639	0	0	0	949
1998-99	294	400	0	0	0	694
1999-2000	280	1,220	0	0	0	1,500
2000-01	300	400	0	0	0	700
	Estimated					
2001-02	300	300	0	0	0	600
2002-03	300	400	0	0	0	700

MISCELLANEOUS RECEIPTS
General Fund

DESCRIPTION

Miscellaneous Receipts cover a broad range of unrelated revenue sources with significant recurring income derived from abandoned property, investment earnings, fees, licenses, fines, and various reimbursements to the State's General Fund. Each year, the reported receipts are also affected by various nonrecurring transactions.

Miscellaneous Receipts
2000-01



SIGNIFICANT LEGISLATION

MISCELLANEOUS RECEIPTS

Subject	Description	Effective Date
Legislation Enacted in 1994		
Assessments	Extended for one year the assessments on health facility providers.	April 1, 1994
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 1994
Legislation Enacted in 1995		
Assessments	Extended for one year the assessments on health facility providers.	April 1, 1995
Love Canal claims	Provided for the deposit into the General fund of moneys received from settlement of Love Canal claims.	April 1, 1995
Power authority of NY	Provided for the one-time payment to the General fund of $15.9 million in lieu of annual payments.	April 1, 1995
Legislation Enacted in 1996		
Assessments	Extended for one year the current assessments on health facility providers and imposed new assessments.	April 1, 1996
Power Authority, MMIA, Workers Compensation	Provided for the deposit into the General Fund of moneys from these entities, respectively: $50 million, $481 million, and $97 million.	April 1, 1996
Fees and Fines	Moved into the General Fund receipts previously deposited into various special revenue accounts.	August 31, 1996

Subject	Description	Effective Date
Legislation Enacted in 1997		
Assessments	Provided for the collection of assessments for prior years from certain health facilities.	January 1, 1995
	Initiated a phase-out of the assessments on private health facility providers.	April 1, 1997
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 1997
Legislation Enacted in 1998		
Assessments	Accelerated the phase-out of assessments on private health facility providers.	April 1, 1998
Legislation Enacted in 1999		
Assessments	Further accelerated the phase-out of assessments on private health facility providers.	April 1 1999
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 1999
Legislation Enacted in 2000		
Assessments	Provided amnesty on interest and penalties for private health facilities that paid any outstanding assessments by March 31, 2001.	April 1, 2000
Legislation Enacted in 2001		
Mandatory Surcharges	Extended for two years the mandatory surcharges pertaining largely to standing or moving violations of the Vehicle and Traffic Law.	October 31, 2001

2000-01 RECEIPTS

In State fiscal year 2000-01, Miscellaneous Receipts totaled $1,553 million. Major revenue sources in that year included: $333 million in unclaimed and abandoned property; $411 million in interest earnings on short-term investments and bank accounts (this amount is net of certain expenses incurred in providing banking services to various State agencies); $509 million in fees, licenses, fines, royalties, and rents; $131 million in medical provider assessments; $141 million in reimbursements; and $4 million in Federal grants. In addition, the receipts included $1.5 million from the Energy Research and Development Authority; $16 million in assessment payments from medical providers under the amnesty law discussed above; $3.9 million in one-time audit recovery payments; and $2.5 million from the Housing Finance Agency.

2001-02 RECEIPTS

Miscellaneous Receipts are estimated at $1,609 million for 2001-02, an increase of $56 million from the prior year. The estimate includes receipts of $393 million in unclaimed and abandoned property; $394 million in net investment earnings; $495 million in fees, licenses, fines, royalties and rents; $133 million in medical provider assessments; $160 million in reimbursements; $2 million in Federal grants; and $32 million from the Thruway Authority, reflecting the early payment of bonds. The estimate for unclaimed and abandoned property reflects the early positive results of an interagency cooperative project. Investment earnings for the current fiscal year reflect large average cash balances.

2002-03 PROJECTIONS

Miscellaneous Receipts are projected at $1,606 million in 2002-03, a decrease of $3 million from the amount estimated for 2001-02. This projection includes receipts of $408 million in unclaimed and abandoned property; $151 million in net investment earnings; $153 million in reimbursements; $496 million in fees, licenses, fines, royalties and rents; $134 million in continuing medical provider assessments; $4 million in Federal grants; $42 million from the PASNY; and $2.5 million from the Energy Research and Development Authority. There are also several transactions reflecting excess funds: (1) $150 million from the State of New York Mortgage Agency, (2) $50 million from the New York State Housing Finance Agency; and, (3) $16 million from the Port Authority of New York and New Jersey. As in 2001-02, the estimate for unclaimed and abandoned property reflects the net gains associated with the interagency cooperative project on abandoned property. Investment earnings in 2002-03 reflect much lower average cash balances and the impact of estimated lower interest earnings on those average balances.

Legislation submitted with the Budget proposes to consolidate the fine schedule related to the heavyweight truck permit program and to amend the Abandoned Property Law in order to improve its administration and enforcement.

MISCELLANEOUS RECEIPTS
(millions of dollars)

	1998-99	1999-2000	2000-01	2001-02	2002-03
	Actual			Estimated	
License, Fees, Etc.	451	556	509	495	496
Federal Grants	4	4	4	2	4
Abandoned Property	293	316	333	393	408
Reimbursements	156	150	141	160	153
Investment Income	215	232	411	394	151
Other Transactions	468	389	155	165	394
Total	1,587	1,647	1,553	1,609	1,606

MISCELLANEOUS RECEIPTS
Special Revenue Funds

Miscellaneous receipts deposited to special revenue funds represent approximately 22 percent of total special revenue receipts, excluding transfers from other funds. These receipts include State University of New York (SUNY) tuition and patient income, lottery receipts for education, programs funded by HCRA, assessments on regulated industries, and a variety of fees and licenses, all of which are dedicated to support specific programs.

STATE UNIVERSITY INCOME

The majority of special revenue receipts that support SUNY's operations are provided by tuition, patient revenue, and user fees. SUNY's three teaching hospitals at Brooklyn, Stony Brook and Syracuse receive patient revenue from third-party payors including Medicare, Medicaid, Blue Cross, commercial insurers, and individuals. User fees, which include fees for food, parking, career placement and recreation, are generated from service users, including students, faculty, staff, and the public.

LOTTERY

A portion of the receipts from the sale of lottery tickets is earmarked for the support of education, as well as administrative costs associated with Lottery operations. The Lottery is discussed in detail in a separate section.

INDIGENT CARE

The Indigent Care Fund allows the State to claim Federal reimbursement for payments to hospitals that provide care for the medically indigent. The State makes payments in the first instance from a bad debt and charity care pool funded with non-Federal Medicaid dollars, and money from various payors including Blue Cross, commercial insurers, and hospitals.

HCRA TRANSFER FUND

HCRA provides funding for several health and mental hygiene programs including prescription drug assistance for the elderly, supplemental Medicare insurance, and other public health services.

PROVIDER ASSESSMENTS

The new provider assessment account proposed in the Executive Budget will receive moneys from a 6.0 percent assessment on nursing homes.

ELDERLY PHARMACEUTICAL INSURANCE COVERAGE PROGRAM (EPIC)

New York's EPIC program helps senior citizens pay for their prescriptions. This program is partially funded by revenues authorized in HCRA.

CHILD HEALTH PLUS

The Child Health Plus (CHP) program subsidizes health insurance coverage for children of low-income families. Revenues authorized in HCRA fund the State's share of CHP.

ALL OTHER

The remaining revenues in this category include fees, licenses, and assessments collected by State agencies, primarily to support all or specific components of their operations. Receipts from assessments primarily reflect reimbursements from regulated industries, which fund the administrative costs of State agencies charged with their oversight. State agencies funded entirely from assessments include the Banking Department, the Insurance Department, the Public Service Commission, and the Workers' Compensation Board.

MISCELLANEOUS RECEIPTS
SPECIAL REVENUE FUNDS
(millions of dollars)

	1998-99	1999-2000	2000-01	2001-02	2002-03
	Actual			Estimated	
State University income	1,561	1,622	1,656	1,759	1,878
Lottery	1,576	1,496	1,587	1,684	2,086
Indigent care	666	763	873	847	1,020
HCRA transfer fund	0	0	246	372	720
Provider assessments	0	0	0	0	463
EPIC	33	40	178	260	500
Child Health Plus	100	183	259	325	431
All other	1,877	1,977	1,847	1,932	2,068
Total	5,813	6,081	6,646	7,179	9,166

LOTTERY

DESCRIPTION

In 1966, New York State voters approved a referendum authorizing a State lottery, and ticket sales commenced under the auspices of the Division of the Lottery (the Division). Under the original lottery legislation, a lotto-type game was offered with 30 percent of gross receipts earmarked to prizes, 55 percent to education, and the remaining 15 percent representing a limit on administrative expenses. Since then, numerous games have been introduced with varying prize payout schedules to make them attractive to the consumer.

The Division manages the sale of lottery tickets and operates as an independent agency within the Department of Taxation and Finance. The Division, pursuant to legislation enacted in 2001, is authorized to operate five types of games:

- Instant games, in which most prizes are won immediately;
- Lotto games, which are pari-mutuel, pick-your-own-numbers games offering large top prizes with drawings conducted eleven times weekly: seven 5-of-39 draws (Take-5), two 6-of-59 draws (Lotto 59) and two multi-jurisdictional drawings. For the Lotto 59 game and the multi-jurisdictional game, the value of any top prize not won is added to the top prize in the subsequent drawing;
- Daily numbers games, which are fixed-odds games with daily drawings in which players select either a three-digit number (Daily Numbers) or a four-digit number (Win 4);
- Keno-like games, which are pari-mutuel pick-your-own 10-of-80 numbers games with drawings conducted either daily (Pick 10) or every five minutes (Quick Draw) during certain intervals. The Division pays top prizes of $500,000 in Pick 10 and $100,000 in Quick Draw; and
- Video Lottery Games, which are lottery games played on video gaming devices. They are allowed at selected thoroughbred and harness tracks with county resolutions required for the participation of some tracks.

Under current law, the Comptroller, pursuant to an appropriation, distributes all net receipts from the lottery directly to school districts for the purposes of providing school aid. This aid includes special allowances for textbooks for all school children and additional amounts for pupils in approved State-supported schools for the deaf and the blind.

The minimum statutory allocation to education for the Lotto 59 game is 45 percent of ticket sales; for the multi-jurisdictional, Take-5, Win 4, numbers and Pick 10 games, 35 percent; for instant games, 20 percent; for Quick Draw, 25 percent; and for Video Lottery Terminals, the allocation can range from 60 percent to 73 percent of net machine income. After the earmarking for prizes, the Division uses a portion of net sales (not exceeding 15 percent) for its administrative expenses of which the unused remainder is available to support education.

SIGNIFICANT LEGISLATION

Subject	Description	Effective Date
Legislation Enacted in 1994		
Limit on Draws per Day	The tickets for Pick 10, Take-5, and Lotto games are to be sold only once a day.	April 1, 1994
Unclaimed Prize Money	The use of unclaimed prize money to supplement other games by the Division is limited to 16 weeks per year.	April 1, 1994
Annual Plan	The Division is required to submit an annual report to the Legislature, the Governor, and the Division of the Budget each year.	April 1, 1994

Subject	Description	Effective Date
Legislation Enacted in 1995		
Quick Draw	Authorized Quick Draw.	April 1, 1995
	Authorized a 60 percent prize payout.	
	Drawings for the game can be held no more than 13 hours each day, of which only eight consecutive hours can be operated.	
	If there is no license for the sale of alcohol, then the premises have to be a minimum of 2,500 square feet.	
	If there is a license to sell alcohol, then at least 25 percent of the gross sales must be from sales of food.	
Legislation Enacted in 1999		
Instant Games	Authorized a 65 percent prize payout.	April 1, 1999
	Reduced the percent dedicated to education from 30 percent to 20 percent.	
Legislation Enacted in 2001		
Multi-jurisdictional	Allows the Lottery Division to enter into agreements to conduct multi-jurisdictional lotto games with a 50 percent prize payout	October 29, 2001
Video Lottery Terminals	Allows the Lottery Division to license the operation of video lottery machines at selected New York State racetracks.	October 29, 2001

2001-02 RECEIPTS

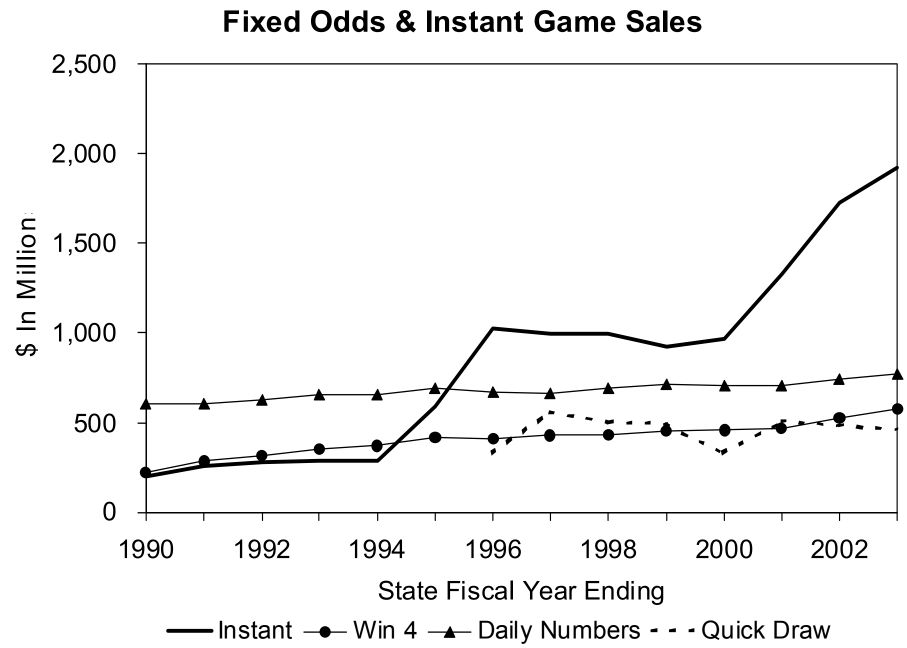
Total sales of all lottery games, estimated at $4.6 billion, are expected to provide $1,330.4 million for education from current ticket sales, which is up $54.6 million or 4.3 percent above 2000-01. After including $183.9 million from unspent administrative allowances, a $47.2 million carry-in from 2000-01, and miscellaneous income, total net lottery receipts earned for education in 2001-02 are expected to total $1,561.5 million. The 2001-02 supplemental lottery appropriation sets disbursements to education at $1,561.5 million. As a result, there will be no carry-out from 2001-02 into 2002-03.

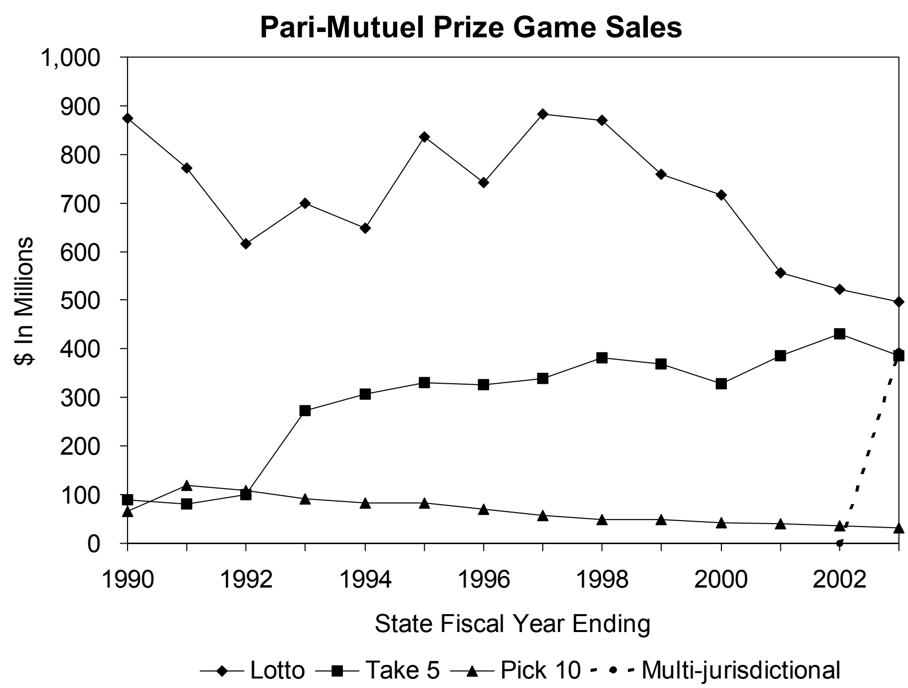
Legislation passed in 1999 allowed the Division to increase the prize payout on instant tickets from 55 percent to 65 percent. On October 2, 1999, the Division began to introduce games with the higher prize payout. By March 31, 2001, the transition was completed and all instant games were offered a 65 percent prize payout. This has resulted in a large increase in instant game sales. Sales are expected to be up 38.3 percent in 2001-02. Due to the increased prize payouts, the continual introduction of new more popular game formats and the implementation of a program to call on large agents every two weeks, there was a significant increase in revenue from sales which was somewhat offset by the lower percentage of sales allocated to education. In total, revenue from instant ticket sales is expected to increase from $283 million in 2000-01 to $367 million in 2001-02. As the higher payout games become more mature, it is expected that sales and revenue growth will moderate.

A gradual weakening in Lotto sales has developed over the past several years, stemming from several factors: (1) dilution of interest in ordinary jackpots, given raised expectations of exceptionally large jackpots, that can be awarded from the Big Game and Powerball games offered in other states; (2) increased competition from Indian casinos in and around New York; (3) reduced consumer interest, based on the maturity of the game, and (4) a decline in the number of very large jackpots — a reflection of reduced participation, which contributes to lower jackpots.

The phenomenon of declining trends in Lotto sales has been experienced in most states with similar Lotto structures. To counteract declining trends in Lotto sales, the Division introduced Lotto 59 on September 9, 2001. The new game offers two plays for one dollar and changed the payout matrix to 6 of 59. The bigger matrix and lower price per play is expected to lead to higher jackpots which will revive interest in the Lotto game and increase sales.

The World Trade Center attack on September 11, 2001, caused an estimated loss of $7.3 million in lottery revenue for State fiscal year 2001-02. Most of the games have rebounded to their pre-September 11, 2001, sales levels except for Lotto. Year-to-date Lotto sales are running 6 percent below last year's sales.





Quick Draw sales in 2001-02 are expected to be down 4.3 percent compared with 2000-01. This is related in part to a reduction in the number of customers entering establishments that have Quick Draw machines.

Numbers game sales are benefiting from the addition of new agents which has fostered player awareness. Revenue from sales is expected to increase moderately from

$247.4 million in 2000-01 to $259.7 million in 2001-02. Beginning in December 2001, a second drawing at noon for the Numbers game and the Win 4 game was added by the Division. The estimated combined revenue effect for State fiscal year 2001-02 is an additional $25.5 million. Number sales are expected to increase by 5 percent and Win 4 sales are estimated to increase by 11.4 percent due, in part, to the second draw per day and to stronger than expected growth in base sales.

The increase in draws for the Take-5 game from five to seven days per week on September 10, 2000, contributed to a 17.6 percent increase in sales in State fiscal year 2000-01. The increase in draws is expected to continue to drive sales up for 2001-02 by an estimated 12 percent, and generate $16.1 million in additional revenues.

Pick 10 is continuing the downtrend exhibited in recent years. Revenue from sales are expected to fall from $14.5 million to $12.9 million.

Table 1
Components of Lottery Receipts
(millions of dollars)

	1997-98	1998-99	1999-2000	2000-01	2001-02 Estimated	Current Law 2002-03 Projected	Proposed Law 2002-03 Projected
Instant Game	298.5	283.2	272.7	283.0	367.0	402.0	414.2
Lotto Games[1]	395.9	338.3	339.5	304.6	235.2	392.0	392.0
Take-5 Games	133.9	128.9	114.8	135.0	151.1	135.1	135.1
Daily Numbers Games	243.9	249.2	246.6	247.4	259.7	270.5	270.5
Win-4 Games	151.7	157.0	159.6	164.5	183.3	203.3	203.3
Pick 10 Games	17.4	17.0	15.1	14.5	12.9	11.2	11.2
Quick Draw	125.8	123.4	82.2	126.7	121.2	3.0	176.2
VLTs	0.0	0.0	0.0	0.0	0.0	61.0	61.0
Subtotal	1,367.1	1,297.0	1,230.5	1,275.7	1330.4	1478.1	1663.5
Administrative Surplus[2]	166.8	145.4	119.2	159.8	183.9	219.4	246.9
Current Receipts Subtotal	1,533.9	1,442.4	1,349.7	1,435.5	1514.3	1697.5	1910.4
Carry-In from Prior Year	0.0	0.0	0.0	4.7	47.2	0.0	0.0
Net Receipts for Education	1,533.9	1,442.4	1,349.7	1,440.2	1,561.5	1,697.5	1,910.4
Carry-Out from Current Year	0.0	0.0	(4.7)	(47.2)	0.0	0.0	0.0
Disbursements for Education	1,533.9	1.442.4	1,345.0	1,393.0	1,561.5	1,697.5	1,910.4

[1]Includes receipts from Millennium Millions, Weekly Millions, and the Multi-jurisdictional games.

[2]Reflects miscellaneous income and the balance of the 15 percent administrative allowance, after deduction actual expenses, vendor allowances, and agent commissions.

2002-03 PROJECTIONS

Current Law

Lottery sales for 2002-03 are projected at $6.1 billion, and receipts for the support of education at $1,697.5 million (see Table 1) including $219.4 million in administrative surplus and miscellaneous receipts.

On October 29, 2001, legislation was signed allowing video lottery machines at Aqueduct, Monticello, Yonkers, Finger Lakes, and Vernon Downs racetracks. Given the need to procure machines and provide capital improvements at the tracks, an assumed start date is November 1, 2002. The operation of video lottery machines at these racetracks will generate an estimated net additional $61 million in revenue in 2002-03. Sales of other games are expected to fall by approximately 2.2 percent due to the competition resulting from the introduction of the video lottery machines.

The legislation also allows the Division to enter into agreements to conduct multi-jurisdictional lotto games with a 50 percent payout. The Division expects to join the Big Game Group. Big Game typically attains a large jackpot from the combination of high odds and significant demand created by the participation of seven states that include several major metropolitan areas. The addition of the Big Game is estimated to increase net revenues for education by $125 million in 2002-03. However, the Big Game is anticipated to reduce sales of Lotto 59 and Take-5.

Total sales from the Lotto-type games, however, are expected to increase by $436.1 million from 2001-02, largely from the introduction of the Weekly Millions, Millennium Millions, and the Big Game. Revenues from Lotto-type games would likewise increase by $156.8 million.

The Division is introducing the Weekly Millions game. This is a Lotto type game with a 40 percent payout that has high odds and high jackpots,. This game is run once a week and at times the jackpot will be higher than the Lotto 59 jackpot. The planned start date is September 1, 2002. The estimated net revenue increment from the addition of this game is $34 million for 2002-03.

The Millennium Millions game will be scheduled again this year since it was such a success in 2000-01. This game also has a 40 percent payout. In fiscal year 2000-01, the Millennium Millions game attained $63.5 million in revenues. The projected start date is June 1, 2002. A conservative estimate of $32 million of additional revenues for 2002-03, is based upon a win on the first draw of the game.

The Quick Draw game will sunset on March 31, 2002, and, if not renewed, only $3 million in Quick Draw receipts from sales in 2001-02 but not deposited until 2002-03 will be available. Therefore, failure to extend the current Quick Draw game would result in a net 2002-03 revenue loss of $147.7 million.

The Division is planning to continue with the implementation of the two-week call cycle for the Instant Games. This initiative will allow Division marketing representatives to visit selected high-selling retailers every two weeks and take a more active part in managing the lottery business for the retailers. Initial staff were hired in October 2000 and the two-week call cycle began in November 2000 in parts of the State. Additional staff requested in the 2001-02 Executive Budget and the continued implementations of the two-week call cycle schedule will increase revenue by $42.7 million for the fiscal year.

Sales of Take-5 games are projected to drop by $45.3 million from State fiscal year 2001-02. The loss of excitement for the game after the initial climb in sales from the increase in draws and competition from the introduction of the Big Game will reduce sales.

Daily Numbers and Win 4 will benefit from the incorporation of the noon draw. The estimated combined increase in revenues for the noon draw is $76 million for fiscal year 2002-03.

Sales from Pick 10 are expected to decrease by $5 million, due to the substitution of the more popular Take-5 and Instant games, and revenues will drop by $1.7 million.

Proposed Law

Legislation submitted with this Budget will: (1) make Quick Draw permanent; (2) eliminate the three restrictions on Quick Draw, which are: that drawings be held during no more than thirteen hours each day, for no more than eight consecutive hours; not less than 25 percent of gross sales must result from sales of food if a licensee holds a license to sell alcohol; and if there is no license to sell alcohol, the premises be not less than 2,500 square feet, and (3) allow three instant games per year with a prize payout of 75 percent.

With the continuation of Quick Draw, the addition of the Big Game, and the above mentioned initiatives, total sales of all lottery games are estimated to be $6.9 billion. This will provide net lottery receipts from current sales of $1,663.5 million. After including $246.9 million from surplus administrative funds and miscellaneous receipts, net lottery receipts for education are estimated at $1,910.4 million.

TABLE 2
NET LOTTERY RECEIPTS FOR EDUCATION
(thousands of dollars)

Actual	
1993-94	1,054,000
1994-95	1,161,850
1995-96	1,441,300
1996-97	1,533,203
1997-98	1,533,904
1998-99	1,442,427
1999-2000	1,345,000
2000-01	1,440,200
Estimated	
2001-02	1,561,500
2002-03	
(current law)	1,697,500
(proposed law)	1,910,400

MISCELLANEOUS RECEIPTS
Capital Projects Funds

Miscellaneous receipts in the Capital Projects fund type include reimbursements from the proceeds of bonds sold by public authorities, fees, and other sources of revenue dedicated to specific funds primarily for environmental or transportation capital purposes.

REIMBURSEMENT FROM AUTHORITY BOND PROCEEDS

Pursuant to statutory authorizations, State agencies enter into contractual arrangements with public authorities to provide for the financing of State capital projects. The State makes payments directly for projects and is reimbursed by the public authority from the proceeds of bonds. The amount of reimbursements received annually is a direct result of the level of bondable capital spending in that year and the timing of bond sales. As bondable spending fluctuates with the progress of capital programs, so do the bond receipts reimbursing such spending. Reimbursements from authority bond proceeds will account for approximately 92 percent of all miscellaneous receipts flowing to capital project funds in 2001-02 and 91 percent in 2002-03.

STATE PARKS FEES

User fees and other revenues generated by State parks are deposited into the State Parks Infrastructure Fund. These revenues, which are projected at $22 million in 2002-03, will be used to finance improvements in the State's park system.

ENVIRONMENTAL REVENUES

Miscellaneous receipts from environmental revenues are projected to increase from $45 million in 2001-02 to $94 million in 2002-03. The $49 million net increase is primarily attributable to $36 million in industry fees which will be deposited to the new Remedial Program Transfer Fund, and used to partially finance the industry's 50 percent share of the cost of State Superfund projects. The balance of the increase is driven primarily by a $10 million increase in reimbursements necessary to satisfy projected advance disbursements used to support the development of the Hudson River Park in New York City.

Environmental revenues also include receipts that are deposited to the Environmental Protection Fund from the sale of surplus State lands, leases of coastal State property, settlements, and the sale of environmental license plates. Other environmental revenues from settlements with individuals and other parties who are liable for damage caused to State environmental properties are deposited in the Natural Resource Damages Fund.

ALL OTHER

Various other moneys are received in the Capital Projects funds to support capital programs and to reimburse the State for capital spending on behalf of municipalities and public authorities, such as the Housing Finance Agency. The remaining receipts are repayments of moneys advanced or loaned to municipalities, authorities, and private corporations.

MISCELLANEOUS RECEIPTS
CAPITAL PROJECTS FUNDS
(millions of dollars)

	1998-99	1999-2000	2000-01	2001-02	2002-03
	Actual			Estimated	
Authority Bond Proceeds					
Transportation	697	859	875	818	890
Public protection	351	245	197	188	188
Education	117	280	413	235	294
Mental hygiene	132	118	40	102	124
Housing	70	66	12	101	102
Other	92	45	42	143	276
State Park Fees	27	25	16	25	22
Environmental Revenues	25	40	28	45	94
All Other	56	97	51	74	77
Total	1,567	1,775	1,674	1,731	2,067

MISCELLANEOUS RECEIPTS
Debt Service Funds

Miscellaneous receipts in the Debt Service fund type include patient revenues, fees, interest income, and other revenues. These revenues are dedicated in the first instance for the payment of lease-purchase agreements, contractual obligations, and debt service, and support about 17 percent of the State's debt service payments. These revenues have been pledged as security for bonds issued for mental hygiene and health facilities, and dormitories, or are used by the State to pay debt service on general obligation housing bonds. After such requirements are satisfied, the balance of most miscellaneous receipts, together with other receipts and transfers, flow back to the General Fund or to Special Revenue funds which are used to offset the cost of State operations.

MENTAL HYGIENE RECEIPTS

Payments from patients and various third-party payers, including Medicare and insurance companies, for services provided by the mental hygiene agencies are deposited in the Mental Health Services Fund as miscellaneous receipts. Additionally, portions of State and local assistance and Federal Medicaid payments to not-for-profit community facilities are earmarked to pay their share of debt service, and are also deposited as miscellaneous receipts in the Mental Health Services Fund. These receipts, together with the transferred Medicaid money, secure bonds sold by the Dormitory Authority for State and community mental hygiene facilities.

DORMITORY FEES

Miscellaneous receipts in the State University of New York (SUNY) Dormitory Fund are composed primarily of fees charged to SUNY students for room rentals in the dormitories. The receipts of the Fund are pledged for debt service on bonds sold by the Dormitory Authority for the construction and improvement of the dormitories pursuant to a lease agreement.

HEALTH PATIENT RECEIPTS

Patient care reimbursements at the Department of Health's hospitals (Roswell Park Cancer Institute Corporation and the Helen Hayes Hospital) and veterans' homes (Oxford, New York City and Western New York) are deposited into the Health Income Fund. Similar to mental hygiene receipts, these receipts are composed of payments from Medicaid, Medicare, insurance, and individuals and are pledged as security for bonds sold by the Dormitory Authority for the construction and improvement of Health Department facilities.

ALL OTHER

The all other miscellaneous receipts category is estimated at $26 million for 2001-02 and 2002-03, and primarily includes receipts from local housing agencies to finance the debt service costs on general obligation bonds. All other receipts from 2000-01 of $291 million included the deposit of $250 million in tobacco receipts to the Debt Reduction Reserve Fund (DRRF). That deposit, together with an additional deposit to DRRF of $250 million from the 1999-2000 surplus was used in 2001-02 to defease high cost State debt and increase pay-as-you-go spending.

MISCELLANEOUS RECEIPTS
DEBT SERVICE FUNDS
(millions of dollars)

	1998-99	1999-2000	2000-01	2001-02	2002-03
	Actual			Estimated	
Mental hygiene patient receipts	269	267	258	232	231
SUNY dormitory fees	202	221	224	262	284
Health patient receipts	126	90	87	86	85
All other	33	33	291	26	26
Total	630	611	860	606	626

FEDERAL GRANTS

To qualify to receive Federal grants, the State must comply with guidelines established by the Federal government. Each Federal grant must be used pursuant to Federal laws and regulations. Also, the State is required to follow specific cash management practices regarding the timing of cash draws from the Federal government pursuant to regulations for each grant award. In most cases, the State finances spending in the first instance, then receives reimbursement from the Federal government.

Total receipts from the Federal government are projected at $26.97 billion in 2001-02 and $30.14 billion in 2002-03. These revenues represent approximately 35 percent of total receipts in governmental funds, excluding general obligation bond proceeds, and are deposited into the Special Revenue and the Capital Projects fund types. The projections for both fiscal years exclude the flow-through of Federal aid to localities for World Trade Center disaster costs.

SPECIAL REVENUE FUNDS

Federal grants account for approximately three-quarters of all special revenue receipts and are used to support a wide range of programs at the State and local government level. Medicaid is the single largest program supported by Federal funds.

Medicaid finances care, medical supplies, and professional services for eligible persons. The State receives moneys from the Federal government to make payments to providers for both State-operated and non-State-operated facilities. The State-operated category includes facilities of the Offices of Mental Health and Mental Retardation and Developmental Disabilities and the Department of Health, as well as teaching hospitals of the State University. These facilities receive Medicaid funds for the delivery of eligible services to patients. Receipts for State-operated facilities represent 13 percent of total Federal Medicaid reimbursements, while receipts for non-State-operated facilities represent the remaining 87 percent.

Other Federal grants in the Special Revenue Funds support programs administered primarily by the departments of Education, Family Assistance, Health, and Labor. These programs include Welfare, Foster Care, Food and Nutrition Services, and Supplementary Educational Services.

CAPITAL PROJECTS FUNDS

Federal grants in the Capital Projects fund type finance transportation planning, engineering, and construction projects. Federal grants also support local wastewater treatment projects financed through the State's Revolving Loan Fund. Other Federal grants are for the rehabilitation of state armories, eligible housing programs, and other environmental purposes.

FEDERAL GRANTS
(millions of dollars)

	General Fund	Special Revenue Funds			Total Special Revenue Funds	Capital Projects Funds	Debt Service Funds	Total All Funds
		Medicaid	Welfare	All Other				
	Actual							
1996-97	0	12,424	1,743	4,838	19,005	1,043	0	20,048
1997-98	0	13,183	2,219	5,109	20,511	1,132	0	21,643
1998-99	0	13,612	1,488	6,322	21,422	1,219	0	22,641
1999-2000	0	14,532	1,017	6,635	22,184	1,381	0	23,565
2000-01	0	15,348	1,450	7,475	24,273	1,509	0	25,782
	Estimated							
2001-02	0	16,239	1,850	7,408	25,497	1,471	0	26,968
2002-03	0	17,814	2,329	8,417	28,560	1,576	0	30,136