

MUNICIPAL ASSISTANCE CORPORATION FOR THE CITY OF NEW YORK

One World Trade Center, Suite 8901
New York, New York 10048
Telephone: (212) 775-0010

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TO: Eugene Keilin FROM: Quentin Spector
MAC

FAX #: 661-3208 FAX #: (212) 775-0042 (XEROX MODEL 7021)

MESSAGE: F.Y.I.

OPERATOR: Giesel

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PLEASE DELIVER IMMEDIATELY

MEMORANDUM

Date: November 2, 1992
To: Felix G. Rohatyn
From: Quentin B. Spector
Re: City Early Retirement Incentive Program

MUNICIPAL
ASSISTANCE
CORPORATION
FOR THE CITY
OF NEW YORK

The City has requested \$37.5 million of MAC's surplus to finance a portion of an early retirement incentive program. As discussed below, the program has considerable merit, but I am not sure there is compelling rationale for MAC's financial involvement in the program as structured.

The program would assist in reducing the employee work force by 1,700 positions and, according to the City's projections, would yield savings, after costs, of approximately \$176 million over a six-year period. The savings are partly attributable to the lower salaries of employees hired to replace retirees, but the major savings are achieved by limiting replacement to one in four retirees.

The proposal has some attractive features that increase its chances of achieving genuine, permanent savings without harming service delivery, unlike previous attempts such as the retirement incentives offered teachers last year. In particular, the scope of the program would be limited to a maximum of 3300 participants employed by the mayoral agencies, with the aim of inducing some 2200 retirements (about 1100 more than would be expected in the target group without an inducement).

Secondly, agency heads would be required to offer the incentive to eligible employees within their agencies. Now-expired statutory authorization for a similar offer last year yielded disappointing results because agency heads were not required to offer the incentive and substituted other cost-saving measures they found more palatable.

Finally, the coupling of the retirement incentive with a 25% replacement limitation is the major source of the program's projected payoff. The Budget Director also hopes to take some of the sting out of the mandate by sharing some of the savings with the agencies. Further, by specifying the shared savings be invested in computers or other one-time productivity measures still further savings could be leveraged. He hopes the MAC money would increase the resources available for this purpose. However, the details of such a program have yet to be worked out.

From a technical perspective, the program seems sound, well thought through (with the exception of the idea to share savings and MAC resources with the agencies), and it appears

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conservatively estimated with respect to costs and benefits.*

Arguably, however, a similar outcome could be achieved without cost by a more restrictive replacement policy on total employee attrition rather than the portion attributable to retirements. At best, an early retirement incentive accelerates attrition that would have occurred anyway. Accordingly, a financial gain is possible only when the incentive program supplements all other downsizing measures. However, the City is unclear or unable to say whether this program adds to or substitutes for its other efforts.

Additionally, it is hard to justify the proposed use of MAC funds as they are not necessary to obtain the payoff outlined above. The retirement incentive program stands on its own. The proposed MAC contribution would simply increase that payoff. There is more potential for a MAC role in Phil Michael's idea of adding our resources to savings produced by the agencies, but that idea could also stand on its own and need not be coupled with the retirement incentive program. Anyway, it is premature to evaluate the idea in its present embryonic form.

Lacking a clear economic justification relative to other downsizing alternatives, and lacking a clear rationale for use of MAC funds, the proposed retirement incentive program is probably more about labor relations than MAC concerns or City budget policy, not that all these are unrelated. I expect that the City will proceed with the incentive offer with or without MAC participation. I suspect the City either hopes its expression of good faith in this respect will be reciprocated by union concessions, or that it is worried a failure to proceed (by allowing the statutory authorization to lapse at year's end) will poison contract talks.

In conclusion, while I feel the City's proposal has significant potential, I'm not sure we should participate yet. I recommend we restate the necessity for more progress in labor negotiations. I also recommend we express interest in Phil's concept of adding MAC resources to a share of savings produced in order to generate still further savings. Finally, we should request the City make a proposal for the full \$200 million surplus to avoid a piecemeal series of petitions from multiple sources, and to minimize problems with the Legislature.

* I do question the City's intent to amortize the extra cost of the retirement incentive over a six-year period at 9%. According to my calculations, an up-front payment would save an additional \$7.7 million even after giving effect to the City's cost of working capital.