New York City Independent Budget Office **Schools Brief**

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State Support for New York City's Education Infrastructure: Understanding School Building Aid

There is currently additional attention on school construction in New York City, given the New York State law mandating smaller class sizes. New York State also recently increased the City's authority to issue city-financed debt and mandated that the City "shall increase planned spending on classroom construction by $2.0 billion."[1] This Independent Budget Office (IBO) report explains how New York State provides funding for education infrastructure projects to New York City.

From fiscal years 2020 through 2024, over 99% of New York City spending on school building projects was financed by the City itself, meaning the City issued the bonds (all years refer to fiscal years, unless otherwise specified). However, financing does not account for a crucial source of funding for school infrastructure from New York State: building aid revenue.[2] Based on a different measure that compares building aid revenue to spending on education debt service (payments to bond holders), New York State funds approximately half of New York City's total spending on school infrastructure. Multiple aspects of the State building aid formula constrain building aid revenue, including the portion of costs the State will cover and the maximum costs the State will consider for reimbursement. This report describes state support for education infrastructure in more detail and reviews the building aid formula, which determines the amount of building aid revenue the State allocates to the City.

Education Infrastructure Financing

New York City pays for education infrastructure projects (such as constructing new school buildings or renovations to existing school buildings) the same way it pays for most infrastructure projects: by borrowing money. To borrow money, the City issues bonds and the proceeds fund New York City's Capital Budget (for more details on New York City's Capital Budget, see IBO's Capital Budget Explainer). This borrowed money is debt, and the principal and interest on bonds is called debt service. Debt service is repaid over long periods of time through the Expense Budget.[3]

Most bonds issued by the City are considered city-financed and are guaranteed by the full faith and credit of New York City or by New York City tax revenues. The New York State Constitution and state legislation limit the amount of bonds New York City can issue. The Transitional Finance Authority (TFA), a state authority that issues some city-financed bonds, also separately issues Building Aid Revenue Bonds (BARBs), which are considered state-financed in budget documents. This is because BARBs are backed by building aid revenue, a state revenue that is determined by the building aid formula. BARBs are not subject to city debt limits that apply to other city borrowing, but state law caps total BARB debt outstanding at $9.4 billion. New York State created BARBs as part of the Campaign for Fiscal Equity (CFE) settlement in 2006.[4] While many BARBs were issued from 2007 through 2015, as debt outstanding neared the $9.4 billion limit, fewer BARBs

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were issued.[5] In addition to the debt limits set by New York State, New York City's Office of Management and Budget (OMB) guidelines limit borrowing to keep debt service payments below 15% of tax revenues.[6]

Because few BARBs have been issued in recent years, city-financed bonds funded over 99% of education capital spending from 2020 through 2024. However, this measure of capital spending does not account for all state support for school infrastructure; it only reflects the legal burden of financing. New York State provides support for education infrastructure spending through building aid revenue, which is reflected in New York City's expense budget. As described in a prior IBO brief, the City receives building aid revenue for eligible projects regardless of how those projects are financed. That is, projects funded by both city-backed bonds and BARBs generate building aid revenue. A full understanding of the State's support for the City's school infrastructure spending includes both the authorization to issue bonds and state revenue to pay the City's debt service. See the Appendix for further details on different types of bonds and education infrastructure financing (city vs. non-city) as reflected in capital commitments.

Figure 1
New York State Building Aid Formula

Building Aid Ratio **x** **Aidable Building Expenditures** **=** **Building Aid Revenue**

Building Aid Formula

For each eligible project—which includes both construction of new school buildings and alterations to existing school buildings—the State calculates building aid using the formula in Figure 1.[7]

Building Aid Ratio. The building aid ratio is the share of aidable building expenditures reimbursed by New York State. The State calculates the ratio annually for each school district based on its fiscal capacity as measured by per-pupil property wealth. A district with average per-pupil property wealth has a building aid ratio of 0.49, which means the State will reimburse 49% of the district's aidable building expenditures. However, rather than using a district's current year building aid ratio, the formula uses a district's highest building aid ratio since 1982, with additional adjustments depending on the district and the year of the project.[8] While New York City's current year building aid ratio for 2024 is 0.366 (36.6%), the building aid ratio applied to most city projects since July 2005 is 0.569 (56.9%).

Because the building aid ratio remains at its highest value year-over-year, districts can expect some stability in the share of state funding for projects. Stability is particularly important for infrastructure projects because they are financed through borrowing and paid off over long periods. However, it also creates a disparity between the intended and actual progressivity of the state share, which aims to provide a greater reimbursement percentage to lower-wealth districts.[9] See the Appendix for more details on the building aid ratio calculation for New York City.

***Aidable Building Expenditures*.** Aidable building expenditures represent the amount of spending the State will consider for building aid revenue. For any given project, the amount is the lesser of either the project's actual cost or the maximum cost allowance (MCA). The MCA is determined by the New York State Education Department (NYSED) and is based on the project size, grades served, and regional costs. The MCA is also adjusted monthly based on a New York State Labor Department index relative to base costs defined in State budget legislation. See the Appendix for additional details on how NYSED calculates the MCA.

When the MCA is lower than the actual cost, the share of actual cost reimbursed by New York State is less than the building aid ratio. In a hypothetical example, if the actual cost of a project is $100 million, but NYSED determines the MCA is $50 million, then aidable building expenditures are only $50 million. The building aid ratio is then applied to this amount. Therefore, for this hypothetical project, building aid revenue only covers 28% of the actual cost (see Figure 2). Depending on the difference between the MCA and the actual cost, the share of actual costs covered by building aid could be any percentage up to 56.9%. For new school construction projects in particular, which have high costs, the MCA is likely to be significantly less than the actual cost.

Figure 2
In a Hypothetical Project When the Actual Cost Exceeds the Maximum Cost Allowance (MCA), State Support Is Lower than the Building Aid Ratio

Actual Cost	$100,000,000
Maximum Cost Allowance (MCA)	$50,000,000
Aidable Building Expenditures	$50,000,000
Building Aid Ratio	56.9%
Building Aid for Project	$28,450,000
Portion of Actual Cost Covered by New York State	28.5%

NOTES: IBO presents New York State payment as a share of the total allowable expenditure for illustrative purposes; New York State makes building aid revenue payments over 15-30 years based on assumed debt service, not a lump sum payment. These figures reflect a hypothetical project. For any project where actual cost exceeds MCA, the share of the actual cost covered by New York State could be any percentage up to 56.9%.
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The maximum cost allowance creates an incentive for school districts to minimize construction costs, because costs above the MCA are fully paid by the district. However, for projects where construction costs make it difficult for districts to complete a project within the MCA, there will be a gap between the building aid ratio and the actual share of costs the State reimburses. That is, building aid revenue is constrained by both the building aid ratio and the MCA.

Building Aid Timing. New York State makes building aid payments over a period of up to 30 years based on assumed debt service. That is, the State does not consider a district's actual debt service spending; rather, the State makes assumptions about the interest rate paid on debt issued to finance the project. See the Appendix for more details on the calculation of assumed debt service and timing of payments.

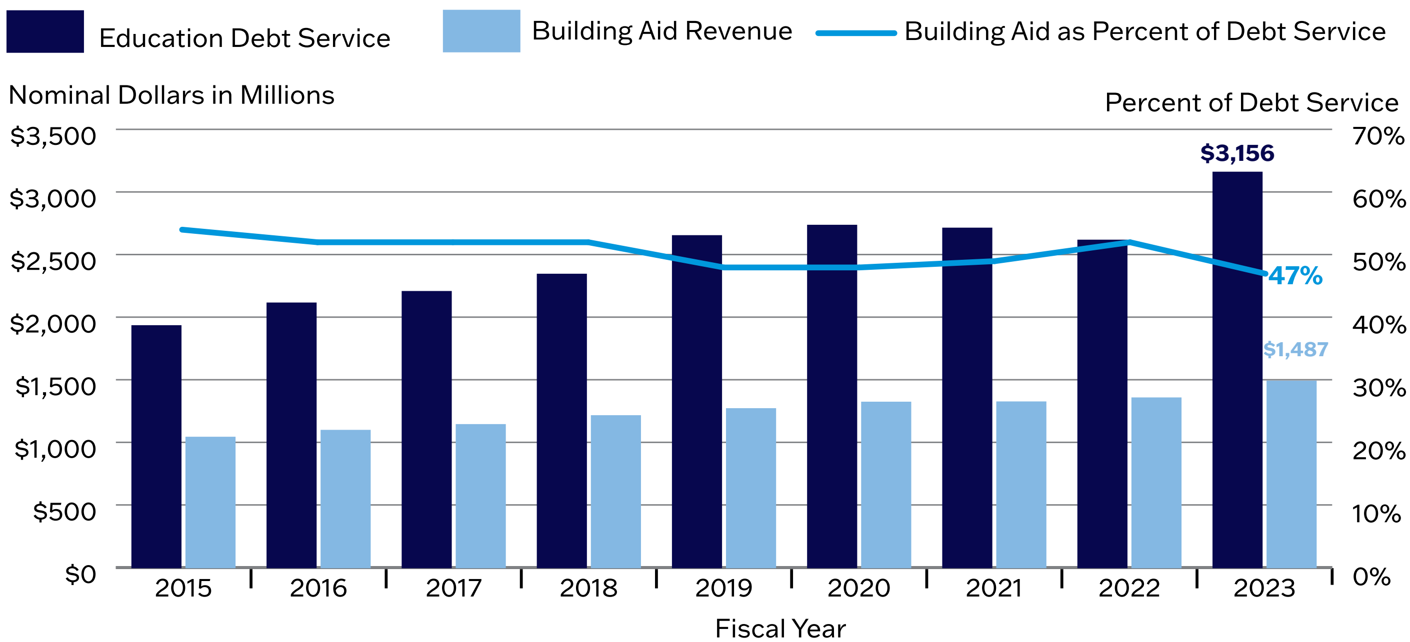
Building Aid Revenue

Because building aid revenue is meant to support debt service payments on education infrastructure projects, comparing building aid revenue to spending on education debt service provides another way to measure state support for these projects. For example, in 2023, New York City spent $3.2 billion on education debt service—this total spending on education debt service includes debt on both BARBs and city-financed bonds. In the same period, New York City received $1.5 billion in building aid revenue from the State. Together, this suggests 47% of education infrastructure spending was supported by the State. Since 2015, building aid revenue has covered approximately half of education debt service costs (see Figure 3).

To put this share of state support for education infrastructure in context, research found that nationally, from 2009 through 2019, only an average of 22% of education infrastructure costs were supported by state governments.[10] However, this research also found New York State supported 61% of education infrastructure costs across all districts.[11]

Building aid revenue as a portion of total debt service may have declined over the 2015 through 2023 period for several reasons. Some of this may be due to phasing out of reimbursement for projects undertaken prior to 2005 with higher building aid ratios (reimbursement rates).[12] In addition, it is possible that the difference between the maximum cost allowance and actual project costs is growing. This would cause New York City's education debt service spending, which reflects total actual costs, to increase more than building aid revenue, which is being provided based on the maximum cost allowance. Finally, it is possible New York City

Figure 3
Building Aid Revenue Supports About Half of Education Debt Service Spending



SOURCES: IBO analysis of Financial Management System data and Mayor's Office of Management and Budget publications
NOTE: Building aid revenue includes revenue for some spending that is not funded through borrowing (and, therefore, not paid for through education debt service), such as leases and water testing. The amount of building aid for these items is small relative to the total, and excluding this revenue would change the percentage of building aid compared to debt service by one to two percentage points. See Table 5 in the Appendix for building aid separated by revenue for leases and construction as reflected in the City's Revenue Budget.

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is spending more on education infrastructure projects not eligible for building aid revenue (e.g., playgrounds, athletic fields, and other projects that do not have a direct impact on instructional space), which would increase education debt service spending without increasing building aid revenue.

Changes in Building Aid Revenue

The building aid formula has remained relatively unchanged for the past twenty years. Changes to the building aid formula would need to be approved by the New York State legislature and the Governor, as with any budget legislation. In 2019, then-Governor Cuomo proposed changing the building aid ratio to the current year ratios for new projects. However, this proposal was not approved by the state legislature.[13] If New York State changed the building aid ratio to the current year ratio (36.6%), which is lower than the ratio currently used (56.9%), the City would receive less building aid revenue for future projects, and building aid revenue as a portion of education debt service spending would decline.

Even without changes to the building aid ratio, or other aspects of the building aid formula, the share of New York City education debt service spending that is covered by building aid revenue could change—and has changed (see Figure 3). For example, if the gap between the maximum cost allowance and actual project costs grows, building aid revenue as a share of education debt service would decline.

Conclusion

When planning education infrastructure spending, the City should consider both how it finances projects through borrowing, as well as how it will repay the associated debt service costs, as New York State constrains both. New York State limits how much New York City can borrow to finance construction projects, including school construction. This means the City must consider debt limits and sources of financing to ensure it has the necessary borrowing capacity to undertake projects. As previously mentioned, OMB also plans City borrowing around affordability of debt service spending, ensuring the City's total debt service costs do not exceed 15% of tax revenues.

However, when planning education infrastructure spending, the City should also consider the amount of state support it will receive through building aid revenue, which supports debt service for all types of borrowing. New York State's building aid formula, through the building aid ratio and the maximum cost allowance, constrains the amount of revenue New York City receives for school infrastructure. These constraints mean the State provides a different share of funding for education projects depending on specific project details. Therefore, the City faces tradeoffs in undertaking different types of education infrastructure projects. Projects that receive a lower share of State reimbursement through building aid revenue, such as new school construction, require more city funds to cover debt service payments, reducing the amount of city funds available for spending on other projects. Consideration of building aid revenue is particularly important as New York City works to meet a new state class size mandate, which may require significant additional new construction.[14] Indeed, as previously mentioned, New York State recently stipulated the City "shall increase planned spending on classroom construction by $2.0 billion" to meet the class size mandate.[15]

Endnotes

[1]N.Y. Public Authorities Law § 2799-gg. https://www.nysenate.gov/legislation/laws/PBA/2799-GG
[2]Office of State Aid. (n.d.) 2023-24 State Aid Handbook: Formula Aids and Entitlements for Schools in New York State. New York State Education Department. Retrieved July 15, 2024 from: https://stateaid.nysed.gov/publications/handbooks/Handbook_2324.pdf
Fiscal Analysis and Research Unit. (2024, March). State Aid to Schools: A Primer Pursuant to Laws of 2023. New York State Education Department. https://www.oms.nysed.gov/faru/PDFDocuments/Primer_2023.pdf
[3]For more details on New York City's Expense Budget, see IBO's guide to understanding New York City's budget.
[4]See a prior IBO brief for additional details on CFE as it relates to BARBs.
[5]As debt service payments reduce the principal owed on BARBs, debt outstanding will decrease, and new BARBs can be issued. In addition, BARBs can be issued to refinance existing debt. For example, the TFA issued $564 million of refunding BARBs on July 28, 2022. Transitional Finance Authority. (n.d.). Current Activities & Operations and Accomplishments. Retrieved July 15, 2024 from https://www.nyc.gov/site/transitionalfinance/about-tfa/current-activities-operations.page.
[6]Mayor's Office of Management and Budget. (2023). "City of New York Debt Management Policy, New York City General Obligation and New York City Transitional Finance Authority." https://www.nyc.gov/site/investorrelations/resources/debt-management-policy.page
[7]In addition to construction of new school buildings and renovations of existing school buildings, the State provides building aid to school districts for some lease costs, for lead water testing, and for assessments of building conditions. However, most building aid revenue is related to construction projects. Construction in areas that do not have a direct impact on instruction space, such as stand-alone playgrounds, are not eligible for building aid.
[8]The building aid ratio was higher in 1999 and 2000 than the current building aid ratio (see Appendix Figure 2) because of these additional adjustments.
[9]The State Aid Work Group. (2002, April). School District Responses to Building Aid Incentives. New York State Education Department. https://www.oms.nysed.gov/faru/Articles/FacilitiesRN_FINAL.htm
[10]Filardo, M. (2021). 2021 State of Our Schools: America's PK-12 Public School Facilities. 21st Century School Fund. https://www.21csf.org/uploads/pub/SOOS-IWBI2021-2_21CSF+print_final.pdf.
[11]Filardo, M. (2021). 2021 State of Our Schools: America's PK-12 Public School Facilities. 21st Century School Fund. https://www.21csf.org/uploads/pub/SOOS-IWBI2021-2_21CSF+print_final.pdf.
[12]Building aid revenue for projects undertaken prior to 2005 is ending as these projects reach their useful life (building aid revenue is paid over 15-30 years). The maximum building aid ratio was slightly higher for projects completed in 1999 and 2000 due to adjustments made in that period (64.7%; see Appendix Figure 2). While the City will receive building aid for additional new projects undertaken each year, the maximum building aid ratio for these projects has been fixed at 56.9% since 2006. That is, building aid revenue as a portion of debt service costs may be declining because new projects are being funded at a lower percentage than some projects previously included in building aid revenue.
[13]Karlin, R. (2019, Feb. 22). State building aid plan could dent some school budgets. Times Union. https://www.timesunion.com/news/article/State-building-aid-plan-could-dent-some-school-13634715.php
[14]New York City Department of Education (2024, July). Class Size Reduction Plan. https://infohub.nyced.org/reports/financial/contracts-for-excellence
[15]N.Y. Public Authorities Law § 2799-gg. https://www.nysenate.gov/legislation/laws/PBA/2799-GG