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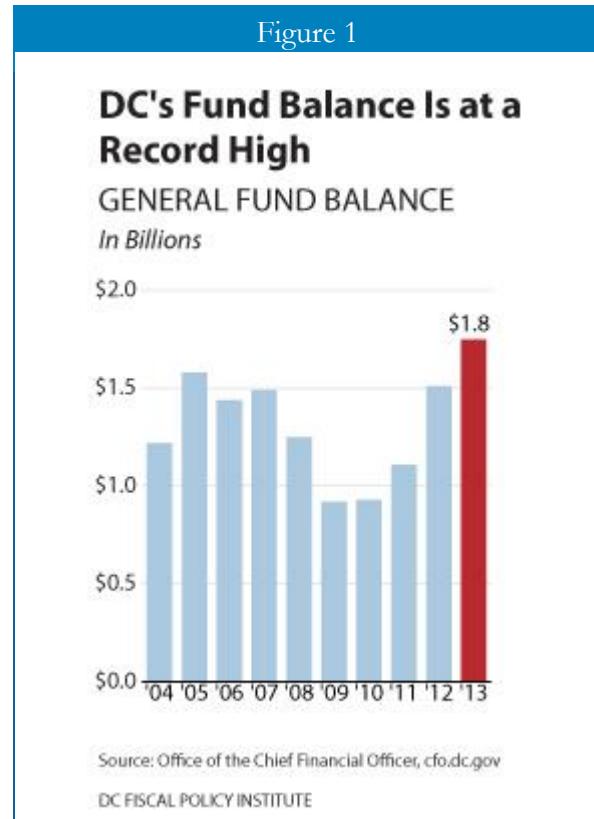
Putting DC's Surplus to Good Use: Save Some, Spend Some Recommendations to the New Mayor and DC Council

Mayor Bowser and the DC Council should change the rules that require DC to save every dollar of its annual surplus, so that half of any year's surplus can be spent on the city's most pressing needs, like affordable housing.

The District runs a budget surplus almost every year – which means revenues for the fiscal year end up being higher than what was spent. These leftover funds create an opportunity to make important one-time investments, such as building affordable housing or buying library books. The size of surplus, which is announced by February of each year, is unpredictable, but has totaled nearly \$1 billion over the last three years combined.

There is an obstacle to taking advantage of the surplus, however. Rules adopted in 2010 require all surplus funds to be set aside until certain reserves are filled. This savings-only approach is extreme given that the District's fund balance — in effect, its savings account — reached a record level at the end of 2013 and is larger than in most states.

- ❖ DC's fund balance dipped between 2007 and 2010 – from \$1.5 billion to \$900 million – as funds were withdrawn during the recession to help maintain important services such as health care and schools.
- ❖ But since 2011, the fund balance has grown to \$1.75 billion, reaching a record level at the end of 2013.
- ❖ The District's fund balance also is larger than in most states, when measured as a share of the budget. DC's \$1.75 billion fund balance equaled 27 percent of the local portion of the city's 2013 budget. In



contrast, the average fund balance across states equals just 11 percent of their budget, and only seven states have a fund balance that is larger than DC's as a share of the budget.

Yet current law will force the District to save all surplus funds announced in early 2015, and perhaps for several years to come. All surplus funds go in a “working capital” fund to help the city with cash-flow needs – that is, having cash on hand to pay bills every month, given that major tax collections are clustered at certain times of the year. There is \$295 million in the working capital fund now, but the target is roughly \$600 million.

The benefits of the working capital fund are modest and building it up should not be prioritized over using surplus funds for other needs. Having working capital limits the District's need to borrow funds for cash-flow purposes in the middle of the year, but such short-term borrowing costs the District just \$2.5 million in fiscal year 2015. This means that the District is setting aside hundreds of millions of surplus funds merely to save a few million per year.

The next surplus announcement is expected in early 2015. Mayor-elect Bowser and the DC Council can make better use of it by changing the rules to save half and spend half. This more balanced approach would allow the city's reserves to continue growing while also leaving funds to support important needs, such as the Housing Production Trust Fund or replacing the DC General family homeless shelter. This would be consistent with approaches taken in the past decade, and with the recently expressed desire of DC policymakers to use future surpluses for key investment needs.

- ❖ When the District experienced substantial annual surpluses in the mid-2000s, then-Mayor Williams used as much as \$500 million per year in surplus funds for a variety of purposes. During that period, the city's fund balance continued to grow or remained stable.
- ❖ Legislation adopted in 2014 will devote 50 percent of future surpluses to the Housing Production Trust Fund to help address the city's serious affordable housing shortage – but only after the working capital fund is filled. This provision is unlikely to result in any new resources for the Housing Production Trust Fund until at least 2016, even though the city's affordable housing needs are urgent and grow worse every year they are not addressed.

A balanced approach to any year-end surplus makes sense. Setting aside huge amounts of city resources in savings, when savings already are sizable, is a wasted opportunity to make investments that will improve the quality of life in the District.