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Safety Net:
Background on the City's Budget Reserves and How the Mayor Plans to Use Them

The de Blasio Administration's 2021 Executive Budget and 2020-2024 Financial Plan relies heavily on billions of dollars of funds held in various reserves to bring the 2021 budget into balance in the face of enormous fiscal pressure spawned by the coronavirus pandemic (all years refer to fiscal years). Compared with IBO's January forecast, we now expect the outbreak to reduce tax revenue for 2020 and 2021 by a total of $9.7 billion; the Mayor's Office of Management and Budget's (OMB) latest tax forecast includes a coronavirus revenue impact totaling $7.3 billion over the same two years.

To help replace this lost revenue, the Mayor's plan uses $1.0 billion of funds in the Retiree Health Benefit Trust (RHBT) as well as $280 million from funds allocated to the general reserve in 2020. To balance the 2021 budget, the city plans to draw down $1.6 billion from the RHBT, $900 million from the general reserve, and $250 million from the capital stabilization reserve. The use of these funds reduces the RHBT's projected balance at the end of 2021 to just below $2.1 billion and leaves the general reserve with just $20 million in the current year and $100 million in 2021, while completely exhausting the 2021 capital stabilization reserve—leaving fewer resources available if the fiscal outlook deteriorates further.

New York relies on multiple sources of reserves rather than a single rainy day fund like most states and some localities because of budget rules originally imposed in response to the 1970s fiscal crisis. While these rules may change in the future following a CIty Charter amendment approved by voters last fall, they remain in effect for now. Under the existing rules, the city budget must be balanced under generally accepted accounting practices (GAAP) at the start and close of the fiscal year. GAAP requires the city to use current year resources to pay current year expenses, preventing the use of surpluses from past years to build up a formal rainy day fund for use in future fiscal emergencies. In contrast, most state and local governments are allowed to follow accounting standards that permit the use of reserves built up in prior years to help balance their budgets when fiscal shortfalls emerge.

Retiree Health Benefit Trust Fund

The establishment of the RHBT was authorized by local law in June 2006. The trust was designed as a mechanism for the city to set aside funds to cover its increasing liability for the provision of health benefits to the city's retirees and their beneficiaries. Funds deposited into the trust could only be used to pay these expenses. The stated intent was to move away from the city's practice of pay-as-you-go funding of retiree health benefits in the current operating budget and to create a fund that could eventually grow to match the long-term liability of the city's retiree health benefit costs, similar to how the city funds its pension liabilities.

The trust acts as a conduit for the city, paying out all retiree health benefits over the course of the year, with the city reimbursing the trust for these payments at year's end. The RHBT can grow through earnings on the fund's investments plus any additional deposits by the city above the amount needed to cover a given year's benefit payments. Absent the ability to maintain a formal rainy day fund, the RHBT's assets have become the city's de facto rainy day fund that even the city's fiscal monitors acknowledge as reserves when they assess the city's fiscal cushion.

After making an initial deposit in 2006 of $1.0 billion the city's annual contributions and interest earned had grown the RHBT's balance to $3.2 billion in 2010, but with

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the economic recession sparked by the 2008 financial crisis depleting the city's resources, the Bloomberg Administration began to use the RHBT's assets to assist in balancing the budget. Whereas in previous years the city would fully fund that year's retiree health benefit cost, beginning in 2010 the city started only partially refunding the trust's current year expenses. By not conveying the full cost of the city's retiree health benefits to the trust, the city was able to reduce its current year expenses, helping to balance that year's budget, at the cost of lowering the RHBT's holdings.

In November 2013, the Bloomberg Administration's final financial plan called for draining the last remaining assets of the RHBT to help balance the 2014 budget. In January 2014, the incoming de Blasio Administration reversed these plans, choosing instead to add funds to the trust. In subsequent years the de Blasio Administration added more funds to the trust and by the end of 2019 the trust's assets had increased to nearly $4.7 billion.

The April 2021 Financial Plan marks the first time that the de Blasio Administration has moved to use the RHBT to help achieve budget balance. The current financial plan uses over half of the assets of the fund. Because the funds in the RHBT must be used exclusively for the city's retiree health benefit costs, the most budget relief the city can generate through the RHBT is that year's liability for retiree health benefits.

The de Blasio Administration estimates that the city's liability for retiree health benefits will total $2.2 billion for 2020 and $2.3 billion for 2021. The current plan to use $1.0 billion of RHBT assets in 2020 means that instead of making a payment of $2.2 billion to the trust to cover the entire 2020 liability, the city will make a $1.2 billion payment and draw down $1.0 billion of assets already in the trust to cover the balance of the 2020 health benefit liability. For 2021, the city will pay $656 million to the RHBT rather than $2.3 billion and draw down $1.6 billion of fund assets.

If needed, the city could generate additional budget relief, up to the total retiree health benefit liability each year. Thus, even with the use of RHBT assets contemplated in the Executive Budget, the city has an additional $1.2 billion available in the current year and $656 million available next year. If no additional RHBT assets are used, the remaining funds in the trust could be drawn down to reduce the 2022 budget gap, which OMB currently estimates at slightly over $5.0 billion.

General Reserve

Another condition originally imposed by the state's 1975 Financial Emergency Act required the city to "provide a general reserve for each fiscal year to cover potential reductions in its projected revenues or increases in its projected expenditures," in an amount no less than $100 million. This reserve fund, in the absence of any permissible way for the city to roll surplus funds from year to year, has been the primary means for the city to set aside funds to gird against unforeseen economic downturns within a fiscal year.

The city's general reserve is a budgeted expenditure that is not allocated to a specific city expense. In times of need OMB can shift funds from the general reserve to cover specific expenses, thus lowering the city's overall expense budget and concurrently the amount of revenue needed to balance the budget.

In recent years, the amount of funds in the current year's general reserve have typically been reduced as the year progresses and used either to address needs that emerge elsewhere in the budget or shifted into the city's budget stabilization account, which holds the current year's surplus.[1]

In the January Preliminary Budget the general reserve for 2021 was $1.0 billion but it has been lowered to $100 million in the Executive Budget; the $900 million freed up was used to help balance the 2021 budget. Even during the downturn following the 2008 financial crisis, the size of the general reserve at the start of the fiscal year was never less than $300 million. The budgeted general reserve of $100 million for the upcoming fiscal year is lower than at any point this century.

Capital Stabilization Reserve

In 2016 the de Blasio Administration created another reserve, the capital stabilization reserve. The capital stabilization reserve was similar to the general reserve in that the budgeted funds were not allocated to specific expenses. This reserve was created ostensibly to fund portions of the city's capital program without having to issue additional debt if projects were delayed or grew in scope. Funds from the reserve have never been allocated to specific expenses, however. Instead, like the general reserve, they have been drawn down through the fiscal year to add to that year's surplus. The depletion of the 2021 capital stabilization reserve prior to the start of the fiscal year marks the first time since the creation of the capital stabilization reserve that a year will begin without allocated funding.

Labor Reserve

The Executive Budget did not draw on another budget item that has been tapped in some previous downturns. The financial plan traditionally incorporates assumptions about pay increases for city workers that would be part of future contracts, in a central budget account known as the labor reserve. While any changes to already-scheduled pay increases would require negotiations with the city's municipal labor unions, the city has no legal obligation to provide increases in future contracts. Based on the assumption that future contracts would include increases of 1 percent annually, the labor reserve includes a total of roughly $2.2 billion in 2022 through 2024 to pay for them.

In the aftermath of the 2008 recession, the Bloomberg Administration reallocated money from the labor reserve for other purposes, leaving the de Blasio Administration a municipal labor force in which every union was working without a negotiated contract and with wages that had, in general, been frozen for several years. While the budget for 2021 is balanced in the Mayor's Executive Budget, the financial plan projects gaps of roughly $5.0 billion each year from 2022 through 2024. Bringing those out-year budgets into balance may require looking at other reserves besides those tapped so far.

Rainy Day Fund Authorization

In November 2019 voters in New York City adopted revisions to the City Charter that would allow for the creation of a revenue stabilization fund "to save money for use in future years, such as to address unexpected financial hardships." While the charter revision would enable the city to establish a true rainy day fund, it cannot do so without also making changes to state law.

New York City's current fiscal outlook is more ominous than at any other time since the city's fiscal crisis of the 1970s. The city is facing an unprecedented loss of actual and projected revenue over a very short time span. The city's inability to allocate funds to a true rainy day fund is one of the reasons that there are limited resources available to lessen the severity of the current fiscal crisis. The use of over $4.0 billion of reserve funds in the current and next fiscal year leaves very little capacity available if the city's fiscal outlook deteriorates further.

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Endnote

[1]In order to maintain GAAP compliance, the city does not roll any surplus forward and use it to pay regular operating expenses in the new fiscal year. Instead it uses up any surplus at the end of the current year to prepay debt service payments otherwise due in the upcoming year and to make required subsidy payments ahead of schedule to related entities such as the library systems, NYC Transit, and NYC Health + Hospitals, which are not part of the city's operating budget.