

**PUBLIC OVERSIGHT HEARING ON  
THE FISCAL YEAR 2006 AND 2007 SPENDING AND  
PERFORMANCE BY THE OFFICE OF THE CHIEF  
FINANCIAL OFFICER (OCFO)**

**Before the  
Committee on Finance and Revenue  
Council of the District of Columbia**

**The Honorable Jack Evans, Chairman**

**February 28, 2007; 11:00 a.m.  
Council Chamber, John A. Wilson Building**



**Testimony of  
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Deputy Chief Financial Officer  
Office of Revenue Analysis**

**Natwar M. Gandhi  
Chief Financial Officer  
Government of the District of Columbia**

Good morning Mr. Chairperson and members of the committee. I am Robert D. Ebel, Deputy Chief Financial Officer for Revenue Analysis and the District's Chief Economist. I am pleased to appear before you today to testify on the activities of the Office of Revenue Analysis (ORA).

### **Mission and Activities**

The mission of the Office of Revenue Analysis encompasses a wide range of fiscal and economic research as directed by the Chief Financial Officer (CFO). This includes responding, through the CFO, to requests by the Council of the District of Columbia and the Executive Office of the Mayor (EOM).

ORA's activities include:

*Preparing Fiscal Impact Statements.* The District of Columbia Home Rule Act of 1973 (Pub.L 93-198) requires that all legislation submitted by the Council of the District of Columbia to the U.S. Congress for review prior to enactment into law be accompanied by a fiscal impact statement (FIS), which estimates the costs that will be incurred by the District of Columbia as a result of enactment of an act in each of the first four (4) fiscal years for which the act is in effect. These estimates are to be accompanied by a statement of the scope of the legislation and the methodology for making the estimate.<sup>1</sup>

Per the District of Columbia Financial Responsibility and Management Assistance Act of 1995 (Pub.L 104 I, Stat. 1995), one of the duties assigned to the newly created Office of the Chief Financial Officer (OCFO) was the preparation of fiscal

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<sup>1</sup> District of Columbia Council rules also require the preparation of fiscal impact statements.

impact statements. This mandate was reiterated and made permanent in the recently approved District of Columbia Omnibus Authorization Act (Pub.L. 109-356, October 16, 2006).

During FY 2006, ORA analyzed and prepared fiscal impact statements for 235 bills, in addition to a host of other documents including contracts and regulations. For FY 2007 ORA's FIS workload is projected to increase significantly as the result of Mayoral and Council initiatives (including, at present, Bill 17-001 relating to the District of Columbia Public Education Reform Amendment Act of 2007). All fiscal impact statements prepared by the OCFO since 2001 are retrievable on the OCFO Web site at [www.cfo.dc.gov](http://www.cfo.dc.gov).

*Providing Periodic Reports on Economic and Revenue Outlook with Accompanying Revenue Estimates.* The OCFO is further responsible for forecasting the economic and revenue outlook for the District government. With respect to this activity, each February the OCFO issues the revenue estimate that is used to develop the Mayor's proposed budget for the next fiscal year (October 1 to September 30). The estimate is then revised quarterly thereafter.

Because of the high degree of attention given at this time to the outlook for the District's economy, as the FY 2008 budget is prepared, today's testimony provides a more detailed review of the revenue and economic outlook.

*Carrying out Special Studies.* In addition to fiscal impact statement and economic and revenue outlook activities, the Office of Revenue Analysis provides to the citizens of the District of Columbia a series of technical reports, all of which are

subject to an extensive internal and external peer-review process prior to release and publication. These include:

- DC Economic Indicators – Published monthly, these provide up-to-date detail on the performance of the District of Columbia with respect to the trends of the overall economy, revenues, and the sectors of labor, industry, office space, and housing.
- Tax Rates and Tax Burdens: Washington Metropolitan Area – Published annually, this report provides not only a comparison of the statutory rates of the District of Columbia *vis-à-vis* its five neighboring jurisdictions (Alexandria and the counties of Montgomery, Prince George’s, Arlington, and Fairfax), but also comparative measures of household tax burden by type of tax and different income levels.
- Tax Rates and Tax Burdens in the District of Columbia: A Nationwide Comparison – Also an annual publication, the nationwide comparison report provides a compendium of statutory tax rate comparisons and estimates of the household burden of major taxes by income class of the District of Columbia *vis-à-vis* the largest city in each of the other 50 states.
- The Economic Report of the District of Columbia: A Fiscal Perspective – New this calendar year (with publication targeted for next month), ORA will publish its first annual data book on the District of Columbia economy and its revenue system, with a text that is accompanied by a set of special analyses and supplemental economic and demographic data trends.<sup>2</sup>
- DC Tax Facts – This important and widely used pocket-sized reference of District tax collections provides descriptions of all the District of Columbia

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<sup>2</sup> Office of the Chief Financial Officer of the District of Columbia, *The Economic Report of the District of Columbia: A Fiscal Perspective*, Forthcoming, March 2006.

revenue (tax and non tax) sources, the history of major revenue changes since 1970, filing and payment dates, and the yield of each type of revenue utilized by the District of Columbia.

- Cash Reports – Each month ORA publishes a report of cash collections by the District of Columbia government. The tracking of these cash flows are particularly important in order to have an ongoing check on the quarterly revenue estimates. Then, at the end of the calendar year, as part of the process of preparing the Comprehensive Annual Financial Report (CAFR), ORA coordinates with the Office of Tax and Revenue to adjust the revenue numbers to reflect the net revenue accruals that then become the final numbers reported in the CAFR.
- Tax Expenditures – The D.C. Code requires the CFO to prepare a tax expenditure budget for Fiscal Year 2003 and biennially thereafter. Tax expenditures are revenue losses that arise from provisions of tax laws that reduce the tax liability of individuals, groups of individuals and/or institutions. The next release is set for spring 2008.
- Bills Subject to Appropriation Monitoring – ORA has initiated a process of tracking the status of legislation subject to appropriation, so that the OCFO, Council and Mayor may have an accurate picture at any one time of the status of legislation that has been approved by the Council but has yet to be funded.

### **Staffing and Budget**

For FY 2007 ORA's staffing at 25 FTEs has not changed from FY 2006. The FY 2007 budget for ORA is \$3.14 million, of which approximately 26% is

allocated to the Economic Development Finance (EDF) function.<sup>3</sup> Total operating expenses for ORA plus EDF through February 13, 2007, total \$1.46 million, or 45 percent of our budget. This expenditure pace reflects a calendar front-loaded requirement to annually purchase a wide range of database, regional modeling, statistical, and other software licenses. ORA's organization chart (excluding EDF) is provided as an attachment to this testimony.

### **Discussion of the Economic and Revenue Outlook**

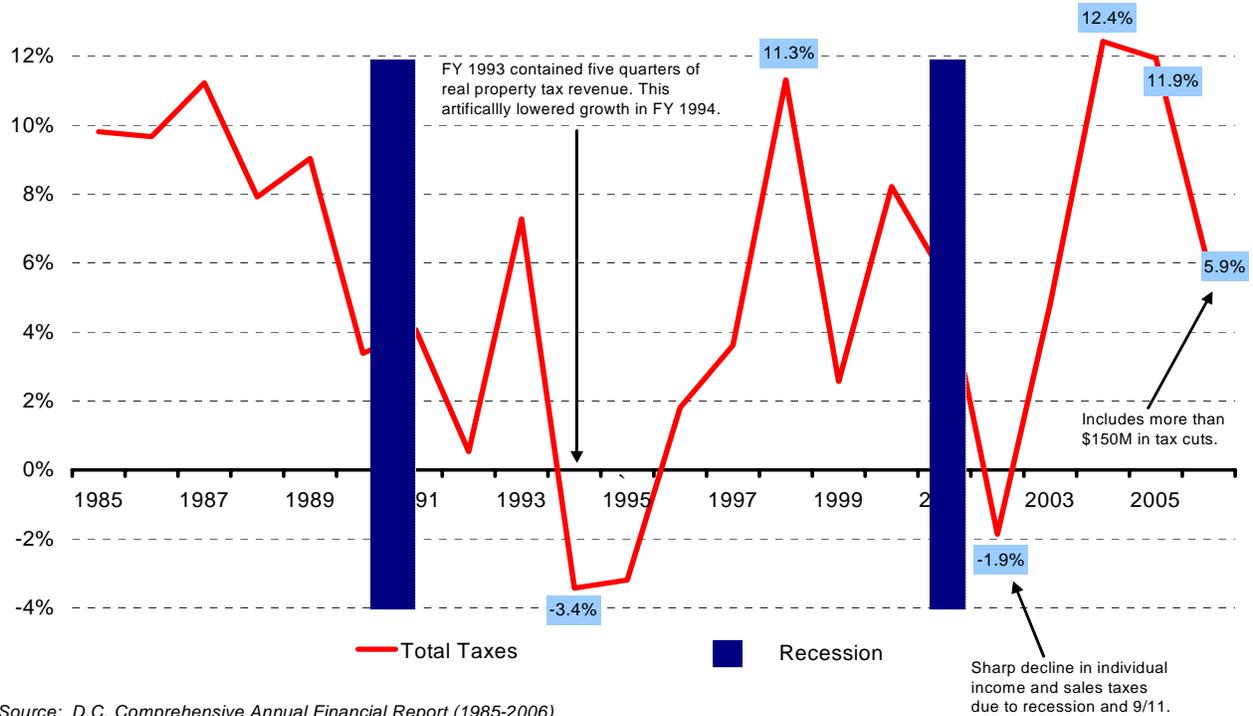
As noted, a key function of ORA is to provide timely and accurate reports on the District's economic and revenue outlook and, with that, estimates of the present and projected performance of the revenue system (with reports issued quarterly). In the time between the May official binding estimate, on which the budget is based, and the end of the forthcoming fiscal year, any number of changes can happen to the economy and the revenue stream – changes that are often exogenous to this revenue system. The chart below shows that the annual change in tax revenue can range widely. One challenge is to find what is “normal” in this growth and plan for a budget supported by normality – and subject to large swings. “Normal” or average growth in the last five years is about 6.8 percent, and in the last three years the percentage is about 10.1 percent. Yet, actual tax revenue did not grow by either of these specific percentages in any one of the last six fiscal years, bouncing from -1.9 percent to 12.4 percent.

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<sup>3</sup> The ORA FTE count includes six FTEs attached to the otherwise independent (of ORA) Office of Economic Development Finance. The key functions of Economic Development Finance are (i) to conduct research supporting the financing of special economic development projects; (ii) to conduct analyses of special finance projects, and (iii) to represent the CFO in economic development-related board commitments and provide research and analytical staff-work related to those commitments. The 26% does not reflect special grant funds for fiscal studies that EDF manages, which supplement its staffing operations.

# Volatile Tax Revenues

Annual Percent Change in Tax Revenue: FY 1985 - 2006



Source: D.C. Comprehensive Annual Financial Report (1985-2006)

Since FY 2000, the District has had to twice grapple with this volatility. First, in FY 2002 income tax revenue fell abruptly and precipitously due to the events associated with September 11, 2001, which included a subsequent recession accompanied by a stock market decline. When these developments were identified in the summer of 2002, the challenge for the Council and the Mayor was to create a balanced budget using revenue enhancements and expenditure reductions.

Adjustments were made in both FY 2002 and 2003, and the District of Columbia closed out both FY 2002 and FY 2003 with small, but positive, budget surpluses.

In FY 2003 the opposite swing began with transactions in both residential and commercial real property. Arising out of a year of no change in FY 2002, by the end of FY 2004 the annual value of transactions had more than doubled.

Moreover, due to in part to the deed tax rate changes that had been enacted to deal with the prior revenue shortfall, deed tax revenues also more than doubled between 2002 and 2004 (DC Tax Facts, various issues).

### **Final Comments on the Outlook for FY 2007 and FY 2008**

ORA projects steady growth in employment, wages, and personal incomes for the District during the next two years, similar to what is projected by most economists for the nation as a whole.

Our estimating assumptions for FY 2007 and FY 2008 include, respectively:

- Job growth of 1.0 percent and 0.8 percent;
- Growth of 1.2 percent and 0.3 percent each year in total resident employment;
- 4.9 percent and 5.2 percent increases in the personal income of District residents; and
- (Low) inflation of 2.4 and 2.3 percent, respectively.

The private sector service industries, such as professional and business services, education, health, retail, and hospitality services will be the drivers of most of the increases in jobs and wages in the District.

Total revenue available for general fund purposes in FY 2007 (that is, revenue available after earmarking for such things as the convention center transfer, tax increment financings and school modernization) is forecast to be 3.5 percent greater than in FY 2006, then rising by 5.5 percent in FY 2008. The growth in total general fund revenue in FY 2006 was 4.7 percent over FY 2005.

Although the national and local economies continue to show considerable strength, recent developments point to a number of possible risks. For example, the U.S. economy continues to grow, but much of this depends upon continued gains in consumer spending. Consumers are heavily indebted, with net saving rates close to zero. Were consumers to cut back on spending, a slowing U.S. economy would eventually impact the District's economy, primarily through its dampening effect on tourism receipts, other retail sales, and corporate profits. District revenues are also vulnerable to a sharp rise in interest rates or declines in the stock market, because these affect the real property market, corporate income, and the non-wage component of the individual income tax.

Another source of risk is the pattern of federal expenditures. Government spending is a significant economic underpinning of the entire Washington, D.C., metropolitan area, including spending by the District of Columbia itself. Security concerns arising out of 9/11 and the Iraq war have resulted in large increases in government spending that benefited the Washington, D.C., area. However, federal government employment is now declining, and there is some evidence that procurement dollars spent in D.C. are not increasing. Efforts to reduce government spending during the next few years to bring greater balance to federal fiscal policy could further dampen growth in the District. Uncertainties about when the D.C. housing market will return to better health and when tourism will rebound also add uncertainties to revenues in the months ahead.

Thank you for the opportunity to testify before you today. I am pleased to respond to any questions that you may have.

**Office of Revenue Analysis**  
Organization Chart

