GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER

Jeffrey S. DeWitt
Chief Financial Officer

September 29, 2014

The Honorable Vincent C. Gray
Mayor of the District of Columbia
1350 Pennsylvania Avenue, NW – 6th Floor
Washington, DC 20004

The Honorable Phil Mendelson
Chairman
Council of the District of Columbia
1350 Pennsylvania Avenue, NW – Suite 504
Washington, DC 20004

Dear Mayor Gray and Chairman Mendelson:

This letter certifies that the revenue estimates for FY 2014 - FY 2018 remain unchanged from the July 1, 2014 certification except for adjustments required by the FY 2015 Budget Support Act. As you will recall, the June estimate did not change the forecast from February, leaving it as the baseline. Accordingly, Table 1 shows the estimate adjusted by the amount of the policy adjustments the Budget Support Act requires.

Table 1: June 2014 Estimate with Legislative Changes

Local Fund Revenue Estimate ($ millions)	Estimate		Projected		
	FY 2014	**FY 2015**	**FY 2016**	**FY 2017**	**FY 2018**
June 2014 Estimate	**$6,334.1**	**$6,690.7**	**$6,896.3**	**$7,119.5**	**$7,276.2**
Legislative changes in the FY 2015 Budget Support Act	-	($29.8)	($26.9)	($28.5)	$35.1
September 2014 Estimate adjusted for Legislative Changes	**$6,334.1**	**$6,660.9**	**$6,869.3**	**$7,091.0**	**$7,311.3**
% change annual	***2.1%***	***5.2%***	***3.1%***	***3.2%***	***3.1%***

While the forecast is unchanged, we are closely monitoring several key revenue sources, where collections are currently trending below forecast, the most significant of which is traffic fines revenue. The February forecast for FY 2014 local source revenue is $6,334 million, projecting that revenue will grow by 2.1 percent (or by $131 million) over FY 2013. As of August, the 11th month of the fiscal year, revenue collections are up by only 1.2 percent, nearly a full percentage point below the rate anticipated in the forecast. If this trend of 1.2 percent continues through the end of FY 2014, the collections would fall short of the FY 2014 estimate. Collections for the year are not complete, and accounting adjustments made as we close the year can be significant, so a definite conclusion about the final tally for FY 2014 cannot be made at this time. It is important to note here that if the final tally of FY 2014 collections is below forecast, there would be consequences for FY 2015 as well, requiring a downward revision in the FY 2015 revenue forecast by $50 to $70 million in the December certification letter that would impact FY 2016 budget planning.

Revenue Highlights

Every year, some revenue sources exceed, and some fall below, expectations. This is also true for FY 2014. The three revenue categories falling behind their forecasted levels (and unlikely to reverse course) are Fines and Forfeitures, Business Franchise (income) taxes, and the Individual Income tax. The biggest gap between current collections and the FY 2014 forecast is in the category of Fines and Forfeitures. If current trends continue, this nontax revenue could come in at about $70 million less than the projected revenue. Revenue from fines was projected to increase because of the rollout of new automated enforcement equipment. Instead, it has declined to levels that are even lower than in FY 2011. The assumption in the February and June forecasts was that automated traffic enforcement revenue would continue to increase as full implementation of these devices occurred, but the implementation has been delayed. The 40 percent decline in fines, which already undermines the FY 2014 forecast, poses the greatest downside risk to the FY 2015 revenue estimate.

Business Franchise taxes are running about $52 million below the estimate, due to large refunds and credit carryovers from prior years and Individual Income taxes are down by about $45 million. The income tax shortfall is driven by larger than expected declines in non-withholding due to capital gains realizations. Like many other states, the District had an "April surprise" with lower final payments than expected. This is because the income acceleration that occurred in FY 2013—that is, shifting of income to FY 2013 in response to federal tax law changes in FY 2014—was even greater than anticipated, reducing collections in FY 2014. (It is worth noting that sales taxes are down, but by a smaller amount of $23 million. Most of this decline was due to weakness in the winter months. Recent trends have indicated growth in line with or exceeding expectations, reversing the impact of the earlier slow-down.)

The above shortfalls are partially offset by increases in deed tax revenues, which were forecasted to decline in FY 2014, but have turned out to be strong and will likely add about $58 million in FY 2014. Miscellaneous Revenue, which includes revenue from unclaimed property and other non-recurring sources, is projected to add at least $43 million. In addition, the withholding component of income, perhaps the most important barometer of the state of the District's economy, is growing at a 5.0 percent rate, a full percentage point higher than anticipated. This has helped to offset, but only partly, the aforementioned weakness in the non-withholding component of income.

Finally, property taxes are on track to rebound by 4.4 percent, and the strength of the real estate market is also manifested in the overall deed transfer and recordation tax revenues which were anticipated to decline by more than 14 percent but are currently running 3.8 percent higher on year over year basis.

As I indicated, there is still some unpredictability regarding FY 2014 revenues. There are a number of reasons for this uncertainty:

- We still do not have full information on 4th quarter income and franchise tax collections.
- Lags in the remittance of sales and withholding taxes mean that there remain two more months of collections for these taxes.
- End-of-year accrual adjustments, which can be quite large, cannot be predicted at this point.
- Based on second-half billing information, real property tax revenues are expected to meet the estimate, but this expectation assumes that the collections will match the billing, and that end-of-year adjustments will lead to no surprises.
- Miscellaneous Revenue includes Prior-Year Cost Recoveries and other highly uncertain year-end entries. Our current estimate for these year-end adjustments is $25 million, compared to over $70 million last year.
- Uncertainty is unavoidable at this time of year because one fifth of all collections occur in September. Well over 40 percent of all real property tax collections occur in the last month.

Our expectation is that the net effect of the uncertainty will be to bring in sufficient revenue to meet the FY 2014 forecast. Yet, a shortfall of $70 million in FY 2014 and a downward revision of $50 to $70 million for FY 2015 cannot be ruled out and depends crucially on what happens to automated traffic fines collections between now and December. I believe it is in the interests of sound fiscal planning to bring these issues to your attention before we have the final accounting for the year.

We will continue to monitor revenue collections and the economy closely and will immediately alert you to any significant developments that affect the District's financial position between now and the next estimate.

If you have any questions regarding this matter, please do not hesitate to contact me.

Sincerely,

Jeffrey S. DeWitt

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