Government of the District of Columbia

Office of the Chief Financial Officer
Office of Financial Operations and Systems
1100 4th Street, S.W. (East Building), 8th Floor
Washington, D.C. 20024
(202) 442-8200
(Fax) (202) 442-8201

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Dr. Natwar M. Gandhi
Chief Financial Officer

The Comprehensive Annual Financial Report (CAFR) of the Government of the District of Columbia (District) for the fiscal year ended September 30, 2010, is herewith submitted. Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with District management and the Office of the Chief Financial Officer. To the best of my knowledge and belief, the enclosed financial statements and schedules are accurate in all material respects and are reported in a manner designed to present fairly the financial position and results of operations of the various funds and component units of the District.

This report has been prepared in accordance with generally accepted accounting principles (GAAP) for governments as promulgated by the Governmental Accounting Standards Board (GASB) and includes all disclosures necessary for readers to gain a useful understanding of the District's financial activities. The city of Washington, D.C. is referred to in this CAFR as Washington, D.C., the City, the District of Columbia, and the District.

The ability to produce a timely and accurate CAFR depends upon the adequacy of the District's internal controls. Internal control is defined as a process, effected by an entity's governing board, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in one of the following categories: (a) efficiency and effectiveness of operations; (b) reliability of financial reporting; and (c) compliance with applicable laws and regulations. Reasonable assurance is defined as a high, but not absolute, level of assurance about whether the financial statements are free of misstatement. The District's management is responsible for establishing and maintaining adequate internal controls. The greatest challenge in establishing and maintaining adequate internal controls is ensuring that the control framework developed by management is comprehensive—that is, broad enough to achieve its intended purpose.

Due to certain inherent limitations, such as prohibitive costs, judgment errors, or potential for management override and collusion, internal control can only provide reasonable assurance that management's objectives will be achieved. However, routine, periodic audits help management to assess, on an on-going basis, the adequacy of the District's internal controls. In accordance with D.C. Code Section 47-119, an independent auditor audited the District's financial statements for the year ended September 30, 2010. The audit was conducted in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards, issued by the Comptroller General of the United States. In addition to issuing an opinion on the District's financial statements, the independent auditor, KPMG, LLP, also prepared a report, which is issued in conjunction with the CAFR, that discusses the auditor's consideration of the District's internal control over financial reporting and the outcome of the auditor's tests of the District's compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters.

Moreover, an audit of compliance with the Federal Single Audit Act Amendments of 1996 and the related OMB Circular A-133 is also performed annually. The District's fiscal year 2010 Single Audit Report will be issued at a later date.

GASB Statement No. 34 requires management to provide a narrative introductory overview and analysis (termed management's discussion and analysis (MD&A)) to accompany the basic financial statements. This letter of transmittal is designed to complement the MD&A and, therefore, does not discuss the District's financial operations and results. For that reason, this letter should be read in conjunction with the MD&A in order to gain a better understanding of the District's financial condition.

PROFILE OF THE GOVERNMENT

Overview: Historical Background of the District

President George Washington established Washington, D.C. (the District of Columbia) in 1791 from territory ceded by Maryland and Virginia. The United States Congress assumed jurisdiction over the District of Columbia, but residents of the District of Columbia did not have voting representation in Congress.

In February 1801, Congress enacted the Organic Act of 1801, that divided the capital district into the counties of Washington (former Maryland area) and Alexandria (former Virginia area). In 1846, Congress passed a law that allowed the return of the City of Alexandria and Alexandria County to the Commonwealth of Virginia. In 1871, Congress consolidated the three remaining municipal governments of the District of Columbia-Georgetown, Washington City and Washington County, into one territorial government. A territorial governor and council were appointed by the President and an elected House of Delegates and a non-voting delegate to Congress were also created. However, in 1874, the territorial government of the District of Columbia was abolished and the non-voting delegate to Congress was also eliminated at that time. The power to elect a territorial governor and council was subsequently eliminated in 1878. In that year, Congress passed legislation which established a three-member Board of Commissioners to govern the District of Columbia. This form of District governance lasted for almost 100 years.

With the ratification of the 23rd Amendment to the U.S. Constitution in 1961, citizens of the District of Columbia were granted the right to vote in a presidential election. As part of a reorganization of city government that also included an appointed council, in 1967, President Lyndon Johnson appointed Walter E. Washington Mayor of the District of Columbia. In 1970, Congress passed the District of Columbia Delegate Act, and in 1971, Walter Fauntroy became the first Congressional Delegate to represent the District of Columbia.

Congress passed the District of Columbia Home Rule Act in 1973, which provides for a popularly elected mayor and a 13-member Council of the District of Columbia (Council). Congress retained and continues to retain the right to review and overturn the legislative acts of the Council if both houses vote within 30 legislative days to do so. The budget for the District of Columbia government must be approved by Congress and the President of the United States.

The Home Rule Act prohibits the taxing of federal property, other property exempted from taxation by federal law and the income of non-District residents who work in the District. In 1983, it was determined that the District could legally issue its own debt and on October 15, 1984, the District issued municipal debt on its own, for the first time, in the form of Tax Revenue Anticipation Notes (TRANs), totaling $150 million. These TRANs were paid in full on September 30, 1985.

Although progress has been made on many fronts throughout the city's history, District of Columbia residents do not have voting representation in Congress. In accordance with the District of Columbia Delegate Act of 1970, U.S. Public Law 91-405, the citizens of the District of Columbia are represented in the House of Representatives by a Delegate, who is elected by the voters of the District of Columbia. Consistent with the Act:

> *The Delegate shall have a seat in the House of Representatives, with the right of debate, but not of voting, shall have all the privileges granted a Representative by § 6 of Article I of the Constitution, and shall be subject to the same restrictions and regulations as are imposed by law or rules on Representatives. The Delegate shall be elected to serve during each Congress.*

Although the current D.C. Delegate, Congresswoman Eleanor Holmes Norton, has no voting power, she has been able to accomplish much for the citizens of the nation's capital. The following are some of her major recent accomplishments:

- Secured $5.8 million in federal Stimulus funding for the construction of a levee in the area near 17th Street and Constitution Avenue. The Federal Emergency Management Administration (FEMA) has identified potential flood zones in the Southeast and Southwest areas of the District, surrounding the U.S. Capitol and monuments; residents within the 100-year flood zones will be required to obtain flood insurance until a levee is constructed by the Army Corps of Engineers.

- Launched inter-city bus service from the District's Union Station as part of efforts to transform Union Station, making it a model inter-modal transportation center that offers AMTRAK, Washington Metropolitan Area Transit Authority (WMATA) rail and bus, Virginia Railway Express (VRE), Maryland Area Regional Commuter (MARC), bike-sharing, taxicab, and low-cost privately-owned bus services. Such transformation is occurring as train service at Union Station is being expanded and plans are under way to develop the air space above the railroad tracks into retail and commercial space.

- Maximized District funding made possible by the passage of the American Recovery and Reinvestment Act (ARRA), or federal "Stimulus Bill" by securing more than $3 billion to be used to save critical city jobs, upgrade schools, and make infrastructure improvements. The District also received Stimulus funds for the U.S. Department of Homeland Security Headquarters, being constructed in the District's Ward 8, and the repair and upgrade of federal buildings located in the District. Secured $135 million in the Stimulus Bill to rehabilitate the National Mall and National Park Service parks within the District.

- Achieved renewal of the $5,000 District homebuyer and small business tax credits in an effort to help District residents through the mortgage crisis and the declining job market.

For more information on the goals and accomplishments of the D.C. Delegate, visit Congresswoman Eleanor Holmes Norton's website at www.norton.house.gov.

Financial Reporting Entity

For financial reporting purposes, the District's reporting entity consists of: (1) the primary government; (2) five discretely presented component units (Housing Finance Agency, University of the District of Columbia, Washington Convention and Sports Authority, Water and Sewer Authority, and the Not-For-Profit Hospital Corporation (the United Medical Center)); and (3) one blended component unit (the Tobacco Settlement Financing Corporation). The District of Columbia Housing Authority and the District of Columbia Courts are considered related organizations because the District is not financially accountable for their operations. The funds and accounts of all agencies, boards, commissions, foundations, and authorities that have been identified as part of the primary government or a component unit have been included in the reporting entity. Further information on the reporting entity can be found in Note 1B, page 56 of the Notes to the Basic Financial Statements.

The District and its component units provide a wide range of services to residents, including elementary, secondary, and postsecondary education; health and human services; economic development and regulation; public safety; transportation; and other general government services.

Budgetary Information

During the first quarter of each fiscal year, agencies begin the budget formulation process for the upcoming fiscal year. Around March of each year, consistent with Section 442 of the Home Rule Act, the Mayor submits a balanced operating budget for the upcoming fiscal year to the Council for review and approval. The Council holds public hearings and adopts the budget through passage of a Budget Request Act. A financial plan for the District's capital projects is also adopted. The Mayor may not submit and the Council may not adopt any budget which presents expenditures and other financing uses that exceed revenues and other financing sources. After the Mayor approves the adopted budget, it is forwarded to the President and Congress for approval. Congress holds public hearings and enacts the District's budget through passage of an appropriations bill, which is signed into law by the President of the United States.

The legally adopted budget is the annual Appropriations Act passed by Congress and signed by the President. The Appropriations Act authorizes expenditures at the agency level and by appropriation title (function), such as Public Safety and Justice; Human Support Services; or Public Education. To revise planned expenditures for any function, Congress must enact the appropriate legislation. However, the District may reallocate budgeted amounts using the District's reprogramming process in accordance with applicable legal requirements.

The District utilizes budgetary controls designed to monitor compliance with expenditure limitations contained in the annual Appropriations Act. Both automation and sound governance provide strong budgetary controls. The annual budget is assigned specific accounting attributes and is uploaded into the District's accounting system of record, thereby establishing the budget authority for each entity within the District government. The budget authority established in the system of record is then reconciled to the levels of funding authorized by the Appropriations Act. In addition, on an annual basis, independent auditors review the budgetary comparison statement to ensure compliance with federally approved amounts and to determine whether budget adjustments are properly documented and approved.

The "*District Anti-Deficiency Act of 2002*" (the Act), which became effective on April 4, 2003, introduced additional budgetary control requirements. This Act requires District managers to develop spending projections, by source of funds, on a monthly basis, which show year-to-date spending, approved budget, year-end projected spending, explanations of variances greater than 5% or $1 million, and planned corrective actions for instances of overspending. Spending projections are required to be submitted to the agency head and the Agency Fiscal Officer. Summarized spending projections must be submitted to the District's CFO no later than 30 days after the end of each month.

Other reporting requirements have also been established to enhance the District's budgetary control policies and practices. Consistent with D.C. Code § 47-355.04, agency heads and Agency Fiscal Officers are to submit jointly a monthly spending plan for the fiscal year to the CFO by October 1 of each fiscal year. In addition, pursuant to D.C. Code § 47-355.05, the District's CFO is to submit quarterly reports to the Council and the Mayor that present each agency's actual expenditures, encumbrances, and commitments, each by source of funds, compared to each agency's approved spending plan. This report is required to be accompanied by the District CFO's observations regarding spending patterns and steps being taken to ensure that spending remains within the approved budget. These reports are used by the District's Anti-Deficiency Review Board to assess cases of overspending.

In addition, the District uses encumbrance accounting as a means of strengthening budgetary controls and financial reporting. Under this method of accounting, purchase orders, contracts, and other commitments for the expenditure of funds are recorded in the financial system of record in order to reserve the portion of the related appropriation that will be needed for the expenditure. Therefore, the recording of encumbrances is a valuable tool used by the District to ensure that expenditures are within budgeted amounts. Generally, encumbered amounts lapse at year-end in the General Fund but not in the Capital Projects Fund, Special Revenue Fund, or the fund for Federal Payments.

Cash Reserves

Through Congressional mandate, the District is required to maintain cash reserves totaling 6% of the previous fiscal year general fund expenditures less debt service cost. The 6% is comprised of a contingency cash reserve of 4% and an emergency cash reserve of 2%. The contingency cash reserve may be used to provide for nonrecurring or unforeseen needs (e.g., severe weather or other natural disasters, and unexpected obligations created by federal law) that arise during the fiscal year or to cover revenue shortfalls experienced by the District for three consecutive months. The emergency cash reserve may be used to provide for unanticipated and nonrecurring extraordinary needs of an emergency nature (e.g., natural disaster or calamity) and may be used in the event that the Mayor declares a State of Emergency in the District.

District Accounting and Financial System

Accounting System

The District's accounting system is organized and maintained on a fund basis. Each fund, which is a separate, distinct accounting entity, has its own assets, liabilities, equity, revenues, and expenditures/expenses. The District uses generally accepted accounting principles (GAAP) when determining the types of funds to be established and is guided by the "minimum number of funds principle" and sound financial management practices when determining the number of funds to be set up within each fund type. Specialized accounting and reporting principles and practices apply to governmental funds. Proprietary funds, component units and pension trust funds are accounted for in the same manner as business enterprises.

Measurement Focus and Basis of Accounting

The District's financial statements are prepared in accordance with generally accepted accounting principles (GAAP). Accordingly, the measurement focus and basis of accounting applied in the preparation of government-wide financial statements and fund financial statements are as follows:

- The government-wide financial statements focus on all of the District's economic resources and use the full accrual basis of accounting.

- Fund financial statements focus primarily on the sources, uses, and balances of current financial resources and use the modified accrual basis of accounting.

- The budgetary basis of accounting is used to prepare the budgetary comparison statement presented in Exhibit 2-d. This basis of accounting differs from the GAAP basis as a result of the following:

  - ***Basis Differences*** - The District uses the purchases method for budgetary purposes and the consumption method to account for inventories on a GAAP basis. Under the purchases method, purchases of inventories are recognized as expenditures when the goods are received and the transaction is vouchered. Under the consumption method, an expenditure is recognized only when the inventory items are used.

  - ***Entity Differences*** - This basis relates to inclusion or exclusion of certain activities for budgetary purposes as opposed to those on a GAAP basis for reporting purposes. Such activities primarily include the following as reported in Exhibit 2-d:

    1. Fund balance released from restrictions
    2. Proceeds from debt restructuring
    3. Accounts receivable allowance
    4. Operating surplus from enterprise funds

  - ***Perspective Differences*** – Perspective differences exist when the structure of financial information for budgetary purposes differs from the fund structure that is used to construct the basic financial statements. If there were significant budgetary perspective differences, the District would not be able to present budgetary comparisons for the District's general fund and major special revenue funds as part of the basic financial statements. In that case, the District would present its budgetary comparisons as required supplementary information (RSI). The District does not have any significant budgetary perspective differences that limit its ability to present budgetary comparisons of its general fund. The District's *Budgetary Comparison Statement* is presented as part of the basic financial statements in Exhibit 2-d beginning on page 47.

- ***Timing Differences*** – Timing differences can exist when there are significant variances between budgetary practices and GAAP, which may include continuing appropriations, project appropriations, automatic re-appropriations, and biennial budgeting. The District has no significant timing differences between its budgetary practices and its GAAP presentation of its financial statements.

Cash Management

It is the District's policy to combine or pool all cash of the primary government unless prohibited by law. Cash that is not needed for immediate disbursement is generally invested in securities which are essentially guaranteed by the federal government. Such investments include but are not limited to mutual funds consisting of federal government obligations or repurchase agreements collateralized by federal agency obligations.

However, pursuant to the Financial Institutions Deposit and Investment Amendment Act of 1997 (D.C. Code §47-351.03), the District may invest in certain obligations that are not guaranteed by the federal government. Such deposits and investments must be fully collateralized with approved securities that are held by the District or by its agent in the District's name.

Risk Management

With the exception of healthcare and life insurance benefits for employees, the District retains the risk of loss arising from the ownership of property or other causes. The District is self-insured for general liability and liabilities associated with unemployment and disability (worker's compensation). A liability is established in the government-wide statement of net assets to reflect certain contingencies; however, this amount is not intended to include all assets that may be required to finance losses. Rather, certain losses are recognized in the affected funds when they occur.

Transparency in Financial Reporting

The Office of the Chief Financial Officer (OCFO) continues to promote openness in government and transparency in financial reporting. Over the last ten years, the District has opened its books to the public by posting online the annual operating budget and capital plan, the comprehensive annual financial report, and the popular annual financial report. In addition, the OCFO's website provides information that allows taxpayers to review and assess the District's financial status, programs, activities and services, and determine how their tax dollars are being used. This information includes: monthly cash collection reports; debt management policy and data regarding bond issuances; monthly reviews of economic trends; other economic indicators and reports; CFO News (including press releases and Council Hearing written testimonies); and links to other useful information, such as the Taxpayer Service Center, the D.C. College Savings Plan, Unclaimed Property Division, and the Office of Contracting and Procurement.

With the receipt of Stimulus Funds, the District broadened its efforts to be transparent in financial reporting by creating the website, www.recovery.dc.gov. This website offers a wealth of information regarding the District's receipt and use of federal Stimulus funds. More specifically, it allows the general public to track the District's applications for Stimulus funds, and the receipt and use of such funds (by project category and District agency). This site also: (a) provides information on how District residents may access the benefits associated with Stimulus funds, such as health care assistance through Medicaid, additional job training and placement programs, unemployment benefits, and nutrition assistance programs; (b) discusses how the District's Stimulus funds are managed; and (c) presents guidance on applying for federal Stimulus awards.

To ensure accurate and consistent accounting for and reporting of Stimulus funding, the OCFO implemented Stimulus 360, a web-based application that provides background information on the Act and details on how Stimulus awards are to be recorded in the District's accounting system of record. It also presents specific guidelines for completing a Stimulus application, drawing down awarded funds from the federal government, and preparing the required financial and programmatic reports. Stimulus 360 also provides information on the key District programs which are funded by Stimulus dollars; presents legislative updates pertaining to the Stimulus Act; presents Stimulus Frequently Asked Questions; and provides links to other pertinent information (*e.g.*, copy of the American Recovery and Reinvestment Act, OMB Memoranda for the Heads of Departments and Agencies, U.S. Department of Education Race to the Top Budget Guidance, etc.) and related websites (*e.g.*, the Mayor's Official Recovery website (www.recovery.dc.gov), the federal government's Recovery website (www.recovery.gov), www.grants.gov, and other related sites.)

ECONOMIC CONDITION AND OUTLOOK

Impact of the Recession on the District in Fiscal Year 2010

The impact of the recession on the District's economy was mixed in fiscal year 2010. During the recession, the District and the entire metropolitan region benefitted greatly from the presence of the federal government, which is the source of jobs from both direct federal hiring and contracts. Jobs located within the District remained strong compared to the rest of the nation; however, unemployment among District residents continued to be high in fiscal year 2010.

The District's economy is strongly influenced by its position as the central city of one of the best performing metropolitan areas in the country. The District accounted for 23.8% of the Washington metropolitan area's wage and salary employment and 10.5% of its resident employment during the quarter ending June 30, 2010.

Some of the factors that demonstrate the District's mixed economic picture in fiscal year 2010 include the following:

- During the three-month period ending July 2010, there were approximately 12,500 (1.8%) more wage and earned salary jobs located in the District than a year earlier. The federal government gained 10,367 (5.2%) more jobs over the past year, while the private sector gained 2,733 (0.6%) more jobs. (The private sector gains were in the relatively low wage miscellaneous business services category.)

- District resident employment during the three-month period ending July 2010 was 3,402 (1.1%) more than a year earlier. However, the total labor force also increased by 3,682 (1.1%), resulting in only a minor reduction in the unemployment rate.

- The District's unemployment rate in July 2010 (9.8% seasonally adjusted) moved closer to the national rate of 9.5%.

- During the summer of 2010, the number of housing sales declined compared with the prior year, while average prices were higher. Single family sales for the three-month period ending July 2010, were down 3.3% from a year ago, and the average selling prices were 2.2% higher. Condominium sales in that three-month period were down 25.8% but average prices were 8.4% higher over the prior year. Due principally to the decline in the number of condominium sales, the value of all home sale contracts for the three-month period ending in July 2010, was 7.7% less than the prior year.

- In the quarter ending in September 2010, occupied office space rose by 1.5% from the prior quarter and 4.8% from the prior year. At the same time, the commercial office vacancy rate fell from 10% (including sublet) in June 2010 to 9.1% in September 2010. The September 2010 vacancy rate was well below the metropolitan area average of 12.2%.

Local Economy

Population

The U.S. Census Bureau estimated that there were 601,723 residents in Washington, D.C., as of July 1, 2010. This represents an increase of 2,066, or 3.45%, from the revised July 1, 2009, estimate of 599,657. The annual census estimates are based on birth and death records, changes in tax return filings, and estimates of the number of immigrants who move into the District each year. **Chart 1** found on the following page presents the District's population trends for calendar years 2006 through 2010.

Employment Trends

Total wage and salary employment in the Washington metropolitan area increased to approximately 2,984,000 in fiscal year 2010 from the revised 2,928,600 for fiscal year 2009, representing a 1.9% increase. These numbers exclude the self-employed, domestic workers, and military and foreign government personnel, which represent a significant portion of the total workforce of the region. Some of the references to the 2009 employment numbers may differ from those presented in the fiscal year 2009 CAFR because of updates and revisions. **Table 1** found on the following page presents 2010 labor market data for the District and the metropolitan region.

During the past three years, total wage and salary employment within the District increased slightly to 24.0% of the metropolitan area's total wage and salary employment. The seasonally adjusted September 2010 unemployment rate in the District was 9.8%, compared to the September 2009 seasonally adjusted rate of 11.1%.

Total employment within the District increased to 718,000 as of September 2010 from the revised 695,700 as of September 2009. As the nation's capital, Washington, D.C. is the seat of the federal government and headquarters for most federal departments and agencies. The total September 2010 federal workforce in the Washington metropolitan area was 379,000; with approximately 212,200 federal employees located in Washington, D.C. and 166,800 additional federal employees who worked elsewhere in the Washington metropolitan area. Federal employment in the region has remained strong due to the activities of and related spending by the Department of Homeland Security and the Department of Defense.

Chart 1 – Population Trends (2006 – 2010)

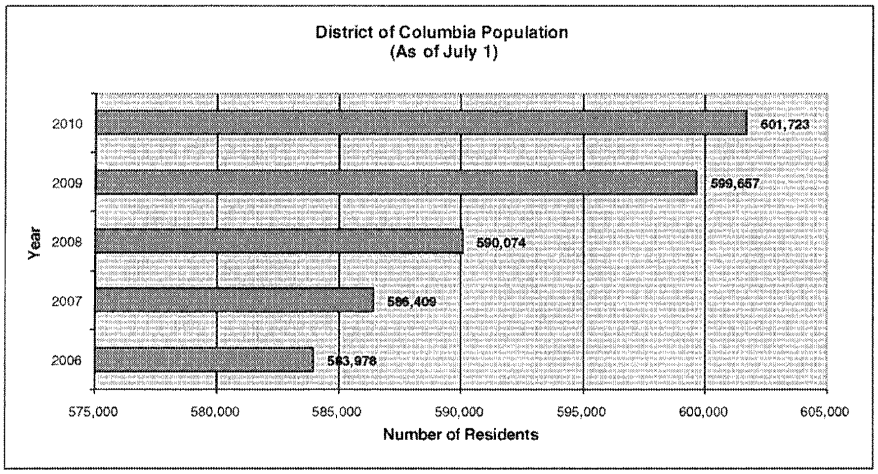


Table 1 – 2010 Labor Market Data for the District and Surrounding Metropolitan Area

Labor Market (000s): FY 2010

	District of Columbia			Metropolitan Area		
Item	Level	1 yr. change (number)	1 yr. change (%)	Level	1 yr. change (number)	1 yr. change (%)
Employed residents	299.7	6.1	2.1	2,870.7	28.0	1.0
Labor force	331.4	0.6	0.2	3,051.9	20.4	0.7
Total wage and salary employment	718.2	22.5	3.2	2,984.7	56.1	1.9
Federal government	212.2	10.6	5.3	379.0	15.7	4.3
Local government	37.4	-1.8	-4.6	308.7	6.0	2.0
Leisure & hospitality	59.3	1.4	2.4	272.6	12.7	4.9
Trade	22.2	0.2	0.9	322.7	9.4	3.0
Education and health	104.9	2.1	2.0	355.0	9.0	2.6
Prof., bus., and other services	219.6	9.8	4.7	866.1	14.6	1.7
Other private	62.6	0.2	0.3	480.6	-11.3	-2.3
Unemployed	31.6	-5.5	-14.8	181.2	-7.5	-4.0
New Unemployment Claims	1.6	-0.2	-12.3			

Sources: U.S. Bureau of Labor Statistics (BLS) & D.C. Dept. of Employment Services (DOES)
All data are monthly averages for the fiscal year and are preliminary, not seasonally adjusted.

Income Trends

In recent years, income has grown considerably in the District. From the third quarter of 2000 to the third quarter of 2010, personal income grew 83.8% in the District, as compared to 45.8% nationally. Over the past five years, personal income in the District grew 31.6% as compared to 19.2% in the U.S. Data regarding the District's 2010 per capita income is not yet available; however, the District's per capita income of $68,013 in 2009 was 71.6% higher than the U.S. average.

The distribution of income in the District differs from that of the nation as a whole, with higher proportions at the higher and lower ends and a smaller proportion in the middle. Consequently, median household income in the District is much closer to the U.S. average. For the two-year period 2008 and 2009, the District's median household income of $54,260 was 8.6% above the U.S. average. The Census Bureau estimates that 18.4% of the District's population was below the poverty line in 2009 as compared to 14.3% for all of the U.S.

Minimum Wage Rate

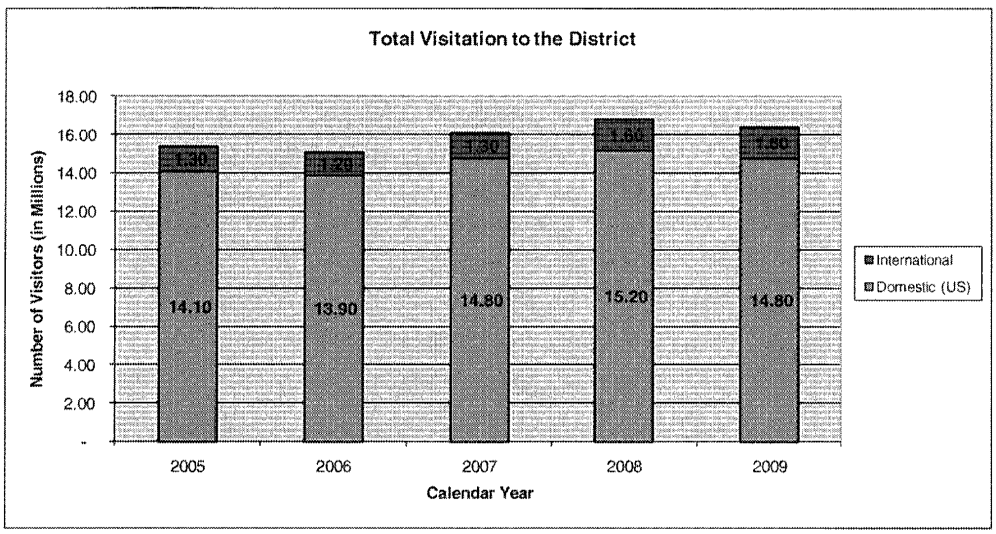
District law requires that the minimum wage rate for District employees be at least $1.00 per hour more than the Federal minimum wage. Beginning on July 24, 2009, the Federal minimum wage rate was increased to $7.25 per hour. Therefore, effective July 24, 2009, the District's minimum wage rate increased to $8.25 per hour.

Tourism and Hospitality

Millions of U.S. citizens and international tourists visit the District's more than 400 museums and historical landmarks each year. During calendar year 2009, the District was the ninth most visited U.S. city among domestic travelers and the seventh most visited destination in the U.S. for international travelers. Popular attractions include sites along the National Mall, monuments to U.S. presidents, war memorials, and other museums. The presence of a large number of foreign embassies, recognized diplomatic missions, and other international organizations in the District helps to boost tourism/ visitation within the District. In calendar year 2009, approximately 14.8 million domestic visitors and 1.6 million international visitors traveled to the District. **Chart 2** presents the trends in tourism for calendar years 2005 through 2009. Tourism data for calendar year 2010 are not yet available.

Direct visitor spending generated additional business activity in related industries (*e.g.*, hotel, restaurant, and retail) and continues to sustain the local and regional economy. The District's hospitality industry generated an estimated $5.25 billion in visitor spending on hotels, retail, transportation and entertainment in 2009, which was a decrease of 7.1% over the prior year. Hotel occupancy was approximately 77.9% at September 30, 2010. Travel and tourism support more than 66,706 full-time jobs in the District, generating approximately $2.6 billion in wages.

Chart 2 – Trends in District Tourism (2005 – 2009)



Source: Data compiled by Destination DC (formerly the Washington Convention and Tourism Corporation)

Construction

The construction sector showed signs of recovery during calendar year 2010 as the vacancy rate for commercial office properties fell. During the year, leased space increased by 5.1 million square feet, outpacing the net addition to inventory of 4.5 million square feet. Consequently, the vacancy rate (including sublet) declined from 10.5% at the end of 2009 to 9.1% at the end of 2010. Federal leasing activities (including 900,000 square feet for the Securities and Exchange Commission) were responsible for the declining vacancy rate, as private sector tenants were hesitant to lease new space. Through 2012, 2.1 million square feet of inventory is scheduled to be delivered from the construction pipeline.

Development in the District continues to be strong in the retail sector. Eleven 7-11 stores will open soon in the District. By the end of calendar year 2010 stores at the following locations were slated to open: 7th Street and Georgia Avenue, N.W.; Florida Avenue and 2nd Street, N.E.; 900 block of H Street, N.E.; 1200 Brentwood Road, N.E.; and 1751 Columbia Road, N.W.

In addition, in June 2010, an Apple Store opened in Georgetown. Although this is the ninth Apple store to open in the metropolitan area, it is the first to open in the District.

Costco, the wholesale grocer, will open a store in the planned Washington Gateway shopping center in 2011. The D.C. Council approved a $10 million loan in 2005 for the shopping center project, which is located in the District's Fort Lincoln neighborhood.

Development in the hospitality sector also continues to be strong. A $59 million, 204-room, 128,500 square foot Hilton Garden Inn will open in 2011. The hotel will be part of the Constitution Square development located in the District's North of Massachusetts Avenue (NoMa) neighborhood.

Plans are also underway to restore the 251-room luxury Watergate Hotel. The renovations, which are expected to cost the developer more than $50 million, include a spa, ample meeting space, restaurants, and bars.

In addition, Capella Hotels and Resorts will open a property in Georgetown. Capella, IGC Properties and Castleton Holdings will redevelop an existing five-story building at 1050 31st Street, NW into the Capella Georgetown Hotel. Construction is expected to begin in January 2011, with an opening scheduled for January 2012. The Capella Georgetown Hotel will include 48 rooms and suites, a premium restaurant and lounge, and a rooftop pool with a bar and spa.

American Recovery and Reinvestment Act (Stimulus Act) Expenditures

On February 17, 2009, the American Recovery and Reinvestment Act (ARRA), or federal "Stimulus Bill" was signed into law. The Stimulus Bill was created to jump start the economy, preserve existing jobs, create new employment opportunities, and promote economic recovery throughout the country. Stimulus funding was made available for investments in infrastructure, energy efficiency, science, and state and local fiscal stabilization.

The District received stimulus funding for a variety of activities, including: road and bridge construction; public transportation improvements; energy efficiency and environmental projects; health care and health research; education; and public safety. Budget authority for stimulus funding was established in the financial system based on the notices of award received by District agencies from the federal government. For fiscal 2009, total stimulus budget authority (operating and capital) available for expenditure was approximately $277 million. By the end of fiscal year 2010, this amount had increased to approximately $655.3 million.

Total stimulus expenditures were approximately $422.7 million in fiscal year 2010, comprised of $360 million in operating expenditures and $62.7 million in capital expenditures. Approximately $330 million, or 91.7%, of the District's total stimulus operating expenditures were made by the following agencies: Department of Health Care Finance, Office of the State Superintendent for Education, Department of Housing and Community Development, Unemployment Compensation Fund, Department of Employment Services, District Department of the Environment, and the Child and Family Services Agency. Approximately $49.4 million, or 78.8%, of the District's stimulus capital expenditures were made by the District Department of Transportation and approximately $13.3 million, or 21.2% of the remaining stimulus capital expenditures were made by the District Department of the Environment.

<u>Bond Rating</u>

Rating agencies assess the credit quality of municipal issuers and assign a credit rating to the issuer based on the results of their analyses. Consequently, rating agencies provide vital information to investors regarding the relative risks associated with rated bond issues. An acceptable credit rating allows the issuer to access the market.

The three primary agencies that rate municipal debt are: (1) Fitch Ratings; (2) Moody's Investors Service; and (3) Standard & Poor's Rating Service. **Table 2** presents the District's bond ratings from these rating agencies for the past four years. The District's ratings for its general obligation bonds have remained high over the last several years. As a result, the District has been able to issue bonds more cost effectively.

During fiscal year 2009, the District issued its first Income Tax Secured Revenue Bonds. These bonds are special obligations of the District, payable solely from the Trust Estate pledged under the indenture. The bonds are without recourse to the District, and are not a pledge of, and do not involve, the faith and credit or the taxing power of the District (other than the pledge of the available tax revenues made by the indenture and the Act). The bonds do not constitute a debt of the District, or lending of the public credit for private undertakings. As presented in **Table 2**, the District's ratings for its Income Tax Secured Revenue Bonds continued to be high in fiscal year 2010.

Table 2 – Bond Rating History (Last Four Fiscal Years)

	General Obligation Bonds				Income Tax Secured Revenue Bonds	
	2007	**2008**	**2009**	**2010**	**2009**	**2010**
Fitch Ratings	A+	A+	A+	**AA-**	AA	AA+
Moody's Investors Service	A1	A1	A1	Aa2	Aa2	Aa1
Standard & Poor's Rating Service	A+	A+	A+	A+	AAA	AAA

Other Factors Affecting the District's Financial Position

The District, as the central urban location of a large metropolitan area, houses a disproportionately large share of the area's poor and needy population. The District's overall poverty rate of 18% and child poverty rate of 30% are significantly higher than the U.S average and that of neighboring counties in Maryland and Virginia. Unlike other urban jurisdictions, the District cannot pool resources across suburban areas to serve its urban poor. Yet, it must provide state-level services such as healthcare, housing and welfare largely through its own resources.

Moreover, the District's service delivery costs are high. Labor costs in the District are 23% above the national average for public services, and the costs associated with acquiring capital goods and services are 54% above the national average. This combination of a significant population in need of services and the high costs of service delivery severely strains the District's financial resources. It has been estimated that if the District were to offer a basket of public services that prevail as "average" among all the state and local governments, it would have to spend 31% more than the national average to deliver it.

The District's ability to pay the high costs of delivering services to its population is constrained by several federal mandates. The federal government has restricted the District's tax base by prohibiting the taxation of federal real property; however, the federal government does not provide a Payment in Lieu of Taxes to compensate for the revenue forgone from this federally-mandated prohibition. In addition, the Home Rule Act prohibits the District from taxing nonresident income. This prohibition significantly reduces the District's income tax base because approximately 66% of the workers in the District are nonresidents.

These restrictions on the revenue collections imply that the District's residents must bear a disproportionate share of the costs of public services, while the benefits generated by the District are shared by a much larger community. It also implies that under slower revenue growth scenarios, District services could become severely impaired.

The U.S. Government Accountability Office (GAO), in its report entitled, "District of Columbia – Structural Imbalance and Management Issues," described the impact of the high cost of living, high poverty and crime rates, and limited tax base on the District's financial operations and estimated the range of the District's structural deficit to be between $470 million to $1.143 billion annually. Although the GAO's report, which was issued in May 2003, discusses conditions that existed at that time, the District's financial operations continue to be negatively impacted by the conditions reported.

Long-Term Financial Planning

As a result of improved financial management practices over the years, the District has been able to develop and operate within more disciplined budgets and address the challenges resulting from the economic downturn.

District officials have developed and implemented a plan for maintaining a strong, stable financial environment, which includes:

- Monitoring and analyzing the District's quarterly revenue estimates and making spending adjustments throughout the year, as necessary;
- Identifying sound measures to enhance revenue streams; and
- Developing and implementing plans to minimize costs without sacrificing essential programs or services.

Major Initiatives

Many initiatives and projects have been completed or planned to help sustain the District's economy and produce strong financial results. Several of the District's major initiatives and projects are discussed briefly below:

- **Waterfront Station:** This is a new pedestrian-friendly, mixed-use project on the site of the former Waterside Mall located at M and 4th Streets, S.W. Waterfront Station, an $800 million multi-phase redevelopment project, will consist of

1.2 million square feet of new office space, approximately 1,000 new residential units, underground parking, and a minimum of 110,000 square feet of retail space.

The office component is complete and is fully leased to the District of Columbia government. In April 2010, employees from several District agencies including the Office of the Chief Financial Officer, Office of Planning, and the Department of Consumer and Regulatory Affairs, moved into Waterfront Station's two office towers.

The retail component includes two existing retailers: Safeway, which opened its new ground-floor store in April 2010, and CVS, which opened its new store in July 2010. Several other new dining and neighborhood service-related retail tenants are planned. In all, approximately 85,000 square feet of retail space will open as a part of the project's first phase.

- **U.S. Department of Homeland Security Headquarters (St. Elizabeth's West Campus)**: In September 2009, the U.S. Department of Homeland Security (DHS) and the U.S. General Services Administration (GSA) broke ground for the $3.4 billion consolidated DHS headquarters. Currently, DHS operates in more than 35 offices around the national capital region and expects to save approximately $163 million over the next 30 years by moving to a consolidated headquarters. DHS is building its headquarters on the west campus of St. Elizabeth's Hospital located in Southeast Washington, D.C. This project is the largest in the Washington area since the Pentagon was built in the 1940s and will help to revitalize and stimulate development in the Anacostia community.

  In August 2009, GSA awarded a $435 million contract to a local contractor to design the site's first phase, the new energy-efficient 1.18 million square-foot Coast Guard headquarters facility. The Coast Guard facility will receive LEED Silver certification from the U.S. Green Building Council, incorporating state-of-the-art efficiency technologies, including green roofs, landscaped courtyards to capture and reuse surface water runoff, and innovative heating, ventilation, and air conditioning systems. Occupancy of the new Coast Guard headquarters is slated to begin in 2013.

  When completed, the DHS headquarters will house approximately 14,000 employees working in the following DHS components: Transportation Security Administration (TSA), Customs and Border Protection, Immigration and Customs Enforcement (ICE), and the Federal Emergency Management Administration (FEMA).

- **Saint Elizabeth's Mental Hospital (New Facility):** After a three-year construction period, the new 450,000 square-foot Saint Elizabeth's Mental Hospital opened in April 2010 on the grounds of the original hospital's East Campus, located at 2700 Martin Luther King, Jr. Avenue, S.E. The $161 million, 448,190 square-foot facility is designed to serve approximately 300 patients. In addition, the new facility will allow patients to receive their meals, treatment, and medical care in one building. The hospital offers treatment areas that include a comfort room for relaxation; enclosed courtyards for use by patients; and an Activities of Daily Living Apartment to help patients prepare for transition back into a home environment.

- **The Park at the Yards:** The grand opening of the Park at the Yards, a 5.4-acre public waterfront park overlooking the Anacostia River, was held in September 2010. The park, which is located between Nationals Park and the Navy Yard, is a key component of The Yards project, which will include the development of a dynamic urban neighborhood spanning 42 acres along the Anacostia Waterfront. When completed, The Yards will also accommodate approximately 2,700 new condos and apartments, 400,000 square feet of restaurants and assorted shops, 1.8 million square feet of office space, and the preservation of unique historical buildings already located on the site. The Yards is projected to house more than 3,700 residents and create approximately 7,700 jobs.

  At a cost of $42 million, The Park at the Yards includes a riverfront promenade, vast open lawns, gardens with benches and colorful plants, a riverfront courtyard enclosed on three sides by retail pavilions, a canal basin and waterfall, a pedestrian bridge, and the restoration of the historic Lumber Shed building. The District's Anacostia Riverwalk Trail runs through the park, providing vital pedestrian and bicycle links to the rest of the Anacostia waterfront.

- **D.C. Streetcar:** The District is planning to build a $1.5 billion network of eight streetcar lines throughout the city by 2020, providing transit links in areas lacking Metrorail access. The first two lines, H Street/Benning Road in Northeast and Martin Luther King Boulevard in Anacostia, are scheduled to begin ferrying riders by spring 2012.

Construction of the line in Anacostia has begun; tracks are being laid on H Street and Benning Road, and planning is underway for the additional segments. The District purchased "modern streetcars" which were shipped from the Czech Republic to the United States in late 2009. These cars are approximately eight feet wide and approximately 66 feet long, about 10 inches narrower and one-third the length of a light rail double car train. They are able to operate in mixed traffic and easily accommodate existing curbside parking and loading.

The D.C. Streetcar will make travel within the District much easier for residents, workers, and visitors, and it will complement the District's existing transit options by: (a) linking neighborhoods with a modern, convenient, and attractive transportation alternative; (b) providing quality service to attract and reach new transit ridership; (3) offering a broader range of transit options for District residents and visitors; (4) reducing short inner-city auto trips, parking demand, traffic congestion, and air pollution; and (5) encouraging economic development and affordable housing options along streetcar corridors.

Several District projects and initiatives have been implemented with a focus on protecting the environment. Two of these initiatives are described more fully below:

- **Capital Bikeshare:** In September 2010, the District launched Capital Bikeshare, a regional bikesharing network of 1,100 bicycles throughout the District and Arlington, Virginia. This new program couples modern electronic gadgetry with 19th century invention to create a system that encourages casual cyclists to pedal around town. Bikes will be docked at bike stations in the District and Arlington, where they will be locked to racks until a Capital Bikeshare member comes along to use one. Anyone can become a Bikeshare member by paying the following fees: for 24 hours, $5; for 30 days, $25; or for a full year, $75.

  Members who sign up for longer than a day receive palm-size cards that have bar codes. These cards are slipped into a slot to release a bike. The first 30 minutes of each ride are free, after which, the meter starts running ($1.50 for the next 30 minutes; $3 for the third half-hour; and $6 for each 30-minute period after that.) The pricing is designed to encourage short trips from place to place rather than leisurely cruising.

  Amounts owed will be billed to the member's credit card and $1,000 will be charged if the bike is not returned within 24 hours. The billing system is activated with the insertion of the bar-coded membership card at the bike station, and another insertion when the bike is returned, both of which are transmitted to Bikeshare headquarters through a wireless, solar-powered communications network.

  Each station will begin the day with about 10 bikes and five empty docking spaces. On the Capital Bikeshare Website, a click of the mouse on each station reveals the number of bikes which are available at any given moment, and the number of docking stations which are open for those who want to return a bike. In addition, smartphone applications will also be available.

  Capital Bikeshare, which expands the District's current SmartBike program, is the nation's largest program of its type.

- **Anacostia River Clean Up and Protection Fund/ Carryout Bag Fees:** During fiscal year 2010, the District established the Anacostia River Clean Up and Protection Fund, which is to be used solely to fund efforts to clean and protect the Anacostia River and the other impaired waterways.

  Funds may be used for the following projects (in order of priority): (a) a public education campaign to educate residents, businesses, and tourists about the impact of trash on the District's environmental health; (b) providing reusable carryout bags to District residents, with priority distribution to seniors and low-income residents; (c) purchasing and installing equipment designed to minimize trash pollution that enters the waterways through storm drains; (d) creating youth-oriented water resource and water pollution educational campaigns for students at District public and charter schools; (e) monitoring and recording pollution indices; (f) preserving or enhancing water quality and fishery or wildlife habitat; (g) promoting conservation programs; (h) purchasing and installing equipment designed to minimize trash pollution, including recycling containers, and covered trash receptacles; (i) restoring and enhancing wetlands and green infrastructure to protect the health of the watershed and restore the aquatic and land resources of its watershed; (j) funding community cleanup events and other activities that reduce trash, such as increased litter collection; (k) funding a circuit rider program with neighboring jurisdictions to focus river and tributary clean-up efforts upstream; (l) supporting vocational and job training experiences in environmental and sustainable professions that enhance the health of the watershed; (m) maintaining a public website that educates District residents on the progress of clean-up efforts; and (n) paying for the administration of this program.

In January 2010, to help fund such environmental conservation activities, the District began levying a five-cent "bag tax" that is to be charged to every consumer in the District. A consumer making a purchase from a retail establishment within the District must pay at the time of purchase a fee of five cents for each disposable carryout bag he or she receives. By the end of fiscal year 2010, the District had collected approximately $1.5 million in bag taxes.

Additional information about these and other initiatives within the District may be obtained from the following:

- **Office of the Deputy Mayor for Planning & Economic Development**
  John A. Wilson Building
  1350 Pennsylvania Avenue, N.W., Suite 317
  Washington, D.C. 20004
  Telephone: (202) 727-6880
  Website: http://dcbiz.dc.gov

- **District Department of Transportation**
  2000 14th Street, N.W., 6th Floor
  Washington, D.C. 20009
  Telephone: (202) 673-6813
  Website: http://ddot.dc.gov

- **Office of Planning**
  1100 Fourth Street, S.W., Suite E650
  Washington, D.C. 20024
  Telephone: (202) 442-7600
  Website: http://planning.dc.gov

- **Department of Parks and Recreation**
  3149 16th Street, N.W.
  Washington, D.C. 20010
  Telephone: (202) 673-7647
  Website: http://dpr.dc.gov

- **Department of Real Estate Services**
  2000 14th Street, N.W., 8th Floor
  Washington, D.C. 20009
  Telephone: (202) 724-4400
  Website: http://dres.dc.gov

- **U.S. General Services Administration**
  1800 F Street, N.W.
  Washington, D.C. 20405
  Telephone: (202) 501-0705
  Website: http://www.gsa.gov

AWARDS AND ACKNOWLEDGMENTS

Awards

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the District of Columbia for its comprehensive annual financial report (CAFR) for the fiscal year ended September 30, 2009. The District has received this award for twenty-six of the last twenty-eight years. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized CAFR. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that the fiscal year 2010 CAFR continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

The District also earned an award from GFOA for Outstanding Achievement in Popular Annual Financial Reporting (PAFR) for the fiscal year ended September 30, 2009, for the seventh consecutive year. The PAFR presents the District's financial results in a format and language that allows information to be more easily understood by the general public. The PAFR is not required to present the same level of detail as the CAFR. It contains very few financial statements, less technical language, and more graphics and photographs.

Like the Certificate of Achievement, the Award for Popular Annual Financial Reporting is valid for one year only. The District expects that the fiscal year 2010 PAFR, which will be issued within 30 days after the CAFR is completed, will conform to the Award for Popular Annual Financial Reporting Program requirements. It will also be submitted to the GFOA to determine its eligibility for another award.

Acknowledgments

I would like to thank the District's accounting and financial management personnel who worked collaboratively with the Office of Financial Operations and Systems throughout the year. I greatly appreciate their efforts, which contribute significantly to the timely preparation of the CAFR. I want to thank my immediate staff, *Bill Slack, Diji Omisore, Tonja Lowe, Wilma Matthias, Vanessa Jackson,* and their respective teams. I am grateful for their dedicated efforts. I would also like to thank the Office of the Inspector General, and the District's independent auditors, KPMG LLP, assisted by Bert Smith & Company, for their efforts throughout the audit engagement.

Respectfully submitted,

Anthony F. Pompa
Deputy Chief Financial Officer
Financial Operations and Systems