

**MANAGEMENT'S DISCUSSION AND ANALYSIS****September 30, 2011**

(Dollar amounts expressed in thousands)

The following is a discussion and analysis of the District of Columbia's (the District's) financial performance for the fiscal year ended September 30, 2011, which includes a narrative overview and analysis of the District's financial activities. This information should be read in conjunction with the transmittal letter, located in the Introductory Section of this report, and the District's basic financial statements and note disclosures, which follow this discussion and analysis.

**FINANCIAL HIGHLIGHTS**

- The District's assets exceeded its liabilities as of September 30, 2011, by \$3,200,793. The District had unrestricted net assets totaling (\$524,146) at the end of fiscal year 2011. (See Table 1)
- The District's total net assets increased by \$138,817 as a result of an increase of \$362,847 in revenues and a smaller increase of \$134,778 in expenses in fiscal year 2011. In addition, due to a change in the method used to apply accounting principles when recognizing property tax revenues, prior year property tax revenues and net assets were adjusted. Consequently, net assets at the beginning of fiscal year 2011 increased by \$40,643.
- General revenues increased by approximately \$403,301 due to significant increases in income and franchise taxes, and other taxes totaling \$222,152 and \$121,115, respectively. Expenses increased by \$134,778 over the one-year period. During fiscal year 2011, the District implemented self-imposed cost reduction plans to address potential budget shortfalls. Such measures proved to be successful in limiting expenses and helping to prevent a year-end deficit. (See Table 2)
- As of September 30, 2011, the District's governmental funds reported combined ending fund balances of \$1,726,634, an increase of \$102,467 in comparison with the prior year. (See Table 3)
- The District's total long-term liabilities increased by \$543,400, or 6.6%, during fiscal year 2011. This increase resulted, in large part, from the District's issuance of Income Tax Secured Revenue Bonds during the year. The District issued \$544,945 in Income Tax Secured Revenue Bonds to fund infrastructure improvements/capital projects and refund certain series of outstanding income tax secured revenue bonds. The amount of income tax secured revenue bonds defeased through the fiscal year 2011 refundings totaled \$63,335. Other factors which contributed to the increase in long-term liabilities include the issuance of General Obligation Bonds (Build America Bonds) totaling \$181,330, Federal Highway Grant Anticipation Revenue Bonds (GARVEEs) totaling \$82,610, and increases in accreted interest totaling \$24,633.

**OVERVIEW OF THE FINANCIAL STATEMENTS****Basic Financial Statements**

In general, the purpose of financial reporting is to provide users of financial statements with information that will help them make decisions or reach conclusions about a reporting entity. Many parties use the District's financial statements; however, they do not always use them for the same purpose. In order to address the needs of as many financial statement users as possible, the District, in accordance with generally accepted accounting principles (GAAP) presents: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the basic financial statements.

**Government –Wide Financial Statements**

The government-wide financial statements focus on the District's overall financial position and activities, and include a *statement of net assets* and a *statement of activities*. These financial statements report on the primary government and its component units. The primary government is further divided into governmental activities and business-type activities.

The purpose of the *statement of net assets* is to report all of the assets held and the liabilities owed by the District at the end of the fiscal year. The difference between the District's total assets and total liabilities is classified as net assets. Total net assets is comprised of three components: 1) *net assets invested in capital assets, net of related debt*; 2) *restricted net assets*; and 3) *unrestricted net assets (deficit)*. Although the District does not focus its operations on accumulating net assets, in general, gauging increases or decreases in net assets is one way to assess the District's financial position over time. Other factors, such as changes in population, the property tax base, infrastructure conditions, and other non-financial matters, should also be considered when assessing the District's overall financial health.

The purpose of the *statement of activities* is to present the District's revenues and expenses. The difference between revenues and expenses is reported as "change in net assets". All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses reported in this statement also include items that will result in cash flows in future fiscal periods (for example, uncollected taxes and earned but unused vacation leave).

The *statement of activities* summarizes both the gross and net cost of the governmental activities and business-type activities. Governmental activities include the District's basic functional services which are generally financed through taxes, intergovernmental revenues and other revenues. Business-type activities include enterprise operations which are primarily funded by fees for services which are expected to cover all or most of the costs of operations, including depreciation. Program or functional expenses are reduced by program-specific earned revenues, and by grants and contributions.

The District's government-wide financial statements are presented on pages 42 and 43 of this report.

### Fund Financial Statements

Unlike the government-wide financial statements, the fund financial statements focus on specific District activities rather than the District as a whole. Specific funds are established to maintain managerial control over resources or to comply with legal requirements established by external parties, governmental statutes, or regulations. The District's fund financial statements are divided into three categories: (1) governmental funds; (2) proprietary funds; and (3) fiduciary funds.

**Financial statements of the governmental funds** consist of a balance sheet and a statement of revenues, expenditures, and changes in fund balance. These statements are prepared using a basis of accounting which differs from that used to prepare the government-wide statements. Financial statements of the governmental funds focus primarily on the sources, uses, and balances of current financial resources and use the modified accrual basis of accounting. However, government-wide financial statements focus on all of the District's economic resources and use the full accrual basis of accounting. Financial statements of the governmental funds have a short-term emphasis, and generally measure and account for cash and other assets that can easily be converted to cash. As such, these statements present the District's financial position at the end of the fiscal year and how the governmental activities were financed during the year.

The balances and activities accounted for in governmental funds are also reported in the governmental activities column of the government-wide financial statements; however, because different accounting bases are used to prepare fund financial statements and government-wide financial statements, there are often significant differences in the totals presented in these statements. Therefore, an analysis is presented at the bottom of the balance sheet that reconciles the total fund balances to the amount of net assets presented in the governmental activities column of the statement of net assets. In addition, there is an analysis following the statement of revenues, expenditures, and changes in fund balances that reconciles the total net change in fund balances for all governmental funds to the change in net assets as reported in the governmental activities column of the government-wide statement of activities.

The District adopted Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, in fiscal year 2011. Consistent with that Statement, the District identified its nonspendable fund balance and further classified spendable fund balance as restricted, committed, assigned, or unassigned based on the relative strength of the constraints controlling how specific amounts may be used. Statement No. 54 also provides guidance for classifying and reporting stabilization amounts and clarifies the definitions of the general fund type, special revenue fund type, capital projects fund type, debt service fund type, and permanent fund type. Accordingly, the District reviewed its use of the various fund types to ensure compliance with the guidance contained in GASB Statement No. 54.

The District presents funds that are significant to the District (major funds) in separate columns. All other governmental funds are aggregated and reported in a single column (nonmajor funds).

The financial statements of the District's governmental funds are presented on pages 44 and 47 of this report.

**Financial statements of the proprietary funds** consist of a statement of net assets; a statement of revenues, expenses, and changes in fund net assets; and a statement of cash flows. These statements are prepared using the full accrual basis of accounting similar to that used to prepare the government-wide financial statements. The District's proprietary funds are used to account for the activities of District entities that charge customers fees for the services provided. The financial statements of the District's proprietary funds present the changes in financial position and condition of the District's two major proprietary funds, the D.C. Lottery & Charitable Games Board and the Unemployment Compensation Fund, and one non-major proprietary fund, Nursing Home Services, which reports the operations of J.B. Johnson Nursing Center. Effective December 13, 2010, the J.B. Johnson Nursing Center was dissolved and the facility (land, building, and improvements) is being leased to a separate entity that continues to provide nursing home services. The District has no further responsibility for the operations of this nursing home facility.

The Unemployment Compensation Fund is reported as a proprietary fund similar to a public entity risk pool because the District is required by law to recover its costs.

The financial statements of the District's proprietary funds are presented on pages 48 through 50 of this report.

**Financial statements of the fiduciary funds** consist of a statement of fiduciary net assets and a statement of changes in fiduciary net assets. These statements are prepared using the full accrual basis of accounting similar to that used to prepare the government-wide financial statements. Assets held by the District (either as a trustee or as an agent) for other parties, that cannot be used to finance the District's operating programs, are reported in the fiduciary funds. The District is responsible for ensuring that the activities reported in the fiduciary funds are consistent with each fund's intended purpose.

The financial statements of the District's fiduciary funds are presented on pages 51 and 52 of this report.

### **Component Units**

Combining financial statements, presented on pages 53 and 54, report the financial data for the District's discretely presented component units.

### **Notes to the Basic Financial Statements**

The Notes to the Basic Financial Statements, which begin on page 55, present additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

### **Other Information**

In addition to the financial statements and accompanying notes, this report also presents certain required supplementary information concerning the District's progress toward funding its obligation to provide pension and other postemployment benefits to District employees. Required supplementary information can be found on pages 127 through 129 of this report.

Financial statements of individual funds, combining statements (in connection with nonmajor governmental funds), and supporting schedules are presented immediately following the required supplementary information on postemployment benefits. Financial statements of individual funds and combining statements and schedules can be found in the other supplementary information presented on pages 131 through 157 of this report.

## **OVERVIEW OF THE DISTRICT'S FINANCIAL POSITION AND OPERATIONS**

The District's overall financial position improved moderately as a result of the year's activities. The District's financial position and operations for the past two fiscal years are summarized in **Tables 1 and 2**. The information for fiscal years 2010 and 2011 is based on the government-wide financial statements presented on pages 42 and 43 of this report.

**Table 1 - Net Assets as of September 30, 2011**

	Governmental activities		Business-type activities		Totals	
	2011	2010 Adjusted	2011	2010	2011	2010 Adjusted
Current and other assets	\$ 3,964,874	\$ 3,571,063	\$ 339,309	\$ 364,234	\$ 4,304,183	\$ 3,935,297
Capital assets	9,815,312	9,228,531	478	4,827	9,815,790	9,233,358
Total assets	13,780,186	12,799,594	339,787	369,061	14,119,973	13,168,655
Long-term liabilities	8,723,811	8,174,105	22,912	29,218	8,746,723	8,203,323
Other liabilities	2,085,790	1,810,264	86,667	93,092	2,172,457	1,903,356
Total liabilities	10,809,601	9,984,369	109,579	122,310	10,919,180	10,106,679
Net assets:						
Invested in capital assets, net of related debt	2,534,538	2,437,385	478	4,827	2,535,016	2,442,212
Restricted	963,694	1,117,560	226,229	233,296	1,189,923	1,350,856
Unrestricted	(527,647)	(739,720)	3,501	8,628	(524,146)	(731,092)
Total net assets	\$ 2,970,585	\$ 2,815,225	\$ 230,208	\$ 246,751	\$ 3,200,793	\$ 3,061,976

**Table 2 - Change in Net Assets for the year ended September 30, 2011**

	Governmental activities		Business-type activities		Total		
	2011	2010 Adjusted	2011	2010	2011	2010 Adjusted	Variance 2011/2010
Revenues:							
Program revenues:							
Charges for services	\$ 490,101	\$ 450,022	\$ 235,884	\$ 250,150	\$ 725,985	\$ 700,172	\$ 25,813
Operating grants and contributions	3,343,747	3,321,671	34,968	36,998	3,378,715	3,358,669	20,046
Capital grants and contributions	172,964	259,277	-	-	172,964	259,277	(86,313)
General revenues:							
Property taxes	1,803,691	1,881,733	-	-	1,803,691	1,881,733	(78,042)
Sales and use taxes	1,121,257	1,081,005	-	-	1,121,257	1,081,005	40,252
Income and franchise taxes	1,656,283	1,434,131	-	-	1,656,283	1,434,131	222,152
Other taxes	682,201	560,490	128,875	129,471	811,076	689,961	121,115
Non tax revenues	569,522	466,524	238,119	243,293	807,641	709,817	97,824
Total revenues	9,839,766	9,454,853	637,846	659,912	10,477,612	10,114,765	362,847
Expenses:							
Governmental direction and support	783,557	871,240	-	-	783,557	871,240	(87,683)
Economic development and regulation	370,592	374,149	-	-	370,592	374,149	(3,557)
Public safety and justice	1,521,863	1,563,505	-	-	1,521,863	1,563,505	(41,642)
Public education system	2,086,722	1,989,518	-	-	2,086,722	1,989,518	97,204
Human support services	3,889,812	3,677,405	-	-	3,889,812	3,677,405	212,407
Public works	489,304	497,027	-	-	489,304	497,027	(7,723)
Public transportation	257,703	243,668	-	-	257,703	243,668	14,035
Interest on long-term debt	356,164	324,319	-	-	356,164	324,319	31,845
Lottery and games	-	-	169,526	163,393	169,526	163,393	6,133
Unemployment compensation	-	-	408,997	480,976	408,997	480,976	(71,979)
Nursing home services	-	-	4,555	18,817	4,555	18,817	(14,262)
Total expenses	9,755,717	9,540,831	583,078	663,186	10,338,795	10,204,017	134,778
Increase in net assets before special items and transfers	84,049	(85,978)	54,768	(3,274)	138,817	(89,252)	228,069
Special item	-	266,942	-	-	-	266,942	(266,942)
Transfer in (out)	71,311	96,624	(71,311)	(96,624)	-	-	-
Change in net assets	155,360	277,588	(16,543)	(99,898)	138,817	177,690	(38,873)
Net assets - Oct 1, as adjusted	2,815,225	2,537,637	246,751	346,649	3,061,976	2,884,286	177,690
Net assets - Sept 30	\$ 2,970,585	\$ 2,815,225	\$ 230,208	\$ 246,751	\$ 3,200,793	\$ 3,061,976	\$ 138,817

Please refer to Note 1W – Reconciliation of Government-Wide and Fund Financial Statements, on page 72 for additional information on the differences between the two bases of accounting that the District used in this report.

**Financial Analysis of the Government as a Whole (Government-Wide Financial Statements)**

- The District's combined net assets (governmental and business-type activities) increased by \$138,817, or 4.5%, from \$3,061,976 in fiscal year 2010 to \$3,200,793 in fiscal year 2011. This increase in net assets resulted from an increase in revenues totaling \$362,847 and a \$40,643 adjustment to net assets related to a change in the method used to recognize personal property tax revenue. In addition, expenses in Governmental Direction and Support decreased by \$87,683 as a result of cost-saving measures implemented by the District and Public Safety and Justice expenses decreased by \$41,642 due to postponed hiring of police officers, delays in filling certain civilian positions, and other operational improvements at the Metropolitan Police Department (MPD). Savings were also achieved as a result of the transitioning of the fire hydrant inspection function from Fire and Emergency Medical Services (FEMS) to the Water and Sewer Administration and the strengthening of FEMS policies regarding overtime and use of sick leave.
- *Restricted net assets* are assets that are subject to use constraints imposed either: (a) externally by creditors (such as through debt covenants), grantors, contributors, laws or regulations of other governments; or (b) by law, through constitutional provisions or enabling legislation. Restricted net assets totaled \$1,189,923 in fiscal year 2011 and \$1,350,856 in fiscal year 2010, representing a decrease of \$160,933, or (11.9%). Most of this decrease is due to more funds being held for debt service, grants, and special purposes.

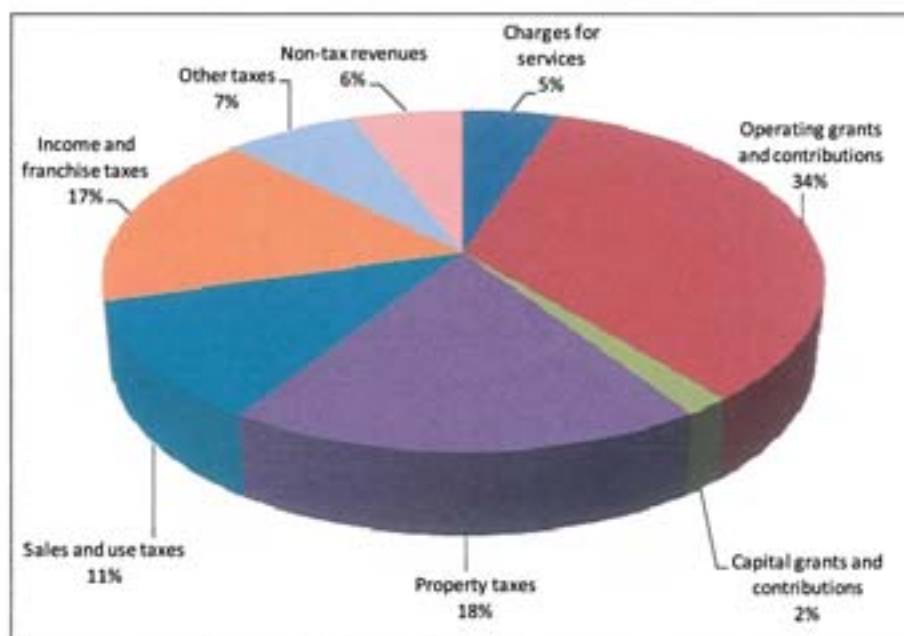
Total net assets of governmental activities was \$2,970,585 in fiscal year 2011, which was \$155,360 or 5.5%, more than total net assets of governmental activities in fiscal year 2010. Governmental Activities expenses increased by \$214,886 from the prior year and Governmental Activities revenues increased by \$384,913.

Total net assets increased mainly because of effective management of expenditures and increases in revenues from property taxes, income and franchise taxes, and sales and use taxes. This was a major contributing factor for the decrease in negative unrestricted net assets to \$524,146 in fiscal year 2011, compared to \$731,092 in fiscal year 2010.

The Lottery and Charitable Games Control Board (the Lottery), an enterprise fund of the primary government, transfers substantially all of its net income to the District at the end of each fiscal year. In fiscal years 2011 and 2010, the Lottery transferred \$62,175 and \$66,750 to the District's General Fund, respectively. In addition, \$9,136 was transferred to the District's General Fund upon the dissolution of the J.B. Johnson Nursing Home in fiscal year 2011. Total transfers from the proprietary funds to the primary government were \$71,311 in fiscal year 2011.

**Chart 1** graphically depicts the District's sources of revenues in its governmental activities as presented in Table 2, *Change in Net Assets* for the year ended September 30, 2011, found on page 26.

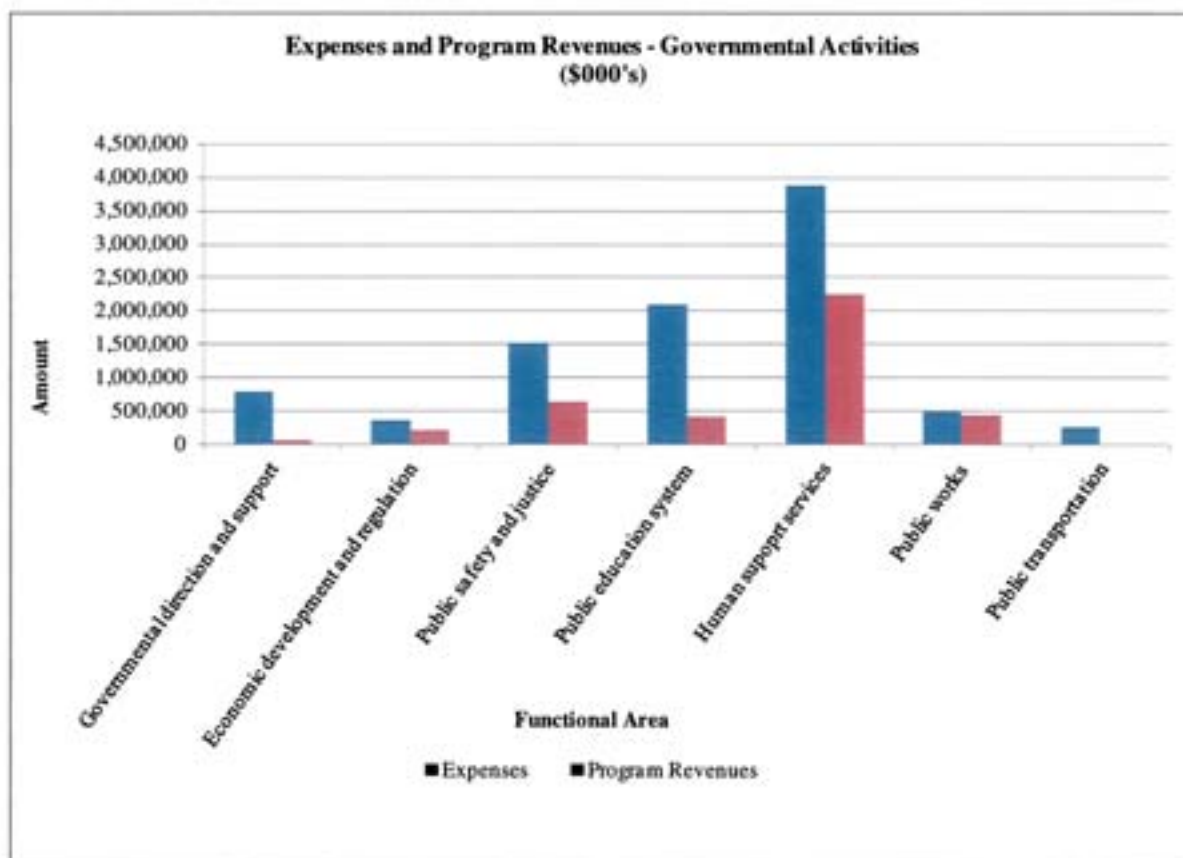
**Chart 1 – Revenues by Source – Governmental Activities**





**Chart 2** displays both expenses and program revenues of selected governmental activities for the fiscal year. The governmental activities are: governmental direction and support, economic development and regulation, public safety and justice, public education, human support services, public works, and public transportation.

**Chart 2 – Governmental Activities Expenses and Program Revenues**



### Reporting on the District's Most Significant Funds

Fund financial statements focus on major funds, instead of fund types. A governmental fund is classified as a major fund if the fund has revenues, expenditures/expenses, assets, or liabilities (excluding extraordinary items) that are at least 10% of the corresponding totals for all governmental or enterprise funds and at least 5% of the aggregate amount for all governmental and enterprise funds for the same item. Major funds, as required by generally accepted accounting principles (GAAP), are presented individually with nonmajor governmental funds combined in a single column. Detailed information for individual nonmajor governmental funds can be found in Other Supplementary Information, Exhibits B-1 and B-2, presented on pages 142 and 143 of this report.

### Governmental Funds

The District's governmental funds provide information that is useful when assessing the District's financing needs, such as data pertaining to near-term inflows, outflows, and balances of spendable resources. For instance, the amount of unassigned fund balance may serve as a useful measure of the government's net resources that are available for spending as of the end of the fiscal year.

Most basic services are reported in the governmental funds, which are further classified as General, Federal and Private Resources, Housing Production Trust Fund, General Capital Improvements, and Nonmajor Governmental Funds. Please refer to Exhibits 2-a and 2-b presented on pages 44 and 45, for more detailed information about these funds.

- **Fund Balances:** The governmental funds reported a combined fund balance of \$1,726,634 in fiscal year 2011 and \$1,624,167 in fiscal year 2010, which represents an increase of \$102,467, or 6.3%, from the prior year. The components of the combined fund balance of the governmental funds are presented in **Table 3**.

**Table 3 – Comparison of FY 2011 and FY 2010 Fund Balance**

Governmental Fund	FY 2011 Balance	FY 2010 Balance Adjusted	Dollar Variance	Percentage Variance
General	\$ 1,104,894	\$ 930,769	\$ 174,125	18.7%
Federal and Private Sources	183,610	191,023	(7,413)	-3.9%
Housing Production Trust	73,436	40,315	33,121	82.2%
General Capital Improvements	4,970	133,438	(128,468)	-96.3%
Nonmajor governmental funds	359,724	328,622	31,102	9.5%
<b>Total Fund Balance</b>	<b>\$ 1,726,634</b>	<b>\$ 1,624,167</b>	<b>\$ 102,467</b>	<b>6.3%</b>

The most significant change in the total fund balance of the governmental funds was in the General Fund, the District's primary operating fund. A more detailed discussion of the District's General Fund is provided below.

- **Revenues:** General Fund revenues increased by \$245,485 as the economy began to show signs of recovery in fiscal year 2011. **Table 4** presents the most significant one-year variances in General Fund revenues.

**Table 4 – Changes in Major General Fund Revenues**

Revenue Category	Fiscal Year 2011	Fiscal Year 2010 Adjusted	Dollar Variance	Percentage Variance
Property taxes	\$ 1,770,185	\$ 1,881,284	\$ (111,099)	-5.9%
Income and franchise taxes	1,656,283	1,434,131	222,152	15.5%
Sales and use taxes	1,066,366	1,081,005	(14,639)	-1.4%
<b>Total (These Categories)</b>	<b>\$ 4,492,834</b>	<b>\$ 4,396,420</b>	<b>\$ 96,414</b>	<b>2.2%</b>

**Property tax.** With the passage of the Clarification of Personal Property Tax Revenue Reporting Act of 2011, the District changed its policy regarding personal property tax revenue reporting. The period of intended use of the personal property tax was changed from 25% in the fiscal year when the assessment is made and 75% in the subsequent fiscal year to 100% in the fiscal year of assessment. Changing the period of intended use did not affect the amount of personal property tax revenue recognized in fiscal year 2011. However, fiscal year 2010 personal property tax revenue was adjusted by approximately \$4.5 million to reflect the increase resulting from this change in revenue recognition methods.

Furthermore, there is a two year lag between the time real property values are assessed and when the revenue from the assessments is realized. Prior to fiscal year 2009, the District experienced significant increases in tax collections as a result of robust growth in property values, as evidenced by a growing number of property sales, and increases in average sales prices. As the housing market declined and the recession worsened, both the number and sales prices of residential and commercial property sales declined in late 2008 and 2009. These declines impacted the fiscal year 2010 assessments, resulting in lower real property tax collections in that year and in fiscal year 2011.

Personal property tax collections also declined in fiscal year 2011 as a result of decreases in the level of business activity and new business investments in the District.

**Income and franchise tax.** Wages and salaries earned by District residents increased in fiscal year 2011 which led to increased income tax collections through withholdings. The non-withholding component of income tax revenue, which includes declarations (estimated payments), also increased in fiscal year 2011. The behavior of the

declarations component is related to the performance of the stock market which declined sharply in recent years. However, the stock market regained some strength in fiscal year 2011 which resulted in an increase in the non-withholding component of income taxes.

Corporate franchise tax revenues increased in fiscal year 2011 due to increases in corporate profits.

**Sales and use tax.** Total sales tax revenues increased by \$40,252 in fiscal year 2011 as the national and local economies began to show signs of recovery. However, the General Fund portion of sales and use taxes decreased by \$14,639 as a result of the District's implementation of GASB Statement No. 54. Consistent with the requirements of that statement, \$54,891 in sales tax revenue is presented in the District's Nonmajor Governmental Funds.

### Dedicated Revenues

The dedicated portions of tax revenues related to the special revenue funds are recorded directly in those funds. However, dedicated taxes for capital project funds are transferred out of the local fund (the major component of the general fund). In fiscal year 2011, the District dedicated a total of \$170,410 in tax revenues to fund the projects shown in **Tables 5**.

**Table 5 – Dedicated Local Tax Revenues**  
(Dollars in 000s)

		Total Dedicated Taxes	Special Revenue Funds			
			Tax Increment Financing Program	Housing Production Trust	PILOT Special Revenue	Baseball Project
Property taxes	\$	30,560	13,569		16,991	
Sales and use taxes		54,891	45,379			9,512
Gross receipts taxes		44,582				44,582
Other taxes		40,377		40,377		
Total taxes	\$	170,410	58,948	40,377	16,991	54,094

- **Expenditures:** The District's general fund expenditures, excluding debt service, increased by \$69,452 from the previous year. Variances by program or function are presented in **Table 6**:

**Table 6 – General Fund Expenditure Variances by Function**

Program/ Functional Area	Fiscal Year 2011	Fiscal Year 2010	Dollar Variance	Percentage Variance
Governmental direction and support	\$ 620,426	\$ 579,457	\$ 40,969	7.1%
Economic development and regulation	220,878	247,355	(26,477)	-10.7%
Public safety and justice	993,978	1,018,335	(24,357)	-2.4%
Public education system	1,507,747	1,400,832	106,915	7.6%
Human support services	1,572,717	1,564,143	8,574	0.5%
Public works	226,783	276,990	(50,207)	-18.1%
Public transportation	257,703	243,668	14,035	5.8%
<b>Total Functional Expenditures</b>	<b>\$ 5,400,232</b>	<b>\$ 5,330,780</b>	<b>\$ 69,452</b>	<b>1.3%</b>

Explanations for significant variances in General Fund expenditures are presented below:

**Public Education** – Certain initiatives and activities of the District of Columbia Public Schools (DCPS) contributed to the \$106,915 increase in Public Education expenditures. DCPS expenditures increased over the one year period between 2010 and 2011 due to increases in enrollment and special student populations. Additional funding was also



used to support a blended Head Start program. DCPS launched an innovative early education model to expand the District's ability to provide comprehensive preschool and pre-Kindergarten programs to ensure that every child attending a Title I school will benefit from comprehensive services typically only offered to Head Start classrooms. Under the new model, an additional 184 classrooms in 70 schools were able to receive all the benefits of a full Head Start program. The new model requires schools that previously received a Head Start subsidy for more than one classroom to fund the full salary of a second classroom teacher.

In addition, programs and activities of the D.C. Public Library (DCPL) also contributed to the increase in Public Education expenditures. With the new Deanwood Recreation Center opening at the end of fiscal year 2010 and six new libraries opening in fiscal year 2011, the DCPL used funding to support its increased staffing needs and pay the costs of moving into the new facilities. The new libraries are substantially larger and provide more services than the older facilities; therefore, additional staff were needed.

**Public Works** – During fiscal year 2011, the Department of Public Works (DPW) implemented several cost-saving measures which proved to be effective in reducing expenditures by \$50,207 in fiscal year 2011. Some of the cost-saving measures implemented by DPW included: (a) transitioning the Household Hazardous Waste and Shred-It program to a once-a-month Saturday collection; (b) streamlining the Fall leaf collection program; and (c) reducing the Small Business Improvement District Litter program. In addition, DPW reduced the number of positions in its Solid Waste Education and Enforcement Program and certain other administrative and financial management areas. Other cost-savings were realized as a result of renegotiating the recycling charges and moving the auction of vehicles to an on-line site.

**Governmental Direction and Support** – The \$40,969 increase in expenditures in Governmental Direction and Support is attributable to the District's enhancement of its operations and processes for administering programs and services. Investing resources to attract and enhance the skills of high-quality employees is of critical importance to the District. Therefore, substantial resources were devoted to and used by the Department of Human Resources Workforce Development Administration for this purpose. In addition, resources were devoted to strengthening the oversight function within the District and to address staffing needs in the Office of the Inspector General and enhance the audit capacity of the Office of the D.C. Auditor.

Funds were also used to establish initiatives and programs consistent with legal mandates made by the Council. For example, Council established an independent Public Education Finance Reform Commission to study and recommend revisions to the Uniform Per Student Funding Formula; and the Office of the Chief Financial Officer used resources to implement the Vacant Property Disincentivization Act of 2010. Another initiative which contributed to the increased expenditures was the use of funds for local non-profit health centers' malpractice insurance.

#### Capital Expenditures and Financing

The District's investments in capital improvements are based on need rather than available current year revenues. It is the District's financial policy to issue bonds to support the expenditures associated with its Capital Improvements Program. In order to minimize the cost of carrying debt, the District has instituted the practice of issuing bonds based on actual expenditures, in some cases, as well as on the annual amount budgeted. However, agencies are authorized to spend their annual appropriated capital budget in advance of financing. The General Fund advances the amount of the funding, and is repaid with the proceeds from the bonds when issued. This allows the District to determine when it will enter the market to issue bonds, based upon cash flow needs, favorable market rates, and the total amount of municipal debt financing and the types of credits that are available. This flexibility helps to minimize borrowing costs and maximize the pool of potential investors for the District's debt issuances.

The District spent \$1,155,116 on general capital improvements which exceeded the general capital improvements revenues of \$184,793 by \$970,323, which is reported as a deficiency in the capital projects fund. This deficiency was subsequently financed with a total of \$841,855 from bond proceeds and other financing sources. The net change in the general capital improvements fund balance was a decrease of \$128,468.

### Proprietary Funds

The District currently has two major Proprietary Funds: the D.C. Lottery & Charitable Games Board (Lottery), and the Unemployment Compensation Fund (Unemployment). There is one nonmajor proprietary fund, JB Johnson Nursing Center, which was dissolved on December 13, 2010.

The total assets for the Lottery decreased by \$6,807, or 14.9%, over the prior year, due to scheduled payments to long-term prize winners.

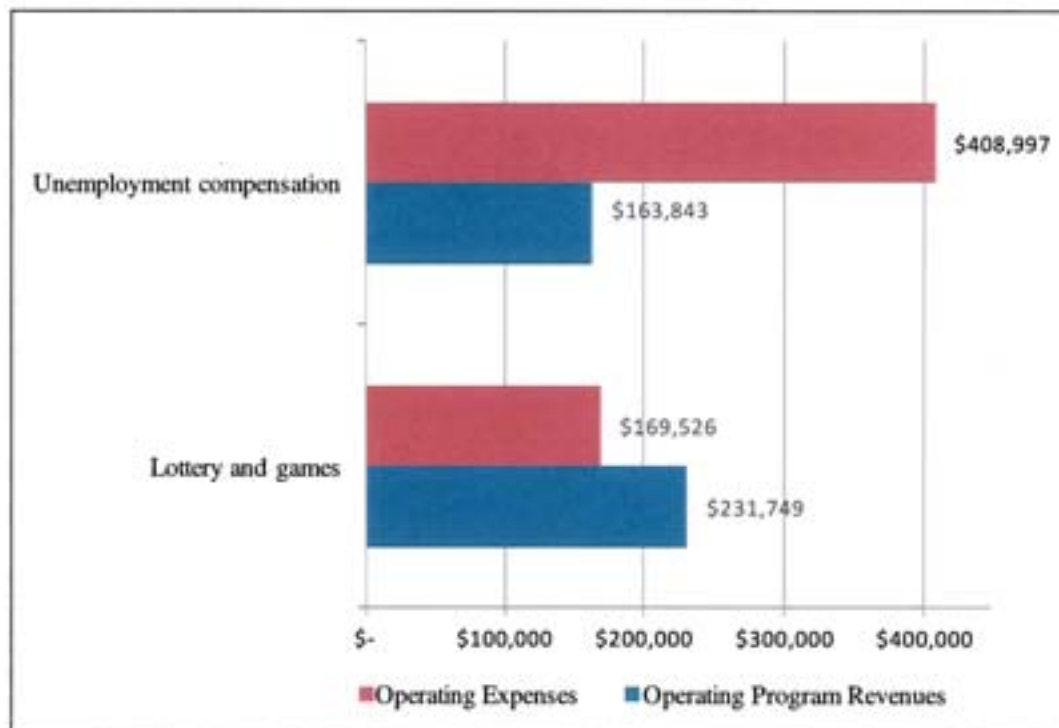
Total assets for Unemployment decreased by \$12,718, or 3.6%, due primarily to: (a) payments of claimants' benefits; (b) a decrease in interest earned on monies held in trust in the District's name at the U.S. Department of the Treasury; and (c) a decline in the amounts owed to Unemployment by employers. The noted decreases in assets were offset by an increase in the amount due from other states.

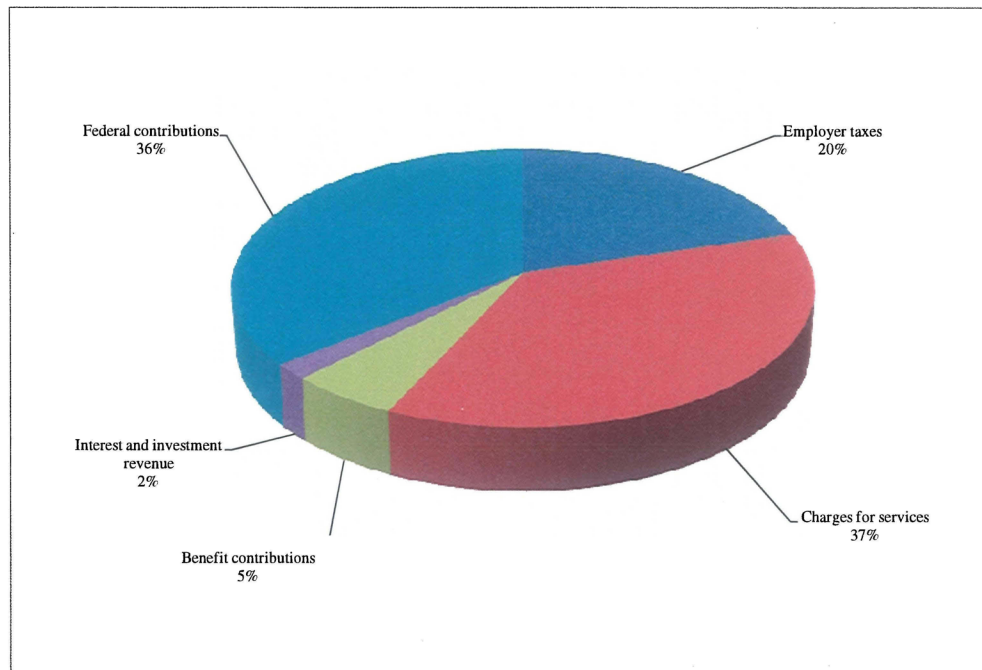
District residents who have exhausted regular District benefits may also participate in the federally funded Emergency Unemployment Compensation (EUC) Program. Pursuant to the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010, the EUC program was extended until March 6, 2012. Between 2010 and 2011, there was a \$1,646 decrease in the amount owed to Unemployment by the federal government for extended benefits.

Overall total net assets of the District's proprietary funds decreased by \$16,543, or 6.7%, over the prior year, due in large part to the factors mentioned above. Exhibits 3-a, 3-b, and 3-c on pages 48 through 50 present the financial statements of the proprietary funds.

**Charts 3 and 4** graphically present comparisons of the revenues and expenses of the District's proprietary funds, based on information contained in the Statement of Revenues, Expenses and Changes in Fund Net Assets - Proprietary Funds, shown on page 49 of this report.

**Chart 3 – Operating Revenues and Expenses – Business-type Activities**



**Chart 4 – Revenues by Source – Business-type Activities**

### Fiduciary Funds

The *Trust and Agency Funds* are used to account for assets held by the District as trustee for individuals, private organizations, or other governments. The District is the *trustee* or *fiduciary* for its employees' pension plans and other postemployment benefits (OPEB). All fiduciary activities are reported in Exhibit 4-a, *Statement of Fiduciary Net Assets* and Exhibit 4-b, *Statement of Changes in Fiduciary Net Assets* on pages 51 and 52, respectively. Exhibits C-1, C-2, and C-3, presented on pages 146, 147, and 148 respectively, provide additional information. These activities are excluded from the District's governmental and business-type activities because these resources are restricted and are not available to support the District's operations.

The changes in the net assets of the Pension Trust Funds and OPEB Trust Fund are presented in **Table 7**.

**Table 7 – Variances in Net Assets of Pension and OPEB Trust Funds**

Trust Fund	Fiscal Year 2011	Fiscal Year 2010	Dollar Variance	Percentage Variance
Police and Firefighters Pension	\$ 3,127,467	\$ 2,925,742	\$ 201,725	6.9%
Teachers Pension	1,340,712	1,317,470	23,242	1.8%
Other Postemployment Benefits	511,486	424,254	87,232	20.6%
<b>Total Net Assets (End of Year)</b>	<b>\$ 4,979,665</b>	<b>\$ 4,667,466</b>	<b>\$ 312,199</b>	<b>6.7%</b>

Net assets of the fiduciary funds increased due to increases in the value of equity investments. In addition, there were reductions in securities lending transactions and other current liabilities in these funds.

Private-purpose trust funds are used to report any trust arrangement not reported in the pension or OPEB trust funds under which principal and income benefit specific individuals, private organizations, or other governments. For instance, the District's 529 College Savings Investment Plan, which is designed to help families save for the higher education expenses of designated beneficiaries, comprises the Private-Purpose Trust Fund.

## Component Units

Component units are legally separate organizations for which the District is financially accountable. The District has five discretely presented component units: (1) Water and Sewer Authority; (2) Washington Convention and Sports Authority; (3) Not-For-Profit Hospital Corporation (d/b/a United Medical Center); (4) Housing Finance Agency; and (5) University of the District of Columbia. The District is financially accountable for these organizations because the Mayor, with the consent of the Council, appoints a voting majority of the governing bodies of these organizations. In addition, the District has an obligation to provide financial support to the Washington Convention and Sports Authority and the University of the District of Columbia.

Other component units have operations that are so intertwined with those of the primary government that they function, for all practical purposes, as an integral part of the primary government. These are reported as blended component units. A component unit should be blended when the primary government and the component unit share a common governing body or when the component unit either: (1) provides service entirely or almost entirely to the primary government; or (2) otherwise exclusively or almost exclusively benefits the primary government, although it does not provide services directly to it. The District has one blended component unit, the Tobacco Settlement Financing Corporation (Tobacco Corporation). The Tobacco Corporation is a blended component unit because it provides services exclusively to the District.

Each of the component units prepares its own independently audited financial statements, which are accompanied by their respective Management's Discussion and Analysis. Exhibits 5-a and 5-b on pages 53 and 54, respectively, present more detailed financial information on the District's component units.

## Short-Term Debt

The District issues short-term debt primarily to finance seasonal cash flow needs. This need occurs due to time lags between the receipt of taxes, grants and other revenues, and the outflow of funds for governmental operations and required disbursements. The District issued \$700,000 in Tax Revenue Anticipation Notes (TRANs) on October 25, 2010, at an interest rate of 2.00%. By law, the District must repay any short-term debt in its entirety by September 30 of the fiscal year in which the debt was incurred. Accordingly, the District repaid the TRANs on September 30, 2011.

## Long-Term Debt

The District is empowered by law (Section 461 of the District of Columbia Home Rule Act, as amended) to issue general obligation bonds to refund indebtedness of the District and to provide for the payment of the cost of acquiring capital assets or undertaking the District's various capital projects. The District also issues income tax secured revenue bonds pursuant to the Bond Authorization Act of 2008 (D.C. Code §§ 47-340.26 to 47-340.36). The payment of principal and interest on these bonds comes solely from the associated trust estate and the available pledged tax revenues. The income tax secured revenue bonds are without recourse to the District, and are not a pledge of, and do not involve the full faith and credit or the taxing power of the District.

The District also issues, on a less frequent basis, other types of long term debt, including Tax Increment Financing (TIF) Bonds, Tobacco Bonds, Housing Production Trust Bonds, Qualified Zone Academy Bonds, and other revenue bonds.

At September 30, 2011, the District had \$8,723,811 in long term debt outstanding, of which \$7,438,214, or 85.3%, was in the form of bonds. Of the outstanding bonds, \$2,829,598, or 38%, were general obligation bonds, and \$3,029,100, or 40.7%, were income tax secured revenue bonds. **Table 8** presents the District's outstanding bonds as of September 30, 2011.

**Table 8 – Outstanding Bonds at September 30, 2011 and 2010**

Type of Bonds	Outstanding Bond Debt			Percentage Variance
	2011	2010	Dollar Variance	
General Obligation Bonds	\$ 2,829,598	\$ 2,781,053	\$ 48,545	1.7%
Income Tax Secured Revenue Bonds	3,029,100	2,570,650	458,450	17.8%
Other Bonds:				
Tobacco Bonds	690,289	699,779	(9,490)	-1.4%
Ballpark Bonds	512,850	517,390	(4,540)	-0.9%
A W C PILOT Revenue Bonds	90,660	96,950	(6,290)	-6.5%
TIF Bonds	87,484	91,807	(4,323)	-4.7%
HPTF Bonds	84,335	85,615	(1,280)	-1.5%
NCRC Revenue Bonds	22,715	30,671	(7,956)	-25.9%
Qualified Zone Academy Bonds	8,573	9,518	(945)	-9.9%
GARVEE Revenue Bonds	82,610	-	82,610	100.0%
<b>Total</b>	<b>\$ 7,438,214</b>	<b>\$ 6,883,433</b>	<b>\$ 554,781</b>	<b>8.1%</b>

The \$458,450 increase in Income Tax secured Revenue Bonds is directly attributable to the following three bond issuances made in fiscal year 2011:

- Issued on November 22, 2010, \$63,860 in Income Tax Secured Revenue Refunding Bonds, Series 2010E, used to currently refund \$63,335 of the outstanding principal amount of the Income Tax Secured Revenue Refunding Bonds, Series 2010C and pay the costs of issuing and delivering the Series 2010E Bonds.
- Issued December 2, 2010, \$342,615 in Income Tax Secured Revenue Bonds, Series 2010F, used to pay and/or reimburse the District for the costs of capital projects and the costs of issuing and delivering the Series 2010F Bonds.
- Issued September 29, 2011, \$138,470 in Income Tax Secured Revenue Bonds, Series 2011A, used to pay and/or reimburse the District for the costs of capital projects and the costs of issuing and delivering the Series 2011A Bonds.

In addition, on February 14, 2011, the District issued \$82,610 in Federal Highway Grant Anticipation Revenue Bonds, Series 2011. This bond issuance was authorized pursuant to the Transportation Infrastructure Improvements Grant Anticipation Revenue Vehicles (GARVEE) Bond Financing Act of 2009 to finance the District's 11<sup>th</sup> Street Bridge Project (Phase 1). The proceeds of the 2011 Bonds were also used to pay the costs of issuing the 2011 Bonds and fund the Senior Lien Bonds Debt Service Reserve Subaccount.

The total debt per capita as of September 30, 2011, was \$12,500 (not in thousands). This represents an increase of \$614 (not in thousands), or 4.6%, over the prior year. This increase is due to the issuance of Income Tax Secured Revenue Bonds totaling \$544,945 and Federal Highway GARVEE Bonds totaling \$82,610. Exhibit S-3C, on page 177, presents ratios of total outstanding debt for the last ten fiscal years.

For more detailed information on the District's long-term debt activity, refer to Note 8, Long-Term Liabilities, found on pages 91 through 110.

## Capital Assets

The General Capital Improvements Fund is used to account for the purchase or construction of capital assets financed by transfers, capital grants, and debt. Capital assets include, but are not limited to, land, buildings, police and fire equipment, office equipment, park facilities, roads, and bridges. In fiscal year 2011, total capital assets increased by \$582,432, or 6.3%, over the prior year. Total overall capital assets has continued to increase because the District has been investing more resources in the construction of new assets and the rehabilitation of existing infrastructure, such as roads, streets, and bridges.

At September 30, 2011, total net capital assets (capital assets less depreciation) were \$9,815,790. Net capital assets of the governmental activities totaled \$9,815,312 and the net capital assets of the business-type activities totaled \$478. The governmental activities depreciation charges for fiscal year 2011 totaled \$336,212 compared to the prior year's amount of \$314,938. **Table 9** presents more detailed information on the District's net capital assets.

**Table 9 – Net Capital Assets as of September 30, 2011**

Asset Category	Governmental Activities		Business-type Activities		Total	
	2011	2010	2011	2010	2011	2010
Land	\$ 919,558	\$ 916,721	\$ -	\$ -	\$ 919,558	\$ 916,721
Buildings	4,111,593	3,429,054	-	3,192	4,111,593	3,432,246
Infrastructure	2,465,943	2,279,590	-	-	2,465,943	2,279,590
Equipment	404,436	427,976	478	1,635	404,914	429,611
Construction in progress	1,913,782	2,175,190	-	-	1,913,782	2,175,190
<b>Total net capital assets</b>	<b>\$ 9,815,312</b>	<b>\$ 9,228,531</b>	<b>\$ 478</b>	<b>\$ 4,827</b>	<b>\$ 9,815,790</b>	<b>\$ 9,233,358</b>

For more detailed information on the District's capital asset activity, refer to Note 5, Capital Assets, found on pages 86 through 90.

## REPORTING THE DISTRICT'S BUDGET

### Overview in Brief

D.C. Code § 47-392.01(c) (1) (A) requires the District to prepare a balanced budget each year. Consistent with D.C. Code §47-392.02, the Mayor is required to submit the budget to Council for review, approval, and submission to Congress. The District's budget is subject to revision and veto by Congress and the President of the United States. As the budget moves through the budgetary process, there may be changes in both amounts and purposes.

The Chief Financial Officer is responsible for forecasting revenue for the District government. Each February, the Chief Financial Officer issues the official revenue estimate that is used to develop the District's budget for the next fiscal year. This estimate is revised as the new fiscal year begins and is periodically reviewed and adjusted at regular intervals throughout the fiscal year to reflect current economic trends and outlook, new legislative mandates, and other similar factors. As the revenue estimates are revised, the District's expenditure budget is also revised to be consistent with the updated revenue estimates.

### General Fund Budgetary Highlights

The General Fund is the chief budgetary operating fund of the primary government. **Table 10** presents a Schedule of Budgetary Basis Revenues and Expenditures for the General Fund for the fiscal year ended September 30, 2011.



**Table 10 – Schedule of Budgetary Basis Revenues and Expenditures**

	<b>Original Budget</b>	<b>Revised Budget</b>	<b>Actual</b>	<b>Variance (Actual to Revised)</b>
<b>Revenues and Sources:</b>				
Taxes	\$ 4,869,807	\$ 5,054,156	\$ 5,203,168	\$ 149,012
Licenses and permits	64,276	59,948	76,020	16,072
Fines and forfeits	166,425	131,261	126,251	(5,010)
Charges for services	43,587	51,505	75,540	24,035
Miscellaneous	173,813	142,559	145,101	2,542
Other sources	410,456	411,276	476,584	65,308
General obligation bonds	15,000	15,000	6,320	(8,680)
Fund Balance released from restrictions	114,704	105,530	55,805	(49,725)
Interfund transfer from lottery and games	68,500	63,257	62,175	(1,082)
Interfund transfer - others	189,550	183,622	79,242	(104,380)
<b>Total revenues and other sources</b>	<b>6,116,118</b>	<b>6,218,114</b>	<b>6,306,206</b>	<b>88,092</b>
<b>Expenditures and Other Uses:</b>				
Governmental direction and support	464,046	455,607	440,427	15,180
Economic development and regulation	256,883	283,509	255,399	28,110
Public safety and justice	976,197	1,010,151	993,786	16,365
Public education	1,485,844	1,521,314	1,497,639	23,675
Human support services	1,453,131	1,500,534	1,466,639	33,895
Public works	540,669	547,708	538,837	8,871
Repay bonds and interest	418,483	413,641	409,550	4,091
Other expenditures and uses	519,541	484,819	464,234	20,585
<b>Total expenditures and other uses</b>	<b>6,114,794</b>	<b>6,217,283</b>	<b>6,066,511</b>	<b>150,772</b>
<b>Excess of Revenues and Other Sources Over Expenditures and Other Uses - Budgetary Basis</b>	<b>\$ 1,324</b>	<b>\$ 831</b>	<b>\$ 239,695</b>	<b>\$ 238,864</b>

**Revenues and Other Sources**

Actual General Fund revenues and other sources were \$88,092 more than the revised budget. As presented in **Table 10**, this variance was primarily due to significant increases in taxes and other sources which are discussed below.

**Taxes** – Tax revenues in excess of the revised budget were primarily in the form of Income and Franchise Taxes and Inheritance and Estate Taxes. Individual income tax revenue exceeded the revised budget by \$81,321 due to strong withholding collections in fiscal year 2011 and a stronger-than-expected recovery in the non-withholding portion of income tax. Unincorporated business franchise taxes exceeded the revised budget by \$21,756 in fiscal year 2011 due to a rebound in the equity markets and increased corporate profits.

In addition, Inheritance and Estate taxes exceeded the fiscal year 2011 revised budget by \$34,230. This excess was due to the death of wealthy District residents who had significantly enhanced their wealth positions in recent years. In light of the recession and continuing uncertainty about the federal estate tax, collections of District estate taxes are expected to decline over the next several years.

**Other Sources** – Revenues generated through other public sources exceeded the revised budget by \$65,308. This excess was due, for the most part, to the certain policy changes, which included but was not limited to the following: (a) taxing prepaid phone cards at a rate of 2%; (b) increasing Department of Health fees; (c) increasing food handler fees; (d) increasing notary public fees; (e) imposing a technology fee for basic business licenses; (f) assessing special events licensing fees; (f)

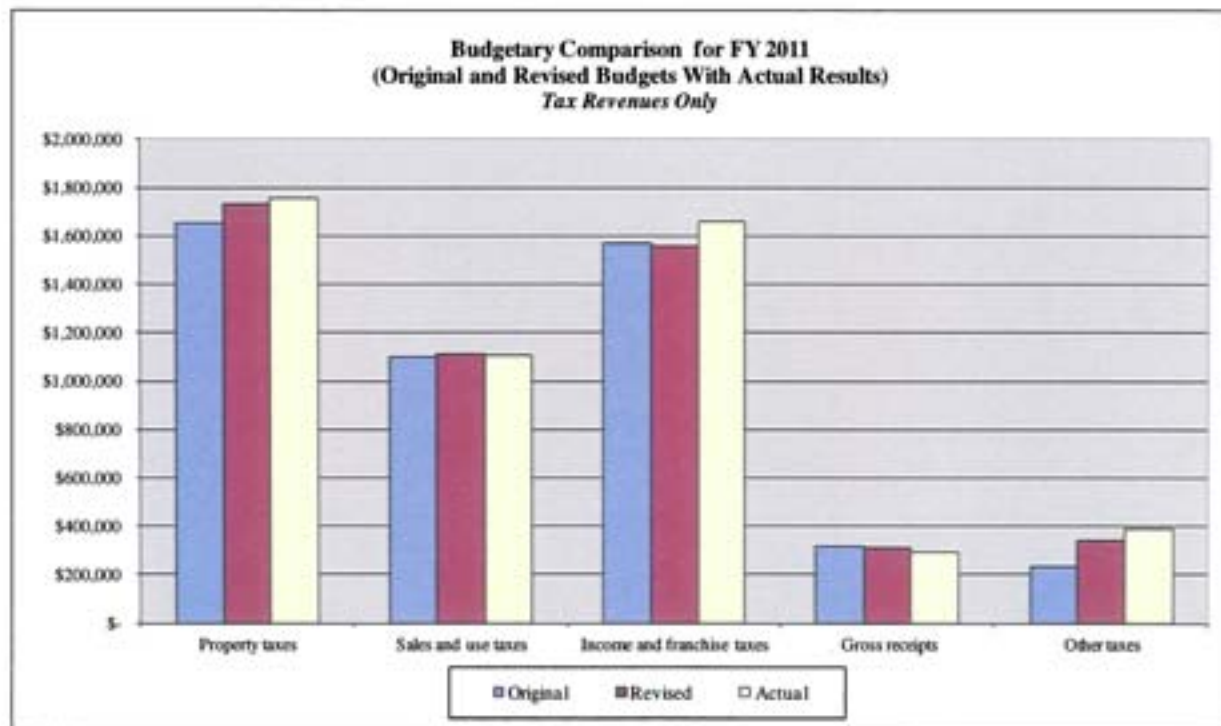
implementing Department of Transportation fee increases (steel plate fee, car sharing space fee, technology fee on public space permits, and permit fee for loading and unloading intercity buses).

**Fund Balance Released from Restrictions** – Fund balance released from restrictions represents the portion of assets that were restricted for either a period of time or for a particular purpose for which the imposed conditions have been met, allowing the assets to become available for use. In other words, this amount of fund balance was used to finance current year's operations. As presented in **Table 10**, the actual amount of fund balance released from restrictions was (\$49,725) less than the revised budget.

**Interfund Transfer – Others** – Interfund transfers are the flows of assets (such as cash or goods) between funds and blended component units of the primary government without equivalent flows of assets in return and without a requirement for repayment. Actual interfund transfers in fiscal year 2011 were (\$105,462) less than the revised budget.

More than 82% of the General Fund's revenues are derived from taxes. **Chart 5** graphically presents differences between the General Fund's original budget, final revised budget and actual revenues (by type of tax) for fiscal year 2011.

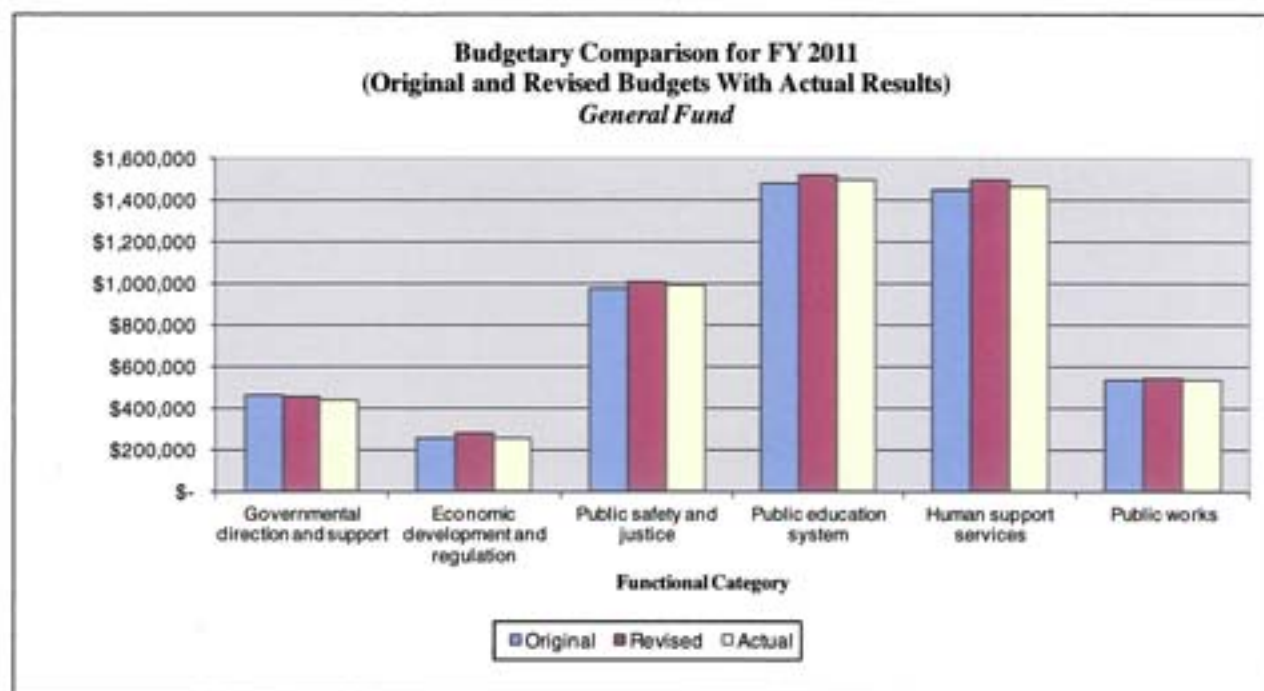
**Chart 5 – Budgetary Comparison – FY 2011 Tax Revenues**



### **Expenditures and Other Uses**

Actual General Fund expenditures and other uses were (\$150,772) less than the revised budget. As presented in **Table 10**, this variance was primarily due to underspending in the areas of Human Support Services, Economic Development and Regulation, Public Education, and Other Expenditures and Uses.

More than 65% of the General Fund's expenditures were in the areas of Human Support Services, Public Education, and Public Safety and Justice combined. **Chart 6** graphically presents differences between the General Fund's original budget, revised budget, and actual expenditures (by functional category) for fiscal year 2011.

**Chart 6 – General Fund Expenditures (by Function)**

For more detailed information, refer to the budgetary schedules for the General Fund, Exhibits A-4 to A-6 which are presented on pages 137 through 139.

### SUBSEQUENT EVENTS

#### Short-Term Debt

On October 6, 2011, the District issued \$820,000 in Tax Revenue Anticipation Notes (TRANs) as a means of financing, on a short-term basis, the District's general governmental expenses in anticipation of receiving or collecting revenues for fiscal year 2012. These fixed rate TRANs were issued at an interest rate of 2.00% and mature on September 28, 2012. By law, the District must repay any short-term debt in its entirety by September 30 of the fiscal year of issuance.

#### Income Tax Secured Revenue Bonds

##### *Series 2011B-C-D-E Bonds*

In November 2011, the District issued \$241,735 in Income Tax Secured Revenue Refunding Bonds (\$95,720, Series 2011B; \$3,415, Series 2011C; \$29,550, Series 2011D; and \$113,050, Series 2011E). The proceeds of the Series 2011B Bonds were used to currently refund \$63,335 of the outstanding principal amount of the District's Income Tax Secured Revenue Refunding Bonds, Series 2010E and pay the costs and expenses of issuing and delivering the Series 2011B Bonds. The proceeds of the Series 2011C Bonds, Series 2011D Bonds, and Series 2011E Bonds were used to advance refund the District's General Obligation Bonds, Series 2003A and pay the costs and expenses of issuing and delivering the Series 2011C Bonds, Series 2011D Bonds, and Series 2011E Bonds.

##### *Series 2011F-G Bonds*

In December 2011, the District issued \$410,470 in Income Tax Secured Revenue Bonds (\$200,000, Series 2011F and \$210,470, Series 2011G), together referred to as the Series 2011F-G Bonds.

The proceeds of the Series 2011F-G Bonds were used to pay and/or reimburse the District for costs associated with capital projects and pay the costs and expenses of issuing and delivering the Series 2011F-G Bonds.

These and other subsequent events are presented more fully in Note 16, found on pages 122 through 125.

#### **CONTACTING THE DISTRICT'S OFFICE OF THE CHIEF FINANCIAL OFFICER**

This CAFR is designed to provide the District's citizens, taxpayers, customers, vendors, investors, and creditors with a general overview of the District's finances and to demonstrate the effectiveness of the District's systems of accountability for the money it receives. If you have any questions regarding this report, suggestions for improvement, or need additional financial information, please contact the following:

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The John A. Wilson Building  
1350 Pennsylvania Avenue, N.W., Suite 209  
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