

MANAGEMENT'S DISCUSSION AND ANALYSIS

September 30, 2008

(Dollar amounts expressed in thousands)

This Management's Discussion and Analysis (MD&A) provides a narrative overview and analysis of the financial activities of the District of Columbia (the District) for the fiscal year ended September 30, 2008. This discussion and analysis should be read in conjunction with the basic financial statements and the related note disclosures. In addition, it is important to also read the Transmittal Letter, which begins on page 1, in conjunction with the MD&A.

OVERVIEW OF THE FINANCIAL STATEMENTS

The District's basic financial statements are comprised of three components:

- (1) *Government-Wide Financial Statements* - Exhibit 1-a, *Statement of Net Assets*, and Exhibit 1-b, *Statement of Activities* on pages 46 and 47 respectively, present information about the financial activities of the District as a whole. These two statements provide an overall view of the District's finances.
- (2) *Governmental Fund Financial Statements* - Exhibit 2-a, *Balance Sheet – Governmental Funds*, Exhibit 2-b, *Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds*, Exhibit 2-c, *Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities*, and Exhibit 2-d, *Budgetary Comparison Statement* on pages 48, 49, 50, and 51, respectively, show the District's financial position at the end of the fiscal year and how governmental activities were financed during the current year.

Proprietary Funds – Exhibit 3-a, *Statement of Net Assets*, Exhibit 3-b, *Statement of Revenues, Expenses, and Changes in Fund Net Assets* and Exhibit 3-c, *Statement of Cash Flows* on pages 52, 53 and 54 respectively, show 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 its one non-major proprietary fund-Nursing Home Services. Proprietary funds account for the activities of District entities that charge customers fees for services provided.

Fiduciary Funds – Exhibit 4-a, *Statement of Fiduciary Net Assets* and Exhibit 4-b, *Statement of Changes in Fiduciary Net Assets* on pages 55 and 56 report activities for which the District acts exclusively as a trustee or agent for the benefit of entities or individuals external to the government.

Discretely Presented Component Units - The District currently has five (5) component units. The financial data of the component units are reported separately from the financial data of the primary government: Exhibit 5-a, *Discretely Presented Component Units Combining Statement of Net Assets* on page 57 and Exhibit 5-b, *Discretely Presented Component Units Combining Statement of Activities* on page 58.

- (3) *Notes To The Basic Financial Statements* - Present additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements, and can be found on pages 59 through 118.

FINANCIAL HIGHLIGHTS

- In the government-wide analysis, assets exceeded liabilities, resulting in total net assets of \$2,961,335. The total net assets consists of *net assets invested in capital assets, net of related debt* of \$1,811,026, *restricted net assets* of \$1,530,495, and an *unrestricted net deficit* of \$(380,186). The total government-wide net assets included \$2,545,533 generated by governmental activities and \$415,802 generated by business-type activities.
- There was a decrease of \$(16,398) over the previous year in the government-wide total net assets. This decrease is attributable to a \$950,049 increase in total assets, which was offset by an increase in total liabilities of \$966,447. (See Table 1, *Net Assets as of September 30, 2008* on page 27).

- The governmental funds reported a combined fund balance of \$2,339,756 which was a decrease of \$(449,824) over the previous year. The fund balance of the General Fund was \$1,244,722 or 53.2% of the combined fund balances, and represented a decrease of \$(249,278) over the previous year.
- \$957,977 of the General Fund's fund balance is reserved for specific purposes: \$330,238 is legally set aside for emergencies and contingencies, and \$209,496 for bond escrow, with \$418,243 reserved for other purposes. \$286,745 of the General Fund's fund balance is unreserved with \$200,020 designated for specific purposes leaving \$86,725 undesignated.
- Total long-term debt related to notes and bonds increased by \$435,086, or 7.9%. There was a net increase of \$ 452,385 in general obligation debt and a decrease of \$(17,299) in other debt. (Table 4, *Outstanding Bonds and Notes at September 30, 2008*, page 36).

NEW GASB PRONOUNCEMENTS

The mission of the Governmental Accounting Standards Board (GASB) is to establish and improve standards of state and local governmental accounting and financial reporting that will result in useful information for users of financial reports and guide and educate the public, including issuers, auditors, and users of those financial reports. GASB is the authoritative body that sets accounting and financial reporting standards for state and local governments.

GASB Statement No. 45

In July 2004, GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. This Statement establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related assets and liabilities, note disclosures, and, if applicable, required supplementary information (RSI) in the financial reports of state and local government employers.

The District implemented this Statement in FY 2008, as required.

GASB Statement No. 48

In September 2006, GASB issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. Governments sometimes exchange an interest in their expected cash flows from specific receivables or specific revenues, for immediate cash payments – generally, a single lump sum. This Statement establishes criteria that governments will use to ascertain whether the proceeds should be reported as revenue or as a liability. This Statement also includes guidance to be used for recognizing other assets and liabilities arising from a sale of specific receivables or future revenue, including residual interests and recourse provisions. The requirements in this Statement improve financial reporting by establishing measurement, recognition, and disclosure requirements that apply to both governmental and business-type activities.

The District implemented this Statement in FY 2008, as required.

GASB Statement No. 49

On December 1, 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. This Statement identifies the circumstances under which a government would have to estimate its expected outlays for pollution remediation, if it knows that a site is polluted. This Statement also requires state and local governments to disclose information about their pollution obligations associated with clean up efforts in the notes to the financial statements.

GASB Statement No. 49 became effective for fiscal years beginning after December 15, 2007, the District's FY 2009.

GASB Statement No. 50

In May 2007, GASB issued Statement No. 50, *Pension Disclosures*. This Statement provides new guidance and modifies the note and required supplementary information (RSI) regarding pensions. The changes in pension disclosures include a

requirement to present a schedule of funding progress as RSI even when a government uses the aggregate actuarial cost method.

GASB Statement No. 50 became effective for fiscal years beginning after June 15, 2007, the District's FY 2008. This Statement was implemented in FY 2008, as required.

GASB Statement No. 51

In June 2007, GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*. This Statement requires that intangible assets possess the following characteristics: (1) lack of physical substance, (2) be non-financial in character, and (3) have an initial useful life extending beyond a single reporting period. The Statement further provides that recognition of intangible assets is only appropriate when they are either separable (e.g. can be sold, transferred, or licensed) or represent contractual or other legal rights, regardless of transferability or separability.

GASB Statement No. 51 becomes effective for fiscal years beginning after June 15, 2009, the District's FY 2010. The District plans early implementation of this Statement.

GASB Statement No. 52

In November 2007, GASB issued Statement No. 52, *Land and Other Real Estates Held as Investments by Endowments*. This Statement requires endowments to report their land and other real estate investments at fair value. Governments are also required to report the changes in fair value as investment income and to disclose the methods and significant assumptions employed to determine fair value, and other information that they currently present for other investments reported at fair value.

GASB Statement No. 52 becomes effective for fiscal years beginning after June 15, 2008, the District's FY 2009. The District plans implementation of this Statement in FY 2009.

GASB Statement No. 53

In June 2008, GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Investments*. This statement requires governments to measure most derivative instruments at fair value in financial statements that are prepared using the economic resources measurement focus and the accrual basis of accounting. Changes in fair value for effective hedges have to be recognized in the reporting period when they occurred.

GASB Statement No. 53 becomes effective for fiscal years beginning after June 15, 2009, the District's FY 2010. The District is reviewing the requirements for implementing this Statement, and may early implement it in FY 2009.

THE DISTRICT'S FINANCIAL CONDITION

The District government's financial responsibility and performance can be measured in various ways. Below are some of the indicators of the District's improved financial position and condition:

- The total expenditures for the District were again within budget.
- The General Fund ended the year with a budgetary surplus of \$191,370. After deducting the use of fund balance released from restrictions and other adjustments required by generally accepted accounting principles (GAAP), the non-budgetary or GAAP deficit was \$(249,278).
- The accumulated General Fund fund balance at September 30, 2008 was \$1,244,722.
- The required legal debt limitation allows the District to use up to 17.0% of its total revenues for debt service in FY 2008. However, the District's debt service cost was only 7.5% of total revenues, or about 43.0% of the legal limit.
- The District continues to allocate large amounts of funds for infrastructure assets.

Reporting the District as a Whole (Government-Wide Financial Statements)

The District, as a whole, reports all assets and liabilities using the *accrual basis of accounting*. This method of reporting is similar to the accounting method used by most private-sector companies. Under this basis of accounting, all of the current year's financial activities are taken into account regardless of when cash is received or paid. The governmental activities and business-type activities are presented in two separate columns and combined to show totals for the primary government. The *Statement of Net Assets* and the *Statement of Activities* are two statements that present information and activities that help the reader determine the overall financial condition of the District.

The District's current financial resources (short-term disposable resources) are reported along with capital assets and long-term obligations in the *Statement of Net Assets*. The *Statement of Net Assets* presents information on all of the District's assets and liabilities, with the difference between the two reported as *net assets*. This statement distinguishes between governmental activities, business-type activities and component units' activities.

The total net assets is the sum of three components: 1) *net assets invested in capital assets, net of related debt*, 2) *restricted net assets*, and 3) *unrestricted net assets*. Over time and accounting periods, changes in the District's net assets are indicators of its financial health. However, changes in population, property tax base, infrastructure condition and other non-financial factors must also be considered in assessing the overall financial health of the District.

The *Statement of Activities* presents information showing how the government's net assets changed from the last fiscal year. 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 only 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 show the District's basic functional services while business-type activities reflect enterprise operations where fees for services are expected to cover all or most of the costs of operations, including depreciation. Program/functional expenses are reduced by program specific earned revenues, and by grants, that reduce net expenses for governmental and business-type activities. The District's general revenues (property, sales, income and franchise taxes) offset remaining costs, resulting in an increase or decrease in net assets.

Fund balances in the governmental fund financial statements will generally differ from net assets in the governmental activities of the government-wide financial statements due to the measurement focus and basis of accounting used in the respective financial statements.

- Fund financial statements focus primarily on the sources, uses, and balances of current financial resources and use the modified accrual basis of accounting.
- The government-wide financial statements focus on all of the District's economic resources and use the full accrual basis of accounting.

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

In fiscal year 2008, the combined total net assets decreased by \$(16,398). This decrease is the combination of a governmental activities decrease of \$(13,795) and a business-type activities decrease of \$(2,603). See Table 2, *Change in Net Assets as of September 30, 2008*, on page 28.

Restricted net assets are assets that are subject to use-constraints that are either: (a) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or, (b) imposed by law through constitutional provisions or by enabling legislation. In FY 2008, total restricted net assets decreased by \$(114,361), or -6.95%, consisting of a decrease of \$(113,495), or -8.94%, from governmental activities, and a decrease of \$(866), or -0.23% from business-type activities.

The Lottery and Charitable Games Control Board, 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 year 2008, the transfer was \$70,300, which was a \$4,924 increase from last year. Please see Exhibit 3-b, *Statement of Revenues, Expenses and Changes in Fund Net Assets – Proprietary Funds*, on page 53.

The negative unrestricted net asset amount of \$(404,959) for governmental activities for FY 2008 was caused mainly by the additional use of current resources to finance capital projects, a significant absorption of Medicaid disallowances and receivable write-off, and the use of available net assets to finance operations. This amount is combined with the unrestricted net assets for business-type activities of \$24,773; resulting in negative total unrestricted net assets for FY 2008 of \$(380,186).

The governmental activities total net assets of \$2,545,533 in FY 2008 represent a decrease of \$(13,795) from FY 2007. The net decrease was composed primarily of an increase of \$597,004 in invested in capital assets, net of related debt, a decrease of \$(113,495) for other restricted net assets, and a decrease of \$(497,304) in unrestricted net assets.

Table 1 - Net Assets as of September 30, 2008

	Governmental activities		Business-type activities		Totals	
	2008	2007	2008	2007 Restated	2008	2007 Restated
Current and other assets	\$ 4,016,319	\$ 4,181,473	\$ 501,051	\$ 489,123	\$ 4,517,370	\$ 4,670,596
Capital assets	7,243,637	6,139,898	16,747	17,211	7,260,384	6,157,109
Total assets	11,259,956	10,321,371	517,798	506,334	11,777,754	10,827,705
Long-term liabilities	7,128,989	6,416,109	41,379	46,725	7,170,368	6,462,834
Other liabilities	1,585,434	1,345,934	60,617	41,204	1,646,051	1,387,138
Total Liabilities	8,714,423	7,762,043	101,996	87,929	8,816,419	7,849,972
Net assets:						
Invested in capital assets, net of related debt	1,794,279	1,197,275	16,747	17,211	1,811,026	1,214,486
Restricted	1,156,213	1,269,708	374,282	375,148	1,530,495	1,644,856
Unrestricted	(404,959)	92,345	24,773	26,046	(380,186)	118,391
Total net assets	\$ 2,545,533	\$ 2,559,328	\$ 415,802	\$ 418,405	\$ 2,961,335	\$ 2,977,733

Table 2 - Change in Net Assets for the year ended September 30, 2008

	Governmental activities		Business-type activities		Total		
	2008	2007	2008	2007 Restated	2008	2007 Restated	Variance
Revenues:							
Program revenues:							
Charges for services	\$ 379,149	\$ 334,977	\$ 290,156	\$ 288,673	\$ 669,305	\$ 623,650	\$ 45,655
Operating grants and contributions	2,178,275	2,309,495	21,191	18,358	2,199,466	2,327,853	(128,387)
Capital grants and contributions	175,841	130,557	-	-	175,841	130,557	45,284
General revenues:							
Property taxes	1,787,365	1,545,325	-	-	1,787,365	1,545,325	242,040
Income and franchise taxes	1,755,894	1,736,361	-	-	1,755,894	1,736,361	19,533
Sales and use taxes	1,101,859	1,056,780	-	-	1,101,859	1,056,780	45,079
Other taxes	716,274	800,966	92,733	90,117	809,007	891,083	(82,076)
Non tax revenues	554,316	580,845	37,672	21,936	591,988	602,781	(10,793)
Total revenues	8,648,973	8,495,306	441,752	419,084	9,090,725	8,914,390	176,335
Expenses:							
Governmental direction and support	834,694	787,392	-	-	834,694	787,392	47,302
Economic development and regulation	499,644	509,874	-	-	499,644	509,874	(10,230)
Public safety and justice	1,384,517	1,264,715	-	-	1,384,517	1,264,715	119,802
Public education system	1,787,635	1,589,652	-	-	1,787,635	1,589,652	197,983
Human support services	3,285,325	2,992,805	-	-	3,285,325	2,992,805	292,520
Public works	586,649	481,702	-	-	586,649	481,702	104,947
Public transportation	214,905	198,484	-	-	214,905	198,484	16,421
Interest on long-term debt	293,339	281,918	-	-	293,339	281,918	11,421
Lottery and games	-	-	182,981	192,336	182,981	192,336	(9,355)
Unemployment compensation	-	-	150,237	99,920	150,237	99,920	50,317
Nursing home services	-	-	40,837	37,490	40,837	37,490	3,347
Total expenses	8,886,708	8,106,542	374,055	329,746	9,260,763	8,436,288	824,475
Special item	153,640	(8,838)	-	-	153,640	(8,838)	162,478
Transfer from lottery and games	70,300	65,376	(70,300)	(65,376)	-	-	-
Change in net assets	(13,795)	445,302	(2,603)	23,962	(16,398)	469,264	(485,662)
Net assets - Oct 1 Restated	2,559,328	2,114,026	418,405	394,443	2,977,733	2,508,469	469,264
Net assets - Sept 30	\$ 2,545,533	\$ 2,559,328	\$ 415,802	\$ 418,405	\$ 2,961,335	\$ 2,977,733	\$ (16,398)

Please refer to Note 1.X – Reconciliation of Government-Wide and Fund Financial Statements, on pages 72-73, for additional information on the differences between the two bases of accounting that the District uses in this Report.

Chart 1 shows various sources of revenues. This chart is a visual presentation of the numbers that were presented in Table 2, *Change in Net Assets* for the year ended September 30, 2008 on page 28.

Chart 1 – Revenues by Source – Governmental Activities

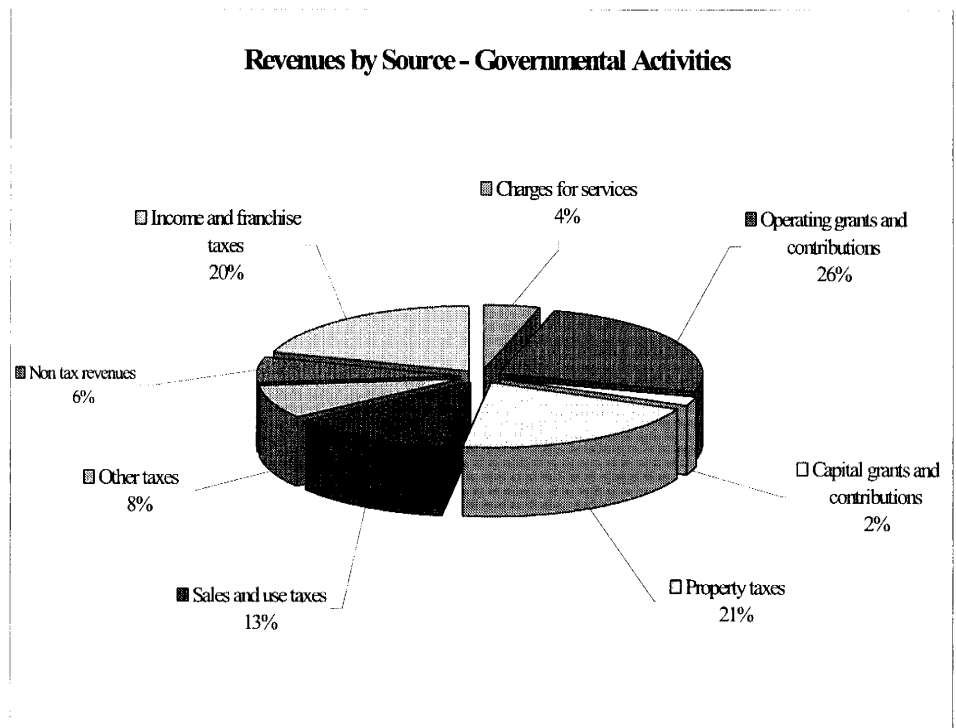
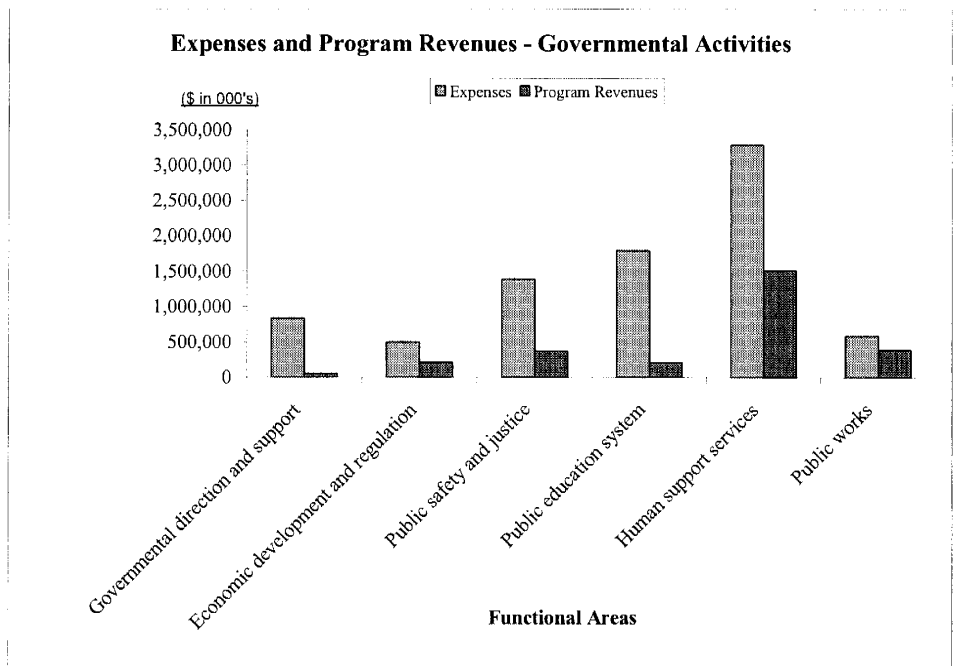


Chart 2 displays both expenses and program revenues of selected governmental activities for the fiscal year. The governmental activities that are shown are: governmental direction and support, economic development and regulation, public safety and justice, public education system, human support services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

Chart 2 - Expenses and Program Revenues – Governmental Activities



Reporting on the District's Most Significant Funds

A fund is a fiscal and accounting entity with a self-balancing set of accounts that the District uses to keep track of specific sources of funding and spending for a particular purpose. In accordance with District law, bond covenants, and other legal stipulations, funds are established for specific purposes and to report on the activities related to the goods and services that the District provides to the general public. The District's funds are presented in three categories or groups: governmental, enterprise, and fiduciary.

The focus of the fund financial statements' presentation is on major funds, and not on fund types. Major funds, as required by 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, *Nonmajor Governmental Funds Combining Balance Sheet* and B-2, *Nonmajor Governmental Funds Combining Statement of Revenues, Expenditures and Changes in Fund Balances*, pages 134 and 135.

Governmental Funds

The District's governmental funds provide information on near-term inflows, outflows, and balances of spendable resources. This information is useful in assessing the District's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. The governmental fund financial statements relate to the governmental activities column in the government-wide statements. The focus is on a shorter-term basis and measures how money flows into and out of these funds and determines the balances left at year-end for future spending.

Most basic services are found in this fund category, which are reported as General, Federal and Private Resources, General Capital Improvements, Baseball Capital Project, and Nonmajor Governmental Funds. These funds are reported using the *modified accrual basis of accounting*, which measures cash and other financial assets that can be readily converted into cash. Please refer to Exhibit 2-a, *Balance Sheet – Governmental Funds* and Exhibit 2-b, *Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds*, pages 48 and 49, for more detailed information about these funds.

- **Fund Balances:** The governmental funds reported a combined fund balance of \$2,339,756, a decrease of \$(449,824) over the previous year. The components of this combined fund balance are as follows:
 - General Fund - \$1,244,722, a decrease of \$(249,278) over the previous year.
 - Federal and private resources - \$83,794, a decrease of \$(50,455) over the previous year.
 - General capital improvements - \$586,934, a decrease of \$(116,829) over the previous year.
 - Baseball capital project - \$19,602, a decrease of \$(93,440) over the previous year.
 - Nonmajor governmental funds - \$404,704, an increase of \$60,178 over the previous year.
- **Revenues:** The collection of taxes and other revenues increased in FY 2008 despite the decline in the U.S. economy. Revenues of the governmental funds increased by \$130,259. Property taxes showed an increase of \$207,191, while other taxes and charges for services showed moderate increases. Commercial retail and office space growth continued, although new construction has slowed, due to the recession, and commercial vacancy rates remained amongst the lowest in the nation.

The primary sources of the increases in General Fund tax revenues are:

- Property taxes increased by \$207,191.
- Sales and use tax increased by \$45,079.
- Income and franchise taxes increased by \$19,533.

The increase in real property tax revenue in FY 2008 reflects the strength of the D.C. real estate market in the previous two years, because there is a two-year lag between the time when real property value is assessed and when the revenue from the increased assessment is realized. As the demand for residential and commercial real estate has soared in the last several years, prices have climbed steeply and the result has been higher assessments and increased tax revenue, despite several rounds of tax relief for the residential sector. The slowdown in both the national and Washington, D.C. economy will place pressure on FY 2009 tax collections as economic activity is affected.

On the residential side, longer commuting times, for non-resident employees, have made Washington, D.C. a more attractive place to live. The growth in the wages and salaries of residents contributed to the increase in individual income tax revenue. The increase in the sales and use tax was due to increased retail and hospitality sales, a result of increased individual income and the growth in the number of conventions and visitors. Many condominium projects that were recently completed have converted to apartment rentals and leases, as property values have declined and financing has become more difficult to obtain.

The rise in individual income tax revenue has slowed considerably from prior years, reflecting the effects of the recession, and its impact on wages and investment returns. This suggests that the next few years will see only moderate growth in returns from the financial markets that, in the previous years, was the main driver of the continued growth in the individual income tax.

Dedicated Revenues

Every year, some portion of various District revenue streams are dedicated to certain purposes. The dedicated portion of the tax revenues is transferred out of the local fund, and is thus not available for general budgeting. In FY 2008, the District transferred a total of \$452,656 in tax revenues out of the local fund budget to fund the projects in Tables 3a and 3b, on this page. There was a total gross collection of \$2,752,818 of tax revenue, subject to dedicated purposes, of which, \$223,684 was transferred, resulting in a net tax collection of \$2,529,134, (Table 3a). There was a gross collection of budgetary dedicated taxes of \$1,466,143, subject to dedicated purposes, of which, \$228,972 was transferred, and resulting in a net tax collection of housing related taxes of \$1,237,171, (Table 3b).

Table 3a – Dedicated Local Tax Revenues (\$ in 000's)

Source	Dedicated Purpose (Transfer to)							Net Collection
	Gross Collection	TIF	DDOT	Convention Center	Highway Trust Fund	Nursing Facility Quality of Care		
Real Property	\$ 1,672,969	(6,654)						1,666,315
Public Space Rental	27,697		(27,697)					-
General Sales	1,015,182	(23,450)	(37,420)	(91,493)				862,819
Motor Fuel Tax	23,199				(23,199)			-
Healthcare Provider Tax	13,771					(13,771)		-
Total	\$ 2,752,818	(30,104)	(65,117)	(91,493)	(23,199)	(13,771)		2,529,134

Table 3b – Dedicated Local Tax Revenues (\$ in 000's)

Source	Budgetary Dedicated Tax Transfers							
	Local Collection	Neighborhood Investment	Ballpark Fund	Nursing Facility Fund	School Modernization	HPTF	Mayor's Housing Fund	Available for General Fund use
Personal Property	59,690	(10,000)						49,690
General Sales	862,819		(12,364)		(100,000)			750,455
Public Utility	178,532		(9,228)					169,304
Toll	65,741		(2,559)					63,182
Healthcare Provider	5,964			(5,964)				-
Baseball gross receipts	24,989		(24,989)					-
Deed Recordation	155,974					(23,853)	(13,819)	118,302
Deed Transfer	112,434					(16,736)	(9,460)	86,238
Total	\$ 1,466,143	(10,000)	(49,140)	(5,964)	(100,000)	(40,589)	(23,279)	1,237,171

Source: Office of Tax and Revenue

- **Expenditures:** The District's expenditures increased in most of its program/functional areas in the total amount of \$1,139,052 over the previous year. Increases by program or functional area were led by: governmental direction and support, \$43,201; human support services, \$247,158; the public education system, \$175,507; public safety and justice, \$128,223; economic development and regulation, \$17,199; and public works, \$87,040.

The District spent \$1,161,941 on general capital improvements which exceeded the general capital improvements revenues of \$190,422 by \$(971,519), resulting in the deficiency shown in the capital projects fund. The District's investments in capital improvements are based on need rather than available current year revenues, before considering current year bond proceeds. This deficiency was subsequently financed with a total of \$854,690 of bond proceeds and other financing sources. The net change in the general capital improvements fund balance was a decrease of \$(116,829).

The District continues to invest in infrastructure and other improvements to encourage residents and businesses to stay in the District and to attract new residents and businesses to the District. Listed below are ten infrastructure projects undertaken in FY 2008, by costs incurred:

1)	Street Repairs & Maintenance, Equipment & Technical Improvement	\$17,718
2)	Asset Preservation in Tunnels	\$12,167
3)	Ward 5 Road Resurfacing/Reconstruction/Upgrades	\$12,133
4)	Traffic Signal Maintenance	\$11,038
5)	Benning Road – 16 th Street to Oklahoma	\$10,671
6)	Pavement Restoration National Highway System	\$10,158
7)	Reconstruction Kenilworth Avenue/NH Burroughs Roadways	\$ 7,204
8)	Streetlight Asset Management	\$ 6,674
9)	South Capital Street Bridge over Anacostia River	\$ 6,465
10)	Reconstruction Kenilworth Avenue Bridge	\$ 5,270

It is the District's financial policy to issue general obligation 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 based on the annual amount budgeted. In practice, 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.

Proprietary Funds

Proprietary funds account for activities of District entities that charge customers fees for services provided, whether to outside customers or to other entities of the District. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. 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, Nursing Home Services, which includes the operations of the Washington Center for Aging Services, the Washington Center for Aging Services Center Care, and the JB Johnson Nursing Center. See *Chart 3, Expenses and Program Revenues – Business-Type Activities* and *Chart 4, Revenues by Source – Business-Type Activities*, both on page 33, which give a visual comparative presentation of the revenues and expenses of the three funds.

The total assets for Lottery decreased by \$(5,177), or -8.4%, over the previous year due to scheduled disbursements to long-term prize winners. The total assets for Unemployment increased by \$16,791, or 4.1%, due to higher tax collections from employers. The net cash provided by (used in) operating activities for Lottery, Unemployment and non-major proprietary funds (Nursing Services) were \$68,602, \$(17,892), and \$(4,344) respectively. See Exhibit 3-a, *Statement of Net Assets – Proprietary Funds*, Exhibit 3-b, *Statement of Revenues, Expenses and Changes in Fund Net Assets – Proprietary Funds*, and Exhibit 3-c, *Statement of Cash Flows – Proprietary Funds*, on pages 52, 53 and 54 respectively for more detailed information.

Proprietary entities provide goods and services to the general public and use the *full accrual accounting* method for reporting purposes.

Charts 3 and 4 are graphic comparisons based on financial information in Exhibit 3b, Statement of Revenues, Expenses and Changes in Fund Net Assets – Proprietary Funds, for the year ended September 30, 2008 on page 53.

Chart 3 – Expenses and Program Revenues – Business-type Activities, by Component

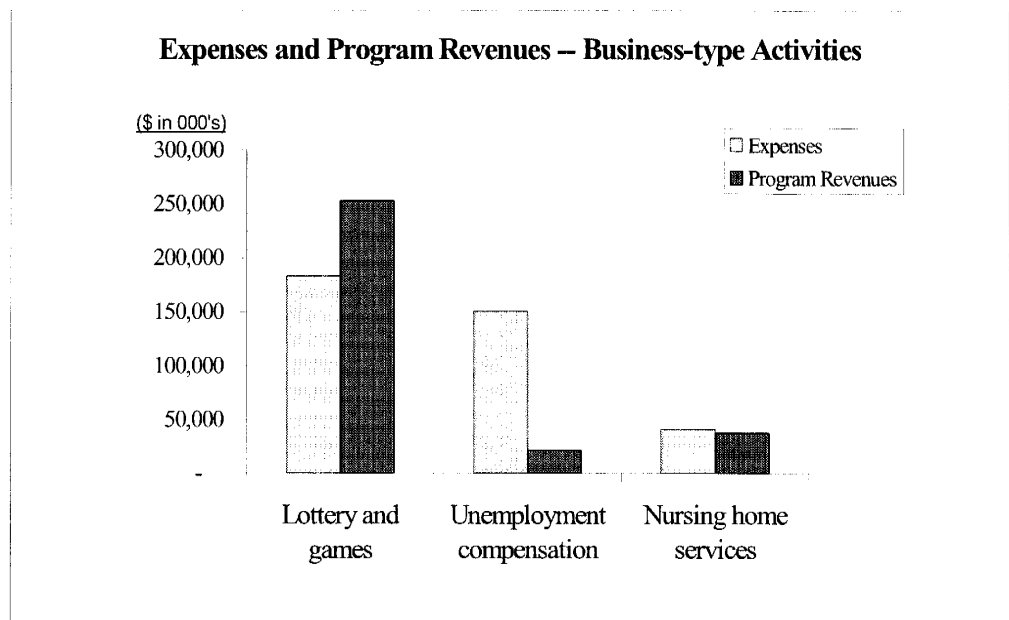
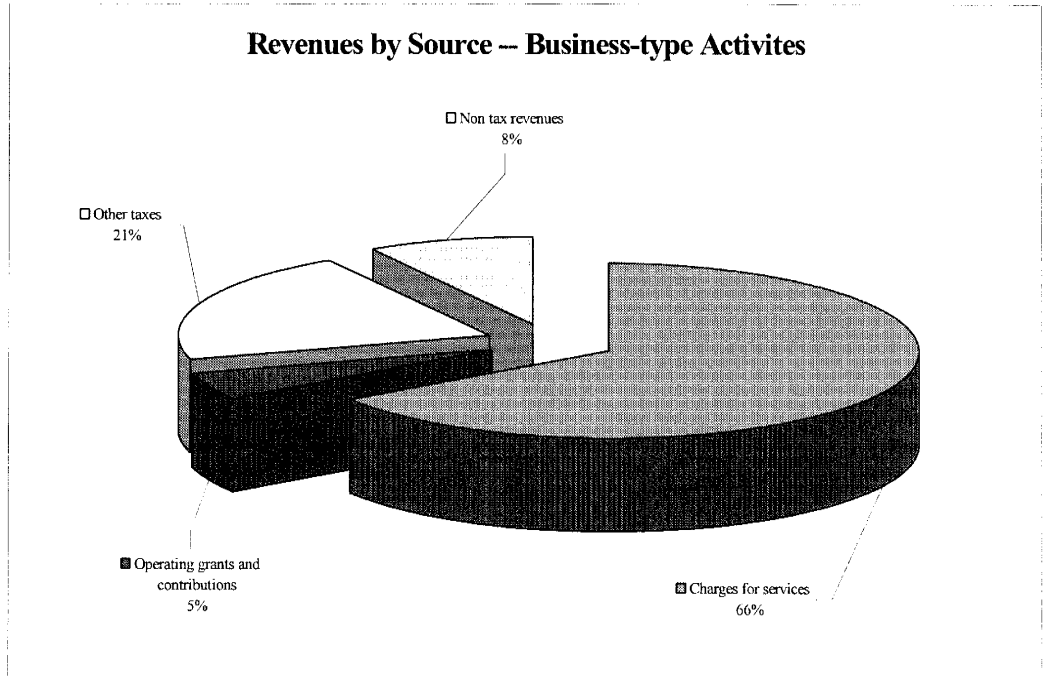


Chart 4 – Revenues by Source – Business-type Activities, Consolidated



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 post employment benefits. 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 55 and 56, respectively. Please also refer to Exhibit C-1, *Pension Trust Funds – Combining Statement of Fiduciary Net Assets*, Exhibit C-2, *Pension Trust Funds – Combining Statement of Changes in Fiduciary Net Assets* on pages 138 and 139 respectively, for more details. 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.

Private-purpose trust funds are used to report any trust arrangement not reported in pension funds or investment trust funds under which principal and income benefit individuals, private organizations, or other governments. The District offers a tax-advantaged 529 College Savings Investment Plan (named after Section 529 of the Internal Revenue Code). The Plan is designed to help families save for the higher education expenses of designated beneficiaries. This plan is reported in the Private-purpose trust fund, and was established during FY 2003. Please see Note 1-E, *Basis of Presentation – Fiduciary Funds – Private Purpose Trust Fund* on page 63.

The net assets of the pension/OPEB trust funds decreased by \$(581,389). Decreases in stock prices, and net investment income reductions are the primary reasons for the decreases. These decreases resulted from the precipitous decline in U.S. equity and non-U.S. equity markets during 2008.

Component Units

The District currently has five (5) discretely presented component units: (1) Housing Finance Agency; (2) DC Sports and Entertainment Commission; (3) University of the District of Columbia; (4) Washington Convention Center Authority; and (5) DC Water and Sewer Authority. Component units are legally separate organizations for which the District is financially accountable. Accountability exists because the Mayor, with the consent of the Council, appoints the governing bodies of all of the component units. In addition, the District has an obligation to provide financial support to the Convention Center, and the University of the District of Columbia. Certain tax revenues are dedicated to each of these organizations. The financial data of the component units are reported separately from the financial data of the primary government.

The District also has one blended component unit: 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 MD&A. Please see Exhibit 5a, *Discretely Presented Component Units – Combining Statement of Net Assets*, page 57, and Exhibit 5b, *Discretely Presented Component Units – Combining Statement of Activities*, page 58, for more detailed financial information on the component units.

Short-Term Debt

The District issues short-term debt primarily to finance seasonal cash flow needs. This need occurs due to the timing variance between the receipt of taxes, grants and other revenues and the outflow of funds for governmental operations and required disbursements. The District issued \$300,000 in Tax Revenue Anticipation Notes (TRANs) on December 12, 2007, at an interest rate of 4.00%, priced to yield 3.13%, which has been repaid. 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. The FY 2008 TRANs were repaid on September 30, 2008.

Long-Term Debt and Bond Ratings

On December 19, 2007, the District issued its Series 2007C General Obligation Bonds in the principal amount of \$333,840. The proceeds of these bonds will be used to finance capital project expenditures and to pay the costs and expenses of issuing and delivering the bonds. The 2007C bonds, together with other outstanding general obligation bonds and bonds to be issued in the future, are general obligations of the District, secured by the District's full faith and credit. These bonds are further secured by a security interest and liens on the funds derived from a Special Property Tax and are issued under Section 461 of the Home Rule Act. The 2007C bonds were issued as fixed-rate bonds with a weighted average interest rate yield of 4.47%. The maturity of the 2007C bonds is June 1, 2033.

On August 27, 2008, the District issued its Series 2008E General Obligation Bonds in the principal amount of \$327,905. The proceeds of the bonds will be used to finance capital project expenditures in the District's capital improvements program and to pay the costs and expenses of issuing and delivering the bonds. The 2008E Bonds, together with the District's outstanding general obligation bonds, are secured by the District's full faith and credit and the Special Real Property Tax, and are issued under Section 461 of the Home Rule Act. The 2008E Bonds were issued as fixed-rate bonds with a yield ranging from 2.0% to 5.02%. The maturity of the 2008E Bonds is June 1, 2033.

On May 21, 2008, the District issued \$524,280 in Series 2008A, 2008B, 2008C and 2008D General Obligation Refunding Bonds (Variable Rate Demand Obligations (VRDO)) with a weighted average interest rate yield of 4.22%, assuming a 3.5% average variable rate in the future plus LOC fees, to refund \$521,025 of outstanding, 2002A 1 and 2, 2002B 1 and 2, and 2004C 1, 2 and 3 General Obligation Bonds with weekly variable interest rates. The general obligation bonds were issued at par and after paying issuance costs of \$3,255, the net proceeds were \$521,025.

On August 27, 2008, the District issued \$151,615 in Series 2008F General Obligation Refunding Bonds with a weighted average interest rate yield of 4.48% to advance refund \$150,585 of outstanding 1998A and 1998B Bonds with an average coupon yield of 5.23%. The general obligation bonds were issued at par plus a premium of \$5,705 and after paying issuance costs of \$2,960, the net proceeds were \$154,360.

In May 2007, Moody's Investors Service upgraded the District's general obligation bond rating to "A1" from "A2 (Positive Outlook)". Standard & Poor's maintained the District's general obligation bond rating of "A+" where it has been since it was upgraded from "A" in November 2005. In May 2007, Fitch Ratings upgraded the District's bond rating from "A (Positive Outlook)" to "A+." Each time the District issues new debt, the current debt rating is reviewed for the new issuance. At that time, the bond rating agencies assess the District's financial condition, and underlying credit worthiness, and change their rating as warranted.

The significantly improved bond ratings allow the District to either refinance (refund) outstanding debt, or to issue new debt, at more favorable rates. In the past, the District's financial and operational difficulties required it to pay substantially higher interest rates on its debt. The District's financial advisors estimate that the effect of the upgrades on the District's recent general obligation bond sale was a savings of approximately 5 basis points, or \$200,000 per year. A basis point is one-percent of a percentage point of interest, or 0.01%. Lower interest rates translate into reduced debt service payments, resulting in a greater percentage of the District's budget being available for the services and operations needed for its citizens.

At September 30, 2008 the District had a total of \$5,950,794 in long-term bonds, TIF Bonds, Ballpark bonds, Qualified Zone Academy Bonds (QZAB), and Tobacco Bonds outstanding. Please refer to Table 4, *Outstanding Bonds at September 30, 2008*. This is an increase of \$435,086 over last year. General obligation bonds represent 77.2% of the District's outstanding long-term debt. TIF bonds, Ballpark bonds, and QZAB represent 10.6% and Tobacco bonds outstanding represent 12.2% of outstanding long-term debt. In FY 2006, the District issued \$534,800 in Ballpark Bonds to finance the new baseball stadium, of which \$526,415 remains outstanding, or 8.9% of the District's outstanding long-term debt. The District's borrowing has been increasing over the past few years because of the continuing need and demand for improvements in infrastructure, such as roads, streets, and bridges. (Please see *Note 8. Long-Term Liabilities*, pages 92-106 for a more detailed discussion).

The general obligation debt per capita (D.C. resident) as of September 30, 2008 was \$7,760. This represents an increase of \$717, or 10.2% over last year. The increase is due to the District's issuance of additional general obligation debt, refunding of outstanding debt, and population increases. The debt per capita figure that was given in the FY 2007 CAFR does not correspond to the figure given in this year's CAFR for FY 2007 because of adjustments in population estimates for Washington, D.C. Please refer to Exhibit S-3A, *Ratios of General Obligation Bonds Outstanding – Last Ten Fiscal Years* on page 166.

Table 4 – Outstanding Bonds at September 30, 2008

Long-Term Debt			
(\$ in 000's)			
	2008	2007	Variance
General Obligation Bonds	\$ 4,592,518	\$ 4,140,133	\$ 452,385
Ballpark Bonds	526,415	528,490	(2,075)
TIF Bonds	100,664	105,229	(4,565)
Qualified Zone Academy Bonds	6,713	4,787	1,926
Tobacco Bonds	724,484	737,069	(12,585)
Total	\$ 5,950,794	\$ 5,515,708	\$ 435,086

Capital Assets

Net capital assets of the governmental activities totaled \$7,243,637, while the net capital assets in business-type activities totaled \$16,747, for a total of \$7,260,384 net capital assets at September 30, 2008. These capital assets include, but are not limited to, land, buildings, police and fire equipment, office equipment, park facilities, roads and bridges. The governmental activities depreciation charges for the current fiscal year totaled \$272,830 compared to last year's \$260,821. The general capital improvements fund is used to account for the purchase or construction of capital assets financed by transfers, capital grants, and or debt. Please see Table 5, *Net Capital Assets*, below for more details.

Total capital assets increased by \$1,103,275 or 17.9%, over last year. This increase was made up of an increase in governmental activities capital assets of \$1,103,739 or 18.0% and a decrease in capital assets from business-type activities of \$(464), or -2.7%. Total overall capital assets are increasing because the District is investing more resources in new and existing rehabilitated infrastructure, such as roads, streets, and bridges. The cost of these assets is being funded primarily by the issuance of debt, and the use of General Fund fund balance. Please see Note 5 - *Capital Assets* for a more complete discussion of the District's capital assets, on pages 86-90.

Table 5 – Net Capital Assets as of September 30, 2008

Asset Category	Governmental Activities		Business-type Activities		Total	
	2008	2007	2008	2007	2008	2007
Land	\$ 311,388	\$ 219,920	\$ 1,264	\$ 1,264	\$ 312,652	\$ 221,184
Buildings	2,591,551	1,679,673	13,061	13,402	2,604,612	1,693,075
Infrastructure	2,020,490	1,884,395	-	-	2,020,490	1,884,395
Equipment	486,163	503,148	2,422	2,545	488,585	505,693
Construction in progress	1,834,045	1,852,762	-	-	1,834,045	1,852,762
Total net capital assets	\$ 7,243,637	\$ 6,139,898	\$ 16,747	\$ 17,211	\$ 7,260,384	\$ 6,157,109

REPORTING THE DISTRICT'S BUDGET

The District's budget is subject to revision and/or veto by the United States Congress and the President of the United States. As the budget moves through the federal budgetary process, there may be changes in both the amounts and the purposes. In addition, when the District's CFO prepares revised revenue estimates, the budget submission must be adjusted to conform to those revisions. During the Congressional review of the FY 2008 budget, the CFO's revised estimates caused the District to revise its budget submission, before the budget was finally approved. Both federal and District laws require that the District present a balanced budget.

General Fund Budget

The original formulation of the General Fund budget estimated total revenues and other sources at \$6,325,114 and total expenditures and other uses at \$6,323,656. The revised General Fund budget, resulted in estimated total revenues and other sources of \$ 6,570,921 and total expenditures and other uses of \$6,557,782, resulting in a projected budgetary surplus of \$13,139 . See Table 6, *Fiscal Year 2008 – General Fund Budgetary Highlights*.

Table 6 - Fiscal Year 2008 General Fund Budgetary Highlights

	Budget		Actual	Variance with
	Original	Revised		Revised Budget
Revenues and Other Sources:				
Property taxes	\$ 1,656,002	\$ 1,756,694	\$ 1,726,005	\$ (30,689)
Other taxes	3,339,498	3,333,396	3,380,958	47,562
Charges for services	332,361	338,546	385,856	47,310
Other sources (O type)	496,804	510,542	448,972	(61,570)
All other sources	500,449	631,743	568,983	(62,760)
Total revenues and other sources	6,325,114	6,570,921	6,510,774	(60,147)
Expenditures and Other Uses:				
Governmental direction and support	387,643	403,947	382,071	21,876
Economic development and regulation	441,141	520,106	438,769	81,337
Public safety and justice	1,036,664	1,055,862	1,044,463	11,399
Public education system	1,306,621	1,370,411	1,355,633	14,778
AY08 public education expenditures	-	91,829	91,829	-
Human support services	1,573,805	1,572,877	1,606,979	(34,102)
Public works	573,069	581,827	563,777	18,050
Other	1,004,713	960,923	835,883	125,040
Total expenditures and other uses	6,323,656	6,557,782	6,319,404	238,378
Excess -- budgetary basis	\$ 1,458	\$ 13,139	\$ 191,370	\$ 178,231

General Fund Budgetary Highlights – Original to Revised Budget

After the original budget has been submitted to the D.C. Council, the Chief Financial Officer updates the District's revenue estimates in June. The District then makes adjustments necessary to bring the expenditure budget into agreement with the revised revenue budget, which account for the differences between the Original General Fund budget and the Revised General Fund budget. Total estimated revenues were increased by \$245,807 and total estimated expenditures were increased by \$234,126. The projected General Fund budgetary basis surplus was increased from \$1,458 to \$13,139, as a result of the revisions. The major changes in the budget are summarized as follows:

Revenues and sources increased by a total of \$245,807

- Property taxes were increased by \$100,692.
- Other Taxes were decreased by \$(6,102).
- Charges for Services increased by \$6,185.
- Other sources (O Type) were increased by \$13,738.
- All other sources were increased by \$131,294.

Expenditures and uses increased by a total of \$234,126

- Government direction and support was increased by \$16,304.
- Economic Development and regulation expenditures were increased by \$78,965.
- Public safety and justice expenditures were increased by \$19,198.
- Public Education System expenditures were increased by \$63,790.
- The advance of Appropriation Year 2008 budget in the amount of \$91,829. for public education expenditures to ready the Charter and public schools for the new school year, which began prior to the District's fiscal year.
- Human support services expenditures were decreased by \$(928).
- Public works expenditures were increased by \$8,758.
- Other expenditures were decreased by \$(43,790).

Variance Explanations

A variance can be defined as “*the difference between one thing and another.*” In this CAFR, variances are discussed and explanations are provided on the differences between the following: (1) the FY 2008 Original Budget and the FY 2008 Revised Budget; (2) the FY 2008 Revised Budget to the FY 2008 Actual Results, and; (3) the FY 2007 Actual Results to the FY 2008 Actual Results. The variance amounts are given for major categories, such as Property Tax, or for groupings of agencies, such as Government Direction and Support. In the case of Property Tax, there are no sub categories explained, but under Government Direction and Support, there are 23 categories, including agencies or accounts. The District is required to explain the reasons for the major revenue and agency grouping variances, but not for every agency or program variance, unless they are considered to be important. The primary reasons for these variances are explained in the following section.

FY 2008 Original Revenue Budget to FY 2008 Revised Revenue Budget

The \$101 million (6%) increase in the revenue estimate for **real property tax** between the original and revised budget reflects adjustments that were made to the real property tax estimate based on an updated real property tax database that was only available after the original estimate was made. The increase in the estimate was mainly due to new construction.

The revenue estimate for the **general sales and use tax** was revised downwards by about \$20 million (2%) as data on cash collections throughout the period between the original and revised estimate showed sales tax collections, reflecting the general slowdown in both the national and Washington, D.C. economies.

The revenue estimate for the **individual income tax** was adjusted upward by \$61 million (5%) as data on revenue collections in the period between the original and revised estimates showed stronger than forecasted growth in non-withholding collections.

The revenue estimate for the **unincorporated business tax (UB)** was revised downward by \$43 million (23%) as the real estate market deteriorated sharply in the period between the original and revised estimate (the bulk of the revenue from the unincorporated business tax comes from the real estate sector) and UB cash collections fell sharply.

The revenue estimate for **deed recordation tax** was lowered by a total of \$67 million (35%) as a review of cash collections data showed that the financial crisis and the resulting credit squeeze was causing a sharp slowing in the D.C. real estate market.

The revenue estimate for the **estate tax** was increased by \$34 million (108%) between the original and revised estimate as data on cash collections at the time of the revised estimate showed that revenue collections from this source was much stronger than anticipated. Revenue from estate tax is notoriously volatile because revenue flows depend on the number of deaths of persons with taxable estate in Washington, D.C. as well as the value of estates, which in turn is tied to the real estate market and the volatile financial market.

The revenue estimate for the **economic interests tax** was increased by \$46 million (575%) between the original and revised estimate to be consistent with the much stronger than anticipated collections from this source after reviewing cash collections report data. Like the estate tax, receipts from the economic interests tax are very volatile because it depends on volume and value of transactions in the very volatile portfolio real estate investment markets (also known as real estate investment trusts or REITs).

FY 2008 Original Expenditure Budget to FY 2008 Revised Expenditure Budget

The \$16,304 increase for governmental direction and support was caused primarily by \$10,000 which was added for Section 103 Judgments. The District settled a lawsuit for \$10,000, in regards to a proposed development of the Children's Island site, near to the RFK Stadium, in the Anacostia River.

The increase of \$78,965 for Economic Development & Regulation was almost entirely caused by: (1) a \$44,099 increase for the Department of Employment Services (DOES), and; (2) a \$30,000 increase for the Housing Production Trust Fund Subsidy (HPTFS). The DOES increase was primarily caused by two items: (1) a \$18,776 increase in the Contingency Cash Reserve, and; (2) a \$10,000 reprogramming for the Summer Youth Program. The \$30,000 HPTFS increase was entirely attributable to a supplemental appropriation of One-Time FY 2008 revenues.

The \$19,198 increase for Public Safety & Justice came from three primary agencies: (1) \$10,564 for Fire and Emergency Medical Services; (2) \$5,277 for the Metropolitan Police Department, and; (3) \$4,069 for the Office of Victim Services.

The \$63,790 increase for the Public Education System was composed primarily of four major changes: (1) a \$(88,092) decrease for Public Charter Schools (PCC); (2) an increase of \$70,515 for the D.C. Public Schools (DCPS); (3) an increase of \$46,994 for the Office of State Superintendent for Education (OSSE), and; (4) an increase of \$29,118 for the Office of Public Education Facilities Modernization (OPEFM). The \$70,515 increase for DCPS was caused primarily by two items: (1) a \$25,088 increase for the workforce investment allocation, and; (2) a \$23,700 increase for current facilities inefficiencies. The \$46,994 OSSE increase was caused primarily by four factors: (1) the \$41,142 transfer of the Early Care and Education Administration from the Department of Human Services to OSSE; (2) the Blackman Jones carry over of \$11,160; (3) the Blackman Jones carry forward of \$(17,756), and; (4) the increase of \$9,600 by moving budget authority from FY 2007 to FY 2008. The OPEFM increase of \$29,118 was caused almost entirely by the \$26,018 transfer of all assets, personnel and funding associated with the maintenance of DCPS facilities, as required under the School Modernization Use of Funds Requirements Emergency Amendment Act of 2007, and the FY 2008 Supplemental Appropriations Emergency Act of 2007.

The \$91,829 increase for AY 2009 Advance for Public Education represents the expenditure of the appropriations for AY 2009 in FY 2008. The FY 2007 D.C. Appropriations Act requires that the advance appropriations be provided on July 1, 2008, based on 10% and 25% of the FY 2009 Proposed Budgets for the D.C. Public Schools (DCPS) and the D.C. Public Charter Schools (DCCS), respectively. When Congress approves the District's budget for the current fiscal year, it does not know the proposed funding level for the next fiscal year. As such, the advance appropriations are not included in the District's Original Budget. The advance appropriations are not known until July 1, and are then made a part of the District's Revised Budget. This figure is composed of: (1) \$88,215 for the AY09 Public Charter School Advance Appropriation and; (2) \$3,614 for the AY09 Public School Advance Appropriations. In prior years, the entire AY School Advance Appropriations went to DCPS. This year, the majority of this funding went to DCCS, and DCPS received a small portion of the funding.

Human Support Services was reduced by \$(928), which was caused primarily by: (1) a decrease of \$(39,566) for the Department of Human Development (DHD), which was offset by; (2) an increase of \$17,179 for the Department of Health; (3) an increase of \$7,418 for Child and Family Services, and; (4) an increase of \$6,781 for the Children Investment Trust. The decrease for DHD was caused by the \$(41,142) transfer of the Early Care and Education Administration from the Department of Human Services to OSSE.

The \$8,758 increase for Public Works was primarily the result of an increase of \$8,042 for the Department of Transportation.

The \$(43,790) decrease for Other was caused by: (1) an increase of \$32,585 for Pay-Go Capital; (2) a \$(19,155) decrease for Repayment of Loans and Interest; (3) a \$(16,659) decrease for Non-Departmental; (4) a \$(13,475) decrease in the Cash Reserve; (5) a \$(10,784) decrease in Equipment Lease Operating; (6) a \$(9,117) decrease in Workforce Investments, and; (7) a decrease of \$(5,485) in Repayment of Interest on Short-Term Borrowing. Most of the amounts that make up these items were small to moderate, and, therefore, there were no major factors which accounted for these differences.

FY 2008 Revised Revenue Budget to FY 2008 Actual Revenue

Actual revenues and other sources were \$(60,147) less than the revised budget. The primary reasons for these changes from the revised FY 2008 budget to the actual FY 2008 results are explained in the following section.

The negative variance of \$13 million (-1%), for the **individual income tax**, is well within the standard 5% deviation. This variance is explained mainly by slower than anticipated growth in the withholding tax. This was offset somewhat by much slower than expected growth in refunds. The withholding tax comprises about 75% of the individual income tax, while refunds comprise just 17%. The slower than expected growth in the withholding tax therefore overwhelms any better than expected growth in the other components.

The large positive variance of \$31.0 million (12%) of actual over budget for the FY 2008 **corporate franchise tax** revenue is mainly due to significantly lower refunds than the previous year. An analysis of the corporate franchise tax by components shows that while estimated payments and final payments grew roughly 4%, refunds fell sharply by 46%. An examination of corporate franchise tax refunds for the past 9-years shows that the FY 2007 level of \$53 million was unusually high compared to FY 2008.

The large negative variance of \$18 million (12%) for the **unincorporated business (UB) tax** to a large extent reflects the downturn of the real estate market because the UB tax is collected primarily from real estate businesses in the District. UB tax collections fell sharply in FY 2008 with the slowdown in the real estate market, a slowdown which was exacerbated by the financial crisis as the credit market for real estate dried up.

The positive variance of \$25 million (16%) for **public utilities** and \$9 million (16%) for **toll telecommunications** are higher than the variances for these taxes in past years. The variance for the toll telecommunications tax is almost certainly related to the exceptionally strong growth in the telecommunications sector, particularly the growth in revenue from data services (email, text messaging, and internet) with the deployment in recent years of mobile technologies such as smart phones. A possible explanation for the public utilities variance is that, as the price for gasoline grew, many people spent more time at home, using higher amounts of electricity and natural gas to light, heat and to cool their homes. But the stronger than expected performance could also be coming from new construction and growth in the Washington, D.C. population in recent years.

The positive variance of \$32 million (26%) for the **deed recordation tax** and \$12 million (11%) for the **deed transfer tax** reflect a very conservative estimate in the September revision of the revenue estimate after a marked deterioration in deed taxes collections over the summer. A conservative estimate seemed prudent given the uncertainty of revenue from real estate transactions amid a general slowdown in the real estate markets. The economic data at the time showed lower prices and a sharply lower volume of sales with no signs of an immediate turnaround.

FY 2008 Revised Expenditure Budget to Actual Expenditure

Total expenditures and other uses were \$(238,378) less than the revised budget of \$6,557,782. The term positive variance, when used for expenditures, means that less money was spent than was budgeted, resulting in more money left for other purposes, or a surplus, at the end of the fiscal year. Conversely, the term negative variance, when used for expenditures, means that more money was spent than was budgeted, resulting in less money for other purposes, or, potentially, a deficit at the end of the fiscal year. The primary reasons for these changes are explained in the following section.

Three agencies primarily accounted for the positive variance of \$81,337 for Economic Development and Regulation: (1) a \$40,520 variance for the Office of the Deputy Mayor for Planning and Economic Development (DMPED); (2) a \$12,884 variance for the Department of Housing and Community Development (DHCD), and; (3) a \$10,378 variance for the Department of Employment Services (DOES). The DMPED variance was the result of new economic development programs that were initiated by the District as a result of consolidating the operations of the National Capital Revitalization Corporation (NCRC) and the Anacostia Waterfront Corporation (AWC) into DMPED.

DMPED had a \$32.5 million excess in unspent budget authority for possible sales dispositions that did not materialize. Three major factors contributed to the \$12,884 variance for DHCD; policy restrictions on spending, reductions in revenue collections, and the repayment of Housing Purchase Assistance Program (HPAP) loans. In FY 2008, no funds were expended from the Land Acquisition and Housing Development Organization, Rehab Repay and Home Again programs. Regulations for these programs restricted how the funds could be used. Unspent funds in these three programs total \$6,072, or 47% of the variance. The \$10,378 variance for DOES was mainly the result of \$4,300 associated with delaying updates to

both the Unemployment Insurance and Workers Compensation information systems until FY 2009, and \$2,600 for vacant position salary lapses in the Workers Compensation and Unemployment Programs.

The negative \$(34,102) variance for Human Support Services (HSS) was caused partly by a Child and Family Services Administration (CFSA) increase in the Medicaid disallowance and receivable write-off of \$82.9 million for FY 2004 – FY 2008. The remaining balance is due to increased costs for services to children in CFSA care. This was offset by a \$34,671 reduction for the Department of Health (DOH). There were two main factors for the DOH variance: (1) \$35,585 in subsidies and transfers were not spent, and; (2) a \$26,293 write-off to local expenditures. The remaining difference is made up of a number of much smaller variances.

The positive variance in the Other category of \$125,040 was primarily the result of \$43,784 less being spent for Bond Fiscal Charges Paid From Bond Proceeds, and \$36,525 that was budgeted for the Cash Reserve that was not used for that purpose.

FY 2007 Actual Revenue to FY 2008 Actual Revenue

In FY 2008 Total Actual Revenues and Other Sources of \$6,510,774 increased by \$723,623 from the FY 2007 Total Actual Revenues and Other Sources of \$5,787,151. The primary reasons for this increase are explained below:

The \$225 million (15%) FY 2008 increase in **real property tax** over the previous year reflects primarily a run up in the commercial real property tax market over the last several years. Although the commercial real estate market has since slowed from its 2005 peak, FY 2008 real property tax revenue is based on price appreciation that occurred in calendar year 2006, before the general real estate slowdown.

Sales and use tax collections were \$1,015,182 in FY 2008 and \$959,968 in FY 2007, an increase of \$55 million, or 6%. However, dedicated transfers from the sales and use tax also rose to \$22 million over last year, resulting in an increase of net collections of \$35 million. Because of the general economic slowdown and lower consumer spending for 2008, the growth in sales tax for FY 2008 over FY 2007 is less than the robust growth of the previous year when it grew about 9%.

The \$29 million (2%) growth in the FY 2008 **individual income tax** revenue over the previous year was slightly less than the forecasted growth of 3%. This slower than expected growth of individual income tax revenue was mainly due to slower than anticipated growth in withholding tax. This was offset somewhat by much slower than expected growth in refunds. The withholding tax comprises about 75% of the individual income tax, whereas refunds comprise just 17%. The slower than expected growth in the withholding therefore overwhelms any better than expected growth in the other components.

The relatively strong growth of \$31 million (12%) in the FY 2008 **corporate franchise tax** revenue over the previous year is mainly due to significantly lower refunds than the previous year. An analysis of the corporate franchise tax by components shows that while estimated payments and final payments grew roughly 4%, refunds fell sharply by 46%. An examination of corporate franchise tax refunds for the past 9-years shows that the FY 2007 level of \$53 million was unusually high and the FY 2008 level is more normal.

The FY 2008 revenue for the **unincorporated business (UB) tax** fell \$40 million (24%) over the previous year. The UB tax is collected primarily from real estate businesses in the District and to a large extent reflects the fortunes of the real estate market. Consequently, UB tax collections have fallen sharply with the recent slowdown in the real estate market, a slowdown which has been exacerbated by the financial crisis as credit for real estate dried up.

The FY 2008 growth of \$25 million (16%) over FY 2007 for the **public utility gross receipts tax** is much stronger than expected and much stronger than the relatively flat growth of previous years. A possible explanation for the public utilities variance is that, as the price for gasoline grew, many people spent more time at home, using higher amounts of electricity and natural gas to light, heat and to cool their homes. But the stronger than expected performance could be coming from new construction and a return to growth in the Washington, D.C. population in recent years.

The \$71 million (31%) decline in FY 2008 revenue over the previous year for the **deed recordation tax** and a \$40 million (26%) decline for the **deed transfer tax** reflect the general slowdown in the real estate markets, both in lower prices and sharply lower volume of sales.

FY 2007 Actual Expenditures to FY 2008 Actual Expenditures Variances

Government Direction and Support increased by \$15,813 over the previous year. The primary causes for this increase were: (1) a \$25,920 increase for the Office of the Chief Technology Officer (OCTO); (2) a \$10,000 increase for Section 103 Settlements, for the Children's Island development case, and; (3) the \$(11,128) decrease for the Deputy Mayor's Office/City Administrator. OCTO's \$25,920 increase was caused almost entirely by an increase of approximately \$25 million for an additional 111 full-time equivalent employees (FTEs) and for operating costs of capital projects that came online in various activities throughout the agency.

Economic Development and Regulation increased by \$58,146 over the previous year. The major causes for this increase were: (1) an increase of \$41,739 for the Department of Employment Services (DOES); (2) a decrease of \$(34,822) for the Housing Production Trust Fund Subsidy (HPTFS); (3) an increase of \$28,313 for the Office of the Deputy Mayor for Planning and Economic Development (DMPED), and; (4) an increase of \$13,896 for the Department of Housing and Community Development (DHCD). The \$41,739 increase for DOES was caused primarily by a \$29,400 increase for the Summer Youth Employment Program (SYEP) and a \$6,600 increase for the Transitional Employment Program (TEP), both of which were driven by an expansion of participants, 18,091 for SYEP and 784 for TEP.

The \$28,313 increase for DMPED was mostly the result of new economic development programs that were initiated by the District as a result of consolidating the operations of the National Capital Revitalization Corporation (NCRC) and the Anacostia Waterfront Corporation (AWC) into DMPED. This accounted for \$16,500 of the variance. In addition, there was an \$8,200 increase in grants awarded to the Neighborhood Investment Fund (NIF), which is used to finance economic development and neighborhood revitalization in twelve targeted areas of the District to include target area grants, predevelopment grants and land acquisition loans. There was also an \$8,300 increase in expenditures related to the Business Improvement District (BID) program. BID activity is used as an economic tool to support economic growth and diversity in the downtown areas. The DHCD variance of \$13,896 was caused almost entirely by an expenditure increase of \$11,434 attributable to the Housing Purchase Assistance Program (HPAP). HPAP expenditures provide closing assistance and down payment support to qualified homebuyers.

Public Safety & Justice increased by \$83,034 over the previous year. The major reasons for this increase were: (1) an increase of \$39,477 for the Metropolitan Police Department (MPD); (2) an increase of \$15,826 for Fire and Emergency Medical Services (FEMS); (3) an increase of \$9,165 for the Office of Victim Services (OVS) and; (4) an increase of \$8,514 for the Office of Unified Communications. The \$39,477 variance for MPD was caused almost entirely by two factors; (1) a \$26.3 million increase due to an increase of 406 Full-Time Equivalent Employees, along with annual pay raises, step increases and overtime, and; an \$11 million increase due mainly to the increase in fixed costs for rent and security.

The \$15,826 increase for FEMS was caused primarily by \$12.5 million in pay raises and step increases for 2,072 employees. The \$9,165 increase for OVS was due to its being created as a new agency in FY 2008. OVS was created in order to establish budget authority over accrued interest for program funds that had been previously going into the General Fund. The programs in OVS were transferred out of the Office of the City Administrator.

The FY 2008 increase of \$200,004 in expenditures for the Public Education System was caused primarily by: (1) an increase of \$88,566 for the State Education Office (OSSE); (2) a \$50,856 increase for the D.C. Public Schools (DCPS); (3) a \$33,700 increase for the Office of Public Education Facilities Modernization (OPEFM), and; (4) \$28,295 increase for Public Charter Schools. The OSSE variance of \$88,566 was entirely attributable to the creation of OSSE, which took over operational responsibility for state education functions from DCPS and the University of the District of Columbia. OSSE also assumed additional responsibilities from the Department of Human Services with the acquisition of the Early Care and Education Administration (ECEA).

The \$33,700 increase for OPEFM was due to the fact that it was created during FY 2007, with a budget of \$2,569. FY 2008 was the first full year of operation for OPEFM, and during the year, \$26,018 in funds was reprogrammed from the DCPS to OPEFM. In June 2008, the District provided OPEFM with an additional \$3,100 in supplemental appropriations. The \$33,700 increase in actual expenditures from FY 2007 to FY 2008 was the result of facilities maintenance activities that were transferred from DCPS to OPEFM in FY 2008.

The increase of \$94,277 in FY 2008 expenditures for Human Support Services was caused primarily by: (1) an increase of \$93,477 for Child and Family Services Administration (CFSA); (2) an increase of \$85,976 for the Department on Disability Services, and; (3) a decrease of \$(135,311) for the Department of Human Services (DHS). The Department on Disability Services (DDS) was established as a new agency in FY 2008. Expenditures of \$92 million were transferred from the DHS

Mental Retardation and Developmental Disabilities Administration (MRDDA) and the Rehabilitation Services Administration (RSA) to DDS. DHS also transferred the Early Childhood Education Administration (ECEA) and \$45 million to the Office of the State Superintendent of Education (OSSE). CFSA's increase was primarily due to the increase in the grant disallowance and receivable write-off of approximately \$80.5 million during the FY 2008 closing. The grant disallowance and receivable write-off is the result of the findings from the Medicaid cost report audit for FYs 2004 and 2005 for the agency in the execution of its targeted case management and cost rehabilitative option claiming. The remaining balance is due to increased costs for services to children in CFSA care.

The Public Works expenditure increase of \$133,806 was caused primarily by: (1) an \$89,424 increase for the District Department of Transportation (DDOT); (2) a \$16,412 increase for Mass Transit Subsidies and; (3) an increase of \$15,634 for the Department of Public Works (DPW). The DDOT increase of \$89,424 was due to an increase of \$76.9 million in Special Purpose Funds to implement the new DOT Unified Fund; \$8 million in Local Funds for construction projects; \$2.7 million Federal Highway Administration and \$1.9 million for information technology. The \$16,412 increase for Mass Transit Subsidies was due to a Washington Metropolitan Area Transit Authority increase in the base subsidy requirement. The \$15,634 increase for DPW was a result of a number of different facts, the largest of which was \$6.3 million for increased salary, wages and step increases and overtime.

The Other Uses increase of \$221,245 was caused primarily by: (1) an increase of \$106,207 for the District Retiree Health Contribution; (2) an increase of \$34,582 for Repayment of Loans and Interest, and; (3) an increase of \$21,876 for Pay-Go Capital.

SUBSEQUENT EVENTS

Short-Term Debt

The District issues short-term debt to finance seasonal cash flow needs. This need occurs due to the timing variance between receipts of taxes, grants and other revenues and the outflow of funds for governmental operations and other required disbursements. On December 2, 2008, the District issued fixed-rate Tax Revenue Anticipation Notes in the aggregate amount of \$400,000. These Notes were issued at an interest rate of 2.50% and priced to yield 1.09%, and are to be paid off on September 30, 2009. By law, the District must repay any short-term debt in its entirety by September 30 of the fiscal year of issuance.

Inauguration Emergency Funding

The federal government announced on January 13, 2009 that it will grant emergency funding to the District to help with soaring costs for the January 20, 2009 inauguration of President-elect Barack Obama. The District requested additional funds, due to the estimates of 1.5 million to 2 million people that were expected to attend, with the resulting increase in expenditures for public safety, transportation, and security related measures. The District estimated that its costs for the events will total more than \$47 million, approximately three times as much as the \$15 million that was originally appropriated for the inauguration. President Bush declared that an "*emergency exists in the District of Columbia*" and that the District would receive the federal money for protective measures "*undertaken to save lives and protect public health and safety.*"

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 show the District's 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 Office of the Chief Financial Officer
The John A. Wilson Building
1350 Pennsylvania Avenue, N.W., Suite 209
Washington, D.C. 20004
(202) 727-2476
www.dccfo.com