

PUBLIC OVERSIGHT HEARING ON
THE FY 2006 AND FY 2007 SPENDING AND
PERFORMANCE OF THE OFFICE OF THE CHIEF
FINANCIAL OFFICER (OCFO)

Before the
Committee on Finance & Revenue
Council of the District of Columbia

The Honorable Jack Evans, Chairman

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



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

Good morning, Chairman Evans and members of the Committee on Finance and Revenue. I am Natwar M. Gandhi, Chief Financial Officer of the District of Columbia government. I am here for your annual budget hearing to testify on the FY 2006 performance and FY 2007 plans of the Office of the Chief Financial Officer (OCFO).

All of my deputy chief financial officers are with me today to help address specific issues or answer questions as needed: Sherryl Hobbs-Newman, deputy CFO for the Office of Tax and Revenue (OTR); Bob Ebel, deputy CFO for the Office of Revenue Analysis (ORA); Lasana Mack, deputy CFO for the Office of Finance and Treasury (OFT); Tony Pompa, deputy CFO for the Office of Financial Operations and Systems (OFOS); and Bert Molina, deputy CFO for the Office of Budget and Planning (OBP). In addition, Jeanette Michael, executive director of the DC Lottery, has testified today on behalf of the Lottery.

OCFO HISTORY SINCE 1995

From junk bond status to A+ bond ratings, from a half a billion dollar fund balance deficit to a billion and a half dollar surplus, the District's financial recovery in less than a decade has been phenomenal. Since 2000 when I assumed the role of Chief Financial Officer for the District of Columbia, with Mayoral guidance and Council oversight, we have transformed the OCFO into one of the most efficient and best-performing agencies of the District government. In that time, our team of experienced and highly professional public administrators has:

- Developed new tax compliance initiatives that have generated millions of dollars in previously uncollected tax revenues – an amazing \$2 billion more in FY 2006 than in FY 1997;
- Integrated into the fabric of the District government highly sophisticated financial systems that have generated operational efficiencies, accountability, and transparency (i.e., CFO\$ource, Dashboard, SOAR, etc.);
- Achieved historic bond ratings from all three rating agencies, thereby reducing the District’s borrowing costs; and
- Aggressively sought ways to save taxpayer dollars through cutting edge finance and investment techniques (i.e., tobacco securitization).

We are committed to enhancing the fiscal and financial stability, accountability and integrity of the Government of the District of Columbia with the residents of Washington, D.C., our federal partners, and the financial markets of this nation.

As we assess the financial management infrastructure of the District, it is clear that the rebuilding of this infrastructure is virtually complete, and it functions well in support of the District’s elected leaders, who demonstrate a strong commitment to maintaining fiscal balance. See Attachment 1 for an organizational chart of the entire OCFO.

We have enjoyed 10 consecutive balanced budgets with an equal number of clean audit opinions. We have a fund balance and cash reserves that are a far cry from the mid-1990s, remarkably improved bond ratings and well-deserved respect in the financial markets. Our annual audit process, which once was deeply flawed and problematic, is now routine with little concern over its timely issuance or whether the District will receive a clean audit opinion. All of this shows that we, as a

jurisdiction, can manage our financial operations well and also take care of emergencies as they arise. Attachment 2 depicts this history in terms of annual surpluses, cumulative fund balances, and bond ratings.

We also take very seriously our responsibility to operate within budgets that comprise the minimum resources necessary to protect the District's financial integrity and preserve and enhance its revenue stream. We seek to maximize gains from technology investments, upgrading of staff skills and organizational improvements as the primary means to address our ever increasing workload. We are currently operating under an approved FY 2007 budget that has 1,060 FTEs, an increase of 62 FTEs from last year, 57 of which are solely dedicated to revenue generating activities within OTR. (The other 5 FTEs relate to the conversion of contract IT staff to District staff.) As a result of streamlining throughout the OCFO, we have been able to add more than 100 revenue generating and compliance FTEs during the past three years and still operate with an FTE total that is less than in FY 2000. The 57 FTEs added in FY 2007 are on track to raise a total of \$249 million in FY 2007–2010 (\$49 million in FY 2007, \$70 million in FY 2008, \$66 million in FY 2009, and \$64 million in FY 2010), at a cost of \$21.5 million during those four years – a ratio of revenues to expenses of almost 12 to 1 during the four-year period.

As you review the performance of the OCFO, we ask the committee to keep this record of fiscal prudence in mind. It is imperative that the District maintains its capability to perform core financial functions: keeping track of the books, financing its operations and collecting revenue due the District. One does not have to go back many years to find a time when we were doing poorly on all of these critical functions.

OCFO OVERARCHING GOALS

As the Chief Financial Officer, my objective is to preserve and enhance the overall financial stability of the District in the short- as well as long-term. My colleagues and I are busy working on this at all times, in activities such as estimating reliable revenues, exercising control of the budget, improving relationships with the financial community, and dealing with Congress.

As we work to further strengthen the District's financial viability, we keep five key goals in mind in formulating our budgets. In all instances, it is our intent to present to this committee, the Mayor and the Council the minimum OCFO resource request consistent with attaining these goals. In each case, I believe the achievement of these goals is absolutely necessary to maintain and increase the District's financial independence. These goals are:

1. Produce Reliable Revenue Estimates

Reliable and timely revenue estimates and fiscal impact statements are critical to the legislative process and building budgets that are realistic. For FY 2006, several re-estimates were issued as the District's economy grew stronger than the original forecast anticipated. The stronger than expected performance of the District's economy was reflected in successive revisions to the revenue estimates. As a result, we anticipated higher fund balances at the end of FY 2006, some of which was appropriated for use in the development of the FY 2007 budget. The higher revenue estimates reported throughout FY 2006 also triggered tax cuts and additional expenditures for FY 2007.

As I have said on many occasions, the District's revenue estimates must be realistically conservative as a matter of both necessity and good financial management. Conservative estimates are at the heart of a balanced budget and adequate cash flow, and the District must end every fiscal year with a balanced budget. As I said in my testimony on the FY 2006 CAFR, the District has revenue sources typically used by states as well as cities. Individual income taxes and the general sales taxes – combined, 43 percent of the total – are particularly sensitive to economic and external effects and, thus, make District's tax revenues volatile. In contrast, cities typically derive 40 to 50 percent of their revenues from the stable property tax, which in the District accounts for only 27 percent. Attachment 3 shows the volatility of the District's tax collections.

Sound financial management also requires a realistic assessment of the costs of achieving the Mayor's and Council's policy goals. To that end, during FY 2006, fiscal impact statements were prepared for 235 bills considered by the Council of the District of Columbia.

2. Assure Balanced Budgets

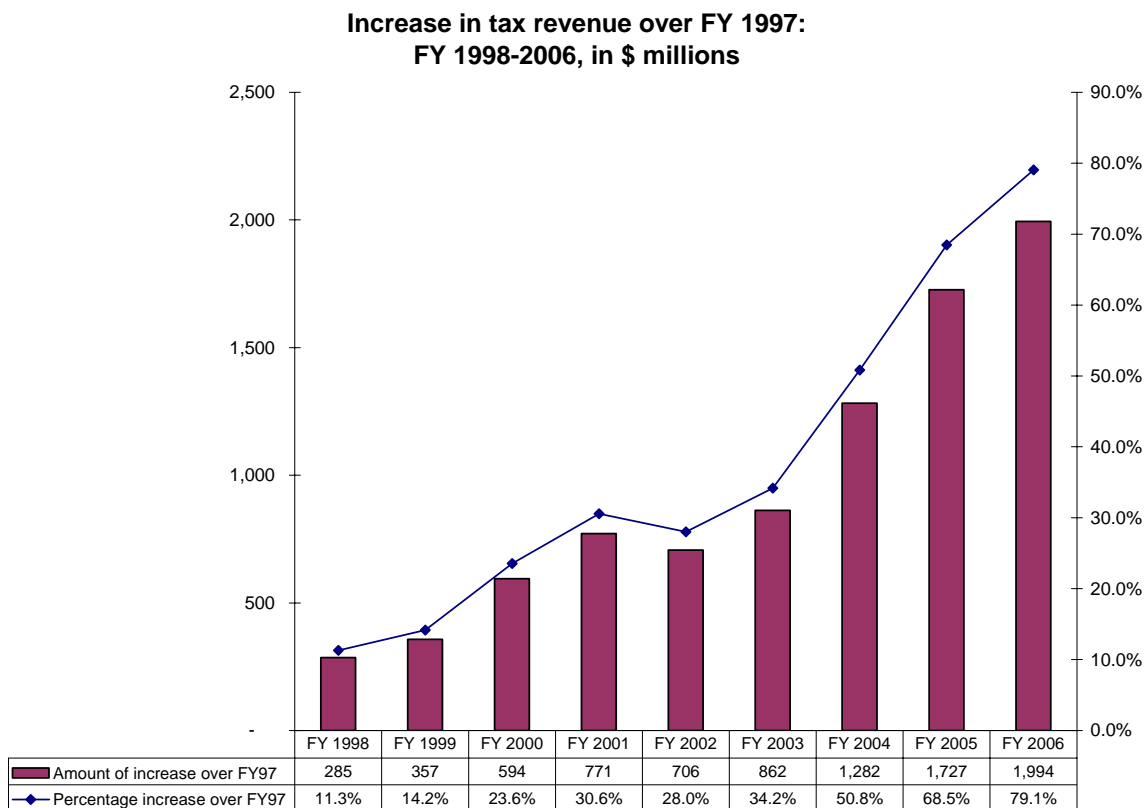
Budgets built on quality analysis that include all foreseeable costs ensure the smooth execution of programs approved by the Mayor and Council. Online monitoring of expenses helps control costs and spots operations that are off-course. During the past few years, we have built capacity in this program area, and I believe the District is now being better served as a result.

3. Protect and Enhance District Revenues

OTR must efficiently process all tax returns voluntarily remitted, and must aggressively pursue enforcement action to both increase revenue and reduce the

rate of noncompliance each year. Every year since 1997, OTR has significantly increased revenue collections – both those voluntarily remitted and those collected as a result of enforcement action.

Of the \$5.2 billion in local source revenue reported to the General Fund in FY 2006, OTR total tax collections equaled about \$4.5 billion, a 6.3 percent increase from FY 2005. The increase was attributed, in part, to increased real property, sales and use, and income tax collections. To put this in perspective, this amount is about \$2 billion more than in FY 1997, when collections were \$2.5 billion.



Revenues collected as a result of enforcement actions more than tripled, from \$26 million in 1997 to \$93 million in FY 2006. As a result of your investments in additional staff and process improvements, productivity in the compliance area

increased 16% between FY 2005 and 2006, a return on investment of more than 3 to 1. OTR has collected \$48.6 million to date for FY 2007 through enforcement activity, of which more than \$17.5 million is attributable to the revenue initiatives.

4. Maintain Financial Controls and Safeguard Assets

Throughout the OCFO, we have the goal of protecting District assets. This requires the maintenance of internal checks and balances, effective internal audits, and the maintenance of systems to record and check financial transactions. During FY 2006, the District's assets were effectively safeguarded, transacted, managed, and invested in accordance with governing law and in accordance with efficient, professional and state-of-the-art financial management practices and standards.

5. Prepare Audited Comprehensive Annual Financial Reports (CAFRs)

Our ability to record financial transactions timely and accurately is critical to our ability to produce audited financial statements on time and maintain and improve the District's bond ratings. Formal activities for the annual fiscal year closing process begin on October 1 and culminate with the issuance of the CAFR prior to the February 1 deadline. This year, like many recent years, the closing process was uneventful in that there were no "surprises" and nothing even remotely threatened the schedule or calendar. This is due in large part to the philosophy that we have regarding the CAFR or closing exercise – it is a 365-days-a-year process. Through "lessons learned" assessments, monthly and quarterly closings, training, Accounting System Manager assignments, closing workshops, and variance analyses, the closing period has become routine.

DISTRICTWIDE OCFO

The OCFO's goals are met not only by the five deputy CFOs with me today, who lead the central offices, but also by the districtwide OCFO staff. The DC Lottery and Charitable Games Control Board is an independent agency; however, because of the significant revenue it generates, it falls under the auspices of the CFO. Their administrative functions (i.e., procurement, personnel, security), as well as their financial management, are centrally coordinated within the OCFO.

Additionally, associate chief financial officers (ACFOs) represent the major appropriation titles in the District's annual budget and manage agency financial operations. ACFOs serve as the OCFO's key representatives to the city administrator, deputy mayors, and agency directors in managing the city's finances and the government's programmatic priorities. ACFOs manage the following financial clusters: Economic Development and Regulation, Government Operations, Government Services, Human Support Services, and Public Safety and Justice.

Additionally, agency chief financial officers for the following independent agencies legally report to the District CFO:

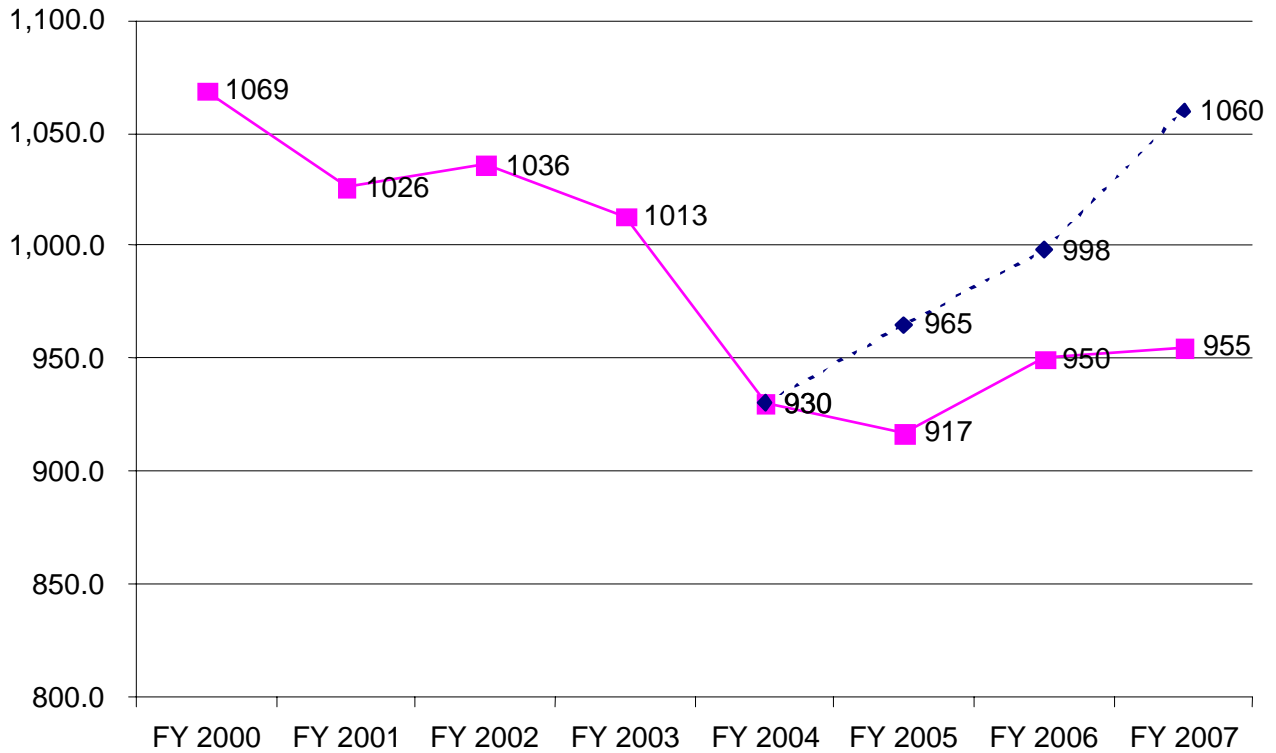
- Anacostia Waterfront Corporation
- National Capital Revitalization Corporation
- DC Public Schools
- DC Sports and Entertainment Commission
- University of the District of Columbia
- Washington Convention Center Authority
- DC Water and Sewer Authority

MULTI-YEAR CHANGE IN NUMBER OF FTEs IN CENTRAL OCFO AND DISTRICT-WIDE

Downward Trend in Central OCFO

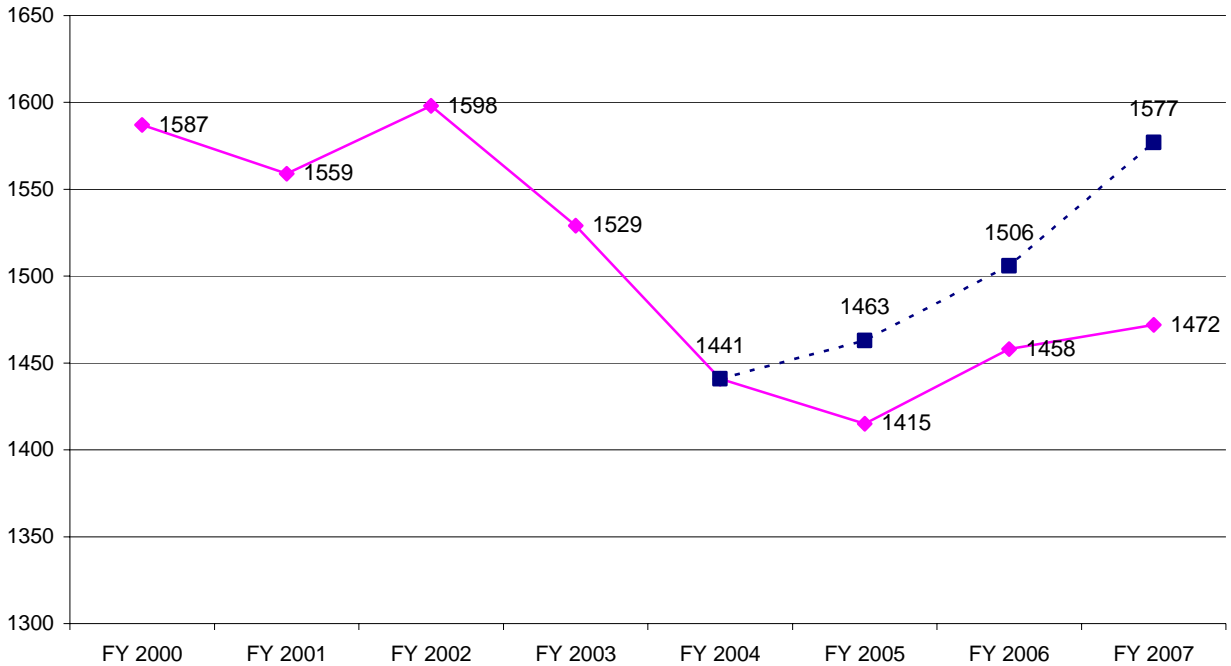
As seen in last year’s budget book special study entitled “Office of the Chief Financial Officer – District-wide,” which was prepared at the Council’s direction, from FY 2000 to FY 2004 the number of FTEs in the central OCFO dropped from 1,069 to 930, or 13 percent. (See the following charts and Attachments 4 and 5.)

Chart 1
Central OCFO Total FTE's FY 2000 - FY 2007



Note: The dotted lines include the effect of FTEs in OTR for compliance initiatives.

Chart 2
Central OCFO and Mayoral Agencies, Lottery, DCPS, and UDC Financial
FTEs,
FY 2000 - FY 2007



The FTE increases since that time have been primarily due to revenue generating initiatives and related revenue compliance activities in OTR. In FY 2005, the Council added 48 FTEs to the OCFO for a tax compliance initiative to produce additional revenue to support District operations. Without this initiative the FTEs would have declined further to 917 in FY 2005, or another 1.4 percent reduction. The FY 2006 approved budget added 33 FTEs in the central OCFO, including 17 for mandated functions and 16 for real property assessors. In FY 2007, an additional 62 FTEs were added for several tax compliance initiatives that are estimated to yield gross amounts of \$49 million for the general District budget in FY 2007, \$70 million in FY 2008, \$66 million in FY 2009, and \$64 million in FY 2010. The overall impact of the streamlining of OCFO operations during the

past several years has enabled more than 100 FTEs to be added to direct revenue generating activities, at the same time as total staffing has decreased. As a rule of thumb, each FTE devoted to compliance raises \$1 million (gross) per year. Once they are trained, working independently, and fully productive, the new auditors and revenue officers (at an annual cost of roughly \$65,000 each) will be instrumental in meeting our increased revenue targets.

Downward Trend in Agency Financial Staff

Since August 2002, financial operations for the Mayoral agencies have been organized into five clusters. Five associate chief financial officers (ACFOs) manage the fiscal officers that reside within these agencies. The ACFO structure has been very successful. The structure contributes significantly to the efficient preparation of the Comprehensive Annual Financial Report (CAFR), as well as budget development and execution. Where before there were accounts payable, payroll, and accounting operations throughout these agencies, there are now five shared service centers – one for each cluster.

By making these operations more efficient, since FY 2002, the last fiscal year before the ACFO structure was implemented, the FTEs in the Mayoral agency fiscal operations declined from 421 to 381 in FY 2005, or 9.5 percent. This has been largely the result of restructurings similar to those we have conducted in the central OCFO and in Lottery. In the Mayoral agency financial operations, restructurings have reduced costs by \$2.6 million on an annualized basis.

Initiatives and Ongoing Work of the OCFO in FY 2007

The total FY 2007 budget for the OCFO from all funding sources is 1,060 FTEs and \$154.7 million. From local sources, we have 932 FTEs and \$118.9 million.

Reflected in the budget are reductions totaling \$2.8 million in local funds, as well as significant increases in both local and special purpose revenue funding to support revenue initiatives in the Office of Tax and Revenue (OTR). (See Attachment 6 for a summary of changes from the FY 2006 to FY 2007.)

Tax Compliance Initiatives in the Office of Tax and Revenue

In FY 2007 the Office of Tax and Revenue is implementing eight distinct tax compliance initiatives that are projected to generate an additional \$49 million for the District's overall budget in FY 2007, with additional amounts projected in the out years.¹ The projected revenue is included in the FY 2007 revenue totals that form the basis for the proposed budget. Attachment 7 summarizes the initiatives.

We are also pursuing the collection of hotel taxes that we believe are due to the District from Internet travel providers. We believe that, in many cases, the Internet travel provider is charging the traveler the hotel tax based on the amount the traveler pays, and then that same travel provider is paying tax to the District on only the amount they are paying to the hotel. For example, a \$150 hotel room may be sold on the Internet for \$100, of which only \$60 is paid to the hotel. However, the Internet travel provider may be charging the traveler tax based upon the \$100, yet only transmitting to the District the hotel tax amount based upon the \$60 paid to the hotel. We intend to pursue the collection of these taxes charged to the consumer but not paid to the District, joining with other jurisdictions pursuing similar action.

¹ Details available in attachment to this testimony.

PLAN TO ADDRESS THE AUDITOR'S FINDING OF MATERIAL WEAKNESS IN DC PUBLIC SCHOOLS

As I covered in my FY 2006 CAFR testimony to the Committee of the Whole, the independent auditor found the DC Public Schools (DCPS) to constitute a material weakness, citing the areas of grants management, human resource/payroll issues, procurement practices, and the Medicaid program. It is incumbent upon me, as the independent CFO, to ensure that the fiscal soundness of the District is protected. To fail to do so could have consequences for all of the District government, including the loss of our favorable bond ratings and our credibility on Wall Street.

Accordingly, I directed the OCFO Office of Integrity and Oversight (OIO) to begin immediately to work closely with DCPS and develop a detailed plan of action, coordinate with the auditors to ensure their approval of the plan, and monitor the plan as it is executed by DCPS. OIO has done this. A task force composed of OCFO staff and DCPS staff has worked diligently the last two weeks to develop a corrective action plan to address each of the five factors that the independent auditor cited. The task force met with BDO Seidman and with representatives of the US Department of Education (DOE), as the DOE's finding of high-risk status was the first factor cited. The corrective action is attached here as Attachment 8.

DEBT MANAGEMENT AND BOND RATINGS

At the beginning of 1997, the ratings the District received from the three major bond rating agencies were B, Ba and BB. These were below investment grade, or "junk bond" ratings (see Attachment 2). Today, due to many reasons, not the least of which is our healthy financial position, the ratings are A+, A2 and A from

Standard & Poor's, Moody's Investors Service and Fitch Ratings, respectively. These are considered to be sound investment grade ratings. These ratings represent a series of upgrades since 1997, the most recent of which was the upgrade to A+ from Standard and Poor's in early FY 2006. It is noteworthy that this A+ rating from Standard & Poor's represents the highest bond rating that the District has ever obtained. These improved ratings help reduce the District's borrowing costs. We estimate that the cumulative effect of these upgrades is an annual savings of more than \$15 million in debt service and fees. These upgrades will also benefit future bond issues. For example, if the District were to issue \$300 million in general obligation bonds, the savings in debt service are estimated at more than \$1 million annually during the life of the bonds. Our steadfast objective is to sustain the ratings we have achieved so far and to continue to make financial strides in order to achieve additional upgrades.

CONCLUSION

The continuing leadership provided by the Mayor, by you, Mr. Evans, and the Council has enabled the District to experience a major financial turnaround. The OCFO is committed to doing everything we can to support continued financial improvements in the city in FY 2007 and beyond.

This concludes my remarks. I would be pleased to answer any questions you may have.

CENTRAL FINANCIAL OPERATIONS - Deputy CFOs

Office of Budget and Planning (OBP)
Bert Molina
(202) 727-6234

Office of Finance and Treasury (OFT)
Lasana Mack
(202) 727-6055

Office of Financial Operations and Systems (OFOS)
Anthony Pompa
(202) 442-8200

Office of Revenue Analysis (ORA)
Robert Ebel
(202) 727-7775

Office of Tax and Revenue (OTR)
Sherryl Hobbs Newman
(202) 442-6200

ORGANIZATIONAL CHART
Government of the District of Columbia
Office of the Chief Financial Officer

D.C. CHIEF FINANCIAL OFFICER
Natwar M. Gandhi
(202) 727-2476

Chief of Staff **Lucille Dickinson**
Director of Operations **Angell Jacobs**
(202) 727-2476

EXECUTIVE SUPPORT

General Counsel
Jerry Malone
(202) 727-9528

Integrity and Oversight Executive Director
Ben Lorigo
(202) 442-6433

Economic Development Finance Senior Advisor and Director
John Ross
(202) 727-2421

Senior Financial Policy Advisor
Marcy Edwards
(202) 727-2476

Agency Chief Information Officer
Mike Teller
(202) 727-8775

Management and Administration Executive Director
Paul Lundquist
(202) 442-6523

Public Affairs Officer
Maryann Young
(202) 727-0058

AGENCY FINANCIAL OPERATIONS - Associate CFOs

Agency Fiscal Officers

Economic Dev. and Regulation
Cyril Byron, Jr.
(202) 442-8684

DCRA: Conrad Bridges
DOES: Ibrahim Koroma
DHCD: George Dines
PSC: Irvin Logan

Government Operations
Barbara Jumper
(202) 727-0333

OAG: Victoria Syphax
OCTO: Mary Bauer
OFRM: Yassin Ahmed
EOM: Michael Bolden
SEO: Robert Jose

Government Services
Mohamed Mohamed (interim)
(202) 671-2201

EO: Shelly Robinson-Smith
DMV: Kimberly Holloway
DPW: Andree Chan-Mann
DDOT: Rumman Dastgir

Human Support Services
Deloras Shepherd
(202) 671-4220

CFSA: Justin Kopca
DOH: Tammie Robinson
DOH-MAA: Ganayswaran Nathan
DHS: Delicia Moore
DMH: Joyce Jeter
DPR/DCPL: (Vacant)
DYRS: Barbara Roberson

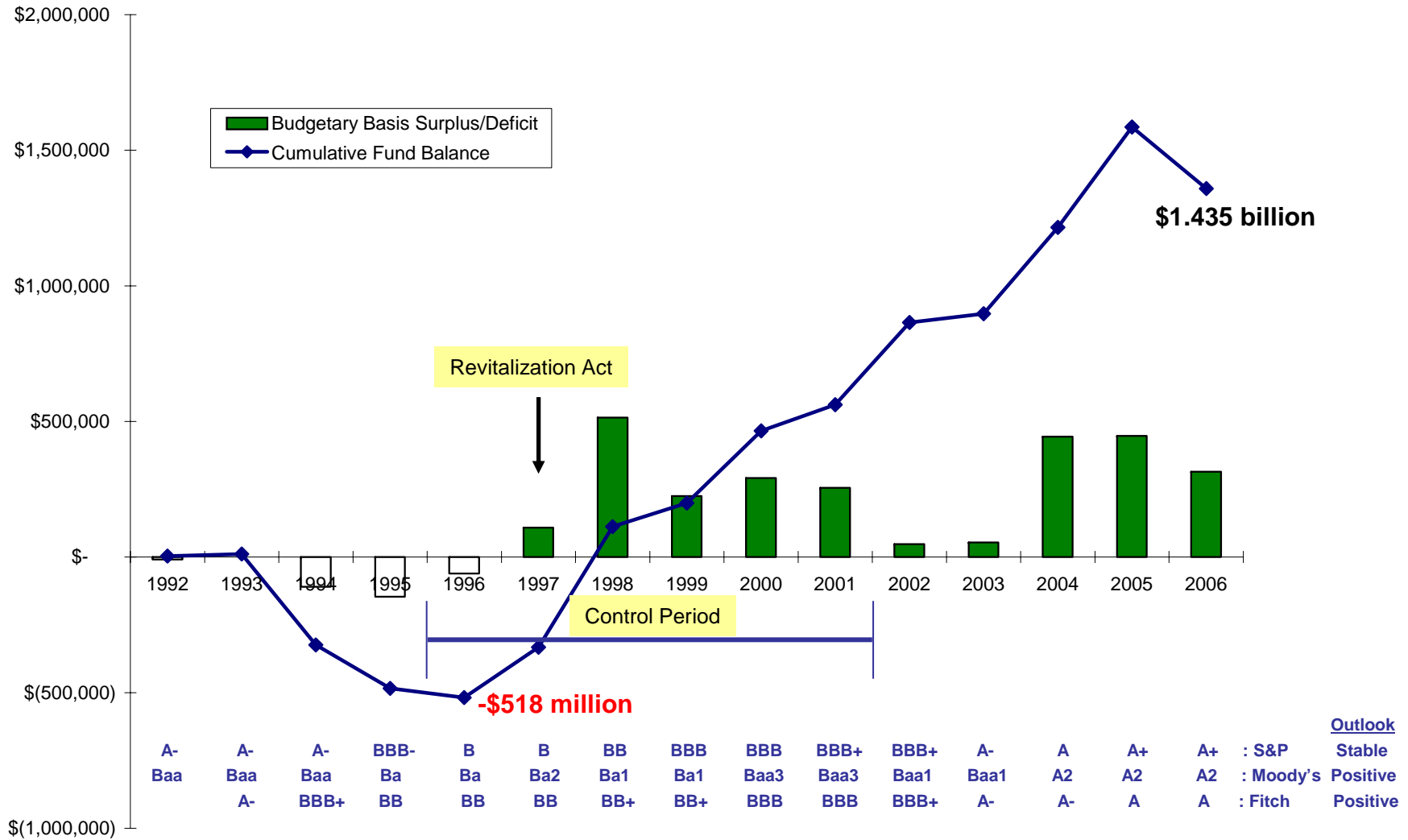
Public Safety and Justice
Angelique Hayes (acting)
(202) 673-3347

DOC: Ronald Peele
FEMS: (Vacant)
MPD: Martin Carmody

AWC: Steve Russo
NCRC: Neil Moran
DCPS: Pamela Graham
SEC: Wilma Matthias
UDC: Myles Mutnick
WCCA: Henry Mosley
WASA: Olu Adebo (interim)

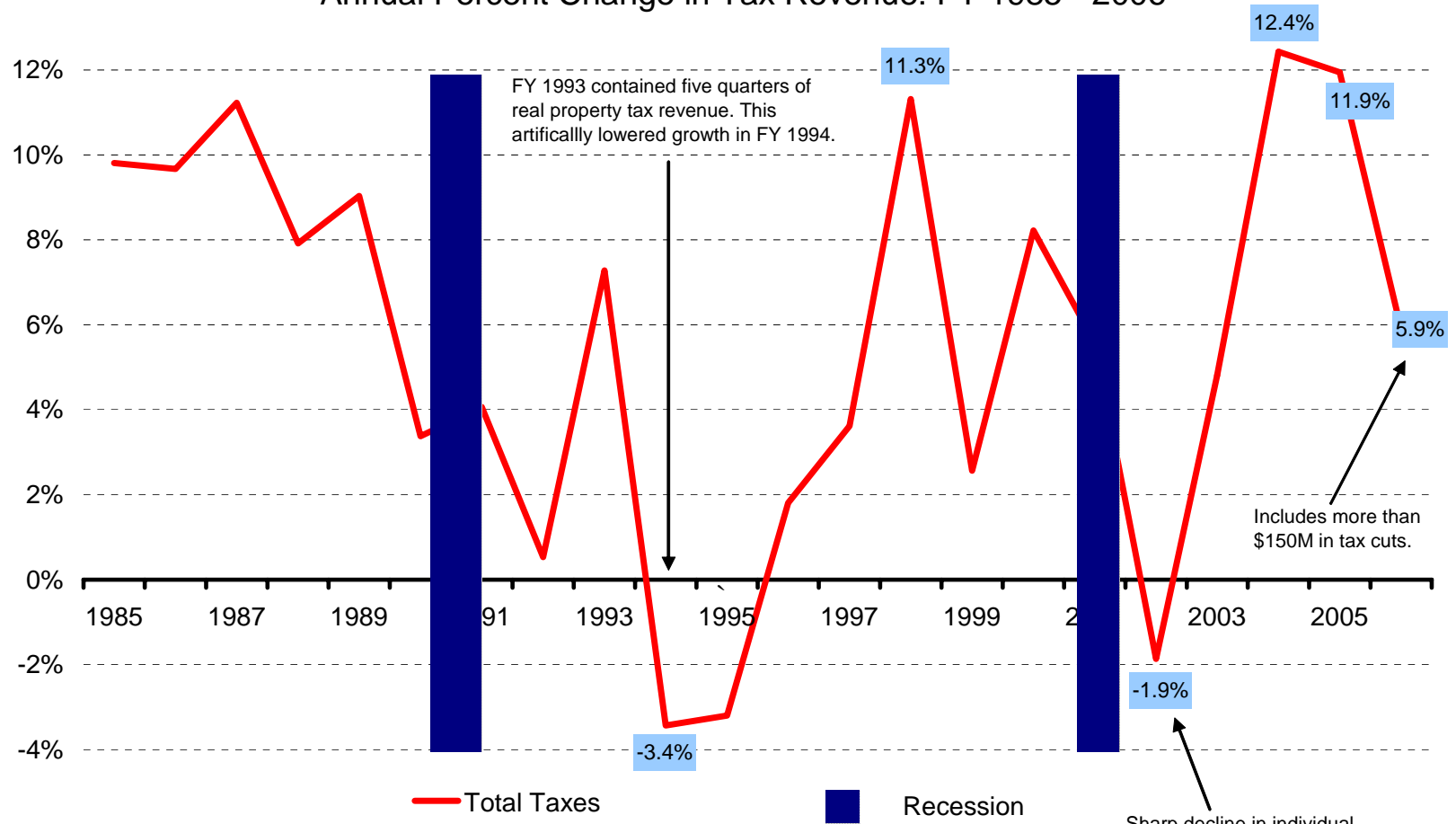
DC Lottery
Executive Director **Jeanette Michael**
Agency Fiscal Officer William Robinson

Surplus and Bond Rating History



Volatile Tax Revenues

Annual Percent Change in Tax Revenue: FY 1985 - 2006



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

Sharp decline in individual income and sales taxes due to recession and 9/11.

OFFICE OF THE CHIEF FINANCIAL OFFICER
FY 2000 - FY 2007

| | FY 2000 | FY 2001 | FY 2002 | FY 2003 | FY 2004 | FY 2005 | FY 2006 | FY 2007 | FY 2000 - FY 2007 |
|---|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|----------------------|
| FTEs | | | | | | | | | |
| OCFO Agency (AT0) without revenue initiatives | 1,069 | 1,026 | 1,036 | 1,013 | 930 | 917 | 950 | 955 | (114) |
| Plus Required Initiatives | | | | | | 48 | 48 | 105 | |
| OCFO Agency (AT0) | 1,069 | 1,026 | 1,036 | 1,013 | 930 | 965 | 998 | 1,060 | (9) |
| Total Mayoral Agencies | 381 | 395 | 421 | 398 | 394 | 381 | 388 | 396 | 15 |
| Lottery AFO | 10 | 10 | 10 | 10 | 10 | 10 | 10 | 11 | 1 |
| DCPS | 89 | 89 | 89 | 70 | 65 | 65 | 69 | 69 | (20) |
| UDC | 38 | 39 | 42 | 38 | 42 | 42 | 41 | 41 | 3 |
| Grand Total OCFO | 1,587 | 1,559 | 1,598 | 1,529 | 1,441 | 1,463 | 1,506 | 1,577 | (10) |
| Annual percent change in AT0 without revenue initiatives | | -4% | 1% | -2% | -8% | -1% | 4% | 1% | -11% |
| Annual percent change AT0 | | -4% | 1% | -2% | -8% | 4% | 3% | 6% | -1% |
| Annual percent change grand total | | -2% | 3% | -4% | -6% | 2% | 3% | 5% | -1% |
| AT0 Budget (\$ millions) | | | | | | | | | |
| Local | 63.9 | 64.9 | 68.2 | 76.9 | 73.4 | 93.2 | 105.1 | 118.9 | 55 |
| O-Type | 10.3 | 9.9 | 9.9 | 9.9 | 8.4 | 9.2 | 14.3 | 31.1 | 21 |
| Total General Fund | 74.2 | 74.8 | 78.1 | 86.8 | 81.8 | 102.4 | 119.4 | 150.0 | 76 |
| Federal grants | 0.9 | 0.9 | 0.9 | 0.9 | 0.9 | 1.0 | 0.9 | 0.9 | - |
| Intra-District | 6.4 | 4.8 | 5.1 | 5.1 | 5.9 | 3.7 | 3.9 | 3.9 | (2) |
| Gross budget AT0 | 81.5 | 80.5 | 84.1 | 92.8 | 88.6 | 107.1 | 124.2 | 154.8 | 73 |
| Gross budget District wide | NA | NA | NA | NA | NA | NA | 178.0 | 211.7 | NA |
| Annual % change in local, AT0 | | 2% | 5% | 13% | -5% | 27% | 13% | 13% | 86% |
| Annual % change in general, AT0 | | 1% | 4% | 11% | -6% | 25% | 17% | 26% | 102% |
| Annual % change in gross, AT0 | | -1% | 4% | 10% | -5% | 21% | 16% | 25% | 90% |
| Annual % change gross, DC wide | | | | | | | | 19% | |

ATTACHMENT 5

**OFFICE OF THE CHIEF FINANCIAL OFFICER
FY 2004 - FY 2007 FTEs**

| | Mandated Increases | Net Impact of Other FTE Changes | Total FTEs |
|---|-------------------------------|--|-------------------|
| FY 2004 Budgeted FTEs | | | 930 |
| FY 05 Revenue Compliance Initiative | 48 | -13 | 35 |
| FY 2005 Budgeted FTEs | | | 965 |
| FY 06 Increases | | | |
| Non Custodial Fathers Initiative | 8 | | |
| Baseball Initiative | 3 | | |
| Anti-Deficiency Act | 4 | | |
| OTR - Counsel (OAH work) | 2 | | |
| Real Property Assessment | 16 | | |
| FY 2006 Proposed FTE Changes | 33 | 0 | 33 |
| FY 2006 Budgeted FTEs | | | 998 |
| Note: other changes in FY 2006 netted to zero | | | |
| FY 07 Increases | | | |
| Revenue Initiatives | 57 | | |
| IT Staff - convert capital to operating | | 5 | |
| (convert contract IT staff to DC employees) | 57 | 5 | 62 |
| FY 2007 Budgeted FTEs | | | 1,060 |

| FY 2004 - FY 2007 Summary | | |
|----------------------------------|--|--------------|
| FY 2004 Budgeted FTEs | | 930 |
| Mandated Increases | | 138 |
| Other FTE changes | | (8) |
| FY 2007 Budgeted FTEs | | 1,060 |

ATTACHMENT 6

OFFICE OF THE CHIEF FINANCIAL OFFICER FY 2006 - FY 2007 Operating Budget Evolution

| | <u>\$000s</u> | <u>FTEs</u> | |
|-----------------------------------|----------------|--------------|---|
| FY 2006 Approved Budget | 124,242 | 998 | |
| Local Fund Changes | | | |
| Reduction of One Time Costs | (900) | | |
| PS Step Increases | 1,022 | | District-wide mandated increase |
| NPS inflation adjustment | 467 | | District-wide mandated increase |
| Fixed Costs | 1,021 | | District-wide mandated increase |
| OTR Revenue Initiatives | 11,155 | 57 | \$48 million included in revenue estimates |
| OTR - Integrated Tax System | 1,448 | | Ongoing maintenance and support |
| OTR - Operating impact of capital | 942 | 5 | Convert contract work to in-house |
| OTR - NPS requirements | 543 | | Postage, software, peak season temp staff |
| Funding for DCPS finance staff | 432 | | Maintain financial services at DCPS |
| Replace loss of ASMP funds | 233 | | Financial oversight of PASS, payroll projects |
| Integrity and Oversight | 51 | | Expand background check programs |
| Budget and Planning | 51 | | Budget book printing and software |
| Mayoral Cut | (2,803) | | Agency-wide adjustments and savings. |
| Nonlocal Fund Changes | | | |
| O type - Hotel tax litigation | 15,000 | | Provides budget to pay from revenue collected if litigation is successful |
| O type - Recorder of Deeds | 1,435 | | Pays for temporary relocation of ROD staff from ROD surcharge fund |
| O type - Recorder of Deeds | 333 | | Pays for expansion of ROD imaging project from ROD surcharge fund |
| FY 2007 Council Submission | 154,672 | 1,060 | |
| Council Adjustment | 150 | | Increase for EITC Outreach |
| FY 2007 Approved Budget | 154,822 | 1,060 | |

ATTACHMENT 7

| | <u>Project Name and Description</u> | <u>Tax Type</u> | <u>FTE's</u> | <u>Total Costs,</u> <u>FY07</u> | <u>Revenue Estimates</u> <u>FY 2007</u> | <u>Revenue per</u> <u>staff year</u> |
|---|--|--|---------------------------|--|--|--|
| 1 | Clean Hands -- Full implementation of clean hands by all DC agencies issuing licenses and those with authority to contract will generate additional "clean hands" requests/reviews which in turn will generate additional city-wide revenue. | All | 10 | \$ 3,050,000 | \$ 8,000,000 | \$0.8 million |
| 2 | Comprehensive Tax Fraud Initiative - Schedule C - EITC - Income and Expense Audits of Major Commercial - Sales - Use Tax | Income Income Real Property/ Business Business Business | 3 3 2 3 3 | \$ 275,000 \$ 260,000 \$ 165,000 \$ 260,000 \$ 260,000 | \$ 1,000,000 \$ 1,000,000 \$ 3,000,000 \$ 3,000,000 \$ 1,000,000 | \$0.3 million \$0.3 million \$1.5 million \$ 1 million \$0.3 million |
| 3 | Vacant property (Class 3): Step up identification and review of vacant properties in the District. Reduce the large number of exceptions to a more manageable level. | Real Property | 8 | \$ 535,000 | \$ 8,000,000 | \$1 million |
| 4 | Homestead Audits: Increase audits on the Homestead program. Currently there are 90,000 properties with the benefit. Assuming a 5% non-compliance rate, recapturing \$1,150 in back homestead benefit, and \$2,000 in back taxes, and a 50% probability of a full 3 years of non-compliance. | Real Property | 5 | \$ 2,235,000 | \$ 10,000,000 | \$2 million |
| 5 | Tax Fraud Detection - W-2's -- Compare Income Tax Filings with DOES withholding filings/records. | Income | 6 | \$ 1,335,000 | \$ 6,000,000 | \$1 million |
| 6 | Productivity Enhancements - A/R Review -- Comprehensive review and correction of accounts will result in a 25% improvement factor in the efficiency/productivity of the Audit and Collection staff, and improve the quality of revenue estimates. | All | 4 | \$ 1,710,000 | \$ 2,000,000 | \$0.5 million |
| 7 | Sales Tax Verification -- Compare listing of licensed businesses with those filings monthly and/or annual Sales Tax returns. | Sales | 8 | \$ 950,000 | \$ 4,000,000 | \$0.5 million |
| 8 | Possessory interest. Capture 100% more of commercial leases within Federal property. | Real Property | 2 | \$ 120,000 | \$ 2,000,000 | \$1 million |
| | Total Revenue Initiatives | | 57 | \$ 11,155,000 | \$ 49,000,000 | |

| | <u>FY 2007</u> | <u>FY 2008</u> | <u>FY 2009</u> | <u>FY 2010</u> | <u>Total, FY07-10</u> |
|---------------------|-------------------|-------------------|-------------------|-------------------|-----------------------|
| Projected Revenues | 49,000,000 | 70,000,000 | 66,000,000 | 64,250,000 | 249,250,000 |
| Expenses | 11,155,000 | 3,460,000 | 3,460,000 | 3,460,000 | 21,535,000 |
| Net Revenues | 37,845,000 | 66,540,000 | 62,540,000 | 60,790,000 | 227,715,000 |

| | | | | | |
|--------------|----------------|-----------------|-----------------|-----------------|-----------------|
| | 4.4 | 20.2 | 19.1 | 18.6 | 11.6 |
| Ratio | 4.4 : 1 | 20.2 : 1 | 19.1 : 1 | 18.6 : 1 | 11.6 : 1 |



Government of the District of Columbia

DCPS PLAN TO ADDRESS FY 2006
MATERIAL WEAKNESS

Council Briefing
Wednesday, February 28, 2007

Composition of the Task Force

The task force included the following representatives:

DCPS:

- Chief Operating Officer
- Medicaid Director
- Executive Director/
Federal Grants
- Procurement Officer
- US Department of
Education liaison

OCFO:

- Deputy Chief Financial
Officer/OFOS
- Chief Financial Officer/DCPS
- Executive Director/ Office of
Integrity & Oversight (OIO)

Task Force Responsibilities

| Area | Responsible Office |
|---|---------------------------|
| Development of the Work Plan | DCPS & OCFO |
| Execution of the Work Plan | DCPS |
| Monitoring & Reporting on the Work Plan | OCFO |

Task Force Actions to Date

- Met with the external auditors, BDO Seidman, to discuss the FY 2006 DCPS material weakness designation.
- Met with U.S. Department of Education representatives to discuss the DCPS high-risk designation. (*DCPS initiated a comprehensive corrective action plan in March FY 2006*)
- Met to develop corrective action plans to address each cited component.

FY 2006 Material Weakness

There are five reasons cited by the independent auditors for the Material Weakness:

- High-Risk Designation by the U.S. Department of Education
- High-Risk Designation by the D.C. OIG
- Procurement
- Human Resources/CAPPS
- Medicaid

Source: Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters based on an audit of Financial Statements Performed in Accordance with Government Auditing Standards, January 26, 2007.

Audit Standards for 2007

- Revised auditing standards promulgated by the AICPA and GAO (Yellow Book).
- Standards for determining deficiencies have become more stringent (*definitions have expanded, documentation requirements have been raised*).
- Under the new definitions, the tolerance for repeat findings has decreased.
- Unaddressed findings may be elevated from a management letter comment to a Yellow Book finding.

DCPS Stand-Alone Audit Results

| Nature of Comment | FY 02 | FY 03 | FY 04 | FY 05 | FY 06 |
|--|-------|-------|-------|-------|-------|
| Retroactive Payments of Salary Step Increases | | RC | MW | MW | MW |
| Insufficient Tracking of Personnel | | RC | RC | RC | RC |
| Benefit Payments for Inactive Employees | | | | MW | MW |
| Official Personnel Folders & Inadequate Supporting Documentation | | MLC | RC | RC | RC |
| Medicaid Cost Reports | | | | MLC | MW |
| Medicaid Provider Accounting & Financial Reporting | RC | MLC | | | MW |

MW = Material Weakness, RC= Reportable Condition, MLC= Management Letter Comment

DCPS Prior Year Single Audit Results

| Nature of Comment | FY 02 | FY 03 | FY 04 | FY 05 |
|------------------------------------|-------|-------|-------|-------|
| Allowable Costs | √ | √ | √ | √ |
| Accrued Expenses | | | √ | √ |
| Lack of Supporting Documentation | √ | √ | √ | √ |
| Equipment/Real Property Mgmt. | √ | √ | √ | |
| Level of Effort | √ | √ | √ | √ |
| Sub-recipient Monitoring | √ | √ | √ | √ |
| Procurement Suspension & Debarment | √ | √ | √ | √ |

Summary of Corrective Action Plans

| | Reasons | Summary of Corrective Action Plans | Responsible Parties |
|----|-----------------------------------|---|-----------------------------|
| 1. | High Risk Designation by U.S. DOE | A detailed corrective action plan has been developed to address the DOE concerns. | DCPS |
| 2. | High Risk Designation by D.C. OIG | Follow-up on FY 2006 OIG audits to ensure implementation of corrective actions. | DCPS & OCFO |
| 3. | Procurement | The Procurement Officer has instituted directives and training for staff to address the weaknesses noted. | DCPS Procurement Officer |
| 4. | Human Resources/ CAPPS | The OCFO/OPRS will assist DCPS in training staff on the use of CAPPS, reporting, and the step process. | DCPS & OCFO/OPRS |
| 5. | Medicaid | Cost reports will be filed for 2004 and 2005. The full accrual basis of accounting will be implemented. | DCPS Medicaid Director/OCFO |

1. High Risk Designation by U.S. DOE Corrective Action Plan

- The District requested and received authorized time extensions for FY04 and FY05 single audits from our cognizant agency, HHS.
- A financial monitoring manual will be developed for DCPS, and staff will receive training in its application.
- A program monitoring manual will be developed for DCPS, and staff will receive training in its application to perform desk audits, program design reviews.
- Will identify state-level functions within the Local Education Agency grants management office and determine functions that should be moved to the State Education Agency without disruption in the management.
- The OCFO will provide training to Human Resources staff to ensure adequate documentation of salary charges is maintained.

2. High Risk Designation by DCOIG Corrective Action Plan

- The Office of Integrity and Oversight (OIO) will obtain all DCPS related D.C. OIG audit reports issued during FY 2006.
- OIO will review the status of corrective actions noted by DCPS in management responses.
- OIO will determine if corrective actions have been implemented and whether findings have been resolved.

3. Procurement Corrective Action Plan

- The DCPS Office of Contracts and Acquisitions (OCA) will provide requisite training on applicable District laws, regulations, and policies. OCA will request the advice of OCP and the National Institution of Government Purchasing (NIGP) on their respective systems of training and if applicable OCA will adopt and/or modify the training process to the meet training needs of its staff.
- OCA completed the migration from ADPICS to PASS in FY 2007.
- Written policies and procedures have been completed.
- A new purchase order database was implemented in FY 2006.

4. Human Resources/CAPPS Corrective Action Plan

- OPRS will identify all teachers eligible for a step increase in CAPPS and update their records prior to the opening of the school year. DCPS will provide OPRS with the rules regarding the waiting periods between steps.
- Pursuant to the training plan, the DCPS Office of Human Resources along with the CFO's office will develop a task force to provide the necessary training needed for the appropriate HR staff.
- From the task force and training, an operating procedures manual will be developed along with a DVD version.

5. Medicaid Corrective Action Plan

- DCPS will get clarification on the cost report filing requirements from the code of Federal Regulations. Additionally DCPS will meet with MAA (the state office) regarding cost reporting procedures.
- The 2004 cost report will be filed by 9/30/2007.
- A letter will be sent from DCPS to all clinicians and service providers reiterating the documentation requirements.
- A cross-functional task force will be formed to codify the process and methodology for estimating costs.
- DCPS will work with OFOS regarding the transition to the accrual-based accounting method.
- DCPS will review the decision on how the Medicaid receivable is booked to ensure that the receivable is properly recorded at the District level as well as at DCPS while avoiding duplication.

Monitoring of Corrective Actions

- The DCPS-CFO/OCFO-OIO will monitor progress on all plans and report to the Council on a monthly basis until all tasks are completed.
- The OCFO/OIO will perform quality control reviews of finance-related areas to ensure corrective actions have been implemented.
- The DCPS Compliance group will perform quality control reviews of program-related areas to ensure corrective actions have been implemented.
- The U.S. Department of Education liaison will monitor progress on the corrective action plan to address the high-risk designation.