HEARING ON

THE MAYOR'S FY 2010
PROPOSED BUDGET AND FINANCIAL PLAN

Before the
Subcommittee on Financial Services and General Government
Committee on Appropriations
U.S. House of Representatives

The Honorable José Serrano, Chairman

May 14, 2009; 9:15 a.m.
2362A Rayburn House Office Building

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

Good morning, Chairman Serrano and members of the subcommittee. I am Natwar M. Gandhi, Chief Financial Officer for the District of Columbia, and I am here to offer brief remarks about the Fiscal Year 2010 proposed budget and financial plan for the District. In this testimony, I will discuss how the current economic situation has affected the District's revenue estimates. I will also address our capital needs and the challenges we face in meeting those needs, and I will briefly describe our very successful new bond program secured by income taxes.

Mr. Chairman, the District's sound financial standing was recently demonstrated again by the results of the FY 2008 Comprehensive Annual Financial Report ("CAFR"): a $191 million General Fund surplus (including $116 million local source funds) marking a dozen consecutive years of balanced budgets. As you can see from the chart in Attachment A, since 1996, the responsible actions of the District's elected leaders have resulted in a $1.8 billion turnaround in the cumulative General Fund balance, from a $518 million deficit to a $1.245 billion positive balance. It is important to note that of the $1.8 billion increase in General Fund balance, over $700 million has been accumulated in the post-Control Board period. Indeed, our turnaround from "junk bond" status to "A" category ratings was faster than every other major city that has undergone a similar period of financial crisis, including New York, Philadelphia, Cleveland and Detroit. We have substantially improved general obligation bond ratings, well-deserved respect in the financial markets and currently, we enjoy a triple-A rating on our income tax bonds.

FY 2010 Budget and Financial Plan

This has been an exceptionally challenging budgeting and planning cycle and I commend Mayor Fenty and City Administrator Dan Tangherlini for sending the D.C. Council a balanced budget proposal. Since the proposed budget was submitted on March 20th, the Council, under the leadership of Chairman Gray, has been hard at work. We will continue to work diligently with everyone in this collaborative process and we expect to submit budget books reflecting the final Council actions to the Congress by June 8.

For the first time in many years we have a local funds budget proposal that is smaller than the previous year's approved budget, $5.4 billion compared to $5.6 billion. Despite lower revenues, the District's FY 2010 proposed budget and five-year plan is balanced, and is our 14th consecutive balanced budget. (See Attachment B.)

In previous years, we looked for ways to spend rising revenues efficiently and effectively. This year, working with less, we have had to find ways to continue to provide the services our residents need at the levels of quality they expect. In addition to producing a balanced budget for FY 2010, we maintain the required levels of "rainy day" funds – the emergency and contingency cash reserves – of at least $360 million throughout the four year plan. (See Attachment C.) And, in our capital budget, we continue to be prudent in our borrowing by imposing an even stricter limit on debt service expenditures than the level set in the Home Rule Act. (See Attachment D.)

It is important to note here that bond rating analysts have stated that economic downturns are the true test of financial management. This balanced budget proposal is testimony to our elected leaders' commitment to manage effectively, in both good times and bad. In summary, the District has continued to demonstrate sound financial management and fiscal prudence.

Economic and Revenue Outlook

The economic outlook for the District has changed dramatically. One year ago, the outlook was for a slowdown in the economy and reduced revenue growth, but the consensus was that the District would likely avoid a recession.

District Employment

But now the U.S. is in its 17th month of recession, the longest since the 1930s. The District of Columbia's total job base has been weakened, but it is faring better than many places. For the fifteen months from December 2007 through March 2009, total jobs located in the District of Columbia grew by 6,700 (1.0 percent) with gains in the federal government, education and health, and food services. However, during the same period, *District resident* employment has fallen sharply, at a rate worse than that of the U.S. as a whole. From December 2007 through March 2009, 15,000 jobs held by D.C. residents were lost and the unemployment rate in the District rose from 5.8 percent to 9.8 percent.

This data is contrary to the "conventional wisdom" that D.C. is recession proof. In all four of the recessions that have occurred since 1980, the percentage declines for D.C. resident employment has been greater than the U.S. as a whole.

Our current economic forecast assumes that District economic conditions will continue to deteriorate as employment and wages edge downward, commercial property vacancies rise, real property transfers slow further, and construction projects are delayed. The unemployment rate is projected to increase from its current 9.8 percent (in March 2009, latest available data) to an annual rate of 11.5 percent in 2010. Similarly, Real Gross State (DC) Product is projected to fall in 2009 (-1.2 percent) and 2010 (-0.7 percent).

Revenue Implications

Certainly the greatest budget challenge for the District this year is the significant drop in estimated revenues over the next four years. Since the June 2008 estimates for the FY 2009 budget and five-year plan, projected revenues have dropped nearly $400 million in FY 2009 and over $800 million in FY 2010 (the equivalent of more than 12 percent of expenditures). For FY 2011 and FY 2012, the decreases are about $1 billion and $1.1 billion, respectively. (See Attachment E.) It will not be until FY 2013 that we expect revenues will exceed FY 2008 levels. Clearly, the national recession has affected the District's revenues.

To ensure a balanced financial plan for the District of Columbia government and to minimize expenditure cuts and their effects on service delivery during the current recession, the proposed budget incorporates a series of revenue adjustments designed to maintain financial balance over the four-year plan period. These adjustments range from adding language to correct and/or improve previously enacted laws that created unintended revenue losses to the General Fund, to increasing selected fees that have failed to keep up with inflation. Each of these proposals will be listed and described in the Revenue Chapter of the Executive Summary of the budget that you will receive in June.

The FY 2010 Mayor's proposed budget uses a total of $183 million in General Fund balance, including $107 million Local fund balance. Of the $107 million in

Local fund balance proposed for use, $57 million was already so designated in the FY 2008 fund balance and $50 million comes from the $86.7 million unreserved and undesignated balance as of September 30, 2008.

Capital Spending, Contemplated Borrowing, and Debt Burden

The District faces a wide variety of infrastructure needs, placing great demands on its Capital Improvements Plan and the resultant borrowing. (See Attachment F.) The Mayor's proposed FY 2010 capital program includes $468.1 million in planned capital expenditures to be financed by $433.5 million in new income tax secured revenue bonds (so long as they remain more cost effective than General Obligation (GO) bonds), $3 million of PAYGO transfers for a Department of the Environment project required by the Environmental Protection Agency, and $31.6 million from the Master Equipment Lease Program. An additional $198 million in income tax revenue bonds will be issued for government centers, the consolidated lab, and capital deficit reduction.

Both for operating and capital expenditures, the District of Columbia is responsible for multiple government functions that normally are associated with those of a city, a county, a school district and a state. Using a ratio of total tax supported debt to population, the District is dramatically out of step with other large cities. Compared to the District's $10,000 per capita for all tax supported debt, New York City's is less than $7,000, Chicago's is $4,400, Boston's is $1,800 and Baltimore's is $1,200.

From the broader viewpoint – that the District shoulders the burdens usually carried by multiple governments – it is proper to use a ratio of debt service to expenditures as the measure for judging debt burden. Our debt service at the beginning of the current fiscal year was around 9.1 percent of expenditures. With currently planned amounts of future borrowing, that percentage is projected to rise to 11.9 percent by the end of FY 2013, just below the new statutory cap of 12 percent and above the Moody's median of 11.5 percent for large cities. (See Attachment D.) This phenomenon highlights the challenge of addressing the District's comparatively high spending needs with a restricted tax base.

High Needs and Restricted Tax Base

The District, as the urban center of a large metropolitan area, houses a disproportionately large share of very poor and needy citizens. The District's overall poverty rate of 16.4 percent and child poverty rate of 22.7 percent are among the highest in the nation and more than three times the comparable rates across neighboring counties.[1] Unlike other urban jurisdictions, the District cannot divert resources from wealthier suburban areas to serve its urban poor.

Higher costs of service delivery compared to the average costs of similar services in the 50 states further threaten the District's fiscal health. Labor costs for public services in the District are 23 percent higher than the national levels, and capital costs (primarily buildings) are 65 percent higher than the national average. Because of this combination of a needy population and high service costs, our expenditure needs are very high. If the District were to offer a basket of public services similar to what is offered across all states and localities in the nation, for each of its residents, it would have to spend 30 percent more than what other states and localities spend on average.

---

[1] The U.S. averages are 13 percent for poverty and 18 percent for child poverty. The average across Arlington, Fairfax, Montgomery and Prince George's counties is 6.0 percent poverty and 7.2 percent child poverty.

In this environment of continuing expenditure needs, the challenge posed by reduced revenues is substantial. The U.S. Congress plays an important role here, and I would like to briefly note two areas that merit continuous attention. Both go to the federal preemptions of the District's taxing authority.

First, consider that two-thirds of the income earned in the District is earned by non-residents, mostly commuters from the suburbs, but the District is prohibited from taxing that income. This limitation illustrates the kind of uniquely restricted tax base with which we are compelled to fund services to our residents

Second, the District has an especially high concentration of non-taxable real property, much of it off the tax rolls due to the presence of the federal establishment. The federal government holds 39 percent of the land area of the District. If we were to add to our tax base the sixty largest federal office buildings in the District, the commercial real property tax base would rise by 20 percent and, in turn, generate additional tax revenues of $270 million. If all commercial-like federal property (excluding the monuments, the Mall, Capitol Hill and the Federal Triangle), the added revenues would add up to another $270 million. Further, the Congressional imposition of a height limitation on buildings prevents the District from maximizing its limited land mass as a revenue source. One only has to look at the office and apartment buildings in every other major city to recognize how the District is penalized by this one restriction.

Because of the inability to tap these resources, our residents must shoulder a disproportionate share of the cost of providing public services, while the benefits generated by the city's taxpayers are shared by a much larger non tax-paying community. Yet, the District's 14th consecutively balanced budget attests to our resolute determination that these disadvantages should not become an excuse for fiscal irresponsibility. However, there is a looming danger. The nation's economic condition, combined with the District's high expenditure needs raise the prospect that, should revenues drop significantly from the already reduced levels, District services could be severely impaired. This is a reality that must not be ignored.

Income Tax Bonds

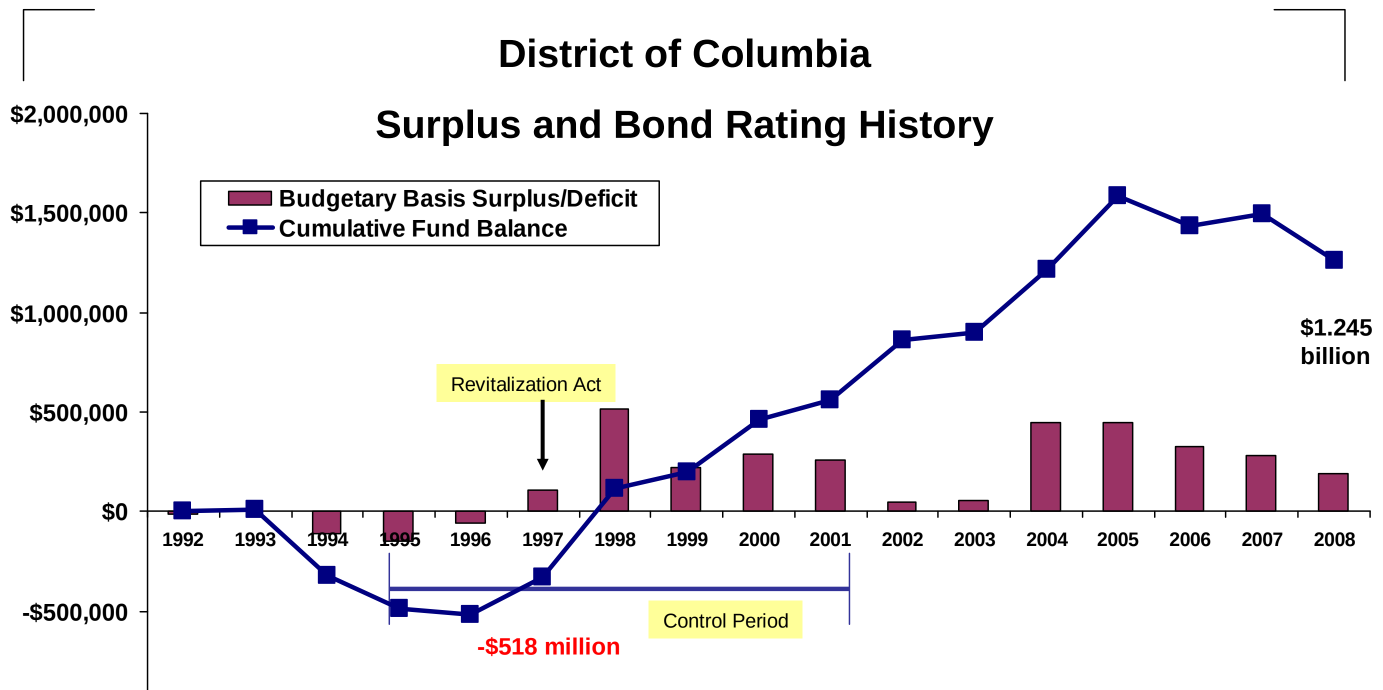
Mr. Chairman, I would like to conclude with positive news. I take great pleasure to inform you and the Subcommittee about the District's new form of borrowing - Income Tax Secured Revenue bonds. As the name makes clear, these bonds are secured by our individual income and business franchise taxes.

Standard & Poor's assigned the bonds their highest possible rating of AAA. Moody's Investors Service and Fitch Ratings assigned double-A ratings (Aa2 from Moody's and AA from Fitch). Together, these ratings are the highest endorsement that District of Columbia bonds have ever achieved. It is a far cry from the Control Period only a decade ago, when, as I noted earlier, the District's bonds were in the "junk bond" category.

When we went to the market with the first issue of Income Tax bonds in March, we were offering to sell about $445 million (and planning to sell more of the bonds later in the year). Investor demand was so great and the interest rates were so advantageous that we increased the size of the issue to meet that demand. We sold over $800 million, most of which will fund projects in the Capital Improvement Plan, including school modernization and transportation projects. The remainder was used to refinance outstanding general obligation bonds at lower interest rates to reduce our debt service obligations.

Conclusion

Mr. Chairman, I would again like to take this opportunity to stress the particular challenges the District faced in preparing this budget in an environment of declining revenues. As I stated at the beginning, the leadership provided by the Mayor and the Council made it possible for the District to produce this balanced budget proposal for FY 2010. As a result, we certified that the FY 2010 budget and financial plan, as proposed, is balanced for FY 2010 and beyond. I would like to thank you, Mr. Chairman, for your leadership and this committee for its diligent and continuous oversight work on the District's finances during this difficult economic period. We look forward to continuing to work with you and the subcommittee during the forthcoming budget deliberations.



General Obligation Bond Ratings

S&P:	A-	A-	A-	BBB-	B	B	BB	BBB	BBB	BBB+	BBB+	A-	A	A+	A+	A+	A+
Moody's:	Baa	Baa	Baa	Ba	Ba	Ba2	Ba1	Ba1	Baa3	Baa3	Baa1	Baa1	A2	A2	A2	A1	A1
Fitch:		A-	BBB+	BB	BB	BB	BB+	BB+	BBB	BBB	BBB+	A-	A-	A	A	A+	A+

2009 Income Tax Secured Revenue Bonds:	**S&P: AAA**	**Moody's: Aa2**	**Fitch: AA**

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

ATTACHMENT B

FY 2010 BUDGET AND FINANCIAL PLAN

FY2010 - FY 2013 General Fund - Local Funds Component

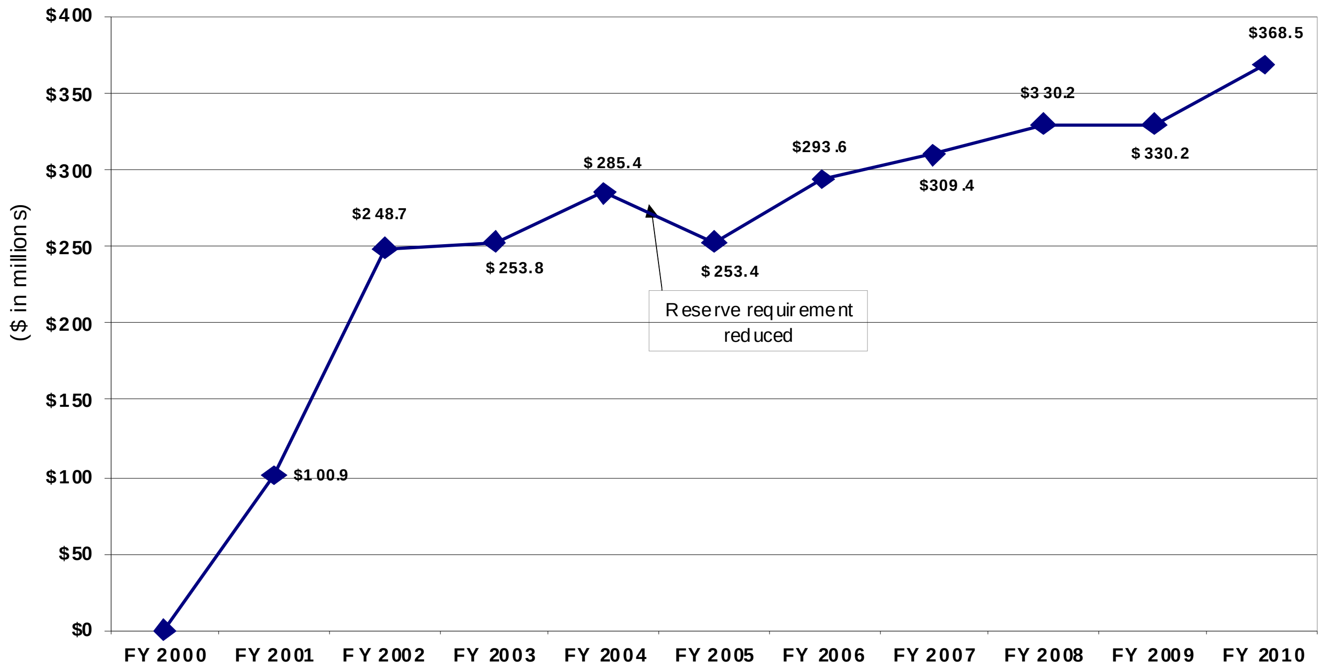
($ thousands)

	FY 2008 Actual	FY 2009 Approved	FY 2009 Adjusted	FY 2010 Proposed	FY 2011 Projected	FY 2012 Proposed	FY 2013 Projected
Revenues							
Local Fund Revenues	$5,436.8	$5,432.2	$5,169.4	$5,029.5	$5,132.0	$5,298.8	$5,540.0
Bond proceeds for issuance costs	$16.2	$15.0	$15.0	$15.0	$15.0	$15.0	$15.0
Transfer from other funds	$6.3	$3.9	$3.9	$3.5	$3.5	$3.5	$3.5
Fund Balance use	$426.6	$146.3	$161.8	$145.7	$0.0	$6.5	$0.0
Revenue Proposals			$4.5	$185.8	$176.3	$193.8	$204.0
Total Revenues	$5,885.9	$5,597.4	$5,354.6	$5,379.5	$5,326.8	$5,517.6	$5,762.5
Expenditures							
Total in Appropriation Titles	$4,971.5	$4,830.9	$4,649.4	$4,672.3	$4,578.8	$4,784.4	$4,929.6
Financing and Other	$547.8	$624.2	$608.8	$615.7	$603.6	$629.4	$653.7
Operating Cash Reserve	$0.0	$46.0	$0.0	$0.0	$40.5	$0.0	$0.0
Paygo Capital	$139.5	$14.7	$14.7	$0.0	$0.0	$0.0	$0.0
OPEB	$110.9	$81.1	$81.1	$88.7	$94.7	$101.2	$108.2
Total Expenditures	$5,769.7	$5,596.9	$5,354.0	$5,376.7	$5,317.6	$5,515.0	$5,691.5
Operating Margin	**$116.2**	**$0.5**	**$0.6**	**$2.8**	**$9.2**	**$2.6**	**$71.0**

Rainy Day Fund

(FY 2008 Actual, FY 2009-2010 Projected)

Congressionally Mandated Emergency (2%)/Contingency (4%) Cash Reserves



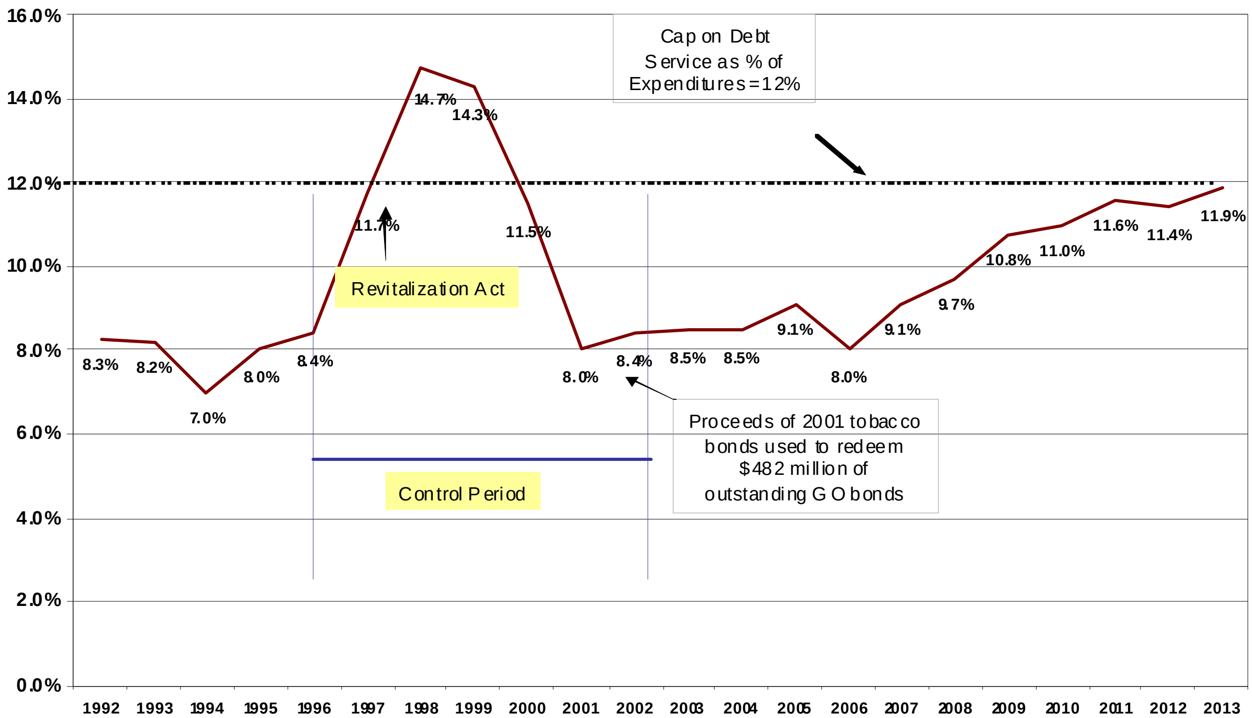
Government of the District of Columbia
Office of the Chief Financial Officer
Natwar M. Gandhi, Chief Financial Officer

1

Growing Debt Burden

Debt Service as % of Expenditures

(as of September 30 of each fiscal year)



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

ATTACHMENT E

	Local Source, General Fund Revenue Estimate ($ millions)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
1	**Revenue estimate included in June budget**	**5,562.9**	**5,831.7**	**6,099.2**	**6,402.5**	**-**
2	Change in the estimate (September 2008)	(130.7)	(151.9)	(148.5)	(162.3)	
3	**Revenue estimate of September 2008**	**5,432.2**	**5,679.7**	**5,950.7**	**6,240.2**	
4	Change in the estimate December 2008)	(127.1)	(303.8)	(330.4)	(327.5)	
5	**Revenue estimate of December 2008**	**5,305.1**	**5,375.9**	**5,620.3**	**5,912.7**	**6,216.9**
6	Change in the estimate (February 2009)	(135.7)	(346.3)	(488.3)	(613.8)	(676.9)
7	**Revenue estimate of February 2009**	**5,169.4**	**5,029.5**	**5,132.0**	**5,298.8**	**5,540.0**
8	Dollar Change in General Fund revenues compared to prior year		**-139.9**	**102.4**	**166.9**	**241.2**
9	Percent Change in General Fund revenue compared to prior year		**-2.7%**	**2.0%**	**3.3%**	**4.6%**
10	Change in the estimate since June budget	(393.5)	(802.1)	(967.3)	(1,103.7)	n/a
11	Loss sustained compared to June budget	-7.1%	-13.8%	-15.9%	-17.2%	n/a

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

ATTACHMENT F

Capital Fund Pro Forma

(Dollars in thousands; excludes Highway Trust and Local Streets Maintenance Funds)

	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	Total, FY 2010 - FY 2015	Percent of FY 2010
Sources:								
G.O. Bonds	$433,522	$501,002	$498,820	$542,851	$425,858	$418,949	$2,821,003	
Master Equipment Lease	31,636	40,894	34,814	30,739	29,468	21,346	188,897	
Pay-As-You-Go (Paygo)	2,984	0	0	0	139,269	147,818	290,071	
Subtotal, Sources	$468,142	$541,896	$533,634	$573,590	$594,596	$588,113	$3,299,971	
Additional G.O. Bonds - Large Scale Financings	16,478	20,000	5,000				41,478	
Total, Sources	$484,620	$561,896	$538,634	$573,590	$594,596	$588,113	$3,341,449	
Uses:								
Office of Public Education Facilities Modernization	$236,435	$250,202	$268,825	$288,886	$306,198	$321,508	$1,672,055	50.5%
Washington Metropolitan Area Transit Authority	72,700	73,700	74,800	78,800	81,200	83,500	464,700	15.5%
Department of Parks and Recreation	31,900	57,610	45,520	42,020	42,810	39,998	259,858	6.8%
Department of Mental Health	15,770	0	0	0	0	0	15,770	3.4%
Fire and Emergency Medical Services Department	11,846	23,686	29,726	29,716	18,896	15,536	129,406	2.5%
Office of the Chief Technology Officer	11,649	20,931	14,685	12,561	11,115	12,565	83,506	2.5%
District of Columbia Public Library	11,238	21,880	17,893	27,000	27,000	27,000	132,010	2.4%
Office of Property Management	10,260	19,570	22,730	38,050	62,620	58,000	211,230	2.2%
University of the District of Columbia	8,540	8,015	5,520	4,150	2,700	0	28,925	1.8%
Department of Consumer and Regulatory Affairs	7,000	9,000	5,000	5,000	2,500	0	28,500	1.5%
Office of the State Superintendent of Education	7,000	0	0	0	0	0	7,000	1.5%
Department of Public Works	6,500	7,560	8,800	8,800	7,800	1,500	40,960	1.4%
Department of Housing and Community Development	6,375	7,675	4,950	7,500	4,250	5,000	35,750	1.4%
Office of the Chief Financial Officer	5,600	6,200	3,200	600	0	0	15,600	1.2%
Metropolitan Police Department	5,000	11,679	9,879	10,200	10,200	10,200	57,158	1.1%
Department of Transportation	4,700	8,300	9,300	7,500	7,500	6,000	43,300	1.0%
Department of Corrections	3,750	3,582	2,000	0	0	0	9,332	0.8%
Commission on Arts and Humanities	3,585	2,700	2,700	2,700	2,700	2,700	17,085	0.8%
Office of Unified Communications	3,500	6,000	5,000	5,000	5,000	2,500	27,000	0.7%
District Department of the Environment	2,984	0	0	0	0	0	2,984	0.6%
Office of Planning	1,311	2,106	2,106	2,106	2,106	2,106	11,843	0.3%
Office of the Deputy Mayor for Planning and Economic	500	1,500	1,000	3,000	0	0	6,000	0.1%
Subotal, Uses:	$468,142	$541,896	$533,634	$573,590	$594,596	$588,113	$3,299,971	100.0%
Large-Scale Financings (Office of Property Management)								
Consolidated Laboratory Financing	$16,478	$20,000	$5,000	$0	$0	$0	$41,478	
Total, Uses	$484,620	$561,896	$538,634	$573,590	$594,596	$588,113	$3,341,449	

Note: Details may not sum to totals due to rounding.