PUBLIC OVERSIGHT HEARING

ON THE

DISTRICT OF COLUMBIA'S CAPITAL IMPROVEMENTS PROGRAM

Before the

Committee of the Whole
Council of the District of Columbia

The Honorable Linda W. Cropp, Chairman

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Council Chamber

Testimony of
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Good morning, Chairman Cropp and members of the Committee of the Whole. My name is Bert Molina, and I am the deputy chief financial officer for the Office of Budget and Planning (OBP). I am pleased to appear before you today to present testimony on the status of the District of Columbia's Capital Improvements Program (CIP). In my testimony, I will provide an update on the Capital Improvements Program, discuss ongoing challenges, and briefly outline our vision for the future.

Current Status of the Capital Improvements Program

As OBP reported at the Committee's last CIP hearing in December 2003, District agencies had made substantial improvements in the implementation of their capital projects. These improvements were also reflected in an increased rate of spending in fiscal years 2002 and 2003. While FY 2004 spending was lower than spending in FY 2003, agencies are continuing to make progress in implementing their programs. Total FY 2004 capital expenditures from local funds for District agencies were $558 million, or 89 percent of the allotment of $629 million. This number is somewhat less than FY 2003 spending of $638 million, reflecting the budget reductions that have been made in the past two budget cycles. However, annual spending continues to exceed the levels of fiscal years 1999 and 2000, when the District spent less than $400 million each year.

The District continues to benefit from improvements to its bond rating. In conjunction with our most recent bond offering, Standard & Poor's upgraded the District's general obligation bonds to A with a stable outlook, from A-, while Fitch Ratings revised its rating outlook for the District to positive from stable.

The leadership and commitment this committee has shown in demanding accountability has resulted in tangible improvements not only within the capital program, but also for the District's bottom line. However, there still remain challenges to overcome.

Ongoing Challenges

Despite the recent success the District has experienced with our improved bond rating, we still have an extremely high debt-to-equity ratio relative to other jurisdictions of comparable size. Our debt per capita, at approximately $6,800, is one of highest in the country, and is more than twice the average of other major cities. Based on these facts, the bond rating agencies consider the District's debt burden to be high, and they factor this into their rating decisions on the District's bonds. Recognizing these factors, the CIP budget was reduced from initial planning levels by $250 million and $99 million in the development of the FY 2003 and 2004 budgets respectively. Further, during development of the FY 2005 capital budget, approximately $100 million was reallocated from ongoing projects to new capital priorities. We anticipate the need for further reductions as we develop the FY 2006 capital budget.

Our current capital needs far exceed our available resources to finance and to pay debt service on the financing of such needs, as the chief financial officer has often noted in his discussion of the city's structural imbalance. Current estimates put the District's gross capital improvement needs at around $775 million annually. To maintain the District's debt burden at manageable levels, in terms of debt service cost to operating revenues and debt per capita, annual planned borrowing will have to be limited to $300 million for FY 2006 and the near future, resulting in about

$475 million of unmet needs annually. However difficult, this action is required to help maintain our bond ratings and standing in the financial markets while providing a steady stream of annual financing for the highest priority capital projects.

As noted in the FY 2003 and FY 2004 Comprehensive Annual Financial Reports (CAFRs), the fund balance for the General Capital Improvements Fund was in a negative position at the end of each year; $141.8 million and $250.2 million for fiscal years 2003 and 2004, respectively. This reflects the decision the city made several years ago to stop borrowing full amounts of budgeted spending in advance, then paying debt service, at higher interest rates, on funds that are sitting in bank accounts and earning lower interest rates. We now borrow only what we believe will be spent in a given year. Because of timing differences between capital expenditures and the receipt of bond proceeds, the General Capital Improvements Fund receives advances from the General Fund to finance capital spending. These advances are repaid when bond proceeds are received. According to the Office of Finance and Treasury, this policy has saved the District approximately $7.5 million in interest costs over the past two years (fiscal years 2003 and 2004).

The OCFO will continue to actively and aggressively monitor this process. Given the present level of the $250 million advance to the Capital Improvement Program, the District's General Fund cannot afford to increase the level of self-financed, interim borrowing for the Capital Improvements Program. Thus, we are aggressively managing this process to attain two goals:

- Continue to achieve savings in interest costs by not borrowing more or sooner than necessary, and

- Ensure that the General Fund advances to the General Capital Improvements Fund remain in a range that does not create cash flow problems and is managed in a manner that is consistent with District policy. As part of this policy, $40 million of the General Fund's fund balance for FY 2004 has been designated as pay-as-you-go capital.

Plans for the Future

As you know, Chairman Cropp and other members of the committee, one of our greatest challenges in the capital program is bringing into alignment our future demands and our projected resources. The demands of our largest capital consumers, namely WMATA and D.C. Public Schools (DCPS), have contributed to a major imbalance between projected expenditures and borrowing capacity. For example, the District is required to contribute approximately $50 million to WMATA in FY 2006, as part of the investment in the system known as "Metro Matters." In addition, DCPS has prepared a 10-year modernization plan that will require over $100 million each year. Given the District's entire borrowing capacity is only $300 million per year, we face a major conflict between resource demand and resource availability.

To address this issue, last year the Mayor and Council created the Master Facility and Program Integration Planning Process. This process ensures a comprehensive assessment of District facilities and should result in an integration plan that will not only improve service delivery at the neighborhood level, but will also propose an allocation of scarce capital dollars according to our highest priorities. As part of this process, a Technical Review Team (TRT) is reviewing FY 2006 capital budget requests and spending plans for technical merit, feasibility, and opportunities for co-location of new facilities.

As we did last year, we have also instructed agencies to have condition assessments completed and submitted prior to their capital budget. Requests will again be ranked and prioritized as the TRT focuses on health and safety projects or mission critical initiatives. Agencies are required to demonstrate their ability to implement their existing capital projects prior to any consideration of new funding.

We are improving our data management and reporting capabilities in the capital area to mirror the progress we have made in the operating budget. To accomplish this goal, we are using CFO$ource (the Web-based tool allowing improved reporting on SOAR data, including the dashboard we have demonstrated for the Council), as well as ARGUS (the new District-wide budget system). For example, agencies are now using a spending plan application in CFO$ource to develop and monitor capital spending plans. We plan to increase transparency by enhancing our reporting on capital activity and putting more capital information on the CFO$ource dashboard.

In addition, OBP will strengthen central budget office oversight and internal control functions with regard to the capital program. We want to ensure that the District's capital budget formulation and execution always stands up to our rigorous budgeting and accounting principles and standards. In support of this effort, I have asked the OCFO's Office of Integrity and Oversight to review our budgetary and financial controls in capital.

As always, the Office of Budget and Planning is committed to working collaboratively with you, Madam Chairman, this committee and the Council, stakeholders and agencies to improve the effective and efficient operations of the capital program.

Madam Chairman, thank you for the opportunity to testify today. I will be happy to respond to any questions that you may have.

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