

**PUBLIC OVERSIGHT HEARING ON
THE FISCAL YEARS 2012 AND 2013 SPENDING AND
PERFORMANCE BY THE OFFICE OF REVENUE
ANALYSIS (ORA) OF THE OFFICE OF THE CHIEF
FINANCIAL OFFICER (OCFO)**

**Before the
Committee on Finance and Revenue
Council of the District of Columbia**

The Honorable Jack Evans, Chairman

**March 7, 2013
10:00 a.m.
Council Chamber, John A. Wilson Building**



**Testimony of
Fitzroy Lee
Deputy Chief Financial Officer
Office of Revenue Analysis**

**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 Fitzroy Lee, Deputy Chief Financial Officer for the Office of Revenue Analysis and Chief Economist. I am pleased to appear before you today to testify on the performance of the Office of Revenue Analysis (ORA) in FY 2012 and thus far in FY 2013.

Mission of the Office of Revenue Analysis

ORA's mission is threefold: (1) to provide quarterly revenue estimates that set the spending ceiling for the District of Columbia's four-year budget and financial plan; (2) to provide policymakers with information to maintain budget balance by estimating the fiscal impact of legislation drafted by the Mayor and Council; and (3) to conduct a wide range of fiscal and economic research and analyses on an ongoing basis and at the request of the Mayor and Council, or as directed by the Chief Financial Officer (CFO).

Revenues and Revenue Estimates

For the second year in a row the District's revenue grew strongly, as the economy continues to rebound from the downturn 4 years ago. The strong revenue growth of almost 11 percent for fiscal year 2012, contributed largely to the \$417 million surplus at the end of the year. Of the \$417 million surplus, \$266 million was due to additional revenues, of which about \$50 million was from a one-time estate tax

windfall and another \$30 million from better than expected performance of newly installed automatic traffic enforcement equipment. But the \$78 million of the surplus that came from business taxes, \$68 million from sales taxes, and \$44 million from individual income taxes is the real measure of the strength of the District's economy in fiscal year 2012.

Sales tax revenue in fiscal year 2012 grew at an unprecedented rate of almost 10%. The District's fast-growing population of relatively high-income earners as well as a growing retail base, which has reduced the leakage of District retail spending to the surrounding suburbs, drove the strong revenue performance of sales tax revenue. The Nationals reaching the playoffs and election year spending by political campaigns also boosted sales tax revenue in fiscal year 2012. Sales tax revenue growth is expected to remain strong in FY 2013, growing 5.6%, but growth in the future will moderate as federal cutbacks take effect.

Individual income tax revenue grew 15% in FY 2012. Some of this growth was from one-time sources (in particular, tax compliance initiatives such as the exclusion of the standard deduction from the withholding tax calculation and the increase in the safe-harbor threshold from 100% to 110% of the prior year's tax liability), but the major cause of the strong growth, as for the sales tax case, was the District's fast growing population of high-income earners. Although the strong stock market

performance of the previous year boosted revenue from capital gains, a greater share of the growth was from the withholding portion of the income tax, which is tied to the wages and salaries of District's residents. Individual income tax revenue growth is expected to remain strong at 6% in FY 2013, after adjusting for one-time impacts in FY 2012. But the full implementation of federal austerity measures, offset somewhat by a windfall from the New Year's Day federal income tax changes (specifically, the exemption phase out for high-income tax payers) , will slow growth to 1.2% in FY 2014 and moderate revenue growth thereafter.

In fiscal year 2012, revenue from business income taxes grew 30%. Unusually high business profits in calendar year 2011, leveraged by several policy changes (such as the requirement for combined reporting, a switch to double-weighted sales apportionment formula, and higher minimum taxes), significantly boosted the revenue from business income taxes. This confluence of factors in the District's favor is not expected to be repeated going forward. With the prospect of federal government austerity, business income tax revenue will grow only 0.8% and 1.4% for FY 2013 and FY 2014, respectively.

Given the solid revenue gains achieved in fiscal year 2012, and continued strong growth in the District of Columbia's population of mostly high-income earners, at

the end of February we revised the revenue estimate upward by \$190 million for fiscal year 2013 and by \$178 million for fiscal year 2014.

Economic and Fiscal Outlook

As was true last year, a high degree of uncertainty still clouds the future course of both the national and local economies. The biggest sources of uncertainty are the measures that the federal government may take to reduce federal deficits in a period of austerity that may last for some time. Our February revenue estimate assumes that some significant measures to reduce federal spending will be enacted in the near future.

As noted above, the latest revenue forecast builds on the solid revenue gains achieved in FY 2012, and anticipates continued strong growth in the District of Columbia's population. Population growth has been a major factor in increasing the District's income and sales tax bases, and is also a major driving force behind rising home values. Over the past year, however, growth in employment located in D.C. has almost come to a halt, commercial office vacancies are rising, and tourism growth has slowed considerably as federal austerity measures begin to bite. The economic effects of this slowing appear likely to affect the tax base for at least the next few years.

Fiscal Impact Statements (FIS)

During fiscal year 2012 the FIS team produced 354 fiscal impact statements. Additionally, the FIS team worked with the Economic Development Finance unit in developing the Economic Development Budget report—they compiled a list of all the abatements and exemptions approved by the Council and the Mayor, and estimated the cost of these tax exemptions through 2020.

Fiscal impact statements are important tools in maintaining budget balance—these analyses ensure that no new legislation is put in place without the necessary funding. In this difficult budget environment, correctly determining the potential cost of proposed legislation is crucial to protecting the city from additional financial risks. The FIS team will continue to carefully research all legislative proposals and scrutinize all input from all agencies of the DC government. They will also continue to work very closely with District government agencies and the Council staff. The FIS team is now organized to be more closely aligned to the committee structure in the Council, and we actively monitor the legislative timeline to ensure we have sufficient time to conduct thorough analyses of proposed bills.

Research and Analyses

In addition to the revenue estimates and fiscal impact statements, ORA provides District stakeholders with a number of fiscal and economic reports, all of which are

subject to an extensive internal and external peer-review process prior to release and publication. These include:

- *DC Economic Indicators*, which is published monthly and provides a two-page “at a glance” overview of four key sectors of the DC economy: (i) “labor and industry” information on District employment trends, along with the composition of resident employment by industry; (ii) “revenue” collections by major tax types; (iii) “DC and US economic information,” including DC personal income, inflation, and unemployment rate trends; and (iv), “real estate” information on home sales volume and prices and commercial office vacancy rates and inventory.
- *A Review of District of Columbia Economic and Revenue Trends*, which is published monthly and provides a wealth of information on all aspects of the DC economy, including employment, wages, housing, commercial office space, and the hospitality and retail industries.
- *Tax Rates and Tax Burdens: Washington Metropolitan Area*, which is published annually and provides not only a comparison of the District’s statutory rates with its five neighboring jurisdictions (Alexandria and the counties of Montgomery, Prince George’s, Arlington and Fairfax), but also comparative measures of household tax burden by type of tax for different income levels.

- *Tax Rates and Tax Burdens in the District of Columbia: A Nationwide Comparison*, an annual publication that provides a compendium of statutory tax rates and estimates of the household burden of major taxes by income class in the District compared with the largest city in each of the 50 states. The summary table from this report is generally reproduced in the annual *Statistical Abstract of the United States*.
- *The Economic Report of the District of Columbia (Data Book)*, an annual publication that provides detailed data on the District's economy and its revenue system.
- *DC Tax Facts*, an important and widely used pocket-sized reference of District tax collections and describes all of the District's revenue (tax and non-tax) sources, the history of major revenue changes since 1970, filing and payment dates, and the yield of each revenue source utilized by the District.
- ORA also publishes a monthly table of *Cash Collections*, as well as a *Cash Collections Narrative Report* that tracks cash collections by source. This report is critical in monitoring the performance of District revenue collections relative to the revenue estimate.
- *Tax Expenditures* is a biennial report that catalogues and quantifies revenue losses from federal and District tax provisions that grant special relief designed to encourage certain kinds of taxpayer behavior or to aid taxpayers in special circumstances.

- Periodically, ORA produces results of its other research findings that are then shared with the Mayor and the Council, as well as the public. During fiscal year 2012, *Special Purpose Revenues* and *Non-Tax Revenues* were two of such reports published by ORA.
- ORA has been instrumental in providing the newly created *Tax Revision Commission* with results of its findings and analysis of alternative tax policies, based on the Commission's requests.
- Each year the ORA is responsible for the preparation of the Revenue chapter that is included in both the Mayor's *Proposed Budget and Financial Plan*, and then, with Council revisions, the Executive Summary of the *Budget and Financial Plan* that is submitted to Congress (June). The Revenue chapter begins with a comprehensive review of the US and District's economic outlook and then proceeds to present in great detail information on the revenue flows by revenue source over the financial plan period. The revenue presentations include detailed as well as summary tables of the baseline revenue estimate and policy proposals included in the budget.

Conclusion

Finally, I want to thank the entire ORA team for their hard work and professionalism during what has been a very challenging year for the District. I would like to thank my entire staff at ORA for their rigorous support and efforts, and especially the

Directors, for the leadership and teamwork they displayed, not only within ORA, but also in working with other agencies within the Office of the Chief Financial Officer as well as with the Executive and the D.C. Council. This concludes my testimony. I would like to thank you for the opportunity to testify before you today. I am pleased to respond to any questions that you may have.

Chart 1

