

**HEARING ON H.R. 960,
“DISTRICT OF COLUMBIA LEGISLATIVE AUTONOMY ACT OF 2009”
AND H.R. 1045,
“DISTRICT OF COLUMBIA BUDGET AUTONOMY ACT OF 2009”**

**Before the
U.S. House of Representatives
Committee on Oversight and Government Reform
Subcommittee on Federal Workforce, Postal Service, and the
District of Columbia
The Honorable Stephen F. Lynch, Chairman**

**November 18, 2009, 10:00 a.m.
Room 2154, Rayburn Building**



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

Good morning, Mr. Chairman and members of the Committee. My name is Natwar M. Gandhi, and I am the Chief Financial Officer for the Government of the District of Columbia. I am here today to testify before this Subcommittee on the issue of budget autonomy for the District of Columbia.

Before I begin, I must note that little has changed since I addressed this body two years ago on the same topic. As I noted then, I wholeheartedly endorse expanding the authority of the District to manage its own financial affairs. Not only do I believe that the District's leadership has demonstrated its ability to adhere to principles of fiscal responsibility, I also believe that greater budget autonomy would provide the citizens of the District as well as visitors with the highest quality of public services in a timely manner.

Today, I will give a short history of the fiscal affairs of the District of Columbia and I will comment on where we stand today with regard to the pressures caused by the national recession. I will address the specific reasons why I believe that greater budget autonomy is warranted for the District.

Fiscal Recovery Since 1996

The chart that appears as Attachment A to my remarks and that appears here before you is a history of the remarkable fiscal comeback achieved by the District over the past dozen years. It is a great testimony to the financially responsible budgeting and fiscal prudence exercised by the District's elected leadership. Our fiscal low point occurred in FY 1996, when the General Fund balance hit a negative \$518 million. Through the efforts of Mayor Williams, the District Council and the Congressionally mandated Control Board, we were able repeatedly

to balance the District's fiscal operations, and the Control Board was de-activated in 2001. Between FY 1996 and the end of FY 2001 there was a \$1.1 billion increase in the fund balance, to a positive \$562 million by the end of FY 2001.

But the real test for the District was the challenge of sustaining fiscal stability in the post-control period. As you can see, at the end of FY 2005, the General Fund balance rose another \$1 billion – to \$1.6 billion total, a turnaround of more than \$2 billion since FY 1996 when the fund balance was a negative \$518 million. This improvement was reflected in the credit ratings assigned to the District by the major bond rating agencies. Our general obligation bond ratings, which were “junk bond” status in the mid – 1990s, were upgraded every year through FY 2005 and again in FY 2007 to the current “A1” and “A+” ratings today. Indeed, the turnaround by the District was faster than any major city that experienced severe fiscal distress, including Philadelphia, Cleveland, Detroit and New York.

In addition, our Income Tax Secured Revenue Bonds, issued for the first time in March of this year, were assigned a rating of triple-A, the highest possible rating, by Standard & Poor's and double-A by Moody's Investors Service and Fitch Ratings, above the general obligation bond rating and the highest ratings ever assigned by those agencies. I should note that the initial offering of \$801 million of the Income Tax Bonds has been nominated for “Deal of the Year” by the *Bond Buyer*, the newspaper that covers the municipal bond industry. This is a remarkable achievement for a city that was in dire financial straits only a dozen years ago.

Since that time, the District's elected leadership has chosen to use some of that fund balance to provide for much needed one-time expenditures, such as

supplements to our contribution to the Other Post-Employment Benefits (OPEB) Trust and pay-as-you-go capital expenditures (PAYGO). As a result, at the close of Fiscal Year 2008 the District’s General Fund balance stood at about \$1.2 billion.

A great deal of the increase in fund balance was driven by the growth in local revenues, specifically by real estate, income and sales taxes resulting from the strong regional economy. Table 1 below compares tax revenues, General Fund balance and reserve funds in FY 1996 and in FY 2008, and reflects the revenue growth (an increase of 111 % in current dollars and 54% in inflation adjusted “real dollar” terms). However, prudent fiscal leadership and responsible financial management provided by both Mayor Williams and Mayor Fenty and the Council contributed substantially to the increased General Fund balance.

Table 1		
Comparison of Key Financial Measures		
<i>(\$ in thousands)</i>		
	FY 1996	FY 2008
Tax Revenues *	\$2,422,144	\$5,106,963
Operating Surplus/(Deficit)	(\$33,688)	\$191,370
General Fund Balance	(\$518,249)	\$1,244,722
Reserves Available for Operations **	(\$332,357)	\$416,963
Operating Reserves as % of Expenditures	--	6.7%

* Net of Dedicated taxes.

** Includes Congressionally-mandated Emergency and Contingency Reserves plus unreserved undesignated General Fund balance.

It is too early to state what the FY 2009 closing fund balance will be, because we are in the midst of the year end procedures that will produce final numbers for the fiscal year. What I can say is that there were significant budget challenges caused by estimated revenue reductions of nearly \$600 million between June 2008 and June 2009, a result of the pressures of the national recession. Mayor Fenty and the

Council reacted quickly each time there was a revenue re-estimate to close the budget gaps that were created by the lower forecasts. Because of this drop in revenue, almost certainly there will be a further drop in the fund balance, but not to the point where the financial viability of the District is endangered. Indeed, the District is obligated to keep Emergency and Contingency Funds of 6 percent of the budget on hand to pay for events such as natural disasters or needs not foreseen at the time of budget formulation.

Let me note here that the District and nearly every other state and local government in the nation have been profoundly affected financially by the depth and duration of the recession. What will distinguish the District when we look back at this period is our absolute commitment to balancing our budget. For the current fiscal year, FY 2010, Mayor Fenty proposed and the District Council, under the leadership of Chairman Gray, adopted the District budget using the same conservative budgeting principles and sound financial practices that the District has followed since the end of the Control period. As pointed out earlier, the measure of this success is reflected in the District's bond ratings.

Budget Autonomy

I would now like to speak about why I believe, from a financial management perspective, the District should have discretion with respect to the allocation of funds raised from local sources.

Under current law, all District of Columbia spending is authorized by the Congress through the federal appropriations process, irrespective of the source of revenue underwriting such spending. In the District's FY 2010 proposed gross budget of \$8.8 billion, about \$6.0 billion, or 68 percent, comes from revenues raised through

local taxes, fees, fines, and user charges. Only \$188 million in federal payments were specifically requested in the FY 2010 President's Budget from federal revenues for programs and projects unique to the District of Columbia. The balance is comprised of formula-based federal grants which are available to all jurisdictions nationwide.

I would argue that only the federal payments that are specifically and uniquely earmarked for District programs or federal initiatives should be appropriated by the Congress. In the case of local funds, the Congress has rarely altered an allocation made by the District. Federal grants to the District have already been appropriated to the federal agency responsible for program administration and awarded to the District. Having already been appropriated to a federal transferring agency, these federal grants should not need to be "re-appropriated" to the District.

Were the Congress to modify current law in the direction of reducing its role in the District's appropriation process, a range of possibilities would still remain to exercise oversight over the District's budget and operations. These might include periodic audits, after-the-fact review of the District's locally enacted budget, or review of the District's locally enacted budget by the appropriate oversight group in the Congress. Federal payments directly appropriated to the District would remain within the federal appropriations process.

Benefits to the District

Faster and smoother enactment of budgets. Because the District currently receives all its authority to spend funds only through the federal appropriations process, the District cannot enact the budget approved by its elected representatives until Congress passes and the President signs the District's appropriations bill. This

situation guarantees a four-month lag between local approval and federal enactment. However, federal appropriations bills are often delayed beyond this period. There are adverse consequences for the District since it is tied to the federal appropriations cycle. In the case of new or expanded programs approved and financed locally or with federal grants, no action can be taken during the fiscal year until Congress passes its appropriations act, or includes language in the Continuing Resolution to permit the District to spend these funds at the approved level. For years, the CR's have included just this language, thereby removing the unnecessary and unfortunate delays in programs that had previously existed. This extra effort with the language in the CR is very much appreciated, but it is never certain. With budget autonomy, it would not be necessary.

Also, the more time that elapses between the formulation of a budget and its execution, the more likely the operating assumptions underlying that budget will not hold true. Thus another critical aspect of faster budget enactment would be that budgets could be based on more current revenue estimates. This became apparent this summer when my office issued a new revenue estimate June 22, after the Council had approved the budget, but before Mayor Fenty had returned it to Council with a single line-item veto.

The June estimate showed a drop of \$190 million of revenue in FY 2009, and a projected drop of \$150 million in FY 2010, forcing the Mayor and Council to go back to the drawing board. To their great credit, both Mayor Fenty and Council moved swiftly to revise the budget to reflect the lower revenues, but this was far from an optimal way of doing business.

If the District Council were able to set its own schedule to enact a budget (for

example, for a fiscal year starting in October, budget enactment might be in September rather than in May), the Mayor and legislators could always rely on revenue estimates based on more current data. Currently, budgets are based in large part on revenue estimates completed in February, some seven months before the start of the new fiscal year in October and a total of 20 months before the end of that fiscal year. The District does not get actual data on how accurate these revenue estimates are, and whether budgeted expenditures are fully covered, until after the end of that fiscal year, almost 2 years after the original revenue estimates were made.

Maximum Local Financial Flexibility. Providing the District with the authority to direct the spending of its locally raised revenue would substantially increase the District's ability to react to changing program and financial conditions during a fiscal year. Under current law, the District must follow the federal supplemental appropriation process to appropriate additional revenues that become available during the course of the fiscal year or to make any significant realignment in resources among its appropriations. All program plans premised on supplemental appropriations are held in abeyance while Congress considers the request.

It should be noted that since the early part of the decade, Congress has provided increasing degrees of budget flexibility to the District. Currently, if our revenues exceed projections, the District is allowed to increase our appropriations ceiling. Specifically, if local tax base revenues increase, spending of that revenue source may be increased up to 6 percent. Similarly, if dedicated revenues or O-type revenues increase, spending in that category may be increased up to 25 percent. However, this authority still requires a 15-day Congressional review

period during which the monies cannot be spent. Also, the authority is not permanent but is derived from a general provision in an annual appropriations bill that must be continually renewed.

As you can see from these examples, because of the lack of permanent budget autonomy, the District cannot always react as swiftly or effectively as possible to meet the needs of residents and visitors. To the best of my knowledge, no other municipality in the nation functions under such restrictions.

Mechanisms and Safeguards for Assuring Financial Integrity

The District of Columbia Financial Responsibility and Management Assistance Act of 1995 (the Act), coupled with the continuation of an independent Office of the Chief Financial Officer, provides the framework for assuring financial integrity without the need for imposing the federal appropriation process on local fund budgets. The Act details specific benchmarks for financial management within the District and provides for the reinstatement of a control board and other constraints if the District fails to meet these major financial obligations. These financial benchmarks remain in effect under the proposed Budget Autonomy legislation.

Further, in October 2006, Congress enacted the 2005 District of Columbia Omnibus Authorization Act, which re-established, within the District's Home Rule Act, a permanent Office of the Chief Financial Officer. The Office of the Chief Financial Officer provides an independent assessment of key financial data – annual comprehensive financial reports, revenue estimates, fiscal impact statements, and all other consequential financial data. The Chief Financial Officer's duties are not changed by the proposed Budget Autonomy legislation. I believe that the existence of an independent Chief Financial Officer, chartered by

the Congress to oversee the fiscal stability of the District, along with the prudent financial leadership demonstrated by our elected officials, is sufficient to ensure fiscal discipline without the added complexity of putting local spending plans through the federal appropriations process.

Fiscal Condition and Financial Improvements

There is no question that the District has the financial infrastructure to permit it to manage its local funds effectively. We have a strong accounting system linked to our budget oversight processes. Monthly closings and cash reconciliation are in place. Financial managers have a clear understanding of expectations. The improved financial reporting infrastructure has enabled the OCFO to supply elected leaders with sound fiscal analysis. Clean audit opinions by the District's independent auditors have become routine. Moreover, since the deactivation of the Congressionally created control board in 2001, the District's elected leaders have achieved an exemplary record of fiscal prudence. Financial markets have recognized it in the form of higher bond ratings and lower interest rates on our borrowing.

In summary, the District's leadership has the will and the necessary resources to make informed decisions and the District has a proven record of functioning in a fiscally responsible manner. Based on this commendable record, our elected leadership deserves a greater degree of confidence in the form of budget autonomy.

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 19 percent and child poverty rate of 33 percent are among

the highest in the nation and more than three times the comparable rates across neighboring counties.¹

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.

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 unfunded mandates that restrict the District's own taxing power.²

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

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 percent poverty and 7 percent child poverty.

² In 2003, the General Accounting Office (now Government Accountability Office) calculated this preemption to be between \$470 million and \$1.1 billion annually. (GAO, District of Columbia Structural Imbalance and Management Issues, May 2003.)

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 and federally-owned commercial-like properties in the District (excluding the monuments, the Mall, Capitol Hill and the Federal Triangle), the commercial real property tax base would rise by 40 percent and, in turn, generate additional tax revenues of \$540 million. Further, the Congressional imposition of a height limitation on buildings prevents the District from maximizing its limited land mass as a revenue source.

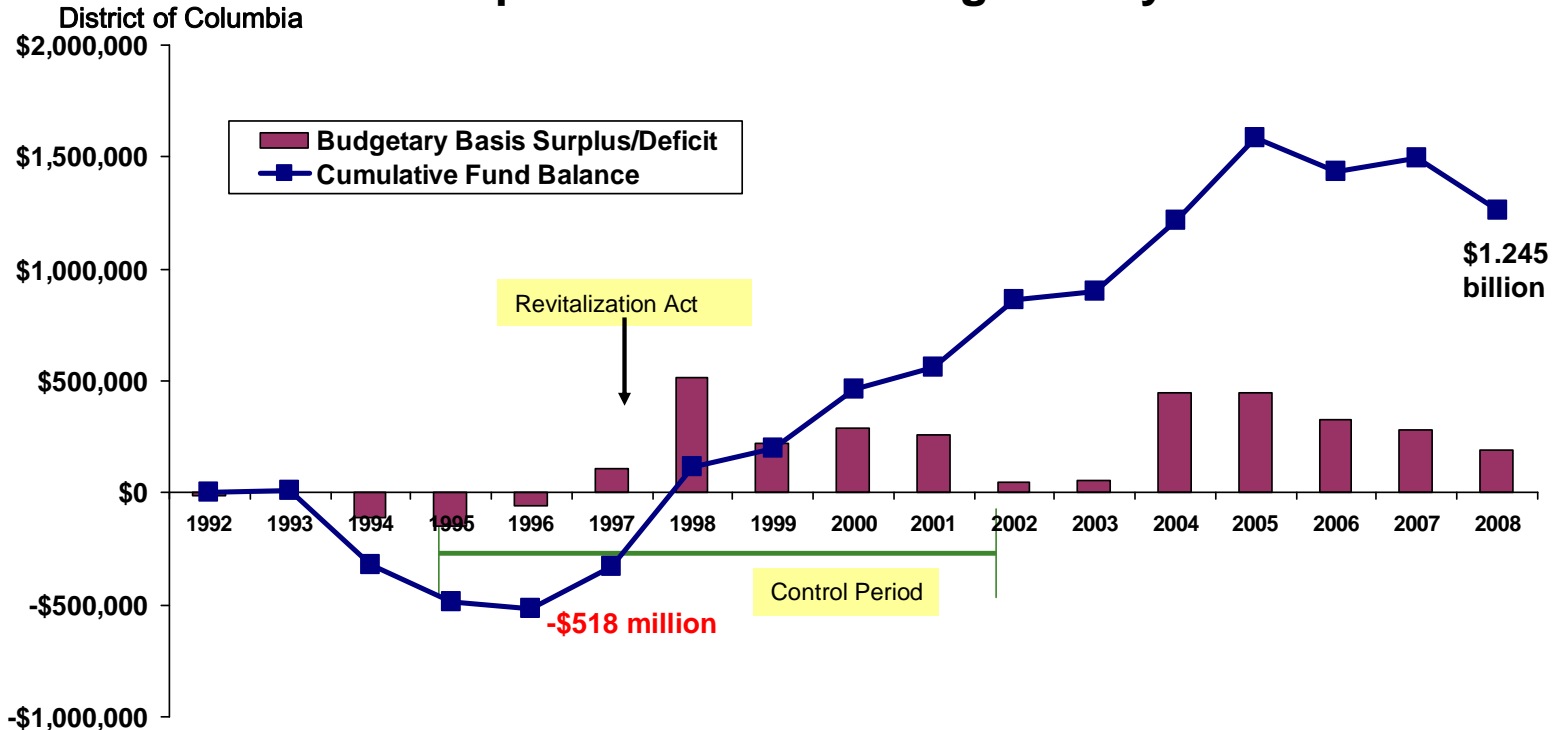
Because of the inability to tap these resources, our residents must shoulder a disproportionate share of the cost of providing public services, while the benefits generated by the city's taxpayers are shared by a much larger non tax-paying community. The nation's current economic condition, combined 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.

Mr. Chairman, this concludes my remarks. I would be pleased to answer any questions you might have.

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Surplus and Bond Rating History



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