PUBLIC BRIEFING

THE MAYOR'S FY 2005

PROPOSED BUDGET AND FINANCIAL PLAN

Before the

Committee of the Whole
Council of the District of Columbia

The Honorable Linda W. Cropp, Chairman

March 29, 2004; 2:00 p.m.
Council Chamber

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

Good afternoon, Chairman Cropp, Mr. Evans, and members of the Committee of the Whole. I am Natwar M. Gandhi, Chief Financial Officer for the District of Columbia, and I would like to offer brief remarks about the Fiscal Year 2005 Proposed Budget and Financial Plan.

The Office of the Chief Financial Officer has worked with the executive leadership team, as well as agency program and budget staff, to address numerous budget issues to produce a balanced budget. We will continue to support this collaborative process as the Council deliberates.

FY 2005 Budget and Financial Plan Overview

The proposed FY 2005 gross funds operating budget is $6.25 billion, an increase of $545.6 million, or 9.6 percent, over the approved FY 2004 gross funds budget of $5.70 billion. The local funds component of this budget is $4.17 billion, an increase of $340 million, or 8.9 percent over the approved FY 2004 local budget of $3.83 billion. The federal funds component of this budget is $756.6 million, an increase of $8.0 million, or 1.1 percent over the approved FY 2004 budget of $748.6 million. The federal Medicaid payment component of this budget is $993.1 million, an increase of $100.8 million, or 11.3 percent over the approved FY 2004 budget of $892.3 million. The private grant funds component of this budget is $13.3 million, a decrease of $453,000, or 3.3 percent from the approved FY 2004 budget of $13.8 million. The special purpose revenue funds component of this budget is $309.8 million, an increase of $65.3 million, or 26.7 percent over the approved FY 2004 budget of $244.5 million. Attached to my testimony are two charts that provide more detail.

Expenditure Growth Rates

The expenditure growth rate for FY 2005 does not set the mold for FY 2006 and beyond. Expenditures are expected to grow at 4.1, 4.6, and 4.3 percent for fiscal years 2006, 2007, and 2008, respectively. It is important to note for these out years that Medicaid is projected to grow at 6 percent annually. It is clear to the District's elected leadership that the FY 2005 local funds expenditure growth of 8.9 percent, or $340 million, is not sustainable. The Mayor's FY 2005 Proposed Budget and Financial Plan includes the impact of $94 million in FY 2004 spending pressures that are recurring in nature. The FY 2005 baseline budget, the starting point for the formulation of the Mayor's proposed budget, includes important budget corrections or increases to recognize the true cost of providing the current level of services, including entitlements, court order compliance costs, attainable projections of Medicaid reimbursements, and operating costs of completed capital projects. Due to the District's history of experiencing chronic spending pressures, the baseline budget was built on a realistic but not an overly conservative assessment of operating costs.

The Balancing Proposal

The executive branch began the formulation of the proposed budget with a $249.8 million gap, the difference between baseline revenues and expenditures. Mayoral enhancements of $45.5 million and baseline budget fixes of $16.9 million increased the FY 2005 budget gap to $312.2 million. After a baseline revenue adjustment of $6.4 million, the Mayor took the following actions to balance the FY 2005 operating budget:

1) Drew down $54.0 million of unreserved fund balance, in addition to the $26.0 million that was already assumed as part of the baseline budget;

2) Utilized $58.8 million of tobacco trust funds;
3) Reduced the contingency reserve contribution by $8.3 million, to set aside only the legally minimum level;
4) Cut expenditures by $62.6 million;
5) Transferred $28.1 million of eligible costs to special purpose funds;
6) Capped the dedicated revenues of the Housing Production Trust Fund to $20 million per year, re-directing $20.5 million to local funds;
7) Raised miscellaneous fees, permits and fines to produce additional revenues of $47.8 million; and,
8) Raised selected taxes by $27.4 million.

On a net basis, the Mayoral gap closing actions produced an FY 2005 operating surplus of $1.7 million.

To balance the remainder of the General Fund five-year financial plan (fiscal years 2006 through 2008), the proposed budget continues the following through FY 2008:

A) the annual $20.0 million cap on Housing Production Trust Fund dedicated revenues;
B) maintenance of the enhanced revenues from fees, permits, fines and taxes; and
C) utilization of Tobacco Trust Funds for local funds purposes.

In addition, the plan requires the deferral of additional tax parity provisions through FY 2007.

The Impact of the Structural Imbalance

It is precisely these types of actions needed to balance the five-year plan that demonstrate the impact of the District's structural imbalance. As noted by the U.S. General Accounting Office, the District has a substantial recurring need for infrastructure improvements and has a disproportionate number of persons living at the federal poverty level who need a wide range of human support and educational services. These factors, combined with a high cost of living, result in a structural imbalance between resources and needs, ranging from $0.5 billion to $1.1 billion per year. This problem is particularly evident during economic downturns, when demands for social services are even higher, but fewer resources from the District's economically sensitive taxes are available to meet program needs.

Impact on FY 2006 and Beyond

It is important to note the impact of the proposals in this budget submission on the subsequent years of the multi-year plan. The first is that virtually all projected subsequent year revenue increases will need to be dedicated to meeting baseline costs. Any flexibility to fund new program initiatives will have to come from corresponding program reductions elsewhere or additional revenue enhancements. Second, the proposal assumes that the provisions of the Tax Parity Act are further deferred for two years, so that tax reductions would resume in FY 2008 rather than FY 2006. Third, the set-aside for the tobacco trust fund has been eliminated and the funds will continue to be used to cover operating expenses.

While I am committed to protecting the fiscal integrity of the District at all costs, I want to emphasize what I believe are some of the effects of the District's long-term fiscal structural imbalance. Due to the structural imbalance, the District is forced to tax its residents and businesses at higher tax rates than the surrounding jurisdictions just to provide basic-level services. As a result, attempts to reduce the tax burden in the District must be delayed, so that we can continue to finance policy priorities and government operations, or essential services will have to be cut to balance the budget in the out years.

As the following charts illustrate, if the District were to proceed with Tax Parity and funding of the Tobacco Trust Fund per current law, expenditures would significantly exceed revenue not just in FY 2005, but for the foreseeable future. By suspending Tax Parity and the Tobacco Trust Fund, the District is able to maintain a balanced budget. Again, these choices are not easy, but the structural imbalance forces us to make these and other difficult choices.

Chart 1: Projected Revenues and Expenditures FY 2005-2008 including Tax Parity and Funding the Tobacco Trust Fund

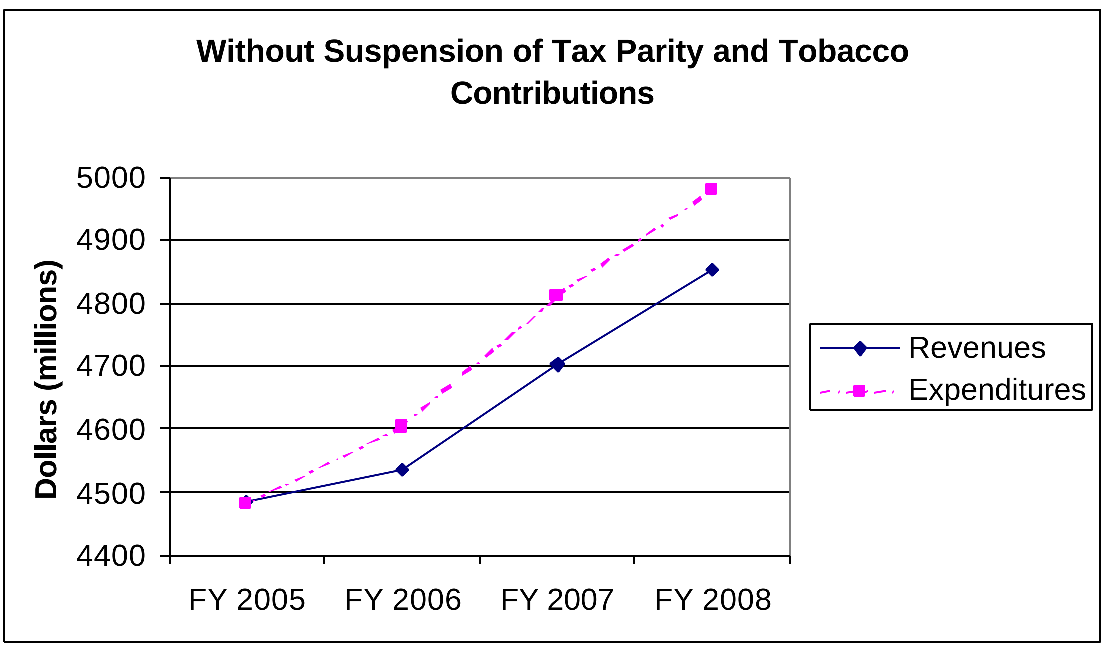
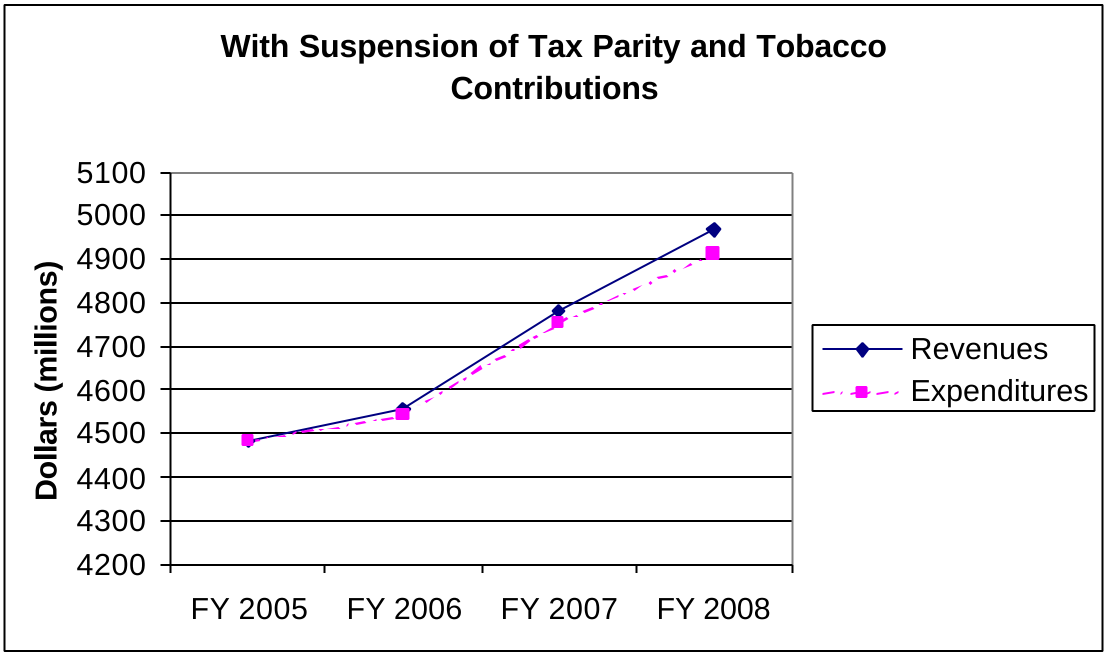


Chart 2: Projected Revenues and Expenditures FY 2005-2008 without Tax Parity and not Funding the Tobacco Trust Fund



The District's FY 2005-2010 Capital Improvement Plan (CIP)

The proposed FY 2005 capital budget is $556 million, and the six-year total budget is $1.96 billion. The FY 2005 –FY 2010 local CIP proposes an increase in funding of $824 million over the next six fiscal years for 97 ongoing projects and 114 new projects, with a rescission of $418 million. The net increase of funding is $406 million. D.C. Public Schools constitutes the majority of the planned expenditures, and a significant portion of the funding also goes to the Washington Metropolitan Area Transit Authority and the Office of the Chief Technology Officer. This budget proposes $389 million in General Obligation Bond funding, $101 million in reallocated General Obligation Bond proceeds, $37 million in Rights of Way funding, $19.5 million in Equipment leases, $5 million in sales of assets, and $3.5 million in other grants.

Performance-Based Budgeting

This budget also continues our progress in implementing performance-based budgeting (PBB), increasing the total number of agencies transitioned to 57. Under PBB there is a clear relationship between the funding agencies receive, the programs they operate, and the results that they must achieve. Agency narratives have been restructured to better emphasize this relationship. In addition, we have begun the process of developing program benchmarks to supplement the program information in the budget documents. The benchmarks will assist all District officials, as well as the public, to more clearly assess the value of the District's programs and determine where opportunities for improvement exist.

While the District continues to face fiscal challenges, I know that the leadership provided by the Mayor and the Council, along with the hard work of the Office of Budget and Planning and others in the Office of the Chief Financial Officer, allowed us to produce a balanced budget for FY 2005. As a result, I am certifying that the FY 2005 Budget and Financial Plan, as proposed, is balanced for FY 2005 and beyond.

I look forward to continuing to work with the Mayor and the Council during the forthcoming budget deliberations.

FY 2005 - FY 2008 Proposed Budget and Financial Plan: General Fund
($ thousands)

	Revenues	FY 2003 Actual	FY 2004 Approved	FY 2004 Adjusted	FY 2005 Proposed	FY 2006 Projected	FY 2007 Projected	FY 2008 Projected
1	Taxes	3,293,374	3,339,913	3,441,217	3,628,730	3,822,365	3,978,086	4,122,775
2	General Purpose Non-Tax Revenues	315,780	289,201	286,672	292,447	284,699	289,940	286,290
3	Special Purpose (O-type) Revenues	164,125	191,943	191,943	208,624	212,023	215,152	218,448
4	Transfer from Lottery	72,050	70,200	70,200	71,100	71,100	71,100	71,100
5	**General Fund Revenues**	**3,845,329**	**3,891,257**	**3,990,032**	**4,200,901**	**4,390,187**	**4,554,278**	**4,698,613**
6	Fund Balance Use	21,527	149,093	182,018	189,621	9,710	9,710	9,710
7a	Revenue Enhancements	0	38,760	0	87,301	127,130	127,687	128,145
7b	Suspension of Tax Parity	0	0	0	0	24,000	77,129	117,000
8	Transfer from Federal and Private Resources	0	0	0	6,361	6,502	6,660	6,827
9	**Total General Fund Resources**	**3,866,856**	**4,079,110**	**4,172,050**	**4,484,184**	**4,557,529**	**4,775,464**	**4,960,295**
	Expenditures (by Appropriation Title)							
10	Governmental Direction and Support	209,864	226,974	241,074	304,928	286,283	294,922	304,008
11	Economic Development and Regulation	135,234	185,446	187,146	222,456	156,956	161,026	165,333
12	Public Safety and Justice	659,479	735,660	747,060	790,455	814,242	841,114	869,934
13	Public Education System	916,725	990,016	1,018,016	1,057,288	1,085,585	1,112,688	1,141,368
14	Human Support Services	1,262,711	1,109,608	1,137,608	1,235,858	1,277,799	1,328,559	1,382,313
15	Public Works	306,668	321,773	319,373	325,940	333,735	347,218	361,389
16	Financing and Other	322,491	398,855	399,955	468,144	524,243	570,462	608,279
17	Tax Increment Financing (TIF)	0	1,940	1,940	9,710	9,710	9,710	9,710
18	Grant Disallowances	0	57,000	57,000	0	0	0	0
19	Cash Reserve (Budgeted Contingency)	0	50,000	300	50,000	50,000	50,000	50,000
20	Tobacco Trust Fund (Program Funds)	0	0	0	0	2,000	4,000	6,000
21	Tobacco Trust Fund (Investment Funds)	0	0	0	0	0	0	0
22	Operating Costs of Capital and Lease Purchases	0	0	0	0	5,000	10,000	35,000
23	Deposit into the Emergency Reserve Fund (4%)	0	0	0	15,500	3,231	7,366	8,145
24	Deposit into the Contingency Reserve Fund (3%)	0	0	0	2,202	2,241	15,130	6,109
25	**Total General Fund Expenditures**	**3,813,172**	**4,077,272**	**4,109,472**	**4,482,481**	**4,551,026**	**4,752,194**	**4,947,588**
26	**Operating Margin, Budget Basis**	**53,684**	**1,838**	**62,578**	**1,703**	**6,503**	**23,270**	**12,707**
27	**Beginning General Fund Balance**	**865,328**	**897,357**	**897,357**	**759,857**	**579,351**	**571,326**	**597,092**
28	Operating Margin, Budget Basis	53,684	1,838	62,578	1,703	6,503	23,270	12,707
29	Projected GAAP Adjustments (Net)	(21,655)	(20,000)	(20,000)	(20,000)	(20,000)	(20,000)	(20,000)
30	Deposits into 4% & 3% Reserve Funds (From Fund Balance)	(5,069)	(31,609)	(31,609)	0	0	0	0
31	Deposits into 4% & 3% Reserve Funds (To Cash Reserves)	5,069	31,609	31,609	17,702	5,472	22,496	14,254
32	Unspent TIF Reserve	0	1,940	1,940	9,710	9,710	9,710	9,710
33	Fund Balance Use	0	(149,093)	(182,018)	(189,621)	(9,710)	(9,710)	(9,710)
34	**Ending General Fund Balance**	**897,357**	**732,042**	**759,857**	**579,351**	**571,326**	**597,092**	**604,053**
	Composition of Fund Balance							
35	Emergency Cash Reserve Balance (4%)	145,029	163,091	163,091	178,591	181,822	189,188	197,333
36	Contingency Cash Reserve Balance (3%)	108,771	122,318	122,318	124,520	126,761	141,891	148,000
37	Fund Balance not in Emergency & Contingency Reserves	643,557	446,633	474,448	276,240	262,743	266,013	258,720
38	**Ending General Fund Balance (Line 34)**	**897,357**	**732,042**	**759,857**	**579,351**	**571,326**	**597,092**	**604,053**

Local Funds Component of the General Fund Financial Plan
($ thousands)

	Revenues	FY 2003 Actual	FY 2004 Approved	FY 2004 Adjusted	FY 2005 Proposed	FY 2006 Projected	FY 2007 Projected	FY 2008 Projected
1	Taxes	3,293,374	3,339,913	3,441,217	3,628,730	3,822,365	3,978,086	4,122,775
2	General Purpose Non-Tax Revenues	315,780	289,201	286,672	292,447	284,699	289,940	286,290
4	Transfer from Lottery	72,050	70,200	70,200	71,100	71,100	71,100	71,100
5	**General Fund Revenues (Local)**	**3,681,204**	**3,699,314**	**3,798,089**	**3,992,277**	**4,178,164**	**4,339,126**	**4,480,165**
6	Fund Balance Use	1,802	96,498	129,423	80,000	9,710	9,710	9,710
7a	Revenue Enhancements	0	38,760	0	95,755	133,674	137,382	140,533
7b	Suspension of Tax Parity	0	0	0	0	24,000	77,129	117,000
8	Transfer from Federal and Private Resources	0	0	0	6,361	6,502	6,660	6,827
9	**Total General Fund Resources (Local)**	**3,683,006**	**3,834,572**	**3,927,512**	**4,174,393**	**4,352,050**	**4,570,007**	**4,754,235**
	Expenditures (by Appropriation Title)							
10	Governmental Direction and Support	199,089	206,824	220,924	258,257	265,930	274,061	282,610
11	Economic Development and Regulation	56,520	53,336	55,036	55,584	57,049	58,662	60,362
12	Public Safety and Justice	646,732	716,715	728,115	765,324	795,709	822,067	850,344
13	Public Education System	909,354	962,941	990,941	1,048,316	1,076,455	1,103,331	1,131,773
14	Human Support Services	1,242,888	1,085,277	1,113,277	1,208,418	1,251,384	1,301,392	1,354,354
15	Public Works	293,952	308,029	305,629	299,826	312,173	325,324	339,146
16	Financing and Other	322,491	390,672	391,772	459,554	514,666	565,692	607,977
17	Tax Increment Financing (TIF)	0	1,940	1,940	9,710	9,710	9,710	9,710
18	Grant Disallowances	0	57,000	57,000	0	0	0	0
19	Cash Reserve (Budgeted Contingency)	0	50,000	300	50,000	50,000	50,000	50,000
20	Tobacco Trust Fund (Program Funds)	0	0	0	0	2,000	4,000	6,000
21	Tobacco Trust Fund (Investment Funds)	0	0	0	0	0	0	0
22	Operating Costs of Capital and Lease Purchases	0	0	0	0	5,000	10,000	35,000
23	Deposit into the Emergency Reserve Fund (4%)	0	0	0	15,500	3,231	7,366	8,145
24	Deposit into the Contingency Reserve Fund (3%)	0	0	0	2,202	2,241	15,130	6,109
25	**Total General Fund Expenditures (Local)**	**3,671,026**	**3,832,734**	**3,864,934**	**4,172,690**	**4,345,548**	**4,546,736**	**4,741,528**
26	**Operating Margin, Budget Basis**	**11,980**	**1,838**	**62,578**	**1,703**	**6,503**	**23,270**	**12,707**

Special Purpose Revenue Component of the General Fund Financial Plan
($ thousands)

	Revenues	FY 2003 Actual	FY 2004 Approved	FY 2004 Adjusted	FY 2005 Proposed	FY 2006 Projected	FY 2007 Projected	FY 2008 Projected
3	Special Purpose (O-type) Revenues	164,125	191,943	191,943	208,624	212,023	215,152	218,448
5	**General Fund Revenues (Special Purpose)**	**164,125**	**191,943**	**191,943**	**208,624**	**212,023**	**215,152**	**218,448**
6	Fund Balance Use	19,725	52,595	52,595	109,621	0	0	0
7a	Revenue Enhancements	0	0	0	(8,454)	(6,544)	(9,695)	(12,388)
9	**Total General Fund Resources (Special Purpose)**	**183,850**	**244,538**	**244,538**	**309,791**	**205,479**	**205,457**	**206,060**
	Expenditures (by Appropriation Title)							
10	Governmental Direction and Support	10,775	20,151	20,151	46,671	20,354	20,860	21,398
11	Economic Development and Regulation	78,714	132,110	132,110	166,873	99,907	102,364	104,972
12	Public Safety and Justice	12,747	18,945	18,945	25,131	18,533	19,047	19,590
13	Public Education System	7,371	27,075	27,075	8,972	9,130	9,356	9,596
14	Human Support Services	19,823	24,330	24,330	27,441	26,415	27,166	27,959
15	Public Works	12,716	13,744	13,744	26,114	21,562	21,894	22,244
16	Financing and Other	0	8,184	8,184	8,590	9,577	4,770	302
25	**Total General Fund Expenditures (Special Purpose)**	**142,146**	**244,538**	**244,538**	**309,791**	**205,479**	**205,457**	**206,060**
26	**Operating Margin, Budget Basis**	**41,704**	**0**	**0**	**0**	**0**	**0**	**0**