PUBLIC OVERSIGHT HEARING

ON

THE FISCAL YEAR 2009 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 6, 2009, 10:00 a.m.
John A. Wilson Building, Council Chamber

Testimony of
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Good morning Chairman Evans and members of the Committee on Finance and Revenue. I am Robert D. Ebel, Deputy Chief Financial Officer for Revenue Analysis and Chief Economist for the District of Columbia (District) government. I am pleased to appear before you today to testify on the activities of the Office of Revenue Analysis (OCFO/ORA).

Mission and Activities

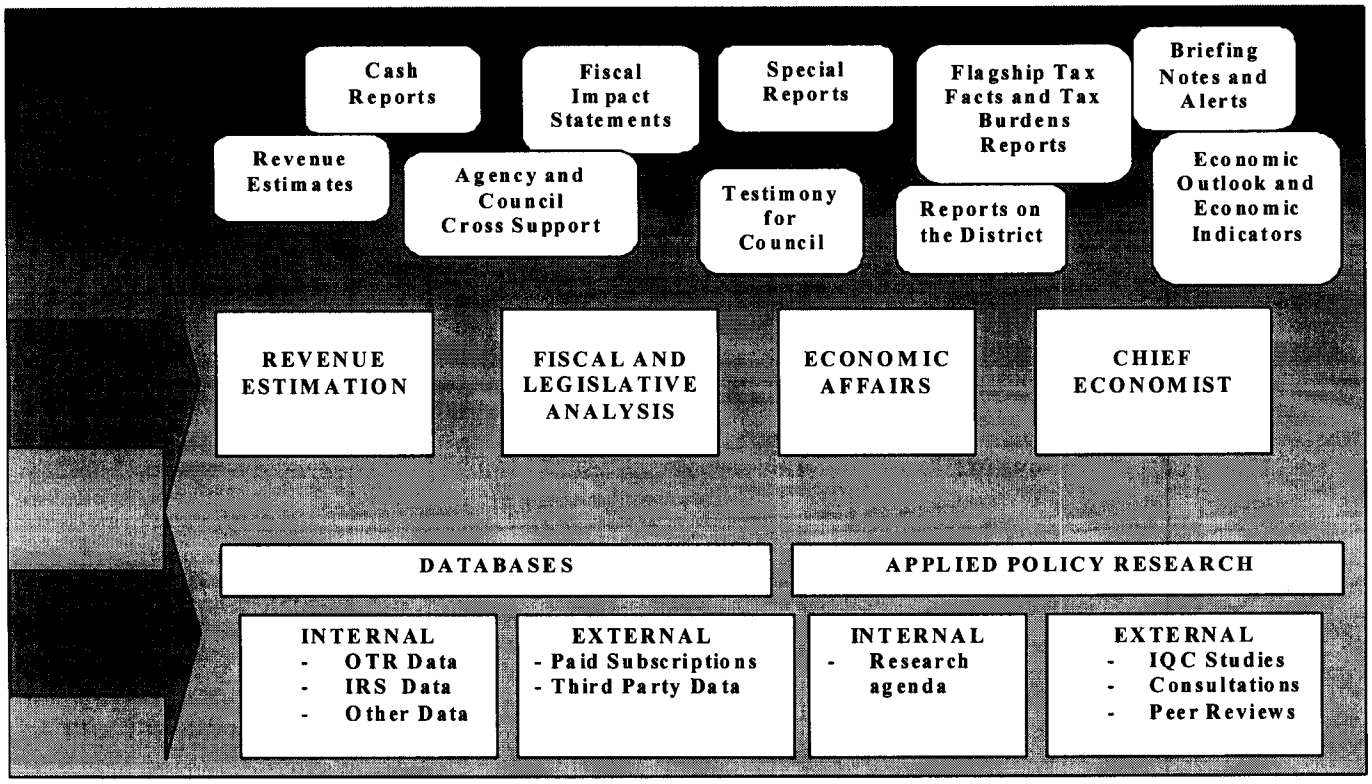
The mission of the Office of Revenue Analysis encompasses a wide range of fiscal and economic research as directed by the Chief Financial Officer (CFO), and, through the CFO, to respond to requests by the Council of the District of Columbia and the Executive Office of the Mayor (EoM). (Figure 1).

Among its activities, the ORA:

Prepares Fiscal Impact Statements. The *District of Columbia Home Rule Act of 1973* (Pub. L no. 93-198) requires that all legislation submitted by the Council of the District of Columbia to the U.S. Congress for review prior to enactment into law be accompanied by a fiscal impact statement (FIS). The FIS discusses the scope of the legislation, the methodology for making the estimate and provides an estimate of the costs and/or revenues that will be incurred by the District as a result of enactment of the Act in each of the first four (4) fiscal years for which the Act is in effect.[1]

[1] District of Columbia Council rules also require the preparation of fiscal impact statements.

Figure 1: Schematic of Content and Work Flow



Act of 1995 (Pub. L 104 I, Stat. 1995) assigned to the then newly created Office of the CFO the preparation of the fiscal impact statement. The *District of Columbia Omnibus Authorization Act* (Pub.L.109-356, October 16, 2006) made this mandate permanent.

During FY 2008, ORA analyzed and prepared fiscal impact statements on approximately 270 bills, contracts and regulations. Additionally, ORA prepared the fiscal impact statement on both the Mayor and the Council versions of the Budget Support Act, which contained 47 and 84 subtitles, respectively. Five months into FY 2009 ORA has already worked on 153 fiscal impact statements, and we are on track to prepare as many (likely more) fiscal impact statements as we did during FY 2008. All fiscal impact statements prepared by the OCFO since May 2001 are retrievable on the OCFO Web site at *www.cfo.dc.gov*.

Also during FY 2008 and FY 2009, ORA made the documentation, tracking, and internal review of all fiscal impact statements entirely electronic. This innovation saves money on paper, printing, and storage costs; reduces the amount of time it takes to finalize a fiscal impact statement; increases the transparency of the review process; and helps to ensure the accuracy of every fiscal impact statement. ORA will continue to refine this process in the out-years in order to ensure that fiscal impact statements are accurate and reliable and are provided to the Council and Mayor in a timely manner.

ORA and the OCFO Communications Office are also working with Council IT staff to provide easier public access to fiscal impact statements by making them available on Council's Legislative Information Management System. While the OCFO will retain its own FIS search-page, having fiscal impact statements appear alongside corresponding bills on the Council's Legislative Information Management System will make the FIS process more transparent to policymakers, practitioners and other stakeholders alike.

Provides Periodic Reports on the Economic and Revenue Outlook with Accompanying Revenue Estimates. The OCFO is further responsible for the quarterly presentation of the District's five-year Financial Plan's economic and revenue outlook and an accompanying set of revenue estimates for the District's Local Source General Fund Revenues. As part of this exercise, each February the OCFO issues the revenue estimate that is used to develop the Mayor's proposed budget for the next fiscal year (October 1 to September 30). As the Council is completing its review of the annual budget, a revised estimate is then prepared in May that becomes the official binding revenue estimate for the fiscal year budget that is transmitted to Congress. The May estimate may be revised as new economic

and financial information becomes available. This review is made during the months of August and December.

Because of the high degree of attention given to the outlook for the District's economy at this time (as the FY 2010 budget is prepared), today's testimony provides below a more detailed review of the revenue and economic outlook.

Conducts Special Studies. In addition to its Fiscal Impact Statement and Economic and Revenue Outlook activities, ORA provides to District citizens a series of technical reports, all of which are subject to an extensive internal and external peer-review process prior to release and publication. These include:

- *Monitoring the District of Columbia Economic and Revenue Trends.* In its complementary role as the Office of the Chief Economist, the ORA produces two monthly reports that monitor the District's economy and its revenue collections performance.
    - *DC Economic Indicators*. Published monthly, the *Indicators* provide a two page 'at a glance" overview of four key sectors of the D.C. economy: (i) labor and industry, including data on the composition of resident employment by type of industry; (ii) revenue collections by major type of tax; (iii) demographic information, including D.C. GDP, the residential unemployment rate, and recent trends in resident population; and (iv), real estate (home sales volume and prices and commercial office vacancy rates); and,
    - A *Review of District of Columbia Economic and Revenue Trends*. Also published monthly, the *Trends* report provides a highly detailed examination (e.g., the current February 2009 report runs 28 pages) on total and residential employment, wages, housing, commercial office space, and the hospitality and retail industry.

- *Tax Rates and Tax Burdens: Washington Metropolitan Area.* Published annually, this report provides not only a comparison of the District's statutory rates *vis-à-vis* 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.* Also an annual publication, the nationwide comparison report provides a compendium of statutory tax rate comparisons and estimates of the household burden of major taxes by income class of the District compared with the largest city in each of the other 50 states. The summary table from this report is reproduced in the Annual *Statistical Abstract of the United States.*
- *The Economic Report (Data Book) of the District of Columbia.* This calendar year (with publication targeted for next month), the ORA will publish its second annual data book on the District's economy and its revenue system.[2] This will become a "flagship" D.C. document, providing historical data in six areas (and 95 tables and figures). Chapters on the District's economy and total revenue are followed by chapters on the taxation of individual income, real estate, sales, and business enterprise. A final chapter examines non-tax revenues.
- *DC Tax Facts.* This important and widely used pocket-sized reference of District tax collections provides descriptions of all the District's revenue (tax and non tax) sources, the history of major revenue changes since 1970, filing

[2] Office of the Chief Financial Officer of the District of Columbia, *The Economic Report of the District of Columbia: A Fiscal Perspective*, Forthcoming, March 2009.

and payment dates, and the yield of each type of revenue utilized by the District.

- *Cash Reports*. Each month the ORA/OCFO publishes a report of cash collections by the District government. The tracking of these cash flows are particularly important in order to have an ongoing check on the quarterly revenue estimates. Then, at the end of the calendar year as part of the process of preparing the *Comprehensive Annual Financial Report (CAFR)*, ORA coordinates with the Office of Tax and Revenue to adjust the revenue numbers to reflect the net revenue accruals that then become the final numbers reported in the CAFR.
- *Tax Expenditures*. The D.C. Official Code requires the CFO to prepare a *Tax Expenditure Budget* for Fiscal Year 2003 and biennially thereafter. "Tax expenditures" are revenue loses resulting from District tax provisions that grant special relief designed to encourage certain kinds of taxpayer behavior or aid to taxpayers in special circumstances. The next release is set for spring 2010.
- *Monitoring the American Recovery and Reinvestment Act.* The ORA has been tasked by the CFO to continually monitor the flow of funds that will accrue to the District under the Obama Administration's *American Recovery and Reinvestment Act* ("Stimulus Plan"). This information, which is presented in spreadsheet format and which is distributed to the Council and Executive Office of the Mayor as it is updated, tracks five classifications of funds flow to the District: (i) increases in Medicaid support, resulting from a temporary increase in the Federal Medical Assistance Percentage (FMAP); (ii) the State Fiscal Stabilization Fund; (iii) Federal Operating Grants; (iv) Federal Capital Grants; and (v) Tax Conformity Estimates. In addition, the ORA tracks allocations to non-General Fund entities such as the D.C. Housing Authority,

the Water and Sewer Authority (WASA), and the Washington Metropolitan Transit Authority (WMATA).

- *Revenue Chapter for the Budget Document.* 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* (March), 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 U.S. and District's economic outlook and then proceeds to present in great detail information on the revenue flows by type of revenues over the financial plan period. The revenue presentations include a detailed summary table of Operating Revenue by Source for a six year period (historical as well as "out year" financial plan numbers) followed by exhibits on General Fund components, policy proposals impacting General Fund revenue, and dedicated tax revenues.

Staffing and Budget

For FY 2009 ORA consists of 26 FTEs, 20 of which are in the ORA/Office of the Chief Economist and six (6) in the functionally separate Office of Economic Development Finance (EDF). The FY 2009 budget for ORA is $3.42 million, of which approximately 23% is allocated to the Economic Development Finance (EDF) function.[3] T otal operating expenses for the entire ORA plus EDF through February 3, 2009 sum to $1.3 million or 38 percent of our budget—an expenditure pace that reflects the requirement to purchase early in the fiscal year a wide range of software

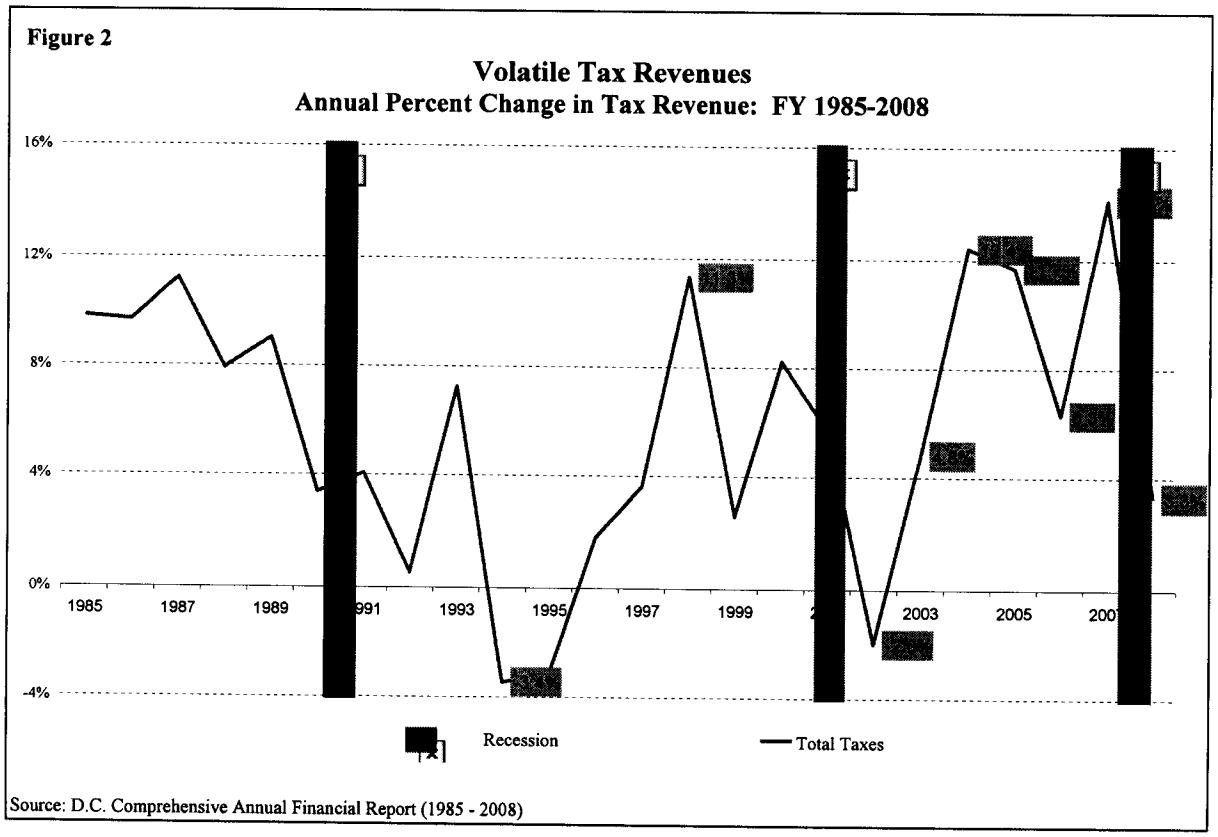
[3] The ORA FTE count includes six FTEs attached to the otherwise independent (of the ORA) Office of Economic Development Finance. The key functions of Economic Development Finance are (i) conduct research supporting the financing of special economic development projects; (ii) conduct analyses of the special finance projects, and (iii) represent the CFO in economic development-related board commitments and provide research and analytical staff-work related to those commitments. The 23% does not reflect special grant funds for fiscal studies that the EDF manages that supplement its staffing operations.

for data base monitoring, regional and local forecasting, and statistical and econometric modeling.

Discussion of the Economic and Revenue Outlook

Revenues and Revenue Estimates

As noted, a key function of ORA is to provide timely, accurate reports on the District's economic and revenue outlook and, with that, estimates of the present and projected performance of the revenue system. In the time between the May official binding estimate on which the budget is based and the end of the forthcoming fiscal year, any number of changes can happen to the economy and the revenue stream – changes that are often exogenous to this revenue system. And, as the chart below shows, the annual change in tax revenue can range widely. One challenge is to determine what is "normal" in this growth and plan for a budget supported by normality – *and* subject to large swings. "Normal" or average growth in the last 5 years is about 9.6 percent, and in the last 3 years the percentage is about 7.9 percent. Yet actual tax revenue did not grow by either of these specific percentages in any one of the last 6 fiscal years, bouncing from -2 percent to 14.1 percent. (Figure 2).



Since FY 2000, the District has had to grapple with this volatility three times.

- First, in FY 2002 income tax revenue fell abruptly and precipitously due to the events associated with September 11, 2001: a subsequent recession accompanied by stock market decline. When these developments were identified in the summer of 2002, the challenge for the Council and the Mayor was to create a balanced budget using revenue enhancements and expenditure reductions. Adjustments were made in both FY 2002 and 2003, and the District closed out both FY 2002 and FY 2003 with small, but positive, budget surpluses.

- In FY 2003 the opposite swing began with transactions in both residential and commercial real property. Arising out of a year of no change in FY 2002, by the end of FY 2004 the annual value of property transactions had more than

doubled. Moreover, due in part to the deed tax rate changes that had been enacted to deal with the prior revenue shortfall, deed tax revenues also more than doubled between 2002 and 2004 (*DC Tax Facts*, various issues).

- However, this fiscal year, the District, as well as the country, is witnessing an astonishing decline in its revenue, facing a challenge not experienced since the Great Depression of 1929. The recent February estimates of FY 2009 and FY 2010 tax revenues (before earmarks) are down 5.0% and 11.7%, respectively, from the amounts shown for those years in the budget submitted to Congress last June. In the first 4 months of FY 2009 deed tax collections are down 55.4% from the same period of last year, corporate income tax collections are down 16.6%, and collections for the non-withholding part of the individual income tax are down 42.8%.

Final Comments on the Outlook for FY 2009 and FY 2010.

ORA projects declines in employment, wages, and personal incomes for the District during the next two years, similar to the fairly pessimistic projections economists have made for the nation as a whole.

Our estimating assumptions for FY 2009 and FY 2010 respectively, include:

- job declines of 0.2 percent and 0.3 percent
- declines of 0.3 percent and 1.4 percent each year in total resident employment
- 0.6 percent and -0.4 percent changes in the personal income of District residents, and
- low inflation of 0.4 and 1.9 percent.

Total revenue available for general fund purposes in FY 2009 (that is, revenue available after earmarking for such things as the convention center transfer, TIFs and school modernization) is forecast to change -0.3 percent from FY 2008, and -2.7 percent in FY 2010 compared to FY 2009.

Further Risks

As with past recessions, the District economy is far from isolated from national trends. In December, for example, the District's unemployment rate rose to 8.9%, the growth in jobs located in the District has come to a virtual standstill, and the value of real estate transactions continued to fall. In this environment, there is enormous uncertainty about the economy. Chief among the risks facing the District is that the national recession may be longer and more severe than is even now generally expected, with perhaps more impact on the District in sectors such as professional services or non-profit organizations. Continued decline in the stock market and continued lack of credit availability provide additional risk and uncertainty regarding the D.C. economy and its revenue tax base.

Another source of uncertainty is the pattern of federal expenditures. Government spending is a significant economic underpinning of the entire Washington, D.C. Metropolitan area, including spending by the District itself. Security concerns arising out of 9/11 and the Iraq and Afghanistan wars resulted in large increases in government spending that benefited the Washington, D.C. area, and, as mentioned, there is the possibility that implementing the economic stimulus program and federal budget changes could increase the federal presence in the District. However, in recent years federal procurement spending in the District has slowed, rising an average of just 3.4% per year from FY 2004 to FY 2007. Efforts to shift government spending over the next few years to bring greater geographical balance to federal spending could also dampen growth in the District.

A Positive Note

Permit me to end on a positive note. Through this period, government (both federal and local) and private sector service industries, such as professional and business services, education, and health sum to about 2/3 of our total employment. These are the sectors that, to date, have been less recession-prone over the past 16 months when compared to manufacturing, finance, and trade. So, this provides DC an element of stability. Moreover, it is possible that implementation of the federal economic stimulus programs together with changes in federal budget priorities may eventually result in increased federal employment in the District, a potential development that the OCFO will monitor closely.

Thank you for the opportunity to testify before you today. I am pleased to respond to any questions that you may have.