



**OFFICE OF THE DISTRICT OF COLUMBIA AUDITOR**

THE PRESIDENTIAL BUILDING  
415 12TH STREET, N.W., ROOM 210  
WASHINGTON, D.C. 20004  
TEL. 202-727-3600 • FAX: 202-724-8814

Deborah K. Nichols  
Interim District of Columbia Auditor

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**Analysis of Projected Fiscal Year 1999  
Dedicated Tax Revenue for the  
Washington Convention Center Authority**

**August 7, 1998**

## **EXECUTIVE SUMMARY**

### **PURPOSE**

Pursuant to D. C. Law 10-188, Section 305(a) of "Washington Convention Center Authority Act of 1994," on or before July 1 of each year, the District of Columbia Auditor shall audit the accounts and operations of the Washington Convention Center Authority (WCCA) and make a specific finding of the sufficiency of projected revenues from taxes imposed pursuant to sections 301, 302, 303, and 304 to meet the projected expenditures and reserve requirements of the WCCA for the upcoming fiscal year.

Section 305(b) of the law further states that if the audit indicates that projected revenues are insufficient to meet WCCA's projected expenditures and reserve requirements for the upcoming fiscal year, the Mayor shall impose a surtax on each of the taxes dedicated to WCCA, excluding the tax on restaurant meals and alcoholic beverages, in order to generate sufficient revenues to cover WCCA's costs. The surtax imposed by the Mayor would become effective on or before October 1 of the upcoming fiscal year.

This letter report sets forth the Auditor's findings regarding the sufficiency of the projected revenues to meet WCCA's projected expenditures and reserve requirements for fiscal year 1999.

### **CONCLUSION**

The Auditor's analysis of information provided by WCCA and the Office of Tax and Revenue indicated that the fiscal year 1999 projected tax revenue of \$48.4 million for WCCA (along with operating revenue and estimated revenue from interest earnings) appears to be sufficient to cover WCCA's projected fiscal year 1999 expenditures.

### **MAJOR FINDINGS**

1. WCCA's Projected Fiscal Year 1999 Dedicated Tax Revenue Appears Sufficient to Cover Projected Expenditures and Projected Reserve Requirements.
2. WCCA's Fiscal Year 1999 Reserve Requirements Are Estimated to Total \$126 Million.
3. Proposed Changes in the Dedicated Tax Structure Eliminated WCCA's Receipt of Franchise Taxes and Repealed the Hotel Occupancy Tax.
4. WCCA's Proposed Dedicated Tax Structure Is Supported By Taxes Levied on the Hospitality Industry.
5. D.C. Act 12-402 Requires That 17.4 Percent of the Dedicated Tax Revenue Be Set-Aside to Fund Marketing Service Contracts.



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The Honorable Linda Cropp, Chairman  
and Members of the Council of the  
District of Columbia  
441 4th Street, N.W. Room 704  
Washington, D.C. 20001

Dear Chairman Cropp and Members of the Council of the District of Columbia:

Pursuant to Section 305(a) of D. C. Law 10-188, "Washington Convention Center Authority Act of 1994," on or before July 1 of each year, the District of Columbia Auditor shall audit the accounts and operations of the Washington Convention Center Authority (WCCA) and make a specific finding of the sufficiency of projected revenues from taxes imposed pursuant to sections 301, 302, 303, and 304 to meet the projected expenditures and reserve requirements of the WCCA for the upcoming fiscal year.

Section 305(b) of the law further states that if the audit indicates that projected revenues are insufficient to meet WCCA's projected expenditures and reserve requirements for the upcoming fiscal year, the Mayor shall impose a surtax on each of the taxes dedicated to WCCA, excluding the tax on restaurant meals and alcoholic beverages, in order to generate sufficient revenues to cover WCCA's costs. The surtax imposed by the Mayor would become effective on or before October 1 of the upcoming fiscal year.

This letter report sets forth the Auditor's findings regarding the sufficiency of the projected revenues to meet WCCA's projected expenditures and reserve requirements for fiscal year 1999.

### **OBJECTIVE, SCOPE AND METHODOLOGY**

The objective of this analysis was to determine whether projected dedicated tax revenues for fiscal year 1999 are sufficient to meet WCCA's projected expenditures and reserve requirements.

The Auditor reviewed D.C. Law 10-188, "Washington Convention Center Authority Act of 1994," and provisions of the D.C. Code concerning the corporate and unincorporated business franchise tax; sales tax on gross receipts for transient lodging or accommodations, food or drink for immediate consumption, spirits sold for consumption on premises, and rental vehicles; the use tax on gross receipts for transient lodging or accommodations, food or drink for immediate consumption, spirits sold for consumption on premises, and rental vehicles; and the Hotel Occupancy Tax. Additionally, the Auditor reviewed D.C. Act 12-402 entitled, "Washington Convention Center Authority Financing Amendment Act of 1998," which amended certain provisions of D.C. Law 10-188.

The Auditor held discussions with WCCA officials regarding dedicated tax revenues and expenditure projections for fiscal year 1999. The Auditor also held discussions with officials in the District's Office of Tax and Revenue (OTR) concerning dedicated tax revenues under the existing tax structure and the proposed tax structure for fiscal year 1999. Additionally, the Auditor met with General Accounting Office (GAO) officials to discuss their review of dedicated taxes. To further the review of dedicated taxes, the Auditor reviewed WCCA's independent annual audit report for the fiscal year ending September 30, 1997 and a WCCA consultant's report on dedicated taxes to determine whether the projected forecast of revenue for WCCA was reasonable and attainable.

The audit was conducted in accordance with generally accepted government auditing standards and included such tests of the records as deemed necessary.

## **BACKGROUND**

D.C. Law 10-188 entitled, "Washington Convention Center Authority Act of 1994," was enacted by the Council of the District of Columbia on September 28, 1994. The law established the Washington Convention Center Authority as an independent authority of the District government. The mission of the WCCA is to construct, maintain, and operate a new convention center in Washington D.C., and to operate and maintain the existing convention center.

The WCCA, as established, consists of a nine member Board of Directors. The Board is currently comprised of the Chief Financial Officer of the District of Columbia, the Director of the Office of Tourism and Promotions, and seven public members that are appointed by the Mayor of the District of Columbia with the advice and consent of the Council of the District of Columbia.<sup>1</sup> While the Board provides operational oversight of WCCA, the day-to-day management of the WCCA is under the direction of a general manager appointed by the Board.

The Washington Convention Center Authority Act of 1994 also authorized the establishment of the Washington Convention Center Authority Fund ("Fund") to be operated by the WCCA. The Fund is capitalized with dedicated tax revenues from sales and use taxes, corporate and unincorporated business franchise taxes, and a surtax on hotel occupancy. The law provides that the District will collect and transfer to WCCA, on a monthly basis, dedicated taxes to be deposited into the Fund to finance predevelopment costs for the proposed new convention center and to cover operating costs associated with the existing convention center. Table I presents the dedicated taxes transferred to the WCCA Fund since its establishment in fiscal year 1995.

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<sup>1</sup>The Council recently passed legislation which affected the Board's membership by replacing the Director of the Office of Tourism and Promotions with another member designated by the Mayor, who along with the Chief Financial Officer, will serve as ex-officio voting members.

**Table I**  
**Dedicated Taxes Transferred Pursuant to D.C. Law 10-188**  
**Fiscal Years 1995 - 1997**

Type of Tax	FY 1995	FY 1996	FY 1997	Grand Total
General Sales and Use Tax	\$25,417,838	\$27,910,999	\$32,113,303	\$85,442,140
Hotel Occupancy Tax 40%	3,673,226	3,560,860	3,481,074	10,715,160
Corporate Franchise Tax	2,959,217	3,051,524	3,531,255	9,541,996
Unincorporated Business Franchise Tax	<u>852,570</u>	<u>831,739</u>	<u>1,033,676</u>	<u>2,717,985</u>
<b>Total Dedicated Tax Transfers</b>	<b>\$32,902,851</b>	<b>\$35,355,122</b>	<b>\$40,159,308</b>	<b>\$108,417,281</b>
Hotel Occupancy Tax 60%	5,175,000	5,400,000	5,400,000	15,975,000
Adjustments			209,693 <sup>2</sup>	209,693
<b>Total Dedicated Tax Transfer per CAFR</b>	<b><u>\$38,077,851</u></b>	<b><u>\$40,755,122</u></b>	<b><u>\$45,769,001</u></b>	<b><u>\$124,601,974</u></b>

Source: D.C. Auditor

As noted in Table I, between fiscal years 1995 and 1997, the District collected and transferred approximately \$125 million in dedicated tax revenues to the WCCA Fund. The fiscal year 1998 tax transfer estimate is \$46 million, which consists of \$40.9 million in dedicated taxes and \$5.4 million in hotel occupancy taxes for payment to the tourism responsibility centers.<sup>3</sup>

### **The Washington Convention Center Authority Financing Amendment Act of 1998**

On June 16, 1998, the Council of the District of Columbia passed D.C. Act 12-402 entitled, "Washington Convention Center Authority Financing Amendment Act of 1998," which amended D.C. Law 10-188. D.C. Act 12-402 contained the following amendments relative to dedicated taxes:

- eliminates the surtax on corporate franchise and unincorporated business franchise taxes;

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<sup>2</sup>This amount represents a fiscal year 1997 adjusting entry made by the District's Office of Financial Operations and Systems.

<sup>3</sup>The tourism responsibility centers consists of the Washington Convention and Visitors Association, the Mayor's Committee to Promote Washington, and the D.C. Chamber of Commerce.

- authorizes the transfer of dedicated taxes collected by the Mayor to the WCCA Fund upon receipt;
- permits WCCA to utilize dedicated tax revenues to finance the costs of the new convention center;
- authorizes the establishment of a Washington Convention Center Marketing Fund and requires WCCA to establish marketing service contracts;
- increases the sales and use tax on hotels from 13 percent to 14.5 percent thereby increasing the surtax for WCCA from 2.5 percent to 4.45 percent; and
- repeals the hotel occupancy tax.

In addition to the proposed changes affecting dedicated taxes, D.C. Act 12-402 would permit WCCA, among other things, to: (1) extend the maturity of revenue bonds issued to finance the construction of the new convention center from 30 to 34 years; (2) enter into interest rate agreements; (3) reconstitute the WCCA Board of Directors to consist of the Chief Financial Officer of the District of Columbia, seven public members, and an ex-officio voting member; (4) establish additional reserves, if necessary; and (5) require the Office of the D.C. Auditor to issue a certification on or before July 15 of each year of the sufficiency of projected revenues to meet projected expenditures and reserve requirements. District officials anticipate approval of the legislation by the Congress before its summer recess.

## FINDINGS

### WCCA'S PROJECTED FISCAL YEAR 1999 DEDICATED TAX REVENUE APPEARS SUFFICIENT TO COVER PROJECTED EXPENDITURES AND PROJECTED RESERVE REQUIREMENTS

The Office of Tax and Revenue's forecast indicates that WCCA will receive approximately \$48.4 million in dedicated tax revenues during fiscal year 1999. The forecast is based upon changes to the dedicated tax structure included in the Washington Convention Center Authority Financing Amendment Act of 1998 (D.C. Act 12-402).<sup>4</sup> The \$48.4 million, which is based on taxing: (1) hotel room charges; and (2) restaurant sales, alcoholic beverages consumed on premises, and automobile rental charges, appears sufficient to cover WCCA's projected expenditures and reserve requirements<sup>5</sup> for fiscal year 1999 as presented in Table II.

**TABLE II**  
**WCCA's Projected Revenues and Projected Expenditures**  
**Fiscal Year 1999**  
**(\$ thousands)**

<b>Category</b>	<b>Amount</b>
<b>Revenue</b>	
FY 1999 Projected Dedicated Taxes	\$48.4
Interest Earnings	2.3
FY 1999 Operating Revenue	<u>7.3</u>
<b>Total Projected FY 1999 Revenue</b>	<b>58.0</b>
<b>Expenditures</b>	
Debt Service	36.0
Operating Expenditures	13.0 <sup>6</sup>
Marketing Contracts (17.4%)	<u>5.9</u>
<b>Total Projected FY 1999 Expenditures</b>	<b>54.9</b>
<b>Excess of Revenue Over Expenditures</b>	<b><u>\$3.1</u></b>

Source: WCCA and the Office of Tax and Revenue.

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<sup>4</sup>As noted earlier in this report, the Council of the District of Columbia passed the "Washington Convention Center Authority Financing Amendment Act of 1998" on June 16, 1998.

<sup>5</sup>The reserve requirements are not expected to impact WCCA's fiscal year 1999 dedicated tax estimate of \$48.4 million because they will be funded through other sources. A discussion of this information is presented later in the report.

<sup>6</sup>Historically, WCCA's operating expenditures have exceeded its operating revenue. According to WCCA's reconciliation of the dedicated taxes bank account, a total of \$12.2 million has been transferred from the building fund to the operating fund to cover deficits for fiscal years 1996 through June 30, 1998. WCCA officials anticipate additional transfers during fiscal year 1998.

Based upon expenditure projections provided by WCCA and barring any unforeseen contingencies, projected revenue dedicated to WCCA are forecasted to exceed projected expenditures by approximately \$3.1 million for fiscal year 1999.

### **WCCA's Fiscal Year 1999 Reserve Requirements Are Estimated to Total \$126 Million**

According to WCCA, the fiscal year 1999 reserve requirements will total approximately \$126 million. WCCA anticipates establishing the following reserves: a \$50 million operations and marketing reserve; a \$44 million debt service reserve; a \$22 million capital renewal and replacement reserve; and, a \$10 million rate stabilization reserve. WCCA officials indicate that the fiscal year 1999 reserves will be funded with accumulated dedicated tax revenue (cash-on-hand) and bond proceeds. According to the Auditor's analysis, the accumulated dedicated tax revenue (cash-on-hand) totaled approximately \$98 million as of June 30, 1998. (See Appendix I)

Because the reserves will not be funded with fiscal year 1999 estimated dedicated tax revenue of \$48.4 million, they were not included in the analysis of projected revenue and projected expenditures for fiscal year 1999 presented in Table II. These reserves will provide WCCA with a cushion of funds to protect against unforeseen contingencies. WCCA's financial advisor noted that these reserves are estimated amounts and may change as data continues to be refined and WCCA's date for entering the bond market approaches.

### **PROPOSED CHANGES IN THE DEDICATED TAX STRUCTURE ELIMINATED WCCA'S RECEIPT OF FRANCHISE TAXES AND REPEALED THE HOTEL OCCUPANCY TAX**

Changes in the dedicated tax allocated to WCCA include: (1) increasing the District's hotel sales tax rate from 13 percent to 14.5 percent which will result in an increase in the tax collected on behalf of WCCA from 2.5 percent to 4.45 percent; (2) repealing the 1 percent hotel occupancy tax; and (3) eliminating the surtax and transfer of corporate and unincorporated business franchise taxes. As a result of the proposed changes, which are scheduled to become effective October 1, 1998, dedicated taxes would only consist of the following:

- 4.45 percent of the District's 14.5 percent sales and use tax on hotel room charges; and
- 1.0 percent of the District's 10 percent sales and use tax on restaurant sales, alcoholic beverages consumed on premises, and automobile rental charges.

WCCA's receipt of 1 percent of the 10 percent sales and use tax on restaurant meals, alcoholic beverages, and automobile rentals remains unchanged. The Auditor notes that, under the new tax structure, dedicated taxes are estimated to increase by approximately 15.8 percent. According to data reviewed by the Auditor, the fiscal year 1999 dedicated tax estimate of \$48.4 million is \$6.6 million (15.8) higher than the dedicated tax estimate under the current structure which was projected to generate approximately \$41.8 million.



## **WCCA's Proposed Dedicated Tax Structure Is Supported By Taxes Levied on the Hospitality Industry**

The legislation changing the dedicated tax revenue structure of the WCCA effectively eliminates all taxes except those levied on the hospitality industry. The success of WCCA's receipt of revenue from these sources depends largely on the stability of the sales associated with hotel and restaurant services. In information provided by WCCA, the Auditor noted that hotel room demand is expected to increase at, or slightly above, the U.S. industry growth trend between 1999 through 2001.<sup>7</sup> At the same time, new hotel construction is expected to increase as a result of favorable economic conditions.

The Auditor reviewed an analysis on the restaurant/automobile industry's taxable sales which indicated that overall sales have remained fairly stable. Further research indicates that sales at restaurants have increased during the last five-year period. Based upon these statistics, the dedicated taxes levied on the hospitality industry are expected to produce collections which match or exceed past results.

### **D.C. ACT 12-402 REQUIRES THAT 17.4 PERCENT OF THE DEDICATED TAX REVENUE BE SET-ASIDE TO FUND MARKETING SERVICE CONTRACTS**

In accordance with the changes proposed under D.C. Act 12-402, WCCA is required to establish a Washington Convention Center Marketing Fund (Marketing Fund) for the purpose of financing marketing service contracts to promote the District of Columbia as a convention, tourism, and leisure travel venue. WCCA would be required to allocate 17.4 percent of dedicated tax revenue collected from sales taxes on hotel rooms to fund marketing services contracts with the Washington Convention and Visitors Association, the Mayor's Committee to Promote Washington, the D.C. Chamber of Commerce, and the Greater Washington Ibero American Chamber of Commerce.

Under the present dedicated tax structure, WCCA receives 60 percent of hotel occupancy taxes for direct transfer (payment) to the Washington Convention and Visitors Association and the Mayor's Committee to Promote Washington. The Chamber of Commerce also received funds from WCCA. In effect, the present funding arrangement for these entities will be replaced with the 17.4 percent set-aside for marketing services contracts that WCCA is required to meet under the new legislation. According to WCCA officials, monthly deposits equal to 17.4 percent of sales taxes on hotel rooms would be forwarded to a trustee for deposit into the Washington Convention Center Marketing Fund and then paid to the marketing entities as appropriate.

Further, the new legislation permits WCCA to use funds earmarked for marketing service contracts to support bond financing, thereby allowing WCCA the capacity to borrow more funds to

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<sup>7</sup>The Auditor reviewed a consultant's report entitled, "Analysis of Dedicated Tax Revenue Related to the Proposed Washington Convention Center," dated June 1, 1998. The report's analysis included information on the lodging market in Washington, D.C., as well as information on the region's economy and the U.S. as a whole.

finance the new convention center. At the same time, the legislation still requires WCCA to set-aside funds to support the marketing of the convention center, however, the proposed legislation specifies that WCCA's bonds, notes, and other obligations have priority over any marketing service contracts. WCCA's financial advisor indicated that should WCCA be unable to fund the marketing service contracts from dedicated tax revenue, WCCA could utilize its reserve funds to cover these costs. However, WCCA's first priority is to fund the financing and construction costs of the new convention center. Table III presents an analysis of the WCCA's dedicated tax revenue for fiscal year 1999 adjusted for the 17.4 percent Marketing Fund set-aside.

**TABLE III**  
**Forecast of Fiscal Year 1999 Dedicated Taxes to the Convention Center**  
**Adjusted for the Marketing Fund Set-Aside**  
**(000)**

<b>Category</b>	<b>Amount</b>
Sales Tax (Restaurant 1%)	\$14,000
Sales Tax (Hotels 4.45%)	<u>34,400</u>
<b>Total FY 1999 Transfer</b>	<b>\$48,400</b>
Marketing Fund Set-Aside (17.4% of Sales Tax on Hotels)	<u>( 5,985)</u>
 <b>Dedicated Taxes Available for WCCA's Use</b>	 <b><u>\$42,415</u></b>

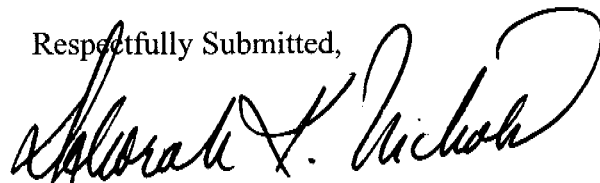
Source: Office of the D.C. Auditor

As indicated in Table III, WCCA will have available \$42 million in dedicated taxes to fund debt service costs and operating expenditures after it has met the required 17.4 percent set-aside to fund marketing service contracts.

**CONCLUSION**

The Auditor's analysis of information provided by WCCA and the Office of Tax and Revenue indicated that the fiscal year 1999 projected tax revenue of \$48.4 million for WCCA (along with operating revenue and estimated revenue from interest earnings) appears to be sufficient to cover WCCA's projected fiscal year 1999 expenditures.

Respectfully Submitted,



Deborah K. Nichols  
Interim District of Columbia Auditor

## **APPENDIX**

**WASHINGTON CONVENTION CENTER AUTHORITY  
DEDICATED TAX CASH BALANCE AFTER DISBURSEMENTS  
AS OF JUNE 30, 1998**

**Receipts**

Dedicated Taxes	\$ 135,643,372 <sup>8</sup>	
Interest from Investments	6,015,023	
Interest on Bank Account Balance	<u>1,048,014</u>	
Total Receipts		\$142,706,409

**Disbursements**

Repayment of Loan from District's		
Rainy Day Fund	4,200,000	
Accrued Interest Purchased	104,756	
Expansion Related Expenditure	28,394,621	
Transfers to Operating Fund	12,225,000	
Bank Charges	<u>13,469</u>	
Total Disbursements		<u>\$44,937,846</u>

**Cash Balance as of 6/30/98** **\$ 97,768,563**

Source: WCCA's Reconciliation of Dedicated Tax Bank Account as of June 30, 1998.

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<sup>8</sup>Of this amount, WCCA has invested \$86,305,763 in Federal Home Loan Bank Notes.