



Certification of Fiscal Year 2016 Total Local Source General Fund Revenue Estimate (Net of Dedicated Taxes) in Support of the District's Issuance of \$431,815,000 in General Obligation Bonds (Series 2016A)

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A Report by the Office of the District of Columbia Auditor
Kathleen Patterson, District of Columbia Auditor

The Honorable Phil Mendelson, Chairman
Council of the District of Columbia
1350 Pennsylvania Avenue, NW, Suite 504
Washington, D.C. 20004

Letter Report: Certification of Fiscal Year 2016 Total Local Source General Fund Revenue Estimate (Net of Dedicated Taxes) in Support of the District's Issuance of \$431,815,000 in General Obligation Bonds (Series 2016A)

Dear Chairman Mendelson:

On May 4, 2016, the Deputy Chief Financial Officer and Treasurer of the District of Columbia requested that the Auditor certify the Office of the Chief Financial Officer revised fiscal year (FY) 2016 estimated total local source General Fund Revenue, net of dedicated taxes.¹ The Office of the Chief Financial Officer (OCFO) requested the Auditor's certification in connection with the District's issuance of \$431,815,000 in General Obligation Bonds (Series 2016A) to finance certain approved capital projects in the District's Capital Improvements Plan.

This report sets forth the results of the Auditor's analysis of the CFO's FY 2016 local source revenue (net of dedicated taxes) estimate of \$6,898,020,000.²

Objectives, Scope and Methodology

The objectives of this analysis were to:

1. Assess the reasonableness and attainability of the OCFO's fiscal year (FY) 2016 local source revenue estimate (net of dedicated taxes) of \$6,898,020,000.
2. Determine if the issuance of the proposed general obligation bonds would cause the District to exceed the 17 percent revenue limitation, as outlined in D.C. Code § 1-206.03(b)(1).

The scope of this review included financial records and data for FY 2011 through FY 2016, as of April 30, 2016, and FY 2016 estimated local source revenues and economic forecasts.

In conducting this analysis, we analyzed actual local source revenues for FY 2011 through FY 2016 (as of April 30, 2016), and reviewed the estimated local source revenue for FY 2016. We also reviewed the District's FY 2016 budget and economic data and the final official statement supporting the bond issuance.

¹ Request sent from the Office of the Chief Financial Officer's (OCFO) Office of Finance and Treasury (OFT) to the Office of the DC Auditor pursuant to D.C. Official Code, Section 1-206.03 (b)(1).

² See revenue certification letter from the Chief Financial Officer to the Mayor and Council Chairman, dated February 26, 2016.

To gain an understanding of the District's current economic outlook, we interviewed the OCFO Office of Revenue Analysis (ORA) staff, reviewed external local economic data sources and interviewed an economist from George Mason University's Center for Regional Analysis.

Background

D.C. Official Code, Section 1-206.03 (b)(1) states, in relevant part, that:

No general obligation bonds... or Treasury capital project loans shall be issued during any fiscal year in an amount which would cause the amount of principal and interest required to be paid both serially and into a sinking fund in any fiscal year on the aggregate amounts of all outstanding general obligation bonds and such Treasury loans, to exceed 17% of the District revenues... which the Mayor estimates, **and the District of Columbia Auditor certifies**, will be credited to the District during the fiscal year in which the bonds will be issued...(emphasis added)

In compliance with D.C. Official Code, Section 1-206.03 (b)(1), the OCFO requested that the Auditor certify the OCFO revised FY 2016 total local source General Fund Revenue (net of dedicated taxes) estimate. The OCFO requested the certification in connection with the District's issuance of:

- \$431,815,000 aggregate principle amount of General Obligation Bonds (Series 2016A). The proceeds of the Series 2016A bonds will be used to (1) finance capital projects expenditures under the District's Capital Improvements Plan, and (2) pay the cost and expenses of issuing and delivering the Series 2016A Bonds.

The Auditor's certification was based upon an evaluation of the \$6,898,020,000 FY 2016 local source revenue estimate certified by the CFO on February 26, 2016. The CFO's estimate was based upon information that can, and often does, change rapidly thus resulting in revisions to the CFO's estimate after the Auditor's certification. The Auditor does not, and cannot, guarantee the stability of the CFO's estimate submitted for the Auditor's certification. Thus, the Auditor only certifies that the revenue estimate, at the time of certification, appeared sufficiently supported and achievable.

Relative uncertainty in the overall estimating process or unforeseen national and local events may substantially change the District's economic outlook and could result in changes to the revenue estimate that differ significantly from the estimate certified by the Auditor. Additionally, the validity and accuracy of the Auditor's certification analysis are predicated upon the extent to which the OCFO Office of Revenue Analysis (ORA) provided a sound and reasonable FY 2016 local source revenue estimate; fully disclosed information to the Auditor; and provided reliable and accurate information to the Auditor regarding the District's FYs 2011 to 2016 (as of April 2016) revenue collections.³

³ A Management Representations Letter concerning the disclosures and accuracy of the financial data on which the Auditor's certification was based on and signed by the District's Deputy CFO and Treasurer June 23, 2016.

Results of the Auditor’s Examination

In reviewing the fiscal year (FY) 2016 local source revenue estimate of \$6,898,020,000, the Auditor relied on revenue collection results for FYs 2011 to 2015, preliminary year to date FY 2016 revenue collections (as of April 30, 2016), as well as economic indicators, trends and projections provided by the OCFO’s Office of Revenue Analysis, external local economic data, and an interview held with a local economist.

Figure 1 presents the FY 2016 local source revenue estimate submitted by the CFO on February 26, 2016.

Figure 1
FY 2016 Local Source Revenue (net of Dedicated Taxes) Estimate Prepared by the CFO and Certified by the Auditor

Revenue Source	CFO’s February 2016, FY 2016 Local Source Revenue Estimate (net of Dedicated Taxes) (in thousands of dollars)
Property Taxes	\$2,406,419
Sales Taxes	1,141,740
Income Taxes	2,277,908
Gross Receipts Taxes	250,835
Other Taxes	344,037
Total Taxes	6,420,938
Total Non-Tax Revenues	422,082
Lottery	55,000
Revised Local Source Revenue Estimate	\$6,898,020

Source: Revenue certification letter from the Chief Financial Officer to the Mayor and Council Chairman dated February 26, 2016.

The Auditor conducted detailed analysis of the following local tax and non-tax revenue sources: property tax, sales tax, income tax, gross receipts, other taxes, non-tax revenue, and lottery revenue to arrive at our conclusions and subsequent certification.

Key observations from our analysis conducted are noted below.

Property Tax

The Auditor determined that the FY 2016 revenue estimate for property taxes of \$2.406 billion is reasonable and achievable. The FY 2016 revenue estimate increased by \$164 million compared to last year’s estimate. According to the Delta Associates First Quarter 2016 Washington Area Housing Outlook, the Washington metro area experienced a slowdown in price growth with the average sales price declining 1.8 percent from the first quarter of 2015. The general outlook for the regional housing market, however, remains optimistic and is expected to keep price growth at a modest rate of 1 percent to 3 percent. Further, for the first time in three years, the first quarter of 2016 finds that office space

leasing is absorbing a portion of underutilized commercial space. Rental rates for commercial property however are not expected to increase soon.

Sales Tax

For the period of FYs 2011 through 2015, the sales tax has generally seen an increase in revenues. Total annual sales tax revenue collections have increased an average of \$60.5 million or 6 percent from FY 2011 through FY 2015. Based on the OCFO's February FY 2016 revenues estimate, the estimated sales tax collection will be \$1.141 billion, a decrease of \$16 million or 1.38 percent when compared to the same period in FY 2015. In addition, year to date April actual sales tax collections for FY 2011 to FY 2016 generally increased an average of \$27.4 million or 4.7 percent each year. For FY 2016, sales tax collections were \$670.5 million as of April 30, 2016, an increase of \$40 million or a 6.3 percent increase when compared to the same period last year. In reviewing data for recent sales tax collections and forecasts, the OCFO's sales tax estimate for FY 2016 appears reasonable and achievable.

Income Tax

OCFO projects that the total income tax revenue will decrease by 1.6 percent in FY 2016 compared with the previous fiscal year, from a level of \$2,315,843,000 to \$2,277,908,000. This is primarily due to less optimistic forecasts of the non-withholding component of personal income taxes (such as capital gains). According to OCFO, this component "is more closely associated with the stock market performance and recent stock market volatility means that revenue from this source will be uncertain." As a result, OCFO revised their projections of non-withholding income downward to a level consistent with the 10 year average.

The Auditor has determined that the FY 2016 revenue estimate for income taxes of \$2,277,908,000 is both reasonable and achievable. In the five most recent complete fiscal years, total actual income tax revenue has largely come in above expectations, with two notable exceptions. In FY 2011, FY 2012, and FY 2015, revenues came in 6.2 percent, 6.7 percent, and 1.1 percent above estimates. Respectively, while in FY 2013 and FY 2014 actual revenues lagged behind estimates by 1.7 percent and 4.6 percent. As of April 2016, year-to-date total income tax revenue collections increased 1.5 percent over the same period last year.

Additional Observations

The Auditor also considered the following data in analyzing the FY 2016 local source revenue estimate of \$6,898,020,000:

- For the period of FYs 2011 through 2015, the other taxes category has generally seen an increase in revenues. Based on the OCFO's February FY 2016 revenue estimate, the estimated other tax revenue collections will be \$344 million, a decrease of \$116.4 million when compared to the same period last year FY 2015.
- The non-tax revenue components of licenses and permits and charges for services have generally increased from year to year while miscellaneous revenue has fluctuated. Licenses and permits and charges for services have increased on average by 4.1 percent and 6.1 percent, respectively, for each year since FY 2011 while miscellaneous revenue has seen greater fluctuations due to one-time collections that may have increased in a given fiscal year.

- As of April 30, 2016, total collections for fines and forfeitures are \$101.8 million, 50 percent more than collections as of the same period in FY 2015. The OCFO is currently projecting a slight increase in FY 2016 revenue in this tax category of \$5.5 million, a 1.3 percent increase when compared to FY 2015.

Based on the Auditor's review and analysis of historical revenue trends and other economic data, the Auditor concluded that the FY 2016 local source revenue (net of dedicated taxes) estimate is achievable.

Debt Limitation

D.C. Official Code, Section 1-206.03 (b)(1) sets forth a debt limit of 17 percent of the District revenues. Specifically, it states that "...the amount of principal and interest required to be paid both serially and into a sinking fund in any fiscal year on the aggregate amounts of all outstanding general obligation bonds and such Treasury loans" may not exceed 17 percent of the District revenues.

Per the DC Code, the District is only required to include the debt from all outstanding general obligation bonds and Treasury capital project loans in the debt limit calculation. Nevertheless, the District has taken a more conservative approach and included the principle and interest payments related to outstanding income tax secured revenue bonds in the debt limit calculation. Based on our review of the limitation on borrowing calculation provided by OCFO, the District's projected aggregate general obligation bond and income tax secured revenue bond debt service (principle and interest) is projected to be 8.18 percent of the District's FY 2016 estimate revenue of \$6,898,020,000. During the period in which debt is outstanding (2016-2041) the percentage of revenue ranges from 2.38 percent (2038) to 9.49 percent (2018). It does not appear that the 17 percent limitation will be exceeded as a result of the issuance of the general obligation bonds (Series 2016A).

Conclusion

Based on an analysis of information provided by the Office of the Chief Financial Officer of the District of Columbia, as of June 23, 2016; the assumptions supporting the fiscal year (FY) 2016 revenue estimate; and other relevant economic data, the Auditor concluded that the February 26, 2016, FY 2016 local source revenue (net of Dedicated Taxes) estimate of \$6,898,020,000 appeared to be reasonable and achievable.

Therefore, on June 20, 2016, the Auditor certified the \$6,898,020,000 FY 2016 local source revenue (net of dedicated taxes) estimate submitted by the OCFO.

Sincerely,



Kathleen Patterson
District of Columbia Auditor

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