

# **Transmittal Letter**



ANTHONY A. WILLIAMS  
MAYOR

March 21, 2005

The Honorable Linda W. Cropp  
Chairman  
Council of the District of Columbia  
John A. Wilson Building  
1350 Pennsylvania Avenue, NW, Suite 504  
Washington, DC 20004

Dear Chairman Cropp:

It is my pleasure to submit to you the *Fiscal Year 2006 Budget and Financial Plan: Lifting All Communities*. With our fiscal house in order, city services improved, and a robust environment for economic and housing development, we now face the challenge and opportunity to ensure that the rising tide we have created lifts all communities. And now, when the District's economy is strong and revenues are available, it is our responsibility to ensure that our renaissance reaches every neighborhood in the District of Columbia.

#### Budget Summary

This budget funds ground-breaking initiatives that will reshape the physical landscape of the District of Columbia and strengthen our social fabric in a fiscally-responsible and balanced manner. I have developed this budget around the core principles of fiscal responsibility, fairness, strategic investments in critical social needs, and improving our infrastructure. With input from residents, I've determined my priorities to be housing, employment, better transportation infrastructure, and targeted services for youth, while maintaining my commitment to education and public safety.

Despite the temptation to allocate all available resources to programs during strong fiscal years, my budget reflects a high standard of fiscal responsibility by providing for \$41 million in new tax relief in addition to \$53 million in tax cuts. This budget also responsibly ensures that we do not rely on one-time funding for long-term programs.

The proposed FY 2006 core budget supports \$6.64 billion in total funding and meets the requirements of the legislated growth cap. The complete FY 2006 budget includes the core budget, critical investments in social needs and our city's infrastructure, as well as debt alleviation. The majority of the increase over the core budget is sustained with responsible one-time use of our fund balance. In total, this budget supports \$7.19 billion in funding and supports 33,609 full-time equivalent (FTE) staff.

### New Budget Initiatives

The FY 2006 Budget and Financial Plan will lift all communities by making major new investments in the following initiatives:

#### **New Communities**

New Communities is a massive investment in the housing and physical infrastructures of the city's most challenged neighborhoods. Although many District neighborhoods are undergoing rapid change and transformation, there are still places in the city where crime, unemployment, and truancy converge to create intractable physical and social conditions. The New Communities initiative is more than the bricks and mortar transformation of neighborhoods. It is a comprehensive community development program aimed at lifting people and neighborhoods by addressing a community's social and economic ills, along with its physical problems.

The long-term goals of New Communities are to meet the needs of lower-income District families and residents by providing critical social support services; decreasing the concentration of poverty and crime; and enhancing access to education, training and employment opportunities, but I will begin this effort immediately with a large-scale investment in our housing infrastructure with a special focus on public housing. The budget includes \$55.4 million for this program, which is a first installment on a long-term District investment of more than \$200 million with plans to leverage total investment in the targeted communities of more than \$1 billion. Long-term local funding for this project will only be possible through the securitization of \$15 million from the Housing Production Trust Fund.

#### **Way-to-Work**

Since the height of the most recent recession, the national unemployment rate has fallen from 6.3 percent in June 2003 to 5.4 percent in November 2004. In the District however, the unemployment rate has climbed to its highest level since August 1998, reaching 9.0 percent in December 2004. Unemployment, income, and social ills data demonstrate that the great majority of chronically unemployed, hard-to-serve District residents are concentrated in a few geographic pockets throughout the District. In order to meet the challenges presented by these pockets of despair, we have developed and funded \$20.4 million in new employment strategies and programs that will help the hard-to-employ to

overcome their barriers to employment, successfully compete in today's labor market, and achieve economic self-sufficiency.

### **Great Streets**

It is important to extend the District's downtown economic success to the neighborhoods throughout the city by leading private investment with public investment. To accomplish this, I propose to securitize new bus shelter revenue to raise approximately \$88 million to invest in the revitalization of the District's corridors, unleashing the commercial potential of Georgia Avenue, H Street, NE, Nannie Helen Borroughs, NE, Benning Road NE and other neighborhood arteries. In order to complement this investment in physical infrastructure with the revitalization of the commerce along these streets, I am dedicating an additional \$16.6 million to attract new businesses and to help existing businesses flourish.

### **Bridges and Roads**

My budget reflects a major new investment in our city's physical infrastructure, starting with a \$212 million local investment in the District's streets and bridges along the Anacostia River. This project, which is funded at \$35 million in FY 2006, will make critical infrastructure improvements needed to alleviate congestion and overflow traffic in surrounding neighborhoods. Long term financing for this project will require the Council's approval of the securitization of \$15 million from the District's annual parking tax revenues.

In addition, I am also dedicating approximately \$15 million per year for improvements to our streets. Furthermore, I have instructed that any additional revenue that may become available before the Council approves the FY 2006 budget shall also be dedicated to improvements in local roads.

### **Education**

My FY 2006 budget includes a total of \$1 billion in local funds to educate approximately 80,000 students within the District of Columbia Public Schools (DCPS) and public charter schools. This funding level represents an increase of \$81.6 million, or 9.0 percent, over the FY 2005 budget. The FY 2006 budget is aligned with the Superintendent's core budget request of \$775 million, provides an additional \$25 million to support strategic educational investments at both DCPS and charter schools, and funds eleven new charter schools. Through this budget we will also provide \$147 million in capital funding to support rehabilitation and modernization of DCPS school buildings.

In addition to supporting DCPS and charter schools, this budget makes major investments in higher education and lifelong learning. This budget includes an additional \$8.3 million to expand and enhance the nursing, teacher education, workforce development, and academic transition programs at the University of the District of Columbia. It will also

enable many more low-income students to attend college by increasing the funding available for Leveraging Education Assistance Program tuition grants.

In support of the Lifelong Learning Initiative, the FY 2006 budget includes an additional \$8.2 million for the District of Columbia Public Library to extend hours of operation from 40 to 52 hours per week, improve reference reading materials, and build and renovate facilities in five neighborhoods. Funding has also been included to continue the Adult and Family Literacy Program which provides literacy coaches and direct instruction to the District adult learner population.

### **Children and Youth**

Children and youth are among the most vulnerable of our residents. This budget supports additional funding to provide education, health, enrichment and other opportunities for our children and youth, which is critical in preventing juvenile violence and providing meaningful supports so that young residents grow into productive, engaged members of the District's community. This budget proposes to allot \$14 million for the construction and renovation of recreation and community facilities. Another \$77.5 million will be dedicated to expanding and enhancing out of school enrichment, recreation and leisure programs, which promote education, socialization and growth of young people and also provide positive alternatives to delinquency. To eliminate the waiting list for subsidized child care, I am allocating \$6.5 million in additional funding for childcare programs. These funds will provide 1,200 children with early learning opportunities that are critical to achieving school readiness. In addition, I am proposing \$6 million to expand juvenile intervention initiatives, including paid internship programs, improved mental health services, and infant mortality reduction activities.

### **Health and Welfare**

In the area of health care, the FY 2006 budget demonstrates my continued commitment to providing health services to residents, particularly those who are underserved. My proposed budget augments primary health care services and increases support for community health centers by \$9 million, which will result in the ability to support additional patients from underserved communities. Building upon the support of school health programs in DC public and charter schools, this budget increases the amount of funding for schools, enabling additional school nurses and aides to be hired. This will result in children having better access to nurses and will also allow medically fragile children to receive increased medical attention. In addition to continuing to support on-going programs and activities for aging residents, funding is requested for the construction of Senior Wellness Centers in Wards 4 and 6. The budget also includes \$73 million to support the District's ten-year plan to end chronic homelessness. This funding will go towards providing enhanced wraparound services for homeless families and individuals, building new housing assistance centers, providing eviction prevention services, and creating subsidized housing.

### Tax Relief

For the first time as Mayor, my budget also includes significant broad and progressive tax relief. Starting in FY 2006, District residents will benefit from \$94 million in new tax relief, including \$53 million in scheduled tax cuts and \$41 million in new proposals. This tax package provides for a balance between income tax relief and property tax relief that is especially targeted to low-income families. All property owners who are coping with rapidly rising home value assessments will benefit from \$211 in tax relief from an increase in the homestead deduction from \$38,000 to \$60,000. Low-income homeowners will be further protected from rising tax bills by a new provision that will allow households earning less than \$50,000 per year to defer any property tax increases until they sell their house. This will provide for neighborhood stability, especially for seniors who have difficulty meeting rising property tax costs in rapidly changing neighborhoods.

I have also proposed changes that will reduce our income tax rates. First, I am increasing the local Earned Income Tax Credit (EITC) program to make the District's program among the most generous in the nation by adding a non-refundable credit of 50 percent on top of our refundable credit that provides 25 percent of the benefits offered by the federal government. Also, for the first time, I will be expanding this benefit to cover non-custodial parents who are paying their child support. This provides a work incentive and ensures the equal treatment of parents. In addition to targeted income tax relief, I am providing for a \$500 increase in the standard deduction and a \$130 increase in the personal exemption, which will benefit all taxpayers in the city. These income tax proposals will provide a more progressive complement to the broad tax changes that will be triggered by tax parity in FY 2006. Tax parity reduces the rates of all three of the District's income tax brackets, including a reduction in the top rate from 9.0 percent to 8.7 percent.

### Conclusion

I have proposed a FY 2006 Budget and Financial Plan that is balanced in a fair and responsible manner, with less bureaucracy, continued fiscal discipline, and major new investments in areas of need. I look forward to the Council's review of my proposal, and I look forward to our continued cooperation in finalizing and executing this package.

Sincerely,



Anthony A. Williams  
Mayor



**FY 2006 Revenues.** In FY 2006, District local source revenue is forecasted to be \$4.51 billion, an increase of 5.6 percent over FY 2005 after tax policy changes. Underlying the District's robust revenue growth is continued strength in the District's real estate market and strong growth in personal income. Substantial increases in prices and the number of transactions in both residential and commercial real estate markets were major sources of revenue gains in FY 2003 and FY 2004, and are expected to contribute significantly to FY 2005 and FY 2006 revenues. Going forward, our revenue projections assume District personal income will grow between 5 and 6 percent annually, and the financial markets will continue their recovery.

The Mayor's FY 2006 Proposed Budget includes tax policy reductions of \$41.1 million and revenue shifts to capital of \$30.0 million. The tax policy reductions include an increase in the homestead deduction, an increase in the local Earned Income Tax Credit, increases in both the standard deduction and the personal exemption, and a property tax deferral for low-income homeowners. The revenue shift to capital is to provide a dedicate stream of revenues to finance major investments in bridges and roads.

**EXPENDITURES – Local Funds**

The magnitude of resources available for budgeting, both from the improved level of current revenues and the sizable accumulated surplus in the fund balance, is a definite factor and an opportunity in the formulation of the FY 2006 local funds operating budget. As is evident from the briefings I have provided, the District's economy and the revenue stream it produces to support District operations have out performed expectations. Further, this level of economic performance, revenue generation, and fund balance build up was not envisioned when the legislative growth caps were instituted for the FY 2006 local funds operating budget. For example, compliance with the 4.7% growth cap leaves approximately \$149.4 million in unprogrammed FY 2006 revenues. As shown in Table 2 below, the Mayor has weighed these financial opportunities in formulating his policy goals for FY 2006, as incorporated into his proposed budget.

**Table 2** **General Fund**  
**Proposed FY 2006 Budget Summary – Local Funds**  
*(\$ in millions)*

Total Revenues	\$ 4,562.9
Core Budget within legislative growth cap	4,413.5
Revenues in excess of legislative growth cap	<u>\$ 149.4</u>
Less Tax Policy Reductions and Revenues Shift to Capital	(71.1)
Adjusted Revenues in excess of legislative growth cap	<u>\$ 78.3</u>
Add Appropriated fund balance	466.9
Sources for Program and Fiscal Policy Initiatives	<u>\$ 545.2</u>
Less Program Policy Initiatives	(352.4)
Less Fiscal Policy Initiatives	<u>(191.8)</u>
Projected FY 2006 Operating Margin	<u>\$ 1.0</u>

The Mayor's FY 2006 local operating expenditure budget submission includes three requests: a core budget; program policy initiatives; and fiscal policy initiatives. The core budget request is in compliance with the legislative growth cap. The program policy initiatives are enhancements composed of both recurring and non-recurring expenditures designed for *Lifting All Communities*. The fiscal policy initiatives are Mayoral recommendations to address the long-standing unfunded liability for post-1987 retiree health benefits and to reduce the impact of previous, accelerated capital spending on the capital fund.

Table 3

**General Fund**  
**FY 2006 Local Budget Submission**  
*(\$ in millions)*

Fund Type	FY 2005	FY 2006	Change	% Change
<b>Core Budget</b> within legislative growth cap	<b>\$4,186.0</b>	<b>\$4,413.5</b>	<b>\$ 227.5</b>	<b>5.4%</b>
<b>Program Policy Initiatives:</b>				
Community Investments	-	78.3	78.3	n/a
Resident Dividends	-	75.2	75.2	n/a
PayGo Capital	-	198.9	198.9	n/a
Policy Shifts to O Type funds	-	(54.4)	(54.4)	n/a
Net Change: Core Budget & Program Policy Initiatives			<u>\$ 525.5</u>	12.6%
<b>Non-recurring Fiscal Policy Initiatives:</b>				
Post Employment Health Benefits	-	138.0	138.0	n/a
Contribution to Capital Fund Balance	-	53.8	53.8	n/a
<b>Total Local Funds Request</b>	<b>\$4,186.0</b>	<b>\$4,903.3</b>	<b>\$ 717.3</b>	<b>17.1%</b>

The Mayor's FY 2006 core local budget proposal is \$4,413.5 million. This budget includes \$28.8 million in general operational enhancements and \$100.8 million in reductions to current programs for a net increase of \$227.5 million, or 5.4%, over FY 2005 revised budget. When the approved FY 2005 local funds budget is adjusted for pending supplemental appropriations, the Mayor's FY 2006 core local budget is consistent with the legislatively mandated expenditure growth cap. FY 2005 supplemental appropriations are Council approved budget revisions, which not only increase the FY 2005 baseline budget but also have out year impacts, and will increase the legislative growth cap from 4.7% to 5.4%.

Next, in addition to the core local budget, the Mayor also has submitted three policy initiatives requiring \$352.4 million in local funds: Community Investments of \$78.3 million, Resident Dividends of \$75.2 million and Paygo Capital of \$198.9 million. Only the \$78.3 million of the Community Investments policy initiative represents recurring costs that will become part of the District's baseline budget and financed by higher, on-going revenues.

A third and final component of the Mayor's submission includes \$191.8 million in nonrecurring fiscal policy initiatives aimed at continuing and improving the District's strong financial position. The discrete components of this initiative include \$138 million for funding post employment benefits (OPEB), a growing liability, and a \$53.8 million contribution to the Capital Projects Fund to pay for previous capital spending.

The Mayor's total local funds budget request for FY 2006 is \$4,903.3 million for an overall increase of \$717.3 million or 17.1% over the prior fiscal year.

**FINANCING THE LOCAL BUDGET REQUEST**

The core budget is financed with revenues within the legislative growth cap. To finance both the program and fiscal policy initiatives, the Mayor utilizes the \$149.4 million in FY 2006 revenues that exceed the cap (mentioned above) and \$466.7 million from the accumulated fund balance. Table 3 demonstrates that

the planned drawdown of fund balance will reduce the accumulated surplus for local funds to a projected \$752.9 million by the end of FY 2006.

**Table 4** **General Fund**  
**FY 2006 Local Fund Balance Analysis**  
*(\$ in millions)*

Projected Beginning Fund Balance (October 1, 2005)	\$ 1,218.8
Appropriated for FY 2006	(466.9)
Projected FY 2006 Operating Margin	<u>1.0</u>
Projected Ending Fund Balance (September 30, 2006)	<u>\$ 752.9</u>

**PROPOSED FY 2006 GROSS FUNDS BUDGET**

The proposed FY 2006 gross funds operating budget is \$7,185.6 million, an increase of \$867.3 million, or 13.7 percent, over the approved FY 2005 gross funds budget of \$6,318.3 million. The \$867.3 million expenditure increase is comprised largely of a \$717.3 million increase in the local budget (including \$465.9 million of one-time spending), which reflects the Mayor's proposed core budget, the program policy initiatives and fiscal policy initiatives discussed above. The other \$150.0 million increase in non-local funds reflects projected expenditures in federally funded programs (\$8.1 million) including Medicaid and in programs supported by user fees, fines, the dedicated portion of deed recordation and transfer taxes (for housing production), and other Special Purpose revenues (\$71.4 million). A small decrease (\$2.5 million) is projected in Private Grants, which slightly offsets the projected expenditure increases in federal funds and Special Purpose Revenues. The local and non-local funding components of the Proposed FY 2006 gross funds budget and the changes from FY 2005 are summarized in Table 5 below.

**Table 5** **FY 2006 Gross Funds Budget**  
**By Fund Type**  
*(\$ in millions)*

<u>Fund Type</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>Change</u>	<u>% Change</u>
Local	\$4,186.0	\$4,903.3	\$ 717.3	17.1%
Federal	821.5	862.6	41.1	5.0%
Federal Medicaid Payment	963.8	1,003.8	40.0	4.2%
Private Grants	14.2	11.7	(2.5)	(17.6)%
Special Purpose (O Type)	332.8	404.2	71.4	21.5%
<b>Total Gross Funds</b>	<b>\$6,318.3</b>	<b>\$7,185.6</b>	<b>\$ 867.3</b>	<b>13.7%</b>

**CAPITAL IMPROVEMENTS PLAN**

The District faces a wide variety of infrastructure needs, placing great demands on its Capital Improvements Plan (CIP). The total proposed appropriation request for the FY 2006 - FY 2011 CIP is \$1.842 billion for all sources (excluding the Highway Trust Fund). This six-year plan includes a net increase in budget authority of \$622 million (\$682 million of new budget authority offset by \$60 million of rescissions). The increased budget authority will be financed by: General Obligation (G.O.) bonds; the

Master Equipment Lease Program; asset sales; and, alternative financing vehicles such as Certificates of Participation. The FY 2006 capital program consists of \$540 million in planned capital expenditures to be financed by \$341.1 million in new G.O. bond issuance and \$198.9 million of pay-as-you-go (PAYGO) transfers from the General Fund balance.

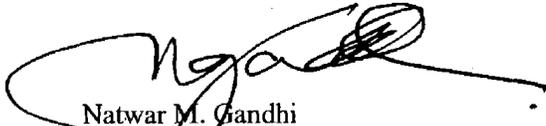
## PERFORMANCE BUDGETING

This budget also reflects our continued progress implementing performance-based budgeting (PBB). In fiscal year 2005, we transitioned 11 new agencies to PBB for a grand total of 67 agencies now fully enrolled in PBB for FY 2006. These 67 agencies account for nearly 63 percent of the District's annual gross operating budget. Transition to PBB is a key accomplishment because it establishes a clear relationship between the funding agencies receives, the programs they operate, and the results that they must achieve. A critical component of PBB is development of programmatic benchmarks to assist policy makers, District executives and the public in assessing the value of the District's programs and determining opportunities for improvement. The current set of benchmarks for District programs has grown from 39 benchmarks for 18 agencies in FY 2005 to 71 benchmarks for 26 agencies in the FY 2006 budget submission.

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The leadership provided by you 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 this balanced budget for FY 2006. As a result, I am certifying that the FY 2006 Budget and Financial Plan, as proposed, is balanced for FY 2006 and beyond. I look forward to continuing to work with you and the Council during the forthcoming budget deliberations.

Sincerely,



Natwar M. Gandhi  
Chief Financial Officer