DC Fiscal Policy Institute

An Affiliate of the
Center on Budget and Policy Priorities
820 First Street NE, Suite 460
Washington, DC 20002
www.dcfpi.org

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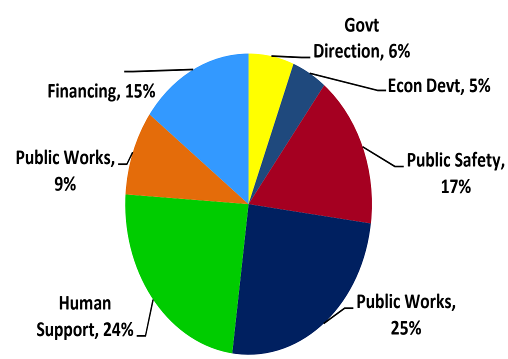
WHAT'S IN THE FINAL FY 2011 BUDGET?

On May 26, the DC Council passed the final budget for the 2011 fiscal year, which begins in October of this year. The proposed general fund budget — the portion supported with local taxes and fees — is $6.16 billion.[1] When federal funds also are considered, the FY 2011 budget is $9.5 billion.

The FY 2011 general fund budget is about $80 million higher than the approved FY 2010 budget, after adjusting for inflation — an increase of about one percent. (Unless otherwise noted, all figures in this analysis are adjusted for inflation to equal FY 2011 dollars.) Yet this modest boost in local spending is needed to replace federal stimulus dollars that were available for 2010 but will not be in 2011, as well as to address rising expenses in some parts of the budget such as special education. When these are taken into account, funding for most services in the FY 2011 budget is less than the amount available for FY 2010.

FIGURE 1: HOW DC'S FY 2011 BUDGET WILL BE ALLOCATED

DC's Proposed FY 2011 General Fund Budget: $6.16 Billion



The coming fiscal year represents the third year the District has faced budget problems caused by the recession, which has reduced the city's revenue collections at a time when a record number of residents are out of work and in need of assistance. DC's revenue collections fell by roughly $500 million between 2008 and 2009 and have been stagnant since then. Base revenues for 2011 (before considering any proposed increases) are approximately $100 million lower than in 2010.

This report reviews the key elements of the FY2011 budget. As Mayor Fenty worked to develop a budget proposal, the city faced a substantial gap between expected resources and the costs of city services. This review finds that several steps were taken to address DC's shortfall, including spending reductions, revenue increases, and use of surplus funds in certain budget accounts. Nevertheless, the FY 2011 budget is a lean one; it reflects very few funding increases and a wide array of cuts — including public safety, public works, and social services.

Moreover, the proposed general fund budget for FY 2011 is roughly $600 million lower than in FY 2008, after adjusting for inflation. The proposed budget for next year keeps in place many cuts that have been made since 2008 — in areas ranging from libraries to child care — in addition to calling for significant additional reductions in services.

This analysis is part of an online "Budget Toolkit" developed each year by the DC Fiscal Policy Institute, which can be found at www.dcfpi.org.

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[1] The general fund budget includes the "local funds budget" – programs supported by the general pool of taxes and fees collected by the District — as well as services supported by "special purpose" revenues or "dedicated taxes."

How Did the Budget Change from FY 2010 to FY 2011?

The FY 2011 general fund budget — the portion of the budget supported by local revenue sources — is $6.16 billion, which represents a 1 percent increase over the $6.08 billion approved budget for FY 2010 budget, after adjusting for inflation. For two reasons, however, the reality is that the District has fewer resources for most of its programs in FY 2011.

- **Loss of federal stimulus funds.** For 2010, the District was able to use stimulus funds instead of local funds to help maintain some DC programs. With stimulus funds largely running out in FY 2010, the FY 2011 budget includes $100 million of local funds for public schools and Medicaid to replace federal stimulus funding. Taking that into account, the FY 2011 budget is smaller than the FY 2010 budget.[2]

- **Increased costs in some parts of the budget.** Over the past two years, DC's budget has seen large increases in a number of areas — caseloads for the city's health care programs, enrollment in public and charter schools, and special education — and funding for those areas has risen as a result. In FY 2011 alone, these three parts of the budget will increase by more than $100 million as a result of caseload growth. In addition, the costs of maintaining government services rise each year due to inflation and other factors.

How Did the Budget Change from the Mayor's Proposal to the Council's Vote?

The DC Council approved a spending plan for Fiscal Year 2011 on May 26, largely adopting the Mayor's proposed budget but making key restorations, including a number of programs that largely help the city's low- income residents. These changes are summarized in Table 1.

TABLE 1
Funding Cuts and Restorations for Selected Low-Income Programs In the FY 2011 Budget (figures in millions)

	Budget Cuts in Mayor's Proposal	Funds Restored by DC Council	Funds Not Restored
Access to Justice	$1.1	$1.7	
Adult Education	$2.3	$1.0	**$1.3**
Adult Job Training	$4.6	$4.6	
Captive Insurance	$8	$7	**$1**
Child Care	$4	$3.5	**$0.5**
Earned Income Tax Credit	$1	$1	
Emergency Rental Assistance	$1.3		**$1.3**
Grandparent Caregiver	$2	$2	
Housing Purchase Assistance Program	$2.1	$2.1	
Healthy Families/Thriving Communities	$1	$1	

[2] The FY 2011 DC budget assumes that federal Recovery Act funds for Medicaid will be provided for three-fourths of the year, based on a proposal included in President Obama's budget for FY 2011. As of the publication of this DCFPI analysis, Congress has not approved that proposal. If not approved, federal Recovery funds for Medicaid will last for one-fourth of DC's 2011budget instead of three-fourths.

The Council found the money mostly in two ways. Some programs had funding restored through the work of specific Council committees. For example, the Committee on Public Safety and Justice decided to shift money from other areas within their budget purview to restore a $1.1 million cut to Access to Justice, as well as adding an additional $600,000, to make a total of $1.7 million restored to the program. Most council committees looked to give money to programs within their oversight, though in a few cases money was transferred from one committee to another. This happened with the grandparent caregiver program, for example.

Other programs received funding through last-minute budget deliberations within the Council's Committee of the Whole. In budget discussions leading up to the Council's vote, council members prioritized programs they wanted removed from the funding chopping block. A list of programs with funding needs was generated by DC Council Chairman Vincent Gray, and monies were identified.

The Council adopted several small tax changes but did not vote in favor of any major revenue increase, limiting its ability to find funds for programs without impacting funding for other programs. A proposal to create a new income tax bracket for households with taxable income above $350,000 was introduced in the form of an amendment to the budget on May 26, but the measure was rejected in an 8 to 5 vote. (Tax and fee changes in the FY 2011 budget are discussed in more detail below.)

Overview of the FY 2011 Budget

The District's budget includes more than 80 operating agencies, with budgets ranging from under $100,000 to more than $600 million in local funds. These agencies are grouped into seven major functional categories, known as "appropriation titles."

Table 2 shows how funding will change for each appropriations title under the FY 2011 budget. It reveals that funding would fall for each program area other than education, which would increase by 5 percent. Yet even in the case of education, the increases generally do not reflect new programs or initiatives. Nearly all of the education increase will come from higher special education expenses and continued expansion of public charter schools. Local funding also would grow for DC Public Schools, but this would be offset by a reduction in federal funds.[3] (A more detailed description of funding changes by appropriations title is included in an appendix.)

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[3] The FY 2011 budget includes several accounting changes that affect the budgets for many agencies. Contracting and human resource functions that had been budgeted in all city agencies in FY 2010 are now included in the budgets for the city's central contracting and personnel agencies. In addition, the FY 2011 budget includes a new centralized agency to reflect DC government rent, utility, and related expenses. Those expenses had been reported in individual agency budgets in FY 2010. To make FY 2011 budget figures comparable with prior-year budgets, this report shifts these fixed costs back to individual agency budgets.

In addition, DCFPI's analysis makes some adjustments to reflect the impact of federal stimulus funding. For example, the FY 2011 budget includes $37 million in local funding to replace federal Medicaid funds that were provided under the stimulus package in FY2010. Because this does not reflect an expansion of local services, this analysis adds $37 million to the FY 2010 local budget to make it comparable with FY 2011 figures.

For this reason, the figures reflected in this report may not match figures reported in the FY 2011 budget.

TABLE 2 CHANGE IN DC's GENERAL FUND BUDGET, FY 2010-FY 2011			
Appropriations Title	**FY 2010 Approved**	**FY 2011 Proposed**	**Change, 2010 to 2011**
Government Direction	$379	$360	-4%
Economic Development	$329	$283	-12%
Less Low-Income Agencies*	$164	$142	-13%
Public Safety	$1,035	$1,021	-1%
Education	$1,465	$1,539	5%
Human Support	$1,469	$1,446	-2%
Plus other Low-Income Agencies*	$1,634	$1,587	-3%
Public Works	$587	$570	-3%
Financing	$924	$897	-3%

NOTES:
All figures are in millions and adjusted for inflation to equal FY 2011 dollars.
These figures include some adjustments to make figures comparable. See footnote 3.
* "low income agencies" include Employment Services, Housing and Community Development, Housing Authority Subsidy, and Housing Production Trust Fund.

The changes reflected in the final FY 2011 budget include the following:

- **Human Services and Health:** The DC Council restored a number of proposed cuts to health and human services programs, including cash assistance for grandparents caring for their grandchildren and adult education and training programs. The Council restored only $1 million of a $7 million cut to the District's Interim Disability Assistance program, which provides cash assistance to residents with disabilities, and did not restore funding for homeless services or reimbursement rates for several Medicaid health services.

- **Public Safety:** The budget cut $16 million from the Metropolitan Police Department, after adjusting for inflation, including savings from "maintaining sworn strength," eliminating vacant civilian positions, and reducing or eliminating services such as the pager contract. It also reduced staffing at the Department of Corrections. The budget for the Fire and Emergency Services Department will increase 5 percent in FY 2011, adjusting for inflation.

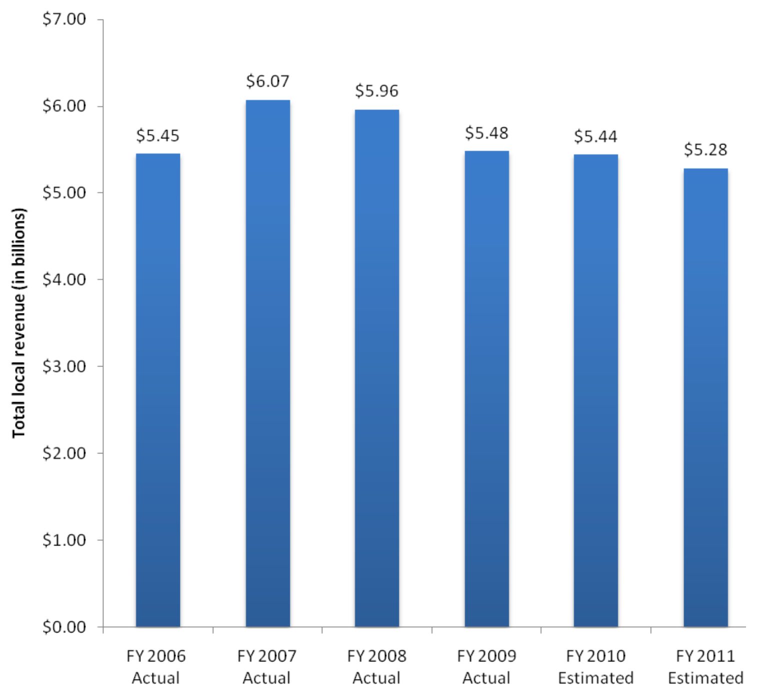
- **Public Works:** Funding for the Department of Public Works will fall eight percent. The Mayor's budget proposed significant cuts to DPW positions for street and alley cleaning, commercial corridors cleaning, the leaf collection program, and the SWEEP program which monitors and fines residents and businesses for trash violations. The DC Council restored funding for those positions through additional anticipated revenue generated from the SWEEP program. Funding for the Department of Transportation also will decline, largely due to a cut in DDOT's "Infrastructure" program. It is unclear how this cut will impact services.

- **Education:** As noted, funding for public charter schools and special education would increase. Local funding also would grow for DC Public Schools, but this would be offset by a reduction in federal funds. The DC Council added $5.9 million to the budget for public charter schools to increase schools' facility allotments from $2,800 to $3,000 per student. The Council also restored $3.5 million of a $4 million cut to child care vouchers for low-income families.

- **Other:** Funding for DC Public Libraries and the Department of Parks and Recreation will remain flat or slightly reduced from FY 2010, even though both agencies are expected to open new locations in FY 2011. The budget also cut $12 million from a Neighborhood Investment Fund that is intended to support improvement projects in 12 selected neighborhoods.

The impact of the recession on DC's finances is even clearer when the FY 2011 budget is compared with 2008, the last year before the recession. As noted, the District's tax collections fell sharply between 2008 and 2009. Excluding changes in tax policy, total tax collections fell nearly $500 million that year. And tax collections have been fairly stagnant since. (See Figure 2.)

FIGURE 2
DC REVENUE COLLECTIONS FELL SHARPLY AFTER 2008



Source: DC Budget and Financial Plan and DC Chief Financial Officer Revenue Estimates

As a result of the drop in revenues, the general fund budget for FY 2011 is $600 million lower than in FY 2008, after adjusting for inflation, and includes significant reductions in all appropriations titles. (See Figure 3.)

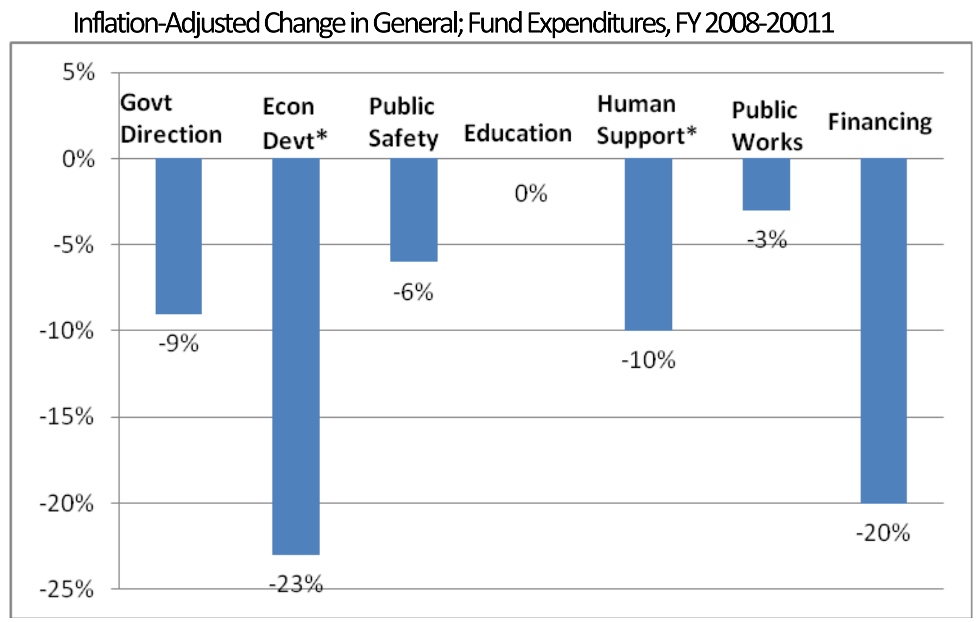
Beyond new cuts described above, the FY 2011 budget also would keep in place many cuts that have been made since 2008, such as:

- **Affordable Housing:** Support for DC's affordable housing programs under the proposed FY 2011 budget would be one third lower ($41 million) than in FY 2008. This includes cuts to all major housing programs, including first-time homebuyer assistance, rent subsidies, and the Housing Production Trust Fund.

- **Child Care:** Funding for DC's child care programs in FY 2011 is nearly one-fifth lower than in FY 2008, even though the reported number of children in child care has held fairly steady at 22,400 in 2007 and 22,000 in 2009.

- **Recreation:** The FY 2011 budget for the Department of Parks and Recreation is one-fourth lower than in FY 2008.

FIGURE 3
DC' BUDGET HAS DECLINED SIGNIFICANTLY SINCE 2008



*For purposes of this comparison, the following agencies and programs are included in Human Support rather than Economic Development: Employment Services, Housing and Community Development, Housing Authority Subsidy, and Housing Production Trust Fund.

- **Social Service Centers:** The FY 2011 budget includes a reduction of 16 eligibility determination workers for nutrition, cash assistance, and health care programs. In FY 2009 and FY 2010, 99 eligibility determination services positions were eliminated and two service centers were closed, at the same time that DC's TANF (welfare to work) caseload was increasing by 11 percent. The reductions in staff and service centers resulted in clients often waiting days to submit paperwork or have their applications processed.

Steps Taken to Balance the FY 2011 Budget

As Mayor Fenty began developing budget proposals for FY 2011, the District faced a gap of roughly $500 million between projected revenues and the cost of maintaining current services. The FY 2011 budget reflects a number of actions taken by the Mayor and the Council to address the shortfall.

- **Use of Federal Stimulus Funds:** While much of the stimulus funding was limited to FY 2010, the District has some remaining stimulus funds, and it will receive roughly $112 million in new stimulus funds in FY 2011 for DC's Medicaid program. Most of this ($75 million) is expected to come from actions taken by the federal government this year to extend Medicaid assistance to states and DC.[4]

[4] The proposal to extend Medicaid assistance was included in President Obama's FY 2011budget. As of the publication of this DCFPI analysis, the Congress has not approved this proposal.

- **Restructuring the City's Debt:** The DC Chief Financial Officer has taken steps to refinance a portion of the city's debt. This will reduce payments in the near-term for principal and interest on bonds the city issues to support capital construction projects, though it also will increase payments modestly over the long-term. The savings will be realized starting in the current year and total $60 million in FY 2011.

- **DC Government Staff Reductions and Salary Freezes:** The FY 2011 budget eliminates nearly 400 government positions, according to a mayoral press release, adding to staff reductions from previous years. Employment by the District government will total 28,200 in FY 2011, down from 31,900 in FY 2008. The Mayor also proposed freezing salaries for DC government employees to save $20 million. The DC Council restored $1.1 million to eliminate the salary freeze for all legislative branch agencies.

- **New Revenues:** Mayor Fenty's proposed FY 2011 budget included about $100 million in additional revenues to help address the city's sharp drop in revenue collections. The Mayor's revenue proposals included increased traffic and parking fees and fines, a one percent fee on hospital patient charges, an increase in business fees, and an increase in a fee applied to phone bills to support 911 services. The Council rejected several of the Mayor's proposals, including the hospital fee, an increase in hourly parking meter rates, and the increase in the phone bill fee. The Council also rejected a proposal to increase income taxes for high-income DC residents and instead voted to expand the sales tax to soda and medical marijuana and replace the hospital fee with a per-bed assessment.

- **Tapping Surpluses in Special Funds:** The District budget includes hundreds of "special purpose" accounts — often referred to as "O-type" funds — that are financed by fees, fines, assessments, or reimbursements, and are dedicated to certain purposes. One example is the Home Purchase Assistance Program (HPAP), which provides low- and no-interest loans to help low-income first-time homebuyers, and it is financed in part through the repayments of the loans granted by the program. In recent years, many of these funds have built up surpluses. The Mayor proposed drawing nearly $100 million from special accounts to cover general budget expenses. While many Councilmembers expressed concern with drawing down the District's fund balance, the Council ultimately voted to accept the Mayor's proposal. (For more information, see the Fund Balance section of this report.)

Revenue Issues in the FY 2011 Budget

Mayor Fenty's proposed FY 2011 budget called for raising about $100 million in additional revenues to help address the city's sharp drop in revenue collections — limiting the amount of budget cuts needed to create a balanced budget. The DC Council rejected and modified several of the Mayor's tax proposals, and it also adopted some new revenue increases. After considering the Council actions, revenue increases in the final FY 2011 budget total $85 million (Table 3).

TABLE 3 REVENUE INCREASES IN THE FY2011 BUDGET		
	Mayor Proposed Budget (In $Millions)	**Council-Approved Budget (In $Millions)**
Traffic and Parking		
Traffic Fines	$28.0	$28.0
Parking Meters	$3.6	—
Residential Parking Permits	$1.2	$1.2
Other	$1.1	$1.1
Health Care		
1% Fee on Hospital Patient Revenue	$25.3	—
2% premium tax applied to Medicaid HMOs	$8.6	$8.6
$1,500 fee per licensed hospital bed	—	$6.3
Tax on Intermediate Care Facilities	$1.7	$4.7
Business Fees		
Steel Plate Fee	$3.1	$3.1
Technology Fee on Building Permits	$2.7	$2.7
Other	$3.8	$3.8
E-911 Fee Increase	$7.1	—
Miscellaneous Taxes and Fees	$4.0	$4.0
EITC Reduction	$1.0	—
High-Tech Tax Incentive Reduction	$1.3	—
Hospital and Medical Services Community Reinvestment	$5.0	$5.0
Apply Sales Tax to Soda	—	$7.9
Apply Sales Tax to Medical Marijuana	—	Unclear
Set 5%property tax rate on vacant property		$2.5
Denying Withholding to Delinquent Taxpayers	--	$4.4

The key tax provisions in the final FY 2011 budget including the following:

Traffic Fines and Parking: The FY 2011 budget will raise $30 million through increased fees and fines in this area.

- **$28 million - Traffic Fines:** The budget authorized the increase of 71 different fines for motor vehicle moving infractions such as speeding, running a red light, running a stop sign, turning from the wrong lane, and passing a stopped school bus.

- **$2.3 million – Other:** Residential parking permits will increase from $15 to $25. The District's current fee is lower than fees charged in Arlington County and Montgomery County. Alexandria charges $15 for the first vehicle registered at an address, $20 for the second, and $50 for the third. The budget also sets a fine when cars are towed out of rush hour lanes.

As discussed below, the DC Council rejected a mayoral proposal to increase parking meter rates by $3.6 million.

Health-Related Taxes and Assessment: The FY 2011 budget will raise $20 million through new or increased levies on health providers.

- **$6.3 million – $1,500 assessment on licensed hospital beds:** The Mayor's proposed budget would have created a 1 percent charge on net patient revenue for hospitals and set penalties on hospitals that do not pay the fee on time, raising $25 million. The Committee on Health rejected this proposal and instead recommended setting a $1,500 assessment per licensed hospital bed. The full DC Council accepted the committee's proposal.

- **$8.6 million – Impose DC's 2 percent insurance premium tax on HMOs for Medicaid receipts:** The District currently levies a 2 percent tax on health insurance premiums, but managed care organizations that provide Medicaid services have been exempted. Starting in FY 2011, Medicaid providers also will be subject to the 2 percent tax. The new revenue will be used in the Medicaid program and will generate $20 million in federal Medicaid matching funds.

- **$4.7 million — tax on intermediate care facilities:** The Mayor's proposed budget reflected $1.7 million from a 1.5 percent tax on the gross revenue of intermediate care facilities that was adopted in 2006, but has not been implemented. The DC Council raised the rate to 5.5 percent, which generated an additional $3 million.

Business Fees: The Mayor's budget proposed raising $10 million by establishing some new business fees and increasing others. This includes $3 million from a new fee that businesses would pay when work on DC streets requires temporary use of steel plates, and an additional $3 million from increases to building permit and corporate registration fees to pay for "enhanced technological capabilities." The Council did not modify these proposals.

Miscellaneous Fees and Taxes: The Mayor's FY 2011 budget proposed raising $4 million through increasing the tax on life insurance from 1.7 percent to 2 percent, requiring payment for copies of the transcripts from special education hearings, creating a fee to use space in the Charles Sumner School, and by creating or increasing a variety of other fees. The Council modified these modestly, including eliminating proposed fees for use of the Charles Sumner School and eliminating proposed fees for acquiring school-related transcripts.

Revenue from Prior Law: The budget reflects a $5 million payment expected from a private health provider under the recent Hospital and Medical Services Corporation Community Reinvestment Act. The Council did not modify these proposals.

Adopted Revenue Increases that Were Proposed by the DC Council

Vacant Property Tax Rate: In recent years, the property tax rate that applies to vacant properties has changed significantly. The FY 2011 budget includes a provision to raise the property tax rate on vacant properties to 5 percent of properties' assessed value.

In recent years, the District set a property tax on vacant properties equal to 5 percent of assessed value, which was subsequently raised to 10 percent. In 2010, the Council voted to limit this 10 percent tax to blighted properties and to lower property tax rates for vacant, non-blighted properties. Properties with vacant buildings that are not considered blighted would be taxed at the basic residential property rate (0.85 percent) or the basic commercial rate (1.85 percent) depending on the zoning for the land. The new changes for FY 2011 will increase the tax for these vacant, non-blighted properties back up to 5 percent. With these changes, the District will have four real property tax rates in FY 2011.

- **Occupied Residential Properties:** 0.85 percent of assessed value for occupied residential properties.
- **Commercial Properties:** 1.65 percent of assessed value for the first $3 million of assessed value, and 1.85 percent for the portion of assessed value above $3 million.
- **Vacant, Non-blighted Properties:** 5 percent of assessed value
- **Blighted Properties:** 10 percent of assessed value

Sales Tax on Soda: The DC Council considered several proposals to cover soda and other sugar-sweetened drinks under DC's sales tax. The Council rejected a proposal to apply a special sales tax on these drinks equal to one penny per ounce. It instead agreed to cover soda under DC's general sales tax, which has a rate of 6 percent. The approved tax of 6 percent is far lower than the proposed penny-per-ounce tax, which would have effectively equaled a rate of 10 percent or more. This will raise roughly $8 million in FY 2011.

The soda tax was considered in the context of funding the DC Healthy Schools Act. The original proposal to levy a tax of one penny per ounce was intended both to raise revenue for this Act and to promote public health. (The Healthy Schools Act, adopted in 2010, will improve the quality of food served in DC public and public charter schools and will increase the amount of time students are engaged in physical activity during the school day.) The tax would have been levied on beverage wholesalers, with the expected effect that retailers would pass on the tax to customers by raising the price of soda and other covered drinks. This, in turn, would be expected to encourage residents, particularly children, to drink less soda.

Sales Tax on Medical Marijuana: Under the budget approved by the DC Council, medical marijuana will be taxed at the 6 percent sales tax rate. It is not clear how much revenue this will generate.

Reduced Income Tax Withholding for Delinquent Taxpayers: The budget adopted by the Council includes a provision to prohibit delinquent taxpayers from reporting any exemptions on their income tax withholding form. This will result in additional taxes being withheld each paycheck from affected residents, which will help the District collect taxes owed from delinquent taxpayers. It will raise more than $4 million in 2011.

Revenue Proposals Considered But Rejected for the FY 2011 Budget

Several proposals to raise additional revenues were proposed by either the Mayor or Council but were not adopted in the final budget.

Parking meter rates: Mayor Fenty's budget proposed increasing the rates on meters that charge

$0.75 per hour to $1 per hour. The budget proposal also would have increased rates for some meters in high-demand areas. This proposal was rejected by the DC Council.

E-911 Fee Increase: Mayor Fenty's budget proposed raising $7 million from a 39-cent increase in a monthly fee applied to phone bills that is used to supports 911 services. The fee applies to phone lines and cell phones held by businesses, residents, and the federal government. The DC Council rejected this increase.

Earned Income Tax Credit Reduction: The Mayor's proposed budget would have reduced the DC EITC, a tax credit for low-income workers, by $1 million. The District's Earned Income Tax Credit boosts take-home pay by providing tax relief and, in many cases, refunds to low-income workers, especially those with children. Nearly 50,000 households receive this credit. Under current law, DC's EITC is set at 40 percent of the federal EITC. This proposal would have reduced the credit to 39 percent of the federal credit. The DC Council rejected this reduction.

Reduction in High-Technology Incentives: The Mayor's budget proposed to reduce a set of tax incentives intended to encourage high-technology companies to locate in the District – called the "NET 2000" incentives. Under NET 2000, some high-technology companies receive a 5-year abatement of corporate income taxes, and after that period pay corporate taxes at a rate of 6 percent, which is below the District's standard corporate income tax rate of 9.975 percent. The incentive package also includes a sales tax exemption for certain purchase and certain sales, as well as tax credits tied to the number of employees hired.

The Mayor's proposal would have scaled back the corporate tax reductions for new applicants for NET 2000 benefits. Instead of receiving a 100 percent abatement of corporate income taxes in the first five years in the city, qualifying businesses would pay a tax rate of 6 percent. This would have save the District $1.3 million in 2011. The DC Council rejected this change.

The DC Fiscal Policy Institute supported the mayoral proposal to scale back the NET 2000 tax subsidies. While this set of incentives — which now costs the District roughly $6 million per year — is intended to boost high-tech employment in the city, a 2008 analysis by the DC Fiscal Policy Institute suggests that this package has not had a notable effect. High-tech employment did not grow faster than overall employment in DC in the 2000s, and DC's high-tech employment did not grow faster than in the suburbs.[5]

Issues related to DC's Fund Balance

DC's fund balance — essentially the city's savings account — has declined in recent years. The decline raised concerns among policymakers during the course of the FY 2011 budget debate and generated a proposal in the FY 2011 budget to begin rebuilding it. While the decline in DC's fund balance merits attention, most states have drawn down their fund balance in order to avoid making severe budgets cuts in the midst of one of the worst economic recessions in history. In fact, despite

[5] DC Fiscal Policy Institute, *DC's High-Tech Tax Incentives Are Not Working: Proposal to Expand Tax Breaks for High-Technology Businesses Has Little Merit*, 2008.

substantial use of the fund balance, DC's fund balance at the end of 2011 will be larger than in 43 states.[6]

DC's fund balance includes funds for a variety of important purposes — including the city's rainy day reserves, escrow funds to back DC's bond payments, and taxes dedicated to specific purposes. When DC's economy is strong, the fund balance also includes accumulated budget surpluses. One important *use* of DC's fund balance is to provide the District with "working capital" — funds that can be used to make payments as revenues don't always come into DC's coffers at the same time that certain expenditures need to be made. A stable supply of working capital thus helps avoid the need for short-term borrowing to cover expenditures.

During the mid-2000's, when the District's economy was booming, the fund balance grew to a high of $1.6 billion — equal to 37 percent of DC's budget at a time when the average for states was eight percent. The fund balance fell to $920 million at the end of 2009 and current projections suggest that the fund balance could fall to $656 million at the end of FY 2011, although this is the worst-case scenario.

DC's use of its fund balance in recent years in many cases reflected conscious decisions to use the surpluses that had built up unexpectedly in the mid-2000's. DC utilized a substantial portion of its fund balance to pay directly for capital improvement projects, rather than borrowing for them, as well as to address a change in government accounting standards that requires the city to set aside large payments for health benefits for DC government retirees. In the current recession, DC has used a portion of its fund balance to prevent severe cuts to city services. Much of the recent use of fund balance comes from a number of "special purpose" funds that were underutilized and had built up large surpluses.

The Council developed a proposed during the FY 2011 budget deliberations to set aside 100 percent of future surpluses – about $530 million – in a new "cash flow reserve." These funds would only be available for working capital needs and would not be available to meet budget shortfalls or spending pressures. Also, the proposal would set aside far more funds for working capital than the city has ever had — the highest was $175 million in FY 2005 — and to the upper limits recommended by the National Association of Government Finance Officers.

The initial Council proposal called for using surpluses to create an operating budget reserve of $120 million for unforeseen spending pressures. This reserve would be funded using 100 percent of surpluses *after* the working capital reserve is filled. Creating this type of reserve makes sense — the District had a $50 million reserve for these purposes until it was eliminated in FY 2009. However, the initial proposal would create a far larger reserve than DC has had for such purposes, which could create disincentives to address spending pressures through budget savings. Moreover, because the proposal called for filling the operating reserve after the $530 million cash flow reserve was fully

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[6] For a more detailed discussion of DC fund balance issues, see DC Fiscal Policy Institute, "DC's Fund Balance Remains Larger than Most States: Current Proposals to Rebuild DC's Reserves May Overly Restrict DC's Ability to Respond to Ongoing Budget Needs," available at: http://www.dcfpi.org/dc%E2%80%99s-fund-balance-remains-larger-than-most-states-current-proposals-to-rebuild-dc%E2%80%99s-reserves-may-overly-restrict-dc%E2%80%99s-ability-to-respond-to-ongoing-budget-needs

funded, it would have resulted in DC having almost no flexibility to deal with budget emergencies as its finances are still recovering from the recession.

The DC Council amended the proposal so that 100 percent of all end year surpluses would be split, with half going to fill the operating reserve and the other half going to fill the working capital reserve. Once the smaller of the reserves was filled, the operating reserve, 100 percent of all end year surpluses would go to fill the working capital reserve.

The change to fill the operating reserve first is a good move that will give the District some flexibility to respond to budget emergencies. This is especially critical as the District's finances remain fragile as they exit the recession. While the District is moving in the right direction by working to replenish the fund balance, the amended proposal passed by the Council still goes too far, too fast.

Every dollar we put into a reserve is a dollar that can't be used to invest in our city. That balance needs to be weighed carefully going forward. DC's most pressing fiscal problem is the $500 million drop in tax collections that has led to cuts in all parts of the budget. DC's finances are likely to be fragile as it comes out of the recession, which means preserving resources for budget should be the top priority right now. It would be more prudent for the District to set aside a smaller percentage of the end-year surplus and lower the amounts of reserves to be in line with more historical use. This would help ensure DC can remain fiscally responsible and have the flexibility to deal with our budget needs now, and in the future.

Budget Transparency Gains in the FY 2011 Budget

The Mayor and Council adopted two significant changes to the transparency of the FY 2011 budget and budget process.

- **Division-Based Budgeting:** The structure of the DC budget was changed in the Mayor's proposed budget for FY 2011. The new structure is referred to as "division-based budgeting" by the Mayor's office but is also more commonly known as "program-based" or "organizational-based" budgeting. Until FY 2011, the District used a "performance-based" budget structure that resulted in many budget line items that are too large to provide meaningful understanding of how funds are being used and that fail to delineate how funds are actually spent on the real programs and services DC residents use. The new structure provides greater detail on the budgets for some programs and services and displays the information in a way that more closely matches how agencies spend dollars on actual programs and services. While the transition to the new form of budgeting was largely successful, some programs, such as homeless services, are still combined into a single line item, making it difficult to track funding changes for specific services over time.[7]

[7] For more information, see DC Fiscal Policy Institute, "Changes in the FY 2011 Budget: A New Budget Structure has the Potential to add Greater Transparency to the DC Budget," available at: http://www.dcfpi.org/changes-in-the-fy-2011-budget-a-new-budget-structure-has-the-potential-to-add-greater-transparency-to-the-dc-budget-2

- **Televising Council Budget Deliberations:** After holding committee hearings and budget mark-ups, the DC Council usually spends the last two weeks before the budget vote meeting behind closed doors to discuss their priorities for the budget. For the first time, and following pressure from advocacy groups, the Council decided to televise their budget deliberations. For three days, members of the public could watch their representatives debate whether to restore funding to programs and whether to raise taxes.

APPENDIX
Summary of FY 2011 Funding Changes by Appropriations Title

NOTE: The FY 2011 budget includes several accounting changes that affect the budgets for many agencies. Contracting and human resource functions that had been budgeted in all city agencies in FY 2010 are now included in the budgets for the city's central contracting and personnel agencies. In addition, the FY 2011 budget includes a new centralized agency to reflect DC government rent, utility, and related expenses. Those expenses had been reported in individual agency budgets in FY 2010. To make FY 2011 budget figures comparable with prior-year budgets, this report shifts these fixed costs back to individual agency budgets.

In addition, DCFPI's analysis makes some adjustments to reflect the impact of federal stimulus funding. For example, the FY 2011 budget includes $37 million in local funding to replace federal Medicaid funds that were provided under the stimulus package in FY 2010. Because this does not reflect an expansion of local services, this analysis adds $37 million to the FY 2010 local budget to make it comparable with FY 2011 figures.

For this reason, the figures reflected in this report may not match figures reported in the FY 2011 budget.

Government Direction and Support: The FY 2011 general fund budget for Government Direction and Support agencies is $479 million. This appropriation title includes funding for the DC Council, the office of the Mayor, and the City Administrator, as well as the Attorney General and Chief Financial Officer's Office.

The FY 2011 budget appears to reflect a significant increase from FY 2010, when the approved budget for these agencies was $379 million. However, this change entirely reflects several accounting changes in the FY 2011 budget. Contracting and human resource functions that had been budgeted in all city agencies in FY 2010 are now included in the budgets for the city's central contracting and personnel agencies. In addition, the FY 2011 budget includes a new centralized agency to reflect DC government rent, utility, and related expenses, when those expenses had been reported in individual agency budgets in FY 2010.

When adjustments for these and other shifts are made, the FY 2011 budget for Government Direction and Support is $360 million. This is $19 million, or four percent, lower than the approved FY 2010 budget, after adjusting for inflation.

The FY 2011 budget eliminates 30 positions from the Office of the Chief Financial Officer and reduces its budget by $10 million (seven percent). The budget for the Office of the Attorney General is $2 million, or three percent lower than the FY 2010 budget. FY 2011 funding for the Board of Elections and Ethics will be $500,000, or 10 percent lower than in 2010.

Finally, Mayor Fenty had proposed eliminating the Public Employee Relations Board and the Office of Employee Appeals and folding them into the Office of Administrative Hearings. The PERB resolves labor-management disputes between the District government and the unions representing DC employees, and the Office of Employee Appeals resolves appeals filed by DC government employees. The Council chose to preserve PERB and OEA as separate entities, although funding for each will be notably lower in FY 2011 than FY 2010.

Economic Development and Regulation: Local funds for Economic Development and Regulation are down 12 percent in FY 2011, after adjusting for inflation, falling from $329 million in FY 2010 to $283 million in FY 2011. This appropriation title includes funding for the Department and Housing and Community Development (DHCD), the Deputy Mayor for Planning and Economic Development (DMPED), the Department of Employment Services (DOES) and the Department of Consumer and Regulatory Affairs (DCRA), among others.

While most agencies would see decreases in funding in FY 2011, there are a few increases. The Housing Production Trust Fund will receive $22 million in FY 2011, an increase of $1 million from FY 2010 which reflects growth in DC's deed taxes that are dedicated to the Trust Fund. The budget for the Board of Real Property Assessments and Appeals (BRPAA) would see the largest increase, nearly doubling in size from $700,000 in FY 2010 to $1.3 million in FY 2011. The increase is to support additional staff to help handle the large increase in appeals that have come to BRPAA in the economic downturn.

Other agencies within this appropriation title, however, would face substantial decreases in FY 2011. Funding for the Department of Employment Services (DOES) would fall 19 percent. While the overall funding for DOES did not change substantially, the programs that received reductions did change. The Mayor's budget proposed a $4.6 million cut for adult job training programs, cuts to the year-round youth employment program and DC's apprenticeship program. The Council restored the majority of those funds by cutting funds from the Summer Youth Employment Program and from some additional funding from the Committee of the Whole.

Funding for DMPED would fall 47 percent in FY 2011, from $34 million in FY 2010 to $18 million in FY 2011. Much of the decrease would come from cutting $12 million from the Neighborhood Investment Fund. NIF funds also were reduced in FY 2010 to help balance the budget.

The FY 2011 budget would cut the budget for the Office of the Tenant Advocate (OTA) by nearly 40 percent, from $3.6 million in FY 2010 to $2.2 million in FY 2011. OTA provides legal assistance to tenant groups, provides education on tenants' rights, and engages in policy advocacy on behalf of tenants.

Public Safety and Justice: The FY 2011 general fund budget for public safety functions is $1.02 billion and includes the Metropolitan Police Department (MPD), Fire and Emergency Services, and the Department of Corrections. The local public safety budget will fall by $10 million, or one percent, from the FY 2010 budget, after adjusting for inflation. MPD's budget is proposed to fall by $16 million, which represents a three percent decline from FY 2010 level. It includes savings from "maintaining sworn strength," eliminating vacant civilian positions, and reducing or eliminating services such as the pager contract. The proposed budget calls for a two percent, or $2.5 million reduction in the Department of Corrections, including staffing reductions. Mayor Fenty had proposed significant reductions to the healthcare contract for inmates and reducing pharmacy expenses, but the DC Council restored most of these reductions. The budget also includes a $1.5 million cut in the Office of Victims Services, due to expected lower court fees that fund this agency.

The FY 2011 budget calls for a five percent increase in funding for the Fire and Emergency Services Department, which largely reflects salary and fringe benefit increases. Another agency slated for a funding increase is the Unified Communications Center, which would get a 27 percent ($11 million) increase, mainly to upgrade its radio system for first responders.

Education: The general fund budget for education in FY 2011 is $1.5 billion. This is five percent, or $75 million, higher than the approved FY 2010 budget, after adjusting for inflation and accounting for the increase in local funds needed to replace expiring stimulus funds. The DC Public Schools and DC Public Charter Schools' budgets include a two percent increase in the per-pupil funding formula. Despite the increase to the funding formula, total funding for DCPS — including federal and local funds — would decline, and funding provided directly to local schools will be held constant at FY 2010 levels. The DCPS budget cuts central office operations, including a $12 million cut to personnel that could involve employee furloughs and staff reductions. The budget also reflects large increases in special education tuition (19 percent adjusting for inflation) and transportation (14 percent) from FY 2010.

The Office of Public Education Facilities Modernization, which renovates and maintains DC Public Schools, will see its general fund budget decrease by $2.6 million or eight percent. Part of the savings from OPEFM will come from reducing preventative maintenance on energy systems to below manufacturer-approved levels. DC Public Libraries essentially will be flat funded, even with the planned addition of six new libraries in FY 2011.

Human Support Services: The proposed FY 2011 general fund budget for human support services is $1.4 billion, or two percent lower than in FY 2010, after adjusting for inflation. Five human service agencies would see their general fund budgets increase in FY 2011: unemployment compensation, disability compensation, the Department of Parks and Recreation, the Department of Youth Rehabilitation Services, and the Department of Healthcare Finance. The other eleven human services agencies — including the Department of Human Services, the Child and Family Services Administration, and the Department of Disability Services — would see their budgets decrease or remain flat from FY 2010.

The Department of Mental Health's budget represents a 13 percent decrease and includes the elimination of 29 direct care positions. The budget for the Department of Human Services includes cuts to Interim Disability Assistance, a cash assistance program for residents with disabilities and to the "general cash assistance" program for low-income residents who are caring for unrelated children. The DC Council restored cuts to programs within the Child and Family Services Administration, including a program to support grandparents caring for their grandchildren and a program that provides "rapid housing" to various groups of vulnerable residents. Many of the smaller agencies, such as the Children Youth Investment Trust Corporation and the Office of Latino Affairs, will see large cuts to their budgets in FY 2011.

Public Works: The FY 2011 general fund budget for public works is $570 million, a decrease of three percent from FY 2010, after adjusting for inflation. This appropriations title includes the Department of Public Works (DPW), the Department of Transportation (DOT), the Department of Motor Vehicles (DMV), the District Department of the Environment (DDOE), the Washington Metropolitan Area Transit Authority (WMATA) and School Transit Subsidies (subsidized public transportation for K-12 students).

Funding for the Department of Public Works will fall eight percent, from $127 million in FY 2010 to $117 million in FY 2011. The Mayor's proposed budget put forth a significant cut in DPW positions for street and alley cleaning, commercial corridors cleaning, the leaf collection program, and the SWEEP program which monitors and fines residents and businesses for trash violations. The DC Council restored funding for those positions through additional anticipated revenue generated from the SWEEP program.

Funding for the Department of Transportation also will decline, falling seven percent from $104 million in FY 2010 to $97 million in FY 2011. This mostly reflects a cut to DDOT's Infrastructure" program. It is unclear how that will impact services. Additional funds will be added to expand service on the Circulator bus, including expanding service east of the Anacostia River. Funding for the District Department of the Environment (DDOE) will fall 13 percent, from $58 million in FY 2010 to $51 million in FY 2011. Reductions in funding include covering the costs of some energy assistance funds with federal dollars instead of local dollars.

Lastly, the School Transit Subsidy funding is down 22 percent, falling from $7.7 million in FY 2010 to $6 million for FY 2011. With a Metro fare increase and higher enrollment levels expected at schools, it's unclear at this point how the cut in funding will not affect services.

Financing: The FY 2011 general fund budget for finance functions is $897 million, a decrease of $27 million or three percent from FY 2010, after adjusting for inflation. The most significant change is a $68 million reduction in payments on the city's long-term debt — typically general obligation bonds used to support construction projects — resulting from restructuring a portion of the city's debt. (This also will produce savings in FY 2010). The restructuring will result in lengthening the time it takes to pay off this debt, but the refinancing also resulted in lower interest rates, so that the overall long-term effect is just a modest increase in debt expenses. Other key changes in the Financing appropriations title include substantial increases in funds needed to repay funds borrowed for economic development projects, and an increase in funds transferred to DC's convention center fund and highway trust fund. The latter two increases result from a growth in tax collections for the taxes devoted to these funds.