

GOVERNMENT OF THE DISTRICT OF COLUMBIA
OFFICE OF THE CHIEF FINANCIAL OFFICER



Jeffrey S. DeWitt
Chief Financial Officer

June 10, 2019

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

**Re: Certification of Council's Proposed Budget and Financial Plan for Fiscal Year
2020 Through 2023**

Dear Chairman Mendelson:

This letter is to provide you detailed information and analysis, both legal and financial, regarding issues with the certification of the Fiscal Year 2020 through 2023 budget and financial plan.

CFO Certification Requirement

As you are aware, under the Home Rule Act, the District CFO is responsible for certifying both the Mayor's proposed budget and financial plan and the Council's final budget. Certification of the Council's budget occurs through the issuance of a fiscal impact statement (FIS) indicating that funds are sufficient to support the enactment of the Local Budget and Budget Support Acts. Without fiscal certification, there is no approved budget to support the operations of the District government for the fiscal year beginning October 1, 2019.¹

WCSA Reserves and Uses

The single concern for certification of the Council's budget and financial plan remains the use of reserve funds of the Washington Convention and Sports Authority (WCSA). After extensive discussions with bond and disclosure counsel, and internal bond lawyers assisting in the comprehensive review and analysis of the issue, it was determined that the WCSA reserves can only be accessed, prior to the full retirement of WCSA bonds (full repayment of outstanding

¹ The CFO's responsibilities and authority are provided in the following statutes. D.C. Official Code Section 1-204.24d(2), (4), (5) (7), (25), (26) (Home Rule Action Section 424a(2), (4), (5), (7), (25), (26)); D.C. Official Code Section 1-206.03(c) (Home Rule Act Section 603(c)).

debt), through an excess reserve calculation that occurs at the end of each fiscal year. The proposed Council budget does not meet this criterion.

Transfer of Reserve Limitations

Our analysis includes a review of District law and the Master Trust Agreement (MTA), the contract with the purchasers of the bonds that were sold to construct the Washington Convention Center. D.C. Code § 10-1202.13(a) provides that if, at the end of a fiscal year, the balance of cash and investments of the Authority in the Convention Center Fund exceeds the balance of current liabilities, reserves, and any amounts that the Authority expects to apply to purchase or redeem its outstanding indebtedness during the upcoming fiscal year, the excess *shall* be transferred, in cash, to the General Fund of the District.

The MTA provides that the bond holders are protected with certain guaranteed levels of reserves in the event of an economic downturn or financial difficulty. Any amount (excess) beyond these reserves is first set aside for a maximum reserve calculation (both operating and capital) as defined in District law and the MTA. If the maximum reserve calculation is exceeded on the last day of the fiscal year (September 30), the WCSA will transfer any excess to the District's General Fund.

Any transfer to the District beyond the excess reserve calculation would violate the MTA and be considered an event of default on the outstanding bonds. This could trigger lawsuits by bond holders in addition to the potential damage to the WCSA and the District's credit rating for intentionally violating the MTA. In addition, all WCSA bond holders would have to be notified of the violation of the MTA through the Electronic Municipal Market Access (EMMA) system, operated by the Municipal Securities Rulemaking Board (MSRB), to enable bondholders to take appropriate action. Furthermore, in discussions with the rating agencies, they expressed significant concerns about any transfer not authorized under the MTA. One rating agency indicated that it would immediately have to take the issue to its rating committee to consider a rating change with respect to the District. The lowering of the District's credit rating would increase the cost of borrowing in the future and require reductions in projects funded in the District's capital program. Attached is a joint letter from the WCSA bond counsel, Ballard Spahr LLP, and District disclosure counsel, Hawkins Delafield and Wood LLP, which provides the legal analysis of the WCSA reserve transfer limitations (See Attachment 1). Based on these factors, I cannot certify the use of funds as proposed.

Maximum Reserve Fiscal Year End Transfer Analysis

In 1994, the District anticipated that excess reserves might accumulate in what later became the WCSA, and the District set limited conditions for transfer of any excess funds. This legislation was updated in 1998, when the Convention Center issued its original bonds, with the specific criteria for maximum reserves further outlined in the MTA. If the year-end balance of cash and investments exceeds the maximum reserves, the excess balance must be transferred to the General Fund. The allowed reserves under District law were then as follows: (1) an operating reserve equal to 3.0 times operating and marketing budget; and (2) a capital reserve of 5% of the

original cost of the convention center updated by the cost of inflation. Other reserves are also required under the MTA as part of the maximum reserve calculation.

Pursuant to District law, the calculation has been done each year since 2007, the date of the first bond refunding after the 1998 issuance, and no excess funds were identified for transfer in any year. However, discussions with you and the Attorney General identified a 2007 Memorandum of Understanding between CFO Natwar Gandhi and the WCSA that lowered the multiplier for the operating and marketing budget from 3.0 to 1.5 times. The 1.5 multiplier had never been applied in the annual calculation, so the calculation was done incorrectly since 2007. To correct the error, I directed the WCSA's CFO to complete the annual calculation with the 1.5 multiplier from 2007 to the most recent fiscal year, 2018, and to document all calculations with the source documents to ensure accuracy. The WCSA CFO's analysis has been reviewed by the District's Treasurer and Controller.

Despite the lower multiplier, there were no excess funds to transfer from WCSA to the General Fund until FY 2017 and FY 2018. The lower multiplier resulted in maximum reserve excesses of \$27.091 million in FY 2017 and \$19.802 million in FY 2018 (for a total of \$46.893 million) that should have been transferred. This means that at the end of those fiscal years, the District did not receive the appropriate transfers to the General Fund reserves as part of the year-end closing process. Enclosed for your information is a table that provides the historical analysis and the basis for the proper transfers (See Attachment 2). Complete source documentation for each calculation will be delivered to your office today.

Standard accounting practice requires that as soon as an error or oversight is identified, the proper accounting should be executed to reflect the correction. The identified excess reserve funds must be properly placed in the General Fund as required by District law. As a result, the FY 2017 and FY 2018 year-end accounting transactions have been updated to reduce the WCSA reserves and increase the General Fund reserves to reflect the proper accounting and funds available to the District. The year-end closing process takes all excess revenue and first places it into the federally mandated contingency and emergency reserves, followed by the locally mandated fiscal stabilization and cash flow reserves. Combined, these reserves, which are now full, represent approximately 60 days of operating cash for the District. District law directs that any excess amount beyond the 60 days must be equally divided between pay-go capital funding and the Housing Production Trust Fund. The results are summarized in the attached tables, which update the FY 2018 Comprehensive Annual Financial Statement (CAFR) "Note 10: Fund Balance/Net Position". The result is a cash flow reserve increased by \$27.091 million in FY 2017 and by \$19.802 million in FY 2018 plus \$0.958 million in interest earned for a total of \$47.851 million. The cash flow reserve is now full as of FY 2018 with \$9.899 million going to pay-go capital and \$9.899 million going to the Housing Production Trust Fund. These transfers have been completed and are available to the District for use as legally permitted. (See Attachment 3).

The WCSA CFO also analyzed the corrected maximum reserve excess transfer for its impact on WCSA's capital needs. The December 2017 long-term capital and financial plan was also reviewed with current revenue and expenses. The transfer does not impact the planned

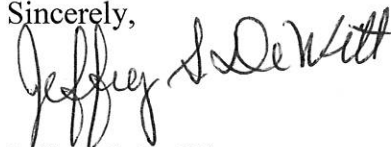
maintenance projects during the six-year capital improvement program and may slightly delay the timing of future strategic initiatives that can be adjusted when the plan is updated. As part of the long-term capital and financial plan update, the timing of projects, the long-term ability to meet required asset maintenance, and the operating and marketing reserve multiplier will be reviewed.

Summary and Requirements for Certification

The Council's FY 2020 budget and financial plan currently includes a \$49 million transfer from the WCSA. The in-depth legal analysis concludes that this transfer for the purposes proposed in the Council's budget is not permitted. The correction of the excess cash calculation that now places funds in the appropriate General Fund reserves is the only legal transfer of WCSA reserves that will not create a violation of the MTA. As a result, all General Fund cash reserves are full, and \$9.899 million have been added to both pay-go capital funding and the Housing Production Trust Fund, pursuant to District law. For fiscal certification prior to the vote on the proposed FY 2020 Budget Support Act, the expenses planned for the \$49 million in the Council's budget must either be reduced, or alternate funding must be identified.

As always, my staff and I are available to work with the Council and Council budget staff to develop and evaluate alternatives that will produce an FY 2020 budget and financial plan that can be certified.

Sincerely,



Jeffrey S. DeWitt

Attachments: Joint Bond Counsel and Disclosure Counsel Letter
Historical Excess Cash Calculation of WCSA Reserves
CAFR Update Note 10 Fund Reserves/Net Position

DISTRIBUTION LIST

Councilmember Anita Bonds (At-Large)

Councilmember David Grosso (At-Large)

Councilmember Elissa Silverman (At-Large)

Councilmember Robert White (At-Large)

Councilmember Brianne Nadeau (Ward 1)

Councilmember Jack Evans (Ward 2)

Councilmember Mary Cheh (Ward 3)

Councilmember Brandon Todd (Ward 4)

Councilmember Kenyan McDuffie (Ward 5)

Councilmember Charles Allen (Ward 6)

Councilmember Vincent Gray (Ward 7)

Councilmember Trayon White (Ward 8)

Jennifer Budoff, Budget Director, Council of the District of Columbia

Ballard Spahr
LLP

Hawkins
DELAFIELD & WOOD LLP

June 7, 2019

Jeffrey S. DeWitt
Chief Financial Officer
District of Columbia

Dear Mr. DeWitt:

You requested an analysis of (i) the operation of D.C. Code § 10-1202.13 and (ii) the related provisions of the Amended and Restated Master Trust Agreement dated as of February 1, 2007, as supplemented (the "MTA") by and between the Washington Convention Center Authority (now Washington Convention and Sports Authority) (the "Authority") and The Bank of New York, as Trustee. Capitalized terms have the meanings set forth in the MTA.

D.C. Code § 10-1202.13 at subsection (a) provides as follows:

If, at the end of a fiscal year, the balance of cash and investments of the Authority in the Convention Center Fund exceeds the balance of current liabilities, reserves, and any amounts that the Authority expects to apply to purchase or redeem its outstanding indebtedness during the upcoming fiscal year, the excess shall be transferred, in cash, to the General Fund of the District.

D.C. Code § 10-1202.13(b) defines "reserves" as used in subsection (a), subject to the exception provided in subsection (c) of that Section.

Section 506 of the MTA at Paragraph Twelfth provides for the transfer of excess funds that is referenced in D.C. Code § 10-1202.13(a). Such Paragraph provides as follows:

On the last day of the Fiscal Year only, to the extent, and only to the extent, that each of the Operating and Marketing Reserve and the Capital Renewal and Replacement Reserve are funded at the Operating and Marketing Reserve Maximum and the Capital Renewal and Replacement Reserve Maximum, respectively, to the General Fund of the District the amount, if any, determined by an Authorized Officer of WCCA to be transferred thereto.

For purposes of determining whether any amount would be available to be transferred pursuant to Section 506 of the MTA at paragraph Twelfth, the funding requirements of Section 506 of the

Jeffrey S. DeWitt
June 7, 2019
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MTA paragraphs First through Eleventh would have to have been satisfied along with other obligations incurred by the Authority so long as such obligations are in compliance with the provisions of the MTA. The operation of Section 506 is explained in more detail in the next paragraph.

All Revenues under the MTA, including all Dedicated Taxes, are required to be deposited to the Revenue Account of the Revenue Fund (subject to certain specified limited exceptions, including for any moneys required to be deposited to the Revenue Stabilization Account of the Revenue Fund). The Bondholders have a lien on and pledge of Revenues, including Dedicated Tax Receipts, until such time as such Revenues are expended for purposes authorized under the MTA or until their Bonds are redeemed, paid at maturity, or defeased by operation of Article XI of the MTA. The only exception to this is the release of funds on the last day of each Fiscal Year by operation of paragraph Twelfth of Section 506. Accordingly, the District could not access the Revenues of the Authority other than by operation of paragraph Twelfth, and any attempt to do so would violate the pledges and agreement of the District established by Sections 208(e) and 212 of the Washington Convention Center Authority Act of 1994, which have been expressly incorporated into the MTA at Section 612 thereof.

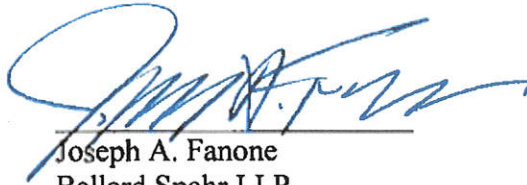
It is an Event of Default under the MTA if the Authority were to default in the due and punctual performance of an agreement or provision contained in the MTA, including by operation of Section 612:

1. In accordance with Section 208(e) of the Act, WCCA does hereby include the pledge and agreement of the District that the District shall not limit, restrict or in any way impair the collection, transfer, deposit or disbursement of revenues in the Revenue Fund until the principal of, premium, if any, and interest on the Bonds has been paid and discharged.
2. In accordance with Section 212 of the Act, WCCA does hereby include the pledge of the District that the District will not limit or alter rights vested in WCCA to fulfill agreements made with Holders of the Bonds, or in any way impair the rights and remedies of the Holders of the Bonds until the Bonds, together with the interest thereon, with interest on any unpaid installments of interest, and all costs and expenses in connection with any action or proceedings by or on behalf of the Holders of the Bonds are fully met and discharged.

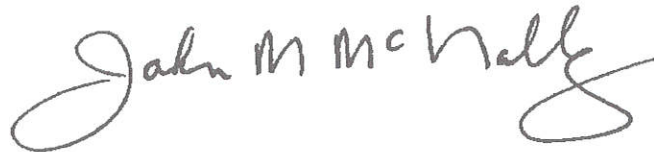
Upon the occurrence of an Event of Default, the Authority would be required, pursuant to its Continuing Disclosure Agreement dated as of March 6, 2018, relating to the Authority's Series 2018 Bonds, to file a material event notice with the Electronic Municipal Market Access ("EMMA") system. Pursuant to Section 1003 of the MTA, the Bondholders would be entitled to seek remedies against the Authority as well as the District. Filings on EMMA are available to the public without charge. Any such filing could have significant negative implications for the credit standing of both the District and the Authority, which we leave to your judgment to assess.

Jeffrey S. DeWitt
June 7, 2019
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Very truly yours,



Joseph A. Fanone
Ballard Spahr LLP
Bond Counsel to the Washington Convention and
Sports Authority



John M. McNally
Hawkins Delafield & Wood LLP
Disclosure Counsel to the District of Columbia

Attachment 2

Events DC
Excess Cash Calculation
FY 2008 - 20018

Per the 1994 Act, at the end of the fiscal year, the balance of cash and investments of the Authority exceeds the balance of current liabilities and reserves, the excess shall be transferred in cash to the general fund of the District.

in \$000

		FY2008	FY2009	FY2010	FY2011	FY2012	FY2013
Reserves and Current Liabilities							
Maximum Debt Service 2007 A Bonds	1	34,923	34,923	34,923	34,923	34,923	34,923
Maximum debt Service 2018A Bonds	2						
Maximum Required Operating Reserve (1.5 times Operating and Marketing Budget)	3	74,016	75,237	85,878	90,859	92,178	94,477
Capital Reserve 5% of project cost	4	62,142	56,940	54,682	55,572	56,804	59,130
Restricted Reserve for ESA	5						
Current Liabilities, per audited statements	6	33,543	34,947	35,592	48,595	58,427	56,890
Total Reserves & Liabilities		204,624	202,047	211,075	229,948	242,332	245,421
Balance of Cash and Investments							
2007A Bonds	7	143,910	160,397	164,782	192,685	219,366	178,668
2018A Bonds	8						
Operating Cash	9	2,927	7,240	14,103	11,611	10,455	12,506
Total Cash & Investments		146,837	167,637	178,885	204,296	229,821	191,174
Excess Cash Due to the General Fund		(57,787)	(34,410)	(32,190)	(25,652)	(12,511)	(54,247)

Support Documents

- 1 Maximum annual debt service per the 2018 Official Statement
- 2 Maximum annual debt service per the 2007 Official Statement
- 3 Board Resolution for Approved Budget and Modificaiton
- 4 See Capital Reserve Calculation worksheet
- 5 Board Resolution authorizing ESA project
- 6 Current Liabilities are from the annual audited financial statements
- 7 Reserve Account - audited financial statements (notes section)
- 8 Reserve Account - audited financial statements (notes section)
- 9 Per the audited financial statements.

Attachment 2

Events DC
Excess Cash Calculation
FY 2008 - 20018

Per the 1994 Act, at the end of the fiscal year, the balance of cash and investments of the Authority exceeds the balance of current liabilities and reserves, the excess shall be transferred in cash to the general fund of the District.

in \$000

		FY2014	FY2015	FY2016	FY2017	FY2018
Reserves and Current Liabilities						
Maximum Debt Service 2007 A Bonds	1	34,923	34,923	34,923	34,923	
Maximum debt Service 2018A Bonds	2					33,779
Maximum Required Operating Reserve (1.5 times Operating and Marketing Budget)	3	95,771	100,557	108,493	118,792	126,429
Capital Reserve 5% of project cost	4	61,731	64,537	67,685	71,039	75,008
Restricted Reserve for ESA	5			37,500	23,600	6,600
Current Liabilities, per audited statements	6	54,575	55,827	55,535	64,840	62,829
Total Reserves & Liabilities		247,000	255,844	304,136	313,193	304,645
Balance of Cash and Investments						
2007A Bonds	7	193,948	233,797	276,479	326,999	-
2018A Bonds	8					309,925
Operating Cash	9	8,828	13,162	10,501	13,285	14,522
Total Cash & Investments		202,776	246,959	286,980	340,284	324,447
Excess Cash Due to the General Fund		(44,224)	(8,885)	(17,156)	27,091	19,802

See Note A

Note A

2018A Bonds Reserve balance per audited Financials	337,016
Less: FY 2017 Excess cash due to the General Fund	(27,091)
	<u>309,925</u>

Support Documents

- 1 Maximum annual debt service per the 2018 Official Statement
- 2 Maximum annual debt service per the 2007 Official Statement
- 3 Board Resolution for Approved Budget and Modificaiton
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- 9 Per the audited financial statements.

Attachment 3
Fund Balance Update to Reflect WSCA Transfers
FY2017

	GENERAL FUND
	Adjusted for
	Convention
	Center Transfer
	Variance
Fund Balances:	General Fund
Nonspendable	Actual
Inventory	\$ 14,969
	\$ 14,969
Total Nonspendable Fund Balance	14,969
Restricted for:	
Emergency and Contingency Cash Reserves	413,901
Debt Service - Bond Escrow	542,081
Budget	40,063
Purpose Restrictions	95,661
Tax Increment Financing Program	28,362
Total Restricted Fund Balance	1,120,068
Committed to:	
Fiscal Stabilization Reserve	190,145
Cash Flow Reserve	615,055
Budget Support Act	41,994
Commodities Cost Reserve	4,205
Soccer Stadium	21,206
Dedicated Taxes	19,233
WMATA Operations Fund	35,777
Subsequent Years Expenditures	438,607
Other Special Purposes	202,123
Total Committed Fund Balance	1,541,254
Assigned	-
Unassigned	-
Total Fund Balance	\$ 2,703,382
	\$ 2,709
	27,091

Attachment 3
Fund Balance Update to Reflect WSCA Transfers
FY2018

	GENERAL FUND			HOUSING PRODUCTION TRUST FUND			GENERAL CAPITAL IMPROVEMENTS		
	General Fund Actual	Adjusted for Convention Center Transfer	Variance	Housing Production Trust Actual	Adjusted for Convention Center Transfer	Variance	General Capital Improvements Actual	Adjusted for Convention Center Transfer	Variance
Fund Balances:									
Nonspendable									
Inventory	8,270	8,270	\$ -	-	-	\$ -	-	-	\$ -
Total Nonspendable Fund Balance	8,270	8,270	-	-	-	-	-	-	-
Restricted for:									
Emergency and Contingency Cash Reserves	419,504	419,504	-	-	-	-	-	-	-
Debt Service - Bond Escrow	520,693	520,693	-	-	-	-	-	-	-
Budget	452	452	-	-	-	-	-	-	-
Purpose Restrictions	132,017	132,017	-	-	-	-	-	-	-
Tax Increment Financing Program	33,052	33,052	-	-	-	-	-	-	-
Total Restricted Fund Balance	1,105,718	1,105,718	-	-	-	-	-	-	-
Committed to:									
Fiscal Stabilization Reserve	203,283	203,283	-	-	-	-	-	-	-
Cash Flow Reserve	712,755	740,808	28,053	-	-	-	-	-	-
Budget Support Act	70,800	70,800	-	-	-	-	-	-	-
Soccer Stadium	16,111	16,111	-	-	-	-	-	-	-
Housing Production Trust Fund	-	-	-	167,397	177,296	9,899	-	9,899	9,899
Pay-as-you-go	-	-	-	-	-	-	-	-	-
Dedicated Taxes	16,869	16,869	-	-	-	-	-	-	-
Subsequent Years Expenditures	428,505	428,505	-	-	-	-	-	-	-
Other Special Purposes	186,825	186,825	-	-	-	-	-	-	-
Total Committed Fund Balance	1,635,148	1,663,201	28,053	167,397	177,296	9,899	-	9,899	9,899
Assigned to:									
Subsequent Year Expenditures	27,247	27,247	-	-	-	-	-	-	-
Total Assigned Fund Balance	27,247	27,247	-	-	-	-	-	-	-
Unassigned									
Total Fund Balance	2,776,383	2,804,436	28,053	167,397	177,296	9,899	(522,345)	(512,446)	9,899

Variance	
General Fund	\$ 28,053
Housing Production Trust Fund	9,899
General Capital Improvements	9,899
TOTAL	\$ 47,851

*NOTE: Reflects corrected transfer calculation for FY 2017 and FY 2018 and interest earnings.