ANTHONY A. WILLIAMS
MAYOR

March 17, 2003

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

Dear Chairman Cropp:

I am pleased to transmit to you my proposed FY 2004 Budget and Financial Plan: *Education, Public Safety, Opportunity for All.* This budget proposes $5.6 billion in total funding and supports 33,638 full-time equivalent (FTE) staff. This change represents a .02% funding decrease from the FY03 approved budget, and increase of 4 FTEs. In local funds, this budget proposes $3.8 billion in funding and supports 26,197 FTEs. This local budget change represents a 5.5% funding increase over the FY03 approved budget and a decrease of 197 FTEs.

As you know, cities and states across the nation are facing the biggest revenue shortfalls since World War II, and many are facing massive deficits. At the source of these troubles are a national economic downturn, a growing trend of unfunded federal mandates, and the daunting threat of war. But while these factors generally affect all states, the District also faces an extra challenge: the federal government requires that we deliver state-level services, but prohibits us from collecting revenue like a state. Add to that the fact that we have no vote in Congress, and the District's challenge is greatly compounded.

There is a difference between an explanation and an excuse, however. So even though the national economy and federal policy may be driving much of our problem, as local elected leaders we must make the tough choices required to solve it. What you will see in this proposal is a budget that addresses the challenge at hand and does so by meeting the highest standards of fiscal discipline and fairness.

By looking across the country, one sees that different governments are facing this crisis in different ways. Some fail to find enough alternatives, so they make draconian cuts in education, child care, and social services. Others spend their reserves, pursue pie-in-the sky revenue

gimmicks, or attempt to balance their budgets by simply pretending that giant looming costs do not exist.

Then there are those who take a different approach -- those who recognize and address the full magnitude of the problem; having the capacity to say one thing is a priority and another is not; having the ability to find areas of low productivity and reallocate resources; and having the courage to call on all members of the community to accept a fair share of the burden. I believe my budget proposal reflects this kind of leadership.

Specifically, I propose an FY04 budget that is balanced through a combination of four key components:

- Focus on community goals
- Strategic spending reductions
- Increases in revenue only as needed
- Recognition of deferred infrastructure needs

The following discussion presents the details of this approach.

Focus on Community Goals

Based on input from thousands of residents, my administration has defined and pursued five main priorities. These priorities have been the focus and organizing guide for our pursuits over the past four years. These priorities are (1) children, youth, families, and elders; (2) building sustainable neighborhoods; (3) economic development; (4) making government work; and (5) unity of purpose.[1]

After ongoing consultation over the past year, citizens have further focused their priorities in the following areas:

- education, including early childhood education, public schools, and adult literacy;

- public safety, including greater police presence in communities and a vastly improved 911 emergency communications system; and

- opportunity for all, which includes the housing, employment, and health care as needed for all residents to become productive and healthy members of the community and economy.

In times of tight resources, some would set their goals aside in order to weather the storm, but I believe the opposite must be done: in these difficult times we must focus on our goals more than ever so that we may protect them and continue making progress toward achieving them. The proposed FY 2004 budget reflects this preservation and focus by proposing no budget reductions in schools, by investing in public safety responsiveness, and by preserving current funding levels in housing, job training, and health care. In order to protect these priorities, however, some

---

[1] The Citywide Strategic Plan that supports these priorities is available at www.dc.gov or by calling 727-2822.

reductions had to be made in other areas of the budget. These reductions are discussed in the following section.

Strategic Spending Reduction

Congress requires the District to provide services like a state, but prohibits the District from collecting revenues like any other state. As a result, the District faces a major imbalance between revenues and required spending. Several years ago, McKinsey and Co. (the firm that helped develop the original Rivlin Commission study) reported that the District could reduce its spending by $150 million as part of a solution to the structural imbalance. In FY 2001, the District achieved $52 million in operating cost reductions. In FY 2002, the government reduced $14 million; and in the FY 2003 approved budget $193 million was reduced.

Much of these savings came from identifying areas of productivity savings and efficiency. Now that the District must reduce spending further, the opportunities for such savings are more elusive. Nonetheless, the formulation of the FY 2004 budget began by pursuing those remaining options where available, then developing other options. Specifically, the approach of my administration consisted of pursuing the following approaches, in the order presented:

1. Identify remaining areas of productivity savings and efficiency
2. Reallocate unspent fund balances
3. Freeze administrative spending
4. Suspend new increases in service levels
5. Reduce non-core programs (i.e., programs not supporting basic safety and health)

Through this approach, the proposed budget preserves core programs and minimizes the service reductions felt by the community. In other words, reduction options were pursued short of the point where core services became unsustainably affected. At that point, further reductions became unsupportable because they would threaten the viability of our community and government. To resolve the remainder of the shortfall, this budget includes revenue increases as defined below.

Increases in Revenue

Prior to this year, the District had avoided tax increases for almost a decade. In fact, laws passed in recent years have provided major taxpayer savings in income, property, and business taxes.[2] Likewise, many fees were maintained at historical levels, not even keeping pace with inflation.

At the beginning of the current year, however, the national economic downturn became so severe that even the extensive spending reductions made could not balance the budget, and revenue increases became necessary. These increases were limited to taxes on property, alcohol, cigarettes, utilities, telecommunications, and general fines and fees.

---

[2] Moreover, current law includes a schedule for further tax reductions in FY 2004-07. As the four-year financial plan demonstrates, however, the proposed budget will not be balanced if the scheduled tax rate decreases take effect. Therefore, as provided for in the Tax Rate Revision Act of 2002, these decreases will not take effect as planned.

In FY 2004, fiscal challenges will require even more spending reductions and revenue increases, and the government must turn to other sources of revenue to ensure a fair and responsible tax structure. To this end, the proposed budget includes three revenue proposals.

The first proposal ends a special sales tax exemption on selected services such as health clubs, theater admission, and private club memberships. Under current law, this exemption singles out a small group for special treatment. Therefore, eliminating it will not only provide additional revenue, it will also enhance the fairness of the tax code.

The second proposed increase will change the current tax rate on commercial parking from 12% to 18%, which will add 60 cents to a $10 parking charge. This rate has not been increased in more than 26 years.

Finally, as part of a third proposed increase, this budget creates a temporary increase in the tax rate on income over $100,000. For each tax return, the tax rate for income below $100,000 will not change. Only earnings beyond that amount will be subject to an additional six tenths of one percent. As a result, an earner with $150,000 in gross income and $125,000 in net taxable income will pay an additional $150. This temporary surcharge is proposed to stay in effect for two years only (calendar years 2004 and 2005).

Through these revenue initiatives (coupled with the expenditure reductions discussed above), the District's FY 2004 and future years' budgets will be balanced, and the standard of fiscal discipline maintained by this government over the past six years will be continued.

Although the operating budget has been responsibly balanced, however, there remains a grave concern about the physical infrastructure of the District. The next section addresses this concern.

Recognition of Neglected Infrastructure Needs

Like many historic cities, the District has an aging infrastructure that requires major capital investment. Unlike other cities and states, however, Congress prohibits the District from accessing the tax base needed to fund infrastructure improvements. To make matters worse, we do not have voting members of Congress who can secure federal infrastructure investments on par with other states.

As a result, the District has financed its capital investment primarily with borrowings secured by its very limited tax base. These borrowings have been managed responsibly, earning the District several upgrades in its bond rating from Wall Street. Because we lack other funding mechanisms, however, the District has reached the limits of its borrowing capacity, and has begun to dramatically scale back its capital investment. This includes the cancellation of renovations for outdated fire stations, libraries, recreation centers, and other essential facilities. Moreover, without the state support neighboring jurisdictions enjoy, the District cannot fund the major new investment needed for the Washington Metropolitan Area Transit Authority system without further neglect of local projects.

As stated above regarding the operating budget, there is a difference between an explanation and an excuse. The District is facing an operating budget gap largely due to the national economy and growing federal mandates, but we do not use that as an excuse to avoid difficult decisions.

On the capital side of this equation, however, no state or city could succeed without the basic revenue tools they have, and it would be irresponsible of this city to pretend that it can.

Therefore, the District has reached the point where it must partner with the federal government to address our joint infrastructure needs. Congresswoman Eleanor Holmes Norton has introduced the *Fair Federal Compensation Act* and the *No Taxation Without Representation Act* to address these issues. It now falls to the President and Congress to create a level playing field for the District of Columbia.

As we pursue this effort in Congress, I look forward to continued cooperation between the Mayor and Council. By demonstrating continued fiscal discipline, we can more effectively encourage the Congress to create a more appropriate funding structure for the District, and will best serve the interests of our citizens. As such, for the good of this cause and for the well-being of our city, I look forward to working with you as the Council begins its review of the proposed FY 2004 Budget and Financial Plan.

Sincerely,

Anthony A. Williams
Mayor