Certification of Revenues for the October 2024 General Obligation Debt Issuance

October 11, 2024

A report by EY/Quantitative Economics and Statistics
for the Office of the D.C. Auditor

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Office of the District of Columbia Auditor

Certification of the Proposed October 2024 General Obligation Debt Issuance: 2024 A,B,C

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I. Introduction

The District of Columbia Home Rule Act states that the Office of the District of Columbia Auditor (ODCA) is required to certify the official revenue figure used to determine compliance with the 17% test before new general obligation bonds can be issued.[1] To support this certification, ODCA engaged EY/Quantitative Economics and Statistics (EY/QUEST) in 2023 to create and update a model for forecasting District revenues (the "Certification Forecast") to certify that the official projections of revenue prepared by the Office of the Chief Financial Officer of the District of Columbia (OCFO) are adequate for proposed debt issuance.[2]

EY provided an initial Certification Forecast in February 2024, which compared data to OCFO's December 2023 revenue estimate. Since that time, OCFO published a June 2024 revenue estimate.[3] This Certification Forecast incorporates the latest information from the June 2024 revenue estimate and the data sources described in further detail in this report.

The forecast presented in this report is data-driven using econometric models. A complete list of inputs and sources for the models is included the appendix (Table A1). In cases where there is information about future tax changes, that information is incorporated through manual adjustments to the econometric results (e.g., the sunset of top deed tax rate). While notable tax amendments were passed in DC's FY 2025 Budget Support Act (BSA), they were not incorporated into the June 2024 OCFO forecast and are expected to be incorporated in a revised OCFO Forecast to be published on September 30, 2024. This analysis includes a baseline to compare to the June OCFO forecast and an adjusted forecast that includes the newly enacted revenue changes.

This Certification Forecast is meant to validate the official forecast prepared by the OCFO Office of Revenue Analysis (ORA) economists and not to replace it and should not be used as an official projection of District revenues.

II. Changes to the Economic Forecast

The Certification Forecast incorporates data from Oxford Economics, CoStar and the Congressional Budget Office (CBO) for forecasts of the economic and demographic variables that drive the revenue projections. Table 1 summarizes the changes in the compound annual growth rates (CAGRs) for 2023 to 2027 in the September 2024 Certification Forecast compared to the prior February 2024 Certification Forecast.

Notably, there are changes in the outlook for the S&P 500 index and for capital gains. The S&P 500 continues to set records and is now expected to grow on average 7.9% annually over the next five years.[4] Connected, the CBO revised their projections of U.S. capital gains realizations, a primary driver of the individual income tax.[5] The outlook for wages, employment and house prices have also improved since February.

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[1] DC Official Code § 1-206.03.

[2] Office of the District of Columbia Auditor. (2024, February 29). Modeling District Revenue to Certify Deby Service Obligations. Retrieved from:https://dcauditor.org/report/modeling-district-revenue-to-certify-debt-service-obligations/

[3] The June 2024 revenue estimate was unchanged from the February 2024 estimate that was the basis for the FY 2025 budget.

[4] Oxford economics. (2024, July 16.) Research Briefing | US. Behind the upward revisions to the long-term outlook. Retrieved from: https://my.oxfordeconomics.com/

[5] Congressional Budget Office. (2024, June). An Update to the Budget and Economic Outlook: 2024 to 2034; Retrieved from https://www.cbo.gov/system/files/2024-06/60039-Outlook-2024.pdf. The forecast for capital gains in the June 2024 update revised the estimate of capital gains downward for 2022 and 2023 relative to the February outlook and then upwards beginning in 2024.

Table 1. Summary of economic variables that can impact the revenue outlook

Indicator	FY 2023 value		FY 2023-2027 annual growth forecast		Use in models
	Sep 2024	*Feb 2024*	*Sep 2024*	*Feb 2024*	
DC GDP ($M)	172,384	167,082	4.2%	4.3%	Business income
DC food & accommodation GDP ($M)*	5,949	3,516	5.7%	3.0%	General sales
DC wage and salary income ($M)**	92,439	91,050	4.4%	4.2%	Individual income, General sales, Deed tax, Lottery
DC office vacancy (rate)	20.2%	20.6%	7.7%	8.6%	Real property (comm. assessed value)
DC office net deliveries (sum, sq ft)***	247,672	247,672	N/A	N/A	Real property (comm. assessed value)
US Capital gains ($M)	1,331,649	1,533,718	-0.2%	-4.5%	Individual Income
S&P 500 (index)	4,129	4,129	7.9%	3.2%	Business income
US Case Shiller housing price (index)	302	300	3.3%	2.1%	Real property (residential assessed value)
US single family home sales	3,759,165	3,765,950	3.7%	4.0%	Deed tax
US gross private domestic inv. ($M)	4,804,328	4,642,317	5.2%	5.6%	Licenses/fees
US nonresidential fixed investment ($M)	3,652,252	3,549,774	4.2%	4.6%	Real property (commercial assessed value)
DC resident population (level)	675,918	678,945	1.2%	1.2%	Licenses/fees, Charges
DC employment (level)****	765,410	773,733	0.9%	0.7%	Fines

Sources: US Congressional Budget Office; US Bureau of Economic Analysis; US Bureau of Labor Statistics; US Census Bureau, CoStar; Oxford Economics (US BEA; S&P; Fiserv; Macro Markets LLC; National Association of Realtors; Haver Analytics). Further details about sources are included in the Appendix.
Notes: The annual growth forecast is calculated as the compound annual growth rate (CAGR) from FY 2023-2027. In some cases, 2023 historical estimates were revised, also contributing to changes in growth rates.
*The prior report provided this value in real 2012 dollars of $3.5 million. This table reports this value in nominal dollars, which are used in the current forecast.
**DC wage and salary income historical values are from recently reported quarterly data from the US BEA.
***Office net deliveries reflect the difference between construction completed and demolition, changing from an aggregate 248 thousand sq ft in FY 2023 to a contraction of 80 thousand sq ft in FY 2027.
****DC employment includes in-commuters, causing total employment in the District to exceed the resident population.

Meanwhile, the outlook for the DC office vacancy rate continues to be weak and represents a key risk to the forecast. DC office vacancy rates remain above 20% for the entire time period, reaching 27.2% by 2027. With remote work stabilizing in the District, reaching office occupancy around 45% according to Kastle Systems, valuations of office buildings in DC are starting to reflect the trend.[6] Over the last year, assessments of office buildings in the District have declined 2.7%, and the assessed value for the 10 largest taxable office properties declined 3.8%.[7] Foreclosures of large offices appear to be rising. For example, one office building in Gallery Place that had been assessed at $225.7 million was acquired out of foreclosure for $39 million.[8] Commercial property assessment is primarily based on net income and so foreclosure acquisitions do not reflect future assessments.

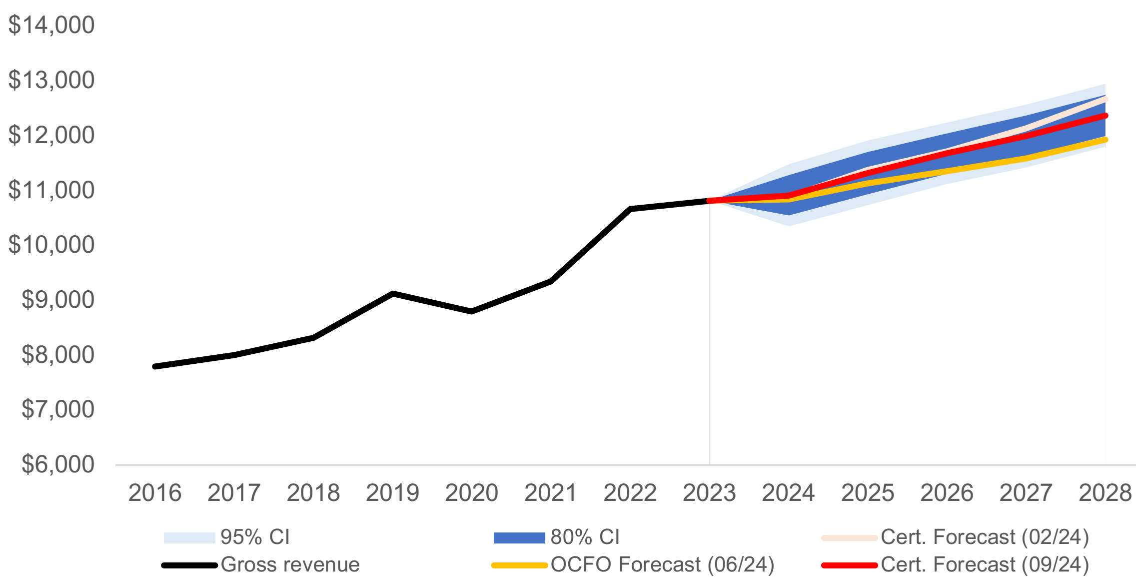
[6] Kastle. (2024, August 26). Kastle Back to Work Barometer: Weekly Occupancy Report from Kastle Access Control System Data. Retrieved from: https://www.kastle.com/safety-wellness/getting-america-back-to-work/#workplace-barometer
[7] Open Data DC. (2024, August 1). Analysis based on Integrated Tax System Public Extract. Retrieved from: www.opendata.dc.gov
[8] Walter-Warner, H. (2024, May 21). Debt, uncertainty slash Gallery Place complex sale price. *The Real Deal*. Retrieved from: https://therealdeal.com/national/washington-dc/2024/05/21/debt-uncertainty-prompt-humongous-gallery-place-discount/

Between forecasts, the 2023 to 2027 compound annual growth rates were also revised down for US single family home sales to 3.7% from 4.0%, US gross private domestic investment to 5.2% from 5.6%, and US nonresidential fixed investment to 4.2% from 4.6%.CBO projects a decrease in US nonresidential fixed investment (a component of gross private domestic investment) due to declining investment in nonresidential structures.[9] Oxford Economics reported that record-high home prices and high mortgage rates contributed to larger than expected declines in existing family home sales in June.[10]

III. Changes to the Baseline Revenue Forecast

Gross revenue. The baseline September 2024 Certification Forecast estimates $11.3 billion in gross General Fund revenue (revenue prior to dedicated revenues being netted out) in FY 2025. When compared to the February 2024 Certification Forecast, the current forecast for gross revenue is $27 million higher in FY 2024 due to increases in general sales and individual income taxes, while it is $65 million lower in FY 2025 and further decreases in subsequent years due to reductions for property and deed taxes. This baseline does not include recently enacted legislation affecting revenue.

Figure 1. Gross revenue forecast, FY 2016-2028 ($ millions)



Sources: OCFO June 2024 Revenue Estimate; ODCA (see Table A1 for inputs).

Figure 1 above shows that the Certification Forecast for gross revenue increases from $10.9 billion in FY 2024 to $12.4 billion in FY 2028. Much of this growth is due to growth in income and sales taxes. Both the Certification Forecast and OCFO's June 2024 Forecast anticipate growth below 1% for FY 2024, while the Certification Forecast predicts 3.7% growth in FY 2025 versus OCFO's prediction of 2.7% growth. The results of the analysis suggest that OCFO's gross revenue estimate

[9] Congressional Budget Office. (2024, June). An Update to the Budget and Economic Outlook: 2024 to 2034; Retrieved from https://www.cbo.gov/system/files/2024-06/60039-Outlook-2024.pdf.
[10] Oxford Economics. (2024, July 22). Data Insight | US: Existing home sales slump while inventory accumulates. Retrieved from: https://my.oxfordeconomics.com/reportaction/b491Ff7bd2DB4c56b3a6b4/Toc?SearchTerms=Data%20Insight%20%7C%20US%3A%20Existing%20home%20sales%20slump%20while%20inventory%20accumulates.

of $11.13 billion in FY 2025 is within the confidence interval of the Certification Forecast. Table 2 compares the September 2024 Certification Forecast to the February 2024 Certification Forecast and to the June 2024 OCFO forecast.

Table 2. Certification Forecast comparisons to prior forecast and to OCFO forecast, FY 2024-2028, ($ in millions)

Certification Forecast – September 2024									
	Real Property	General Sales	Individual Income	Business Income	Deeds	Nontax	All Other	Gross	Annual change
2024	2,812	2,053	3,246	1,140	328	661	669	10,909	0.9%
2025	2,794	2,169	3,339	1,298	346	688	682	11,317	3.7%
2026	2,846	2,269	3,398	1,384	383	713	682	11,676	3.2%
2027	2,864	2,368	3,474	1,432	425	745	686	11,993	2.7%
2028	2,906	2,467	3,582	1,487	478	758	690	12,367	3.1%

Certification Forecast – February 2024									
	Real Property	General Sales	Individual Income	Business Income	Deeds	Nontax	All Other	Gross	Annual change
2024	2,812	2,038	3,200	1,146	370	649	668	10,882	0.8%
2025	3,024	2,142	3,264	1,169	430	672	681	11,382	4.6%
2026	3,011	2,244	3,339	1,263	478	699	680	11,715	2.9%
2027	3,068	2,344	3,432	1,339	536	733	684	12,136	3.6%
Certification Forecast - September 2024 variance from February 2024									
	Real Property	***General Sales***	***Individual Income***	***Business Income***	***Deeds***	***Nontax***	***All Other***	***Gross***	***Annual change***
2024	*0*	*+15*	*+46*	*-6*	*-41*	*+12*	*+1*	*+27*	*+0.1pp*
2025	*-230*	*+26*	*+76*	*+129*	*-84*	*+16*	*+2*	*-65*	*-0.9pp*
2026	*-165*	*+25*	*+59*	*+121*	*-95*	*+14*	*+2*	*-39*	*+0.2pp*
2027	*-205*	*+24*	*+43*	*+93*	*-111*	*+11*	*+2*	*-143*	*-0.9pp*
2028	*N/A*	*N/A*	*N/A*	*N/A*	*-41*	*N/A*	*N/A*	*N/A*	*N/A*

OCFO Forecast – June 2024									
	Real Property	General Sales	Individual Income	Business Income	Deeds	Nontax	All Other	Gross	Annual change
2024	2,812	1,959	3,159	1,102	344	803	658	10,836	0.2%
2025	2,794	2,017	3,284	1,107	393	876	662	11,133	2.7%
2026	2,817	2,081	3,419	1,106	442	826	667	11,357	2.0%
2027	2,851	2,130	3,553	1,105	490	785	671	11,585	2.0%
2028	2,888	2,186	3,694	1,173	536	770	682	11,929	3.0%
Certification Forecast (September 2024) variance from OCFO Forecast (June 2024)									
	Real Property	***General Sales***	***Individual Income***	***Business Income***	***Deeds***	***Nontax***	***All Other***	***Gross***	***Annual change***
2024	*0*	*+94*	*+87*	*+37*	*-16*	*-142*	*+12*	*+73*	*+0.7pp*
2025	*0*	*+151*	*+55*	*+192*	*-48*	*-188*	*+21*	*+183*	*+1.0pp*
2026	*+29*	*+189*	*-21*	*+279*	*-59*	*-113*	*+16*	*+319*	*+1.2pp*
2027	*+12*	*+238*	*-79*	*+327*	*-65*	*-40*	*+15*	*+408*	*+0.7pp*
2028	*+18*	*+281*	*-112*	*+313*	*-58*	*-12*	*+8*	*+438*	*+0.2pp*

Source: ODCA; OCFO June 2024 Revenue Estimate.

The September 2024 Certification Forecast reduces gross revenue by $220 million over the 2024-2027 period from the February 2024 Certification Forecast. There is a small upward revision to FY 2024 based on the year-to-date performance of revenue collections and then relatively small downward revisions due to changing economic variables. The projected revision is primarily driven by a reduction in the property tax forecast, which is aligned with the OCFO estimates in FY 2024 and

FY 2025,[11] as well as a reduction in the deed tax forecast due to a downward revision in the growth forecast for US single family home sales. Meanwhile, the forecast for business income taxes increases notably due to the upward revision in the S&P 500 Index. The forecasts for general sales tax and individual income tax are revised up to reflect stronger DC wages and salaries, a key input for both revenues.

Compared to the June 2024 OCFO forecast, the September 2024 Certification Forecast is, on average, $300 million higher for each year beginning in FY 2025. Business income is stronger due to increases in the S&P 500 Index. DC wage and salaries increased general sales and individual income estimates for the Certification Forecast in FY 2024 and FY 2025, though it did not raise the forecast for individual income taxes above the OCFO forecast in subsequent years. By FY 2028, the Certification Forecast projects about $400 million more in revenue than OCFO due to combined increases of business income, general sales, and real property taxes.

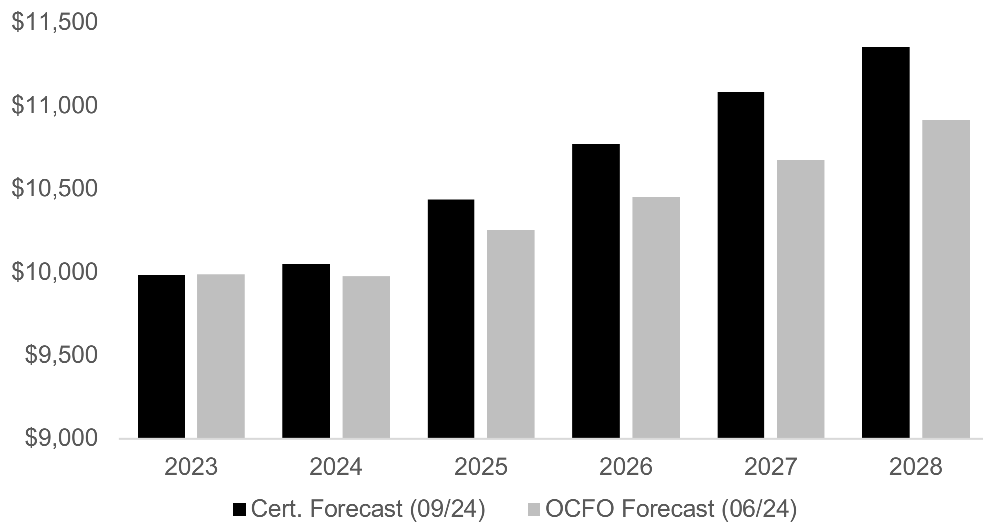
Dedicated revenue. For the dedicated revenue to other agencies or funds, the Certification Forecast uses the most recent OCFO forecast of dedicated revenues. The bulk of the $832.1 million dedicated revenue is dedicated from sales tax, where over $550 million, or about one-fourth of total sales tax collections, is dedicated. This includes $176.8 million (in FY 2023) in hotel and restaurant tax revenue that was dedicated to the convention center and $178.5 million that is dedicated annually to support WMATA capital investments.

Local revenue. Local revenue is calculated as gross revenue less dedicated revenue and is used for the 17% test (further defined in Section IV).

Figure 2 shows that the Certification Forecast estimates local revenue will grow from $10.0 billion in FY 2023 to $11.4 billion in FY 2028. The variance in local revenues for the Certification Forecast compared to the June 2024 OCFO estimate is less than $75 million for FY 2024, though this increases to a variance of $183 million in FY 2025, with a progressively larger Certification Forecast variance through FY 2028. Both forecasts shown in figure 2 exclude the impact of the BSA.

[11] Real property is assessed as of January 1 of each year and mailed to owners in February. Following the assessment, property owners have until April 1 to appeal their assessments. In February of the following year, bills based on the final assessments (after appeals) are mailed to taxpayers and payments are due on March 30th and September 15th. Because of this schedule, the OCFO has reliable data on real property for the one year out estimate.

Figure 2. Local fund revenue, FY 2023-2028 ($ in millions)



Note: The revised OCFO forecast is expected to be published September 30, 2024, which is too late for inclusion in this report.
Sources: OCFO June 2024 Revenue Estimate; ODCA

Legislation. The FY 2025 Budget Support Act (BSA) completed the Congressional review period and took effect on September 18, 2024.[12] The BSA contains several revenue changes that will have both positive and negative impacts on the budget. These changes were not incorporated into this Certification Forecast in order to permit direct comparisons with our February 2024 Certification Forecast and the June 2024 OCFO forecast; however, the changes are expected to be included when the OCFO revises the forecast at the end of September, too late to include here. The magnitude of the combined impact of the proposed amendments would include over several hundred million dollars in net increases for local revenue, mostly from an increase in the payroll tax from 0.26% to 0.75% to finance universal paid family leave with excess revenue not needed for program costs distributed to the general fund. This tax increase was effective July 8, 2024.[13] OCFO projects the combined total increase in revenues in FY 2025 to be $534.1 million, of which $401.8 million is increased local fund (Table 3).[14] When including the BSA's changes, the Certification Forecast estimates $11.8 billion in gross revenue and $10.8 billion in local revenue in FY 2025.

[12] Council of the District of Columbia. (2024). B25-0784 – Fiscal Year 2025 Budget Support Act of 2024. Retrieved from: https://lims.dccouncil.gov/Legislation/B25-0784.
[13] The FY 2025 Budget Support Act took effect on a 90-day emergency basis while the Congressional review period was pending.
[14] FY 2025 Approved Budget and Financial Plan, pages 3-25 to 3-26

Table 3. Revenue proposals for the FY 2025 Budget Support Act, ($ in millions)

Proposals	FY 2025	FY 2026	FY 2027	FY 2028
Universal paid leave (Local)	322.2	334.5	347.3	355.9
Sales tax increase (Local)	15.7	66.7	115.6	140.5
All other Local	63.9	53.1	74.4	144.2
Total Local proposals	***401.8***	***454.3***	***537.3***	***640.6***
Medicaid Hospital direct payment (Dedicated)	130.8	131.3	133.8	136.3
All other Dedicated	1.5	3.5	3.5	(76.8)
Total Dedicated proposals	***132.3***	***134.8***	***137.3***	***59.5***
Total Local and Dedicated Revenue proposals	**534.1**	**589.1**	**674.6**	**700.0**

Source: FY 2025 Approved Budget and Financial Plan, pages 3-25 to 3-26.

IV. Certification

District law states that ODCA is required to certify the official revenue figure that is used to determine compliance with the 17% test before new general obligation bonds can be issued. OCFO's June 2024 estimate of $10.25 billion in local fund revenue in FY 2025 is within the confidence interval of the Certification Forecast, adjusting for revenues dedicated to other funds.

The proposed General Obligation (GO) debt service of $586.4 million, $501.9 million for outstanding bonds plus new debt service of $84.5 million, would be 5.6% of the forecasted FY 2025 local fund revenue. Including Income Tax Secured (ITS) debt as well, the proposed debt service of $1,057.0 million would be 10.1% of the forecasted FY 2025 local fund revenue, meeting the 17% test.[15] For comparison, debt service would be 10.3% of OCFO's forecasted revenue. When considering an addition of $402 million in local fund revenue associated with the FY 2025 BSA amendments, debt service would be 5.4% of GO bonds and 9.8% of combined GO and ITS bonds.

Table 4 details the calculation for the 17% test for both the Certification Forecast and the forecast with the FY 2025 BSA amendments.

Table 4. Calculation of debt certification, FY 2025 ($ in millions)

	Certification Forecast		**Certification Forecast with FY 2025 Budget Support Act Amendments**	
	Debt service on GO indebtedness only	***Debt service on GO and ITS indebtedness combined***	***Debt service on GO indebtedness only***	***Debt service on GO and ITS indebtedness combined***
Debt service	$586.4	$1,057.0	$586.4	$1,057.0
Local revenue	$10,438	$10,438	$10,840	$10,840
Share of local revenue	**5.6%**	**10.1%**	**5.4%**	**9.8%**

Source: Certification Forecast revenue analysis; Final Calculation of Limitation on Borrowing received 9/19/2024 from OCFO; FY 2025 Approved Budget and Financial Plan, pages 3-25 to 3-26.

Another test is to estimate the maximum annual debt service (MADS) as a share of revenue. MADS occurs in FY 2026 when debt service is $628.2 million for GO bonds and $455.2 million for ITS bonds, a total of $1.08 billion. This represents 10.1% of forecasted FY 2026 revenue and 9.7% of

[15] DC Official Code § 1-206.03.

forecasted FY 2026 revenue with legislated changes. To reach 17% of local revenue, annual debt service would need to exceed $1.8 billion.

V. Conclusions

The Certification Forecast estimates $11.3 billion in gross revenue (local fund plus dedicated revenue) in FY 2025 and $10.4 billion in local revenue. The results of the analysis suggest that OCFO's June 2024 estimate of $10.3 billion in FY 2025 local fund revenue is within the confidence interval of the Certification Forecast. The proposed debt service of $1.1 billion, composed of $586.4 million of GO debt service, including the 2024ABC series, and $470.6 million of ITS debt service, would be 10.1% of the Certified Forecast for FY 2025 local fund revenue, meeting the 17% test.

Including the recently enacted FY 2025 Budget Support Act, the Certification Forecast estimates $11.9 billion in gross revenue and $10.8 billion in local revenue in FY 2025. In this scenario, the proposed debt service of $1.1 billion represents 9.8% of forecasted FY 2025 local fund revenue.

Appendix

Table A1. Certification Forecast sources for explanatory variables

Explanatory variable	Source	Last update
DC GDP ($M)	Oxford Economics (US BEA)	June 2024
DC food and accommodation GDP ($M)	Oxford Economics (US BEA)	June 2024
DC wage and salary income ($M)	US BEA, DC OCFO, US CBO	February 2024
DC office vacancy (rate)	CoStar	June 2024
DC office net deliveries (level)	CoStar	June 2024
Capital gains ($M)	US CBO	June 2024
S&P 500 (index)	Oxford Economics (S&P), S&P Dow Jones Indices LLC	May 2024
US Case Shiller housing price (index)	Oxford Economics (S&P, Fiserv, Macro Marks LLC, Haver Analytics)	May 2024
US single family home sales	Oxford Economics (National Association of Realtors, Haver Analytics)	May 2024
US gross private domestic investment ($M)	US CBO	June 2024
US nonresidential fixed investment ($M)	US CBO	June 2024
DC population (level)	Oxford Economics (US Census Bureau)	June 2024
DC employment (level)	Oxford Economics (BLS)	June 2024

Note: Acronyms are as follows: Office of the Chief Financial Officer (OCFO) US Bureau of Economic Analysis (BEA), US Congressional Budget Office (CBO), US Bureau of Labor Statistics (BLS).

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To fulfill our mission, we conduct performance audits, non-audit reviews, and revenue certifications. The residents of the District of Columbia are one of our primary customers and we strive to keep the residents of the District of Columbia informed on how their government is operating and how their tax money is being spent.

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