

**STABILITY THROUGH SCANDAL: A REVIEW OF  
THE OFFICE OF THE CHIEF FINANCIAL OFFICER**

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**HEARING**

BEFORE THE

OVERSIGHT OF GOVERNMENT MANAGEMENT,  
THE FEDERAL WORKFORCE, AND THE  
DISTRICT OF COLUMBIA SUBCOMMITTEE

OF THE

COMMITTEE ON  
HOMELAND SECURITY AND  
GOVERNMENTAL AFFAIRS  
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CHIEF FINANCIAL OFFICER**

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**TUESDAY, MARCH 31, 2009**

U.S. SENATE,  
SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT  
MANAGEMENT, THE FEDERAL WORKFORCE,  
AND THE DISTRICT OF COLUMBIA,  
OF THE COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Subcommittee met, pursuant to notice, at 10:03 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Daniel K. Akaka, Chairman of the Subcommittee, presiding.

Present: Senators Akaka and Voinovich.

**OPENING STATEMENT OF SENATOR AKAKA**

Senator AKAKA. The Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia will come to order.

Good morning, everyone. Thank you so much for joining us today, as the Subcommittee on Oversight of Government Management, the Federal Workforce, and the District of Columbia meets to examine the Office of the Chief Financial Officer (OCFO) for the District of Columbia. This morning, we will evaluate the current state of D.C.'s financial management, the progress it has made since its financial crisis in the 1990s, and how D.C. is addressing future financial challenges.

Over the past 14 years, D.C.'s finances have undergone major change. In the 1990s, longstanding budget deficits and a general lack of accountability resulted in the District's inability to provide adequate public services to its residents. Ultimately, Congress stepped in and passed the District of Columbia Financial Responsibility and Management Assistance Act of 1995. The act established a Control Board to oversee D.C. finances, expanded the powers of the D.C. Inspector General, and created the Office of the Chief Financial Officer.

The Senate held a series of oversight hearings shortly after the Control Board and OCFO were established to examine the problems leading up to D.C.'s financial collapse and reforms happening in other cities facing similar financial and social hardships. Recommendations from these hearings served as a starting point for D.C.'s fiscal recovery.

Thanks largely to reform efforts by the D.C. Mayor's Office and the OCFO, the Control Board was disbanded and the District resumed management of its own finances in 2001. In the years since the financial crisis, D.C. has achieved 12 consecutive balanced budgets. While many States and cities struggled with budget shortfalls, D.C. posted a budget surplus for fiscal year 2008.

Despite these accomplishments, the District faces many financial hurdles. The OCFO predicts decreases in revenue in the coming fiscal years. The OCFO's most recent revenue estimate shows a \$393.5 million decrease for fiscal year 2009, compared with its original revenue estimate from June of last year. The struggling economy and higher unemployment rates are contributing to D.C.'s weak revenue forecast.

Additionally, D.C. does not have the ability to increase revenues as other cities do. Much of the District's land is Federally owned and, therefore, not subject to D.C. taxes. Additionally, because a high proportion of people who work in the District do not live here, the city's residents pay for the upkeep of roads, bridges, sidewalks, and other infrastructure used by many non-residents who are not subject to D.C. income taxes.

The District also continues to struggle with financial management weaknesses. Due to insufficient internal management controls designed to prevent, detect, and deter fraud, the District repeatedly has suffered the loss of millions of dollars in taxpayer money.

In 2007, two employees from the Office of Tax and Revenue (OTR), a division of the OCFO, were arrested for the embezzlement of more than \$12 million. Investigations revealed a property tax refund scheme, beginning in the 1980s, in which fraudulent refund requests were submitted by a Tax and Revenue official and paid without detection for decades. At the time, there were no internal controls within Tax and Revenue to prevent such fraud. It appears that diligence in protecting the taxpayers' money was not part of the office's culture.

The scheme was discovered when the OCFO implemented an internal control in 2007 to flag refund checks over a certain dollar amount. A Tax and Revenue official tried to issue a fraudulent refund check, a warning went up, and she eventually was caught. Had the new internal control not been implemented, it is possible the fraud scheme would still be going on today.

I am also concerned by what appears to be a chronic problem with Medicaid management in the District. The D.C. Inspector General's audits of the D.C. Department of Mental Health Programs found that there was no process for revising and resubmitting denied Medicaid claims. Audits also uncovered incomplete documentation for Medicaid claims, causing the District to be denied Federal Medicaid reimbursement for services that had been provided. As a result, D.C. residents must bear this financial burden. I believe that is unacceptable and must be remedied by the OCFO.

Before I conclude my statement today, I would like to address an incident that took place earlier this month in the Office of the Chief Technology Officer (OCTO). An official was arrested for allegedly accepting bribes and engaging in a money-laundering scheme by approving fraudulent time sheets for non-existent employees

and charging the District for software products it never actually received. While I understand the official arrested was not under the direct purview of the OCFO, I believe this occurrence highlights general problems of accountability in contracting and procurement.

In 2007, the Government Accountability Office issued a report identifying a number of weaknesses in the District's procurement process, including the need for the OCFO to work more closely with the Mayor's Contracting and Procurement Office to bridge the gap between the program and finance components of contracting. It is my hope that the OCFO, while not directly responsible for the recent scandal in the Chief Technology Office, uses this unfortunate event as an opportunity to re-evaluate the environment in which contracting occurs and creates internal controls and robust anti-fraud policies where needed.

I hope today's hearing allows us to gain a greater understanding of how the OCFO has addressed recent scandals and has worked to implement new policies to improve the overall health of the agency and District Government. In this difficult financial climate, I believe it is important for Congress and District residents to know how the OCFO is safeguarding their hard-earned tax dollars.

I now turn to my friend Senator Voinovich for any opening statement that he would like to make. Senator Voinovich.

#### **OPENING STATEMENT OF SENATOR VOINOVICH**

Senator VOINOVICH. Thank you, Mr. Chairman. I thank you for holding this hearing to discuss both the progress and challenges still facing the District of Columbia.

The District's progress since the 1990s has been something Senator Akaka and I have followed close while serving on this Subcommittee, and I look forward to learning today from our witnesses about their next steps. As Senator Akaka said, a testament to the leadership of Dr. Gandhi, the District recently announced its 12th consecutive balanced budget amidst national economic hardship while continuing to boast an annual surplus.

I remember when you took over, Dr. Gandhi, we were in real trouble, and it reminded me very much of when I took over as mayor of the city of Cleveland when our books were inauditable and we had a financial supervisor involved. And I think the fact that you stayed on board and have worked over the years is something that we all can be thankful for. So often what happens, someone like yourself comes in and then they do their thing and then leave.

And I must say today, Senator Akaka, one of the real joys that I have—and there are not too many with the economy the way it is—is that the books of the city of Cleveland remain auditable and they get good marks because of the fact that we put in place a new system and then made sure that we attracted the people that were necessary, the professional people to get the job done. And in a lot of municipalities around the country, in too many cases, a lot of them get jobs because of who they know, and I know, Dr. Gandhi, that you hire people on what they know and their experiences so that they can give you the team that you need to get the job done.

I am sure that you are worried about where we are with the economy, but, again, you are better off than a lot of other places

in the country, because I think that you have been prudent, and the mayor has been working with you.

On the other hand, I think that there have been some recommendations on how you can improve the operation. We will be hearing about those from Mr. Willoughby today. I am sure that you are interested in those suggestions. And the main issue today, I think, is have you been able to attract the folks that you need to get the job done? I noticed in your testimony you are talking about getting a new person to come in. Are they out there? Can you get them?

So, Mr. Chairman, I am just glad to be here today and feel very good that when we got started with this, things did not look like they were going to go well. And we had confidence in you. I think we have been fortunate also to have Mayor Williams and now our new mayor, who seem to be professional people, who are running the city based on good public policy and financial management, and that helps a great deal, too.

Senator AKAKA. Well, thank you very much for your statement, Senator Voinovich.

I would now like to welcome today's witnesses to the Subcommittee: Natwar M. Gandhi, who currently is the Chief Financial Officer for the District of Columbia; and Charles Willoughby, who currently is the Inspector General for the District of Columbia.

As you know, it is the custom of this Subcommittee to swear in all witnesses. I would ask you to stand and raise your right hand. Do you solemnly swear that the testimony you are about to give the Subcommittee is the truth, the whole truth, and nothing but the truth, so help you, God?

Mr. GANDHI. I do.

Mr. WILLOUGHBY. I do.

Senator AKAKA. Thank you. Let the record show that our witnesses answered in the affirmative.

I want the witnesses to know that while your oral statements are limited to 5 minutes, your entire statements will be included in the record.

Dr. Gandhi, will you please proceed with your statement?

**TESTIMONY OF NATWAR M. GANDHI,<sup>1</sup> CHIEF FINANCIAL OFFICER, OFFICE OF THE CHIEF FINANCIAL OFFICER, DISTRICT OF COLUMBIA**

Mr. GANDHI. Thank you, Mr. Chairman. Mr. Chairman, Senator Voinovich, and Members of the Subcommittee, I am Natwar M. Gandhi, Chief Financial Officer for the District of Columbia. I am here to offer remarks about our progress in financial management generally and since the tax scandal broke in November 2007.

Mr. Chairman, in 1995, as you pointed out, the Congress created the Office of the Independent Chief Financial Officer to work with the mayor and the council. Since then, we have completed 12 consecutive balanced budgets, with two more in the pipeline, and turned a cumulative \$550 million deficit into an impressive \$1.2 billion fund balance. Further, we transformed a nearly bankrupt

<sup>1</sup>The prepared statement of Mr. Gandhi with attachments appears in the Appendix on page 25.



District Government plagued with junk bond ratings into a financially credible jurisdiction with strong ratings. Attachment 1 to my testimony and the display board right here in the testimony room tell the story of the District's successful return to fiscal solvency and financial stability.<sup>1</sup>

This turnaround is a case study in a commitment to improve financial management and practices. Our general obligation bond ratings have improved at an unprecedented speed. They now stand at A plus and A1 level from all three rating agencies simultaneously. In addition, we recently received a triple A rating from Standard & Poor's and double A ratings from Moody's and Fitch on our inaugural issuance of the income tax revenue bonds. These ratings will lower our borrowing cost by an estimated \$28 million over the next 4 years.

Another significant area of financial improvement has been in the management of our debt burden. In June 2007, I recommended to the mayor and the council a hard cap of 12 percent in the ratio of total debt service to total expenditures. It is now the law. Attachment 2 to my testimony shows the District's debt burden since 1992.<sup>2</sup>

Now I will turn to the improvements we have made since the tax fraud. This criminal enterprise was able to thrive over 20 years because of a failure of managerial oversight and internal controls. Immediately following the discovery of the fraud, we strengthened both the automated and manual controls over the refund process, replaced the tax office management, and removed numerous employees who benefited from the fraud and failed to report suspicious activities. In addition, we established an independent Audit Committee composed of distinguished professionals and chaired by former IRS Commissioner Sheldon Cohen to provide financial advice and review the financial management and internal controls of our office. We also hired Stephen Cordi, a distinguished tax administrator, as our tax commissioner. Mr. Cordi and his new management staff have made significant progress in instituting changes at the tax office. Each year, the Inspector General retains an external accounting firm to audit the District's financial statements and internal controls. The auditing firm of BDO Seidman gave us a clean audit opinion on our Comprehensive Annual Financial Report (CAFR), for fiscal year 2007 and 2008. However, they found the manual tax refund process to be a material weakness in fiscal year 2007. We worked hard to improve our controls in the refund process and other areas. As a consequence, in the just-released CAFR for fiscal year 2008, the auditors reduced the severity of their finding. Attachment 3 to my testimony shows the history of the auditors' detailed analysis of our internal controls.<sup>3</sup> I want to assure you that we have been working hard to reduce these and other areas of weakness in our controls.

Now I shall turn to our revenue situation, and I want to assure you that we are gathering the requirements for the procurement of both a new integrated tax system and a real property tax system as we strengthen our revenues.

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<sup>1</sup> The chart referred to appears in the Appendix on page 38.

<sup>2</sup> The chart referred to appears in the Appendix on page 39.

<sup>3</sup> The chart referred to appears in the Appendix on page 40.

In terms of our revenues, the economic outlook of the District of Columbia has changed dramatically from that of a year ago. The current forecast assumes that the economic condition will continue to deteriorate as employment and wages edge downward, commercial property transfers slow further, and construction projects are delayed. Even with this grim outlook, we are managing our fiscal affairs well.

On the plus side, we are fortunate to be a center for these growth areas: Government, education, and health. And even though our revenues are shrinking, the diversity of our tax base will help us to pull through these times in better shape than many other States and localities.

On the negative side, a significant portion of our population is not well educated or trained to fill jobs in the growing employment areas. The services that they will need, and that we must provide, will continue to tax our resources at increasing levels.

In summary, Mr. Chairman, the District has accomplished much—some might even say miracles—in the last decade. Its fiscal condition is sound. Our mayor and the council, the entire elected leadership, possess a steadfast commitment to fiscal responsibility that has become widely recognized.

This concludes my oral remarks, and I request that my written testimony be made part of the record, and I will be delighted to answer any questions you may have. Thank you, sir.

Senator AKAKA. Thank you very much, Dr. Gandhi.

Mr. Willoughby, will you please proceed with your statement?

**TESTIMONY OF CHARLES J. WILLOUGHBY,<sup>1</sup> INSPECTOR GENERAL, OFFICE OF THE INSPECTOR GENERAL, DISTRICT OF COLUMBIA**

Mr. WILLOUGHBY. Yes, Mr. Chairman. Good morning, Chairman Akaka, Senator Voinovich, and Members of the Subcommittee. I am Charles J. Willoughby, Inspector General for the District of Columbia, and I am pleased to speak before you this morning at your hearing entitled “Stability Through Scandal: A Review of the Office of the Chief Financial Officer,” also referred to as OCFO.

You asked me to address specifically: First, the independent auditor’s report relative to material weaknesses identified in the Comprehensive Annual Financial Report (CAFR); second, to address progress that the Chief Financial Officer has made in responding to recommendations from the Office of the Inspector General (OIG); third, to address cooperation between the OIG and the OCFO to achieve efficiency and improve accountability; and, fourth, ways that the OCFO can improve its financial management.

William J. DiVello, the D.C. Assistant Inspector General for Audit, is accompanying me today. With your permission, a longer version of my opening statement has been submitted for the record.

By law, the Inspector General must enter into a contract with an independent auditing firm to audit the city’s financial statements. On January 30, 2009, the District of Columbia received an unqualified opinion on its financial statements for fiscal year 2008 from its independent auditors, BDO Seidman. It is noteworthy to mention

<sup>1</sup>The prepared statement of Mr. Willoughby appears in the Appendix on page 57.

that this is the 12th consecutive year in which the District received a clean opinion on its financial statements from independent auditors. While an unqualified opinion provides that the financial statements were presented fairly in all material aspects, the independent auditors also issued a report on internal control and compliance over financial reporting, commonly referred to as the “Yellow Book” Report. The Yellow Book Report noted a continuing need to address significant internal control deficiencies and material weaknesses.

The fiscal year 2008 Yellow Book Report cited two material weaknesses: The first was the Office of the Chief Financial Officer’s treasury functions; and the second, was the management of the Medicaid program. The treasury functions contributing to the material weakness involved the failure to reconcile cash and investment account activities. The Office of the Chief Financial Officer generally responded positively to these findings, providing detailed actions to reconcile all accounts on a monthly basis.

The second material weakness involved management of the Medicaid program, which has been a longstanding problem for the District, having been reported as a reportable condition in prior CAFR years and a material weakness for fiscal years 2007 and 2008. Recognizing that many of the city’s Medicaid’s problems reside in the billing and accountability areas, the District recently created the Department of Health Care Finance to better manage the Medicaid program.

In the fiscal year 2007 CAFR Yellow Book Report, the independent auditors cited conditions at the District’s Office of Tax and Revenue (OTR), as a material weakness that contributed to a \$50 million fraud perpetrated by an OTR manager working collusively with several other individuals. Given the severity of the fraud, the District’s City Council established a Tax and Revenue Investigation Special Committee to review the OTR fraud.

The special committee retained Wilmer Cutler Pickering Hale and Dorr, LLP, to examine the facts and circumstances surrounding the fraud scheme and to make recommendations to prevent a recurrence. Approximately 38 recommendations were directed to the OCFO that addressed the failure of internal controls, a culture of apathy and silence, which was pervasive among many OTR employees, and the lack of effective oversight.

In the past several years, the OIG has issued numerous reports that addressed improvements in various OCFO areas. One important report was a Management Implication Report (MIR), that we issued in October 2007 concerning systemic internal control deficiencies. These deficiencies addressed such issues as ineffective policies and procedures, ineffective controls to prevent or detect fraud, lack of documentation, and ineffective management oversight. In another MIR issued in January 2009, the OIG focused on internal control weaknesses in the District’s payment process. Overall, the findings and recommendations the OIG has directed to the OCFO have been met with approval, acceptance, and implementation of corrective actions.

Because the OCFO plays an essential role in maintaining the integrity of the city’s finances and serving as the primary accountant for all fiscal matters on a local budget of about \$8 billion, we have

engaged the OCFO on several levels to improve interagency cooperation and oversight efforts. For example, while not a voting member of the CAFR committee chaired by the OIG, the OCFO enjoys a tenured role as an active participant in regularly scheduled CAFR meetings. CAFR committee meetings serve an extremely important function in getting management of District agencies and independent components, along with the OCFO, to cooperate and coordinate efforts to permit timely completion of the independent auditors' financial statement audit.

While the OCFO has taken many corrective actions relative to its operations, we believe there are several areas where additional management actions should be taken to improve its operations:

First, given the impact that sound internal control has on accountability, effective, and efficient government operations, the OCFO should issue a citywide directive requiring managers to establish, assess, correct, and report on internal controls.

Next, regarding the payment process, the OCFO needs to assign accounts payable officials more accountability by developing written policies and procedures that require due diligence prior to the payment of invoices. For example, steps must be taken to ensure that the payment of contractors' invoices is made only pursuant to the approval of authorized agency personnel.

Next, recent frauds perpetrated against the District disclosed a need for an intensified anti-fraud program. By intensifying its anti-fraud preventive and detective controls, the OCFO can better create a culture of ethical behavior in the workplace.

Next, recruiting and retaining qualified personnel, and then properly supervising its staff, to include management review of transactions and processes, and timely and accurate employee evaluations.

In summary, my office will continue to provide an independent assessment of the OCFO to help maintain the highest standards of conduct, integrity, efficient, and effective government operations.

Mr. Chairman, my staff and I will be happy to answer any questions that you may have. Thank you.

Senator AKAKA. Thank you very much, Mr. Willoughby.

Dr. Gandhi, as you may know, before coming to Congress I was an educator and a principal in the Hawai'i public school system. I was troubled by the D.C. Inspector General's report that identified payroll and financial monitoring problems within the D.C. public school (DCPS) system. I understand your office responded by assembling a task force to focus on deficiencies within DCPS. I have a two-part question for you.

Please elaborate on the changes you have made to address problems with DCPS finances. And to others, how do these changes correspond with the mayor's education reform initiatives?

Mr. GANDHI. Thank you, Mr. Chairman. Those are important issues for us as we deliberate on the mayor's major initiative on school reform. School finances have been an issue for several years, if not a decade or more. In our so-called Yellow Book, schools have appeared most of the time, and we have been plagued in the schools with antiquated payroll and managerial systems. What we have done at the schools, first, is to make sure that our Chief Financial Officer there remains very aggressive in terms of exercising

internal controls; second, installed a new payroll system; and third, we have installed all the relevant financial management techniques and procedures immediately going forward.

We work very closely with the chancellor and the deputy mayor in charge of education to collaborate and enhance the mayor's effort to improve the education of our children. So, we are equal partners in the mayor's effort to improve our school system.

Senator AKAKA. Dr. Gandhi, as you know, a report for the Tax and Revenue Investigation Special Committee concluded that the tax refund scheme was not identified sooner in part because of a pervasive culture of apathy and silence. As you know, Ranking Member Voinovich and I believe human capital investments like strategic planning, supervisor training, and mentorship programs can have far-reaching positive effects on morale and performance.

Please describe the investment your agency has made in strategic planning, supervisor training, and other efforts to bring about a culture of transparency and accountability. I am particularly interested in the details of the integrity and accountability training mentioned in your testimony.

Mr. GANDHI. Yes, sir. The lessons that I have learned, that we have all learned, from the tax scandals are the following:

One, the cliché about eternal vigilance is extremely important and quite relevant as we manage the complex finances of the District.

Two, establishing internal controls is simply not enough. Of course, you have to have effective internal controls, but what you really need is to make sure that you keep testing them, and make sure that people are following those controls effectively.

Three, you pointed out, sir, is the importance of creating a climate of accountability and ethical behavior. That is the heart of the matter.

As this scandal went on for more than 20 years, it was not detected, nor was it reported even by the people who were there for all those 20 years receiving money, and the managers had no clue.

What we have done is: One, reinstitute strong internal controls; two, when I became the head of the Office of Tax and Revenue in 1997, every employee had to take a course in ethics, ethical behavior, and our Code of Conduct; three, we started the background investigation of all of our employees, new employees; and then have that investigation and training recur on a regular interval.

But more important than anything else, I think, is the example that we need to set at the managerial level, at the highest level. One reason why on the day the scandal broke, I simply removed 12 managers right from top to bottom, who were responsible in terms of providing managerial oversight and had profoundly failed. We basically took them out of the office. Roughly 40 people have left the office because of the scandal.

We have zero tolerance because of the remarkable financial recovery that we brag about all the time in the District. We went from a \$500 million deficit to \$1.2 billion of fund balance from junk bonds to triple A ratings, but it will be for nothing if we do not instill the sense of ethics, sense of accountability within our midst.

So this is a paramount issue for all of us in the District, and particularly in the area of the Chief Financial Officer's operations.

Senator AKAKA. Well, thank you very much. It is good to hear what you have done and are still trying to do.

Let me now call on Senator Voinovich for his questions.

Senator VOINOVICH. Thank you, Mr. Chairman.

I have looked at this chart that you have prepared,<sup>1</sup> and it is very impressive. But when you are talking about a \$1.2 billion—what is it? Is that a surplus?

Mr. GANDHI. That is a savings account. That is the accumulated surpluses over the years. That is where—if you look at the household, that is our savings account.

Senator VOINOVICH. So that is money that is available in the event that you are not able to meet your revenue estimates to run the city? You would tap that in order to make sure that you balanced your budget?

Mr. GANDHI. Part of it. What has happened here is—

Senator VOINOVICH. It would be like in the State government we would call it our “rainy-day fund?”

Mr. GANDHI. Exactly right. That is the rainy-day fund. But I want to be careful here. Strictly, of that \$1.2 billion, about \$330 million is what you would call, as you pointed out, the rainy-day fund comprised in our case of emergency and contingency cash reserves, which is about 6 percent of our budget. Congress requires that we put in that rainy-day fund 6 percent of our budget. In addition to that, our escrow fund, other reserves, when you add it all up, it is \$1.2 billion.

Now, in terms of making sure that we balance our budget, so far we have been able to do that from our regular operating revenues.

Senator VOINOVICH. OK, but I want to get a better idea of this. By the way, this increased rating by rating agencies, that is impressive because they really look at you, and I think that is something that you should be very proud of—although you have a 12-percent cap on borrowing?

Mr. GANDHI. Yes, sir, 12 percent.

Senator VOINOVICH. In the State government and city, we were at 5 percent. Is that a traditional number of 12 percent? Isn't that quite a large number?

Mr. GANDHI. Well, under the Control Board, we used to have a 17-percent cap. But when we checked with the financial markets, our financial advisers, Moody's basically said that of the large cities, it is around 11.5 percent.

Senator VOINOVICH. So it is about average.

Mr. GANDHI. It is about average.

Senator VOINOVICH. Across the board.

Mr. GANDHI. Yes, of the large cities.

Senator VOINOVICH. And that basically is for the public's understanding, that is the portion of the budget that is being used to amortize the bonds that the city has issued over the years in order to do the capital improvement and other things that you need to do.

Mr. GANDHI. Exactly right. Or, to put it another way, 88 cents of every dollar is available to provide services to our citizens and

<sup>1</sup>The chart referred to appears in the Appendix on page 38.

12 cents of every dollar is, as you pointed out, to take care of our debt service.

Senator VOINOVICH. Do you have a provision where you restrict the amount of money that can be used for payroll and so forth? In other words, what we had, when we passed the increase in income tax, we restricted a certain amount of money to amortize debt and to pay debt. Or is that just something that there is nothing in the past law that says you have to restrict X number of the dollars to take care of that.

Mr. GANDHI. Well, what is required of us is that we provide a balanced budget; that is, at no time will we spend more money than we take in and that we would balance this over a 5-year period, not just 1 year. We provide to you a 5-year plan.

Senator VOINOVICH. Yes, I see that. Now, tell me, what are the numbers again? Here it says that you have the revenue estimate was back in—

Mr. GANDHI. June.

Senator VOINOVICH. June, yes, And you are down 7.1 percent.

Mr. GANDHI. Right.

Senator VOINOVICH. In other words, you have a nut to crack here because of the economy. How much of it is that? And how do you intend to take care of that?

Mr. GANDHI. Right. So just to recap the numbers that you pointed out, in 2009 we would lose approximately \$400 million from what we had estimated. In 2010, that would be about \$800 million, and in 2011, around \$1 billion. So the way we are trying to manage this, first above all, is that we would cut our expenditures. That revenue estimating is done by the independent Chief Financial Officer. We provide to the mayor what the revenue estimates are. We cost out for the mayor what the budget items, budget projects, and budget programs are going to cost, and then we assure the Congress that when we come before you, we will have a balanced budget.

Senator VOINOVICH. OK. So those are the recommendations that you are going to make to the mayor. He has got between now and—you are on a budget that begins July 1?

Mr. GANDHI. No. October 1. We are on a fiscal year.

Senator VOINOVICH. You are on the Federal schedule. You have between now and October 1 to figure out ways that they can deal with this \$400 million.

Mr. GANDHI. Actually, \$800 million, because we are now talking about the 2010 budget. The 2009 budget is already taken care of. We already cut about \$400 million off our revenue.

Senator VOINOVICH. OK. So that is taken care of, and you are looking now at 2010.

Mr. GANDHI. Yes, sir. So the mayor has already submitted a balanced budget to the council earlier last week. Now the council will work at it, and in June, we will come back to the Congress and give our 2010 balanced budget.

Senator VOINOVICH. OK. But the question I have is if you have taken care of the problem for 2009—

Mr. GANDHI. Right.

Senator VOINOVICH [continuing]. He has made some changes.

Mr. GANDHI. Yes, sir.

Senator VOINOVICH. The issue becomes will those changes that he made be continual changes that would impact on the \$800 million so that rather than having \$800 million to deal with, he is going to have to find another \$400 million?

Mr. GANDHI. Absolutely right. I think that is the whole issue of providing a 5-year plan; that is to say, we cannot have a recurring expenditure without a recurring source of revenue. So what the mayor has done in 2010, actually, for the first time in a long time, we have submitted a budget which is lower than the previous year.

Indeed, what the mayor has done—and I greatly commend the mayor for that—is that he has simply bent the curve. In the past, we have had budget increases that are 6, 7, 8, 10 percent every year. We had revenues like that, too.

Senator VOINOVICH. So the point is that you are going to try to take that within the operation of the city, and you are not going to touch the rainy-day fund, you are going to try not to do that.

Mr. GANDHI. Absolutely right,

Senator VOINOVICH. If you have an emergency, you probably might have to do it.

Mr. GANDHI. The Congress has put very strict conditions on this. In other words, for us to be able to touch the rainy-day fund, emergency fund, we need to have a real emergency, a FEMA-type emergency—floods, earthquakes, stuff of that sort. And the decline in revenue also has to be far more substantial than what you see here. So by any measure, that fund is untouchable.

Senator VOINOVICH. So the point is that for 2010 you are estimating a flat budget—

Mr. GANDHI. Actually, a lower budget.

Senator VOINOVICH. A lower budget than you had, so that the council and the mayor are going to have to make some significant additional changes.

Mr. GANDHI. The mayor has already done that for 2010, and the council is deliberating it now.

Senator VOINOVICH. So they have that before them right now, and they are trying to figure out how they can do it. If they are able to do that, then you take care of the additional \$400 million for 2010.

Mr. GANDHI. And I am confident that we will do it. Indeed, we will never send a budget to you, sir, which is not balanced.

Senator VOINOVICH. All right. And, of course, you have had to estimate what you think the revenues are going to be for the District.

Mr. GANDHI. Absolutely. The Chief Financial Officer (CFO) has the exclusive right to estimate the revenues. So we cannot have a so-called rosy scenario doing the revenue estimate.

Senator VOINOVICH. OK. I have gone over my time. Senator Akaka, thank you.

Mr. GANDHI. May I take just a comment to compliment Senator Voinovich here. We learned the lessons from Cleveland. We learned what you did. The fiscal prudence and fiscal discipline that you, sir, provided when you were the mayor was a guide to us. And Tony Williams used to mention that to us. So we are very grateful to you for that.

Senator VOINOVICH. Thank you.

Senator AKAKA. Thank you for that comment, Dr. Gandhi.



Dr. Gandhi, I understand that your office has recovered nearly \$1 million lost in the tax refund scheme and has filed for restitution for almost \$4 million in real and personal property. I am encouraged by your efforts to recover these funds.

I would like to know what other steps the office is taking to get back the lost taxpayer money?

Mr. GANDHI. Our Attorney General has filed a lawsuit against Bank of America for \$105 million, including the original tax loss plus the penalties and other damages that we have suffered. And we will vigorously pursue that. And I think, as I pointed out earlier, we want to remain totally vigilant whenever the taxpayer dollars are involved.

Senator AKAKA. Dr. Gandhi, I mentioned in my statement the issue of Medicaid management concerns, and they concern me especially. The District loses millions of dollars every year because the Federal Government denies incomplete Medicaid claims from the District.

Will you please describe the steps your office is taking to remedy chronic Medicaid reimbursement problems?

Mr. GANDHI. Thank you, sir. The very first step I do take, and have been taking over the last 10 years, every time I meet a new city administrator in the city, I tell him that the three things you must do immediately is Medicaid, Medicaid, and Medicaid, because that is where 20 percent of the budget is. Over the last 10 years, we have lost close to \$343 million, and that we cannot afford to do.

Second, our fundamental problem here is that the Medicaid effort has somewhat disintegrated into three provider agencies: The Department of Mental Health, Child and Family Services; the Department of Human Services; and the school system. And each one of them was trying its own way of reclaiming the money.

Third, the social workers in Child and Family Services, which is where the major problem is, their primary concern is to provide services to needy children. A Medicaid claim is the last thing on their mind.

We have been urging the council and the mayor to consolidate that effort. Fortunately, what we have now under Mayor Fenty is a new Department of Health Care Finance. All of our Medicaid efforts are concentrated now under one roof. I am quite encouraged by the leadership of that new department. Indeed, we just met last week with them to see what progress they have made, and the contention here is that they would follow aggressively to document the services that are being provided and make sure that we claim every dollar that should be coming to the District.

Senator AKAKA. Mr. Willoughby, I understand that the D.C. Inspector General conducts year-round audits of the District's Medicaid system. Medicaid management continues to be a consistent problem. Do you believe there are still billing and accountability flaws that are not being addressed? Or do the reforms made just need time to take root?

Mr. WILLOUGHBY. I think based on our recent audits, I think that there are still problems in the Medicaid area, and to that extent, we continue to audit Medicaid continuously. Within my office, we have set up a particular—we have assigned a unit or a compo-

ment within the Audit Division that is broken down or assigned by risk areas, of which Medicaid is one of those risk areas.

So I guess the answer is, yes, I believe there still are problems. My office continues to try to explore ways—my office cannot make management take certain actions, but I think my office can help management to focus on those areas where we believe there are weaknesses, of which Medicaid is clearly one. And so what we have done, not only do we do the audits, we do follow-up audits; once we issue a report or a finding of some sort, we then will go back informally and find out what the agency or division is doing with respect to addressing the problems that we cited. I can say that we have worked closely with the CFO's office in that regard.

I would like to say that I do not want my office to be viewed as what I call a "gotcha" office. I believe we are all working for the same thing—an efficient and effective Government. Medicaid is a serious problem. Within the confines of the role of an Inspector General, I want to utilize the resources and the auspices of my office as much as possible without going over that line of performing management's job of assisting management in correcting what we see as a serious deficiency.

Senator AKAKA. Thank you.

Dr. Gandhi, I am pleased with the working relationship that is mentioned here between your office and also with the Government Accountability Office (GAO) to ensure responsible management of the economic recovery funds the District received. Please tell us more about the District's plans for managing recovery funds and the support that GAO is providing.

Mr. GANDHI. Thank you, sir. We work very closely with the Office of the Inspector General and also with the District's auditor regarding GAO. Sir, I spent 20 years at the GAO before I came to the District, so I am thoroughly familiar with the way GAO does its work.

Just last week, we had a meeting with the GAO people. As you know, what GAO is trying to do is to closely examine the spending of the stimulus money, roughly two-thirds of the money, in 16 States and the District of Columbia. So we are going to work very closely with GAO, but in addition, I have a task force in my own office which coordinates with the mayor's office the effort that we are making to spend the stimulus package, which is around \$400 million in terms of the fiscal relief, and I would say \$500 million or so for Metro, Water and Sewer Authority (WASA), and other capital projects.

We will provide all this information as to how the money is being spent on our website, working with GAO and with the Inspector General's office. So we are on the case.

Senator AKAKA. Thank you for your response.

Senator Voinovich, do you have further questions?

Senator VOINOVICH. Yes. This is fun. [Laughter.]

Fun because it just puts me back to where I was a few years ago.

How much of a match do you get from the Federal Government on Medicaid?

Mr. GANDHI. We got 70–30. Basically, for every \$100 locally spent, we are entitled to get \$70 back.

Senator VOINOVICH. That is a very generous contribution from the Federal Government compared to lots of other places. I know in Ohio it is 60–40. What is it in Hawaii, do you know?

Well, the point is you have to raise the local 30 percent.

Mr. GANDHI. Right. But, sir, if I may point out, we are a city. We are not a State. So we would wish that we would have a State that would take care of responsibilities, but we are not complaining.

Senator VOINOVICH. I understand that. You are like the county welfare department. So the real issue here is to try and do a better job of getting control of your Medicaid costs, and you are talking about the reorganization, and, Mr. Willoughby, you are looking at it. Is the determination about how that welfare agency or Medicaid administrator in the hands of the mayor and city council—it is not in your hands, is it?

Mr. GANDHI. No, sir.

Senator VOINOVICH. You can make recommendations to them about how to get it done, but they, in fact, are the ones that have to put the plan in place. And you are saying that a lot of people that are more interested, let's get the money on the street, not are so much worried about whether we are working harder and smarter and doing more with less.

Has the District, to your knowledge, looked at any place around the country to see if there are best practices about how do you go about—because I can tell you this: Medicaid is the Pac-Man of any budget?

Mr. GANDHI. Absolutely.

Senator VOINOVICH. At the State level, it just sucks up money, and then you would have less money for education, higher education, secondary, primary, and the rest of it. Do you know that? Have they looked at any—I know the mayor has done this, but is there a model that he has looked at that would serve as a best practice?

Mr. GANDHI. Exactly right, and on that issue, you are absolutely right about it being Pac-Man. In our case, as I said, it is 20 percent of the budget. About a quarter of our residents are Medicaid eligible, and it costs about \$7,000 per Medicaid recipient as opposed to, say, about \$5,000 in Maryland or Virginia. Because we are a city, it costs more. So we are very much aware of the problem that we face in Medicaid.

What we are currently doing, working with consultants and others, is to see what is going on in other States and how can we make sure that, one, we are effective in providing services and, two, claiming from the Feds what should be coming to the city. Our new city manager, who is in charge of this, he is very much on the case on that, sir.

Mr. WILLOUGHBY. Mr. Chairman.

Senator VOINOVICH. Yes, Mr. Willoughby.

Mr. WILLOUGHBY. I may have some information. I understand that the city looked at best practices when it established that Health Care Finance entity, and that my office is currently looking at best practices with regard to that matter.

The other thing I would point out is that within the Office of the Inspector General, there is a Medicaid Fraud Control Unit, and one

of the few to have that kind of unit within the Inspector General's office. We work closely with the Health Care Finance entity. Individuals within that unit prosecute providers for improperly—I guess fraud within the Medicaid program as well as prosecution of individuals who are mistreated in Medicaid-funded facilities.

One of our priorities is to try to recoup as much money as possible through that vehicle. We work closely with this—something called the National Association of Medicaid Fraud Control Units. My office is very active in that. So one of the things we are trying to do is to recoup money through the Medicaid program, through prosecution and others joining in joint settlements and that sort of thing.

Senator VOINOVICH. Good. That is very good.

I want to comment, Dr. Gandhi, about the fact that these people, the management people, were let go. Good for you. Most places, the person that gets involved is penalized, and then you do not go up the chain of command and hold people responsible. I think that is really important because it sends a message out from the top all the way down that you better pay attention and not be on watch. That is great.

You are getting stimulus money, and I have asked Tom Bishop, our staff member, to give me a printout of it. Do you have the capacity now—I mean, is the amount of money coming in, to the extent that you have to hire more people in order to properly watch over how it is being spent, or are you able to do it with the people that you now have?

Mr. GANDHI. I think in our case, we have enough people to basically monitor how the money is going to be spent, but we are working very closely with GAO; and if it were to be determined that we would need more people, I will not hesitate to go to the mayor and the council and say, look, I need five more people to make sure that money is spent well.

But right now, we are OK. We have already pointed out where the money is coming from, how much it is, and we have been working with people at the Office of Management and Budget (OMB), GAO, and in the city administrator's office, giving them our analysis of the Medicaid stimulus package that we will get.

Senator VOINOVICH. Well, I hope if you need them you get them, so that GAO does not come back to us—because I am watching those reports on the 16 States. Ohio is one of them that they are watching. You better anticipate it rather than have them come back and say they do not have enough people to get the job done.

Mr. GANDHI. Right.

Senator VOINOVICH. But that is something you can decide.

Mr. Willoughby, you made 38 recommendations, and the question I have is: How responsive has Dr. Gandhi been to those recommendations that you have made? Have any of them been completed? Have you a priority list of what are the most important recommendations of the 38? How are we doing there?

Mr. WILLOUGHBY. Well, from what I understand, there has been progress, there is progress made with regard to putting in place some of the internal controls. There are still areas that need to be addressed. I do know this: We are currently—the council has asked us to review the recommendations made by the special committee,

and we are in the process of assessing what of those recommendations—how they have been handled by the CFO's office, I guess.

Senator VOINOVICH. Mr. Chairman, would it be appropriate for use to ask for a report in 6 months about how these recommendations have been made so that we can monitor that?

Senator AKAKA. I think it would be appropriate, yes. We would like to keep—

Mr. WILLOUGHBY. We will be glad to do that.

Senator VOINOVICH. If you could do that, I would appreciate it.

Mr. GANDHI. May I make a comment on that, sir? Our policy on casework reports that we get from the Inspector General and also from the city auditor is to immediately make sure that we sit down and understand the recommendations and start implementing them as soon as we can.

Second, the so-called Wilmer Hale report that was issued by the council in the wake of our tax fraud, we have immediately followed all the recommendations, and we are nearly complete with the implementation of those recommendations as well.

The idea here is not to argue with them on semantics and say, look, we have been doing this. As the IG can testify, we work very closely with them not only on this, but also our so-called annual report that is under the IG's purview.

Senator VOINOVICH. Thank you.

Senator AKAKA. Thank you very much.

Mr. Willoughby, as you know, internal control weaknesses have led to mismanagement of D.C. funds, in your testimony, you recommend that the OCFO issue a citywide directive requiring the assessment and monitoring of internal controls.

How would you propose the OCFO formulate appropriate performance measures to assess and monitor internal controls?

Mr. WILLOUGHBY. I guess I am always, as an Inspector General, reluctant to perform the role of management. But I think one basic thing—and I think the CFO has referred to this—I believe at the core of many of the problems that exist there is a lack of sufficient oversight and supervision. And I think it is important that you have—I would like to say you have levels of supervision, and I think it is important that the supervisors exert their supervisory and oversight authority. They have to personally monitor. I have said this before: I believe that you can restructure and reorganize, as I like to say, until the cows come home. But at the end of the day, you still have to have someone who is supposed to be doing what they are supposed to be doing, whatever that task or function is. And then you have to have someone who is going to be holding them accountable. So supervisors have to inspect and review the work that is being done.

I know with the OTR matter, for example, what was there, it was clear there was a lack of supervision and oversight. There was a lack of systems or methods in place to detect fraud. If you look at the WilmerHale report, one thing that jumps out at you, it talked about bogus or phony documentation being used to substantiate refunds. Well, if you had appropriate supervision and oversight, then someone should have caught that along the way.

I just do not want to wait until after a matter or a problem has been discovered. I try to do preventive things, and that is where

the MIR from October 2007—we did a compilation of reports of audits that had been done between, I think, 2004 to 2007. We cited specific areas: Lack of mechanisms in place to detect fraud, lack of sufficient oversight, lack of appropriate policies and procedures. And we cited agencies of which the CFO's office, OCTO, and the Contract Procurement Office were also cited. Those are things to try to help. A MIR is an instrument by which we try to put agency directors and heads on notice that these are problem areas that may have city-wide ramifications.

And so I guess that is how, I mean, what you need to do at the end of the day is you have to make sure people are held accountable. But it does not necessarily just mean disciplining them, it is making sure that they do what they are supposed to do. I, for one, believe that most of the city employees in the District of Columbia are good, honest, hard-working individuals, and I think it is incumbent upon those of us in oversight and supervisory capacities to ensure by monitoring—and I mean getting down sometimes in the weeds or laboring in the vineyards sometimes, as I like to say—to make sure that work is done because at the end of the day that is what is going to determine whether or not there is improper or proper activity taking place.

Senator AKAKA. Dr. Gandhi, I would like to hear your views on that recommendation and on that question, and then ask you whether you plan to implement those.

Mr. GANDHI. I think very specifically as to procurement, which has been a perennial problem in the District, what we have done from our corner of the city is to make sure that no amount will be paid until we are assured of a proper contract, of a proper invoice, a legitimate authority, procurement authority that would have approved the contract as well as the invoice, and assurance that the goods and services have been received.

No amount will be paid or has been paid that does not satisfy this requirement of the procurement and the requirement that the goods have been received and payments properly authorized. And that has been also true of the recent OCTO scandal in the Technology Office. All that we have done was proper.

The other thing that we should note here is that an employee, our own employee, basically alerted authorities about this. To facilitate this, we also have a toll-free hotline managed by an outside vendor. So if any of our employees were to find out that something is going on here, they do not have to tell us. They can just call the hotline, which is managed, as I said, by an outside vendor.

So we have taken all possible steps that could prevent fraud happening again in the city.

Senator AKAKA. Dr. Gandhi, I am pleased that you are setting up a 24-hour hotline.

Mr. GANDHI. Yes, sir.

Senator AKAKA. Operated by a third-party, as you said, to allow employees to report fraud and mismanagement without fear of retribution. What other protections are in place to ensure that whistleblowers feel comfortable coming forward to report fraud and financial mismanagement in the District?

Mr. GANDHI. Well, we have the whistleblower protection law, which is rather a strict law, and goes beyond the Federal law in

protecting any of our employees who would alert the management either through internal channels or through the fraud hotline. But more than anything else is the climate that we would create of not being afraid to speak up, not to be fearful to tell the authorities or colleagues if something untoward is happening. It is extremely important that we create that level of climate and collegiality within the Administration.

Senator AKAKA. Mr. Willoughby.

Mr. WILLOUGHBY. I would also like to point out that the Inspector General's office also has a hotline. We also have a website on which people can file complaints. And they can also walk in and file complaints anonymously.

I can also say that in my office we have increased our outreach efforts. We now have what we call corruption seminars where we go out to the various agencies and speak—and I personally participate in that—and where we encourage people to report matters to our office. And we also impress upon them or try to impress upon them their obligation. Under the personnel regulations for the District of Columbia, employees are obligated to report matters to the Inspector General's office. And so we try to inform people and let them know that they need to report matters, and if they have a question, what I tell the employees is that if it is a question—even if it is just something that they are thinking or they think there may be a problem, they should contact the Office of the Inspector General, and they should never feel reluctant to do so.

And so we have expanded our outreach efforts to try to encourage individuals and, also, I think probably the most important thing in my mind is to try to impress upon people the importance of what they are doing, because what they are doing affects individuals' lives.

Senator AKAKA. Well, let me ask both of you my final question. What response result have you had on the hotline?

Mr. WILLOUGHBY. We always have thousands of calls. Now, with the OTR matter, we did not get—well, my office was involved with the OCTO matter and with the OTR matter from a law enforcement standpoint. But we regularly get numerous—hundreds, thousands of calls that come in, and we do report that information to the Congress on an annual basis.

Senator AKAKA. Dr. Gandhi.

Mr. GANDHI. The same. We have been receiving numbers of calls on the hotline, tips. Indeed, one of the tax scandals that had appeared was discovered through tips, and that we are able to resolve those issues.

I think the issue of training is very important, this kind of climate does not just happen. You have to train. Any new employee who joins our office has to go through an orientation training where we tell them these are the things you do, these are the things you do not do, do not even think about. That is very important for us.

Senator AKAKA. Thank you. Senator Voinovich.

Senator VOINOVICH. The procurement people, are they under your jurisdiction?

Mr. GANDHI. No, sir.

Senator VOINOVICH. Again, it is the city, so you can comment on procurement. One of the things that is coming up everywhere is we have a major procurement problem everywhere in the Federal Government, and you have it in the local government. Is it because of the fact that procurement people are not out there? Or is there a special kind of education that they should be getting? And have you ever talked to anybody about maybe working with the University of the District of Columbia or some other place to talk about the kinds of people that you need to work in procurement?

Mr. GANDHI. In general, it has been very difficult to hire people for the District. To get people with specialized training, such as procurement, such as technology, such as finance, is additionally difficult.

Our problem here is that we are competing against the Federal Government; we are competing against the accounting firms and the consulting firms. And there is no way we can provide the kind of attractive salary packages—

Senator VOINOVICH. How do you compare with the Federal Government?

Mr. GANDHI. Not well. Our fringe benefits—how shall I put it—compare very poorly.

Senator VOINOVICH. Well, can you submit that for the record. I would like to have that information about it.<sup>1</sup>

Mr. GANDHI. We will do that.

Senator VOINOVICH. Because if you cannot compete for the people, how do you expect to bring them on board?

Mr. GANDHI. Absolutely.

Senator VOINOVICH. Or, for that matter, keep them. Because I suspect if you get somebody that is good, somebody offers them a job in the Federal Government or someplace else.

Mr. GANDHI. To cite an example, sir, I am a Federal annuitant and I enjoy, because of my service at GAO, health benefits coming from the Federal Government. Had it not been the case, I would have been very reluctant to join the District Government.

Now, I must say that, despite all this, the city is the place to be if you want challenging work, if you want to change a life. That is the place to be.

Senator VOINOVICH. Well, it is a combination of both things. I always tell people if you are working in city government, part of your compensation has to be that you are making a difference in people's lives that is important.

Mr. GANDHI. Exactly right.

Senator VOINOVICH. But I think also they have to feed their families and take care of all the other things that need to be taken care of.

Do you have pay for performance in the city government, or is it just the regular salary?

Mr. GANDHI. Well, we do have bonuses. Of course, these are not the American International Group (AIG) bonuses, but we provide some bonuses as an attraction.

Senator VOINOVICH. So you do performance evaluation in your shop of people that work for you?

<sup>1</sup>The information submitted for the record appears in the Appendix on page 65.



Mr. GANDHI. Yes, sir. Everyone has to go through the performance evaluation, yes, sir.

Senator VOINOVICH. Alright. Is that the same case in other departments in city government?

Mr. GANDHI. Right, absolutely.

Senator VOINOVICH. They really do performance evaluations?

Mr. GANDHI. Yes, sir.

Senator VOINOVICH. Is it pay for performance based on the—

Mr. GANDHI. Well, promotions and the pay raises would depend upon how you have performed.

Senator VOINOVICH. OK. What is the biggest revenue raiser? Your revenues are down, but if you look at the sources of revenue for the city, give me the top two.

Mr. GANDHI. Absolutely right. Income tax is about 33 percent; real property taxes, another 33 percent; sales taxes—

Senator VOINOVICH. Income tax, one-third.

Mr. GANDHI. One-third. Real property, another third. Sales tax, 15 percent; gross receipts, around 5 percent; and then the rest of them, around 14 percent.

Senator VOINOVICH. So that the hit you are taking in terms of your revenues would be probably the sales tax? Where do you see the shrinkage most?

Mr. GANDHI. Most of the shrinkage here is in our commercial real property taxes. That has been an engine for us.

Senator VOINOVICH. So that point is the brunt, most of the—about 50 percent of the real estate taxes come from commercial, or is it more than that?

Mr. GANDHI. Yes, more than that. The reason for that is that the District real property has been among the hottest real property markets in the country, if not in the world. We are second only to Manhattan in terms of real property, commercial real property.

Also, the residential real property is doing comparatively well when you compare it with other regions. However, lately, because of the freeze in the financial markets, nothing moves. So the deals are not being made in the District. So-called deed and recordation transfer taxes, we used to get about \$400 million a year. Now we cut that in half.

Senator VOINOVICH. In what, the transfer taxes?

Mr. GANDHI. Transfer taxes, deed and recordation and transfer taxes, we cut that in half, primarily because the financial markets are frozen, no deals are being made. The city cannot get that level of taxes on deed transfers and recordations.

Senator VOINOVICH. Have you seen an acceleration of people filing claims to have their property values reduced?

Mr. GANDHI. Absolutely right. We have an explosion of so-called appeals, particularly from the commercial real property holders, and we have provided huge sums of discounts in those areas because we know that we are going to lose money there. And that is why the \$1 billion that we have reduced in our total taxes, the bulk of that comes from the real property and income taxes.

Senator VOINOVICH. All right. And, of course, you cannot tax Federal buildings or universities or hospitals.

Mr. GANDHI. Since you raised the issue, sir, I want to point out that we used to have offices on Judiciary Square, on the 11th floor.

I looked outside my office, and I saw museums, monuments, galleries—nothing I could tax. That is a fundamental problem.

Senator VOINOVICH. You can tax the income from the people that are building them, but you cannot tax the buildings.

Mr. GANDHI. But even there, we have a problem, what we have is that most of the people, professional people, I should say, working in those firms, consulting firms, the law firms, they live in the suburbs.

Senator VOINOVICH. They what?

Mr. GANDHI. Live in Maryland and Virginia. Of every \$100 that are earned in the city, we get to tax only \$34; \$66 are taxed in Maryland and Virginia. It is like going to a restaurant, and you would say of all the people who are eating here, only one-third will pay, two-thirds will not pay, and everyone will complain about bad food and bad service. It is as simple as that. We are the only place in the world where income is not taxed at the source.

I recall coming to you, sir, with Tony Williams, and we talked about this at that time. And you said, "Well, how do you pay your bills?" Well, I must say that is difficult. But with a great credit to the mayor and the council, the elected leadership, and the help that we get from Congress, we are able to show performance here which is the envy of many cities.

Senator VOINOVICH. Thank you very much.

Senator AKAKA. Dr. Gandhi, because I consider Senator Voinovich as a champion of human capital, I want to ask this question of you. I understand the OCFO is struggling with recruiting and retention. In the wake of the Office of Tax Revenue scandal, investment in human capital and incorporating accountability and oversight into your human capital planning are particularly important.

What do you see as the OCFO's greatest human capital challenges? And have you developed a strategic human capital plan to address them?

Mr. GANDHI. I think that is the heart of the matter, sir, to find the right kind of people, people with skills that we need, people with training that we need, people with experience that we need. Those are not available to us as freely as elsewhere, particularly in the areas of tax, economics, financial analysis, and technology. We have a hard time finding the right mix of people.

I am very proud of the staff that we do have. They do wonderful work. But, still, I can do more if I had more people of that requisite skills and expertise.

Senator AKAKA. Thank you

Mr. Willoughby, I applaud the cooperative partnerships that seems to exist between the D.C. Inspector General, the OCFO, and D.C. Council in the wake of the Tax and Revenue scandal. Aside from increased interagency communications, what benefits do you see these partnerships yielding? And how do you believe they will contribute to improvements in the management of District funds?

Mr. WILLOUGHBY. I believe that the partnerships will contribute or are worthwhile because of the fact, as I said, we are striving for the same thing—an effective and efficient government. I believe that by having open channels of communication, agency heads and agency staff will be more willing, I guess, to share information with us that would be helpful to us in the performance of our duties,

that they realized the role of this office and, I guess, not only their obligation to cooperate with the office, but the importance of them doing so.

When you asked the question, Mr. Chairman, it came to mind that one of the risk areas we have is the school system, DCPS, as you referred to earlier. We have an on-site presence at DCPS, and one of the reasons we have that is to encourage the communication and encourage our understanding of operations there. And it cuts down on, I guess, delays that we may encounter and gives us a better appreciation of operations and, consequently, makes our reports more meaningful.

So, in essence, I guess, I believe that many problems stem from—and this is just life—many problems stem from a lack of communication, and I think it is very important, if you are going to solve a problem, that you have open channels of communication.

Now, as I like to tell agency directors, the nature of the work of the IG is such that sometimes I can tell them things and sometimes I cannot. Sometimes I wish I could do more to help them, but because of the nature of the operation of the IG's office, the whole concept, I cannot. But I try to be as forthright and as honest because I think in the long run that is beneficial, because then we can work together to solve a problem, whereas it is not a situation of us against them. So I think the communication is extremely important and beneficial for that purpose.

Senator AKAKA. Thank you. I have one last question for Dr. Gandhi and one for you, Mr. Willoughby.

Dr. Gandhi, given the financial management challenges of the past and anticipated challenges for the future, what are your top three priorities for District finances as we move forward?

Mr. GANDHI. The most important priority I have is to make sure that we balance the budget going forward and the commitment that we have made to the Congress and to the citizens that we will remain balanced, not only in the current year but on a 5-year plan.

The second important consideration I have is that the AAA ratings that we have received lately from Wall Street, the credibility that we enjoy on Wall Street, financial viability, we want to make sure that we do not deviate from that.

And the third priority I have is to make sure that we protect the taxpayer dollars. We are the guardian of the District's taxpayer dollars, that we never want to deviate from that mission, from that stewardship, that we keep enjoying the confidence of the taxpayers who trust their hard-earned tax dollars to us.

So those are the three important priorities I keep in my mind as I wake up in the morning.

Senator AKAKA. Thank you very much for that, Dr. Gandhi.

Now, Mr. Willoughby, now that you have heard this, how do you plan to aid the OCFO in achieving these priorities?

Mr. WILLOUGHBY. Well, I guess briefly, to continue to do what we have been doing. One of the things, when you asked the question, Mr. Chairman, about finances, in determining areas to look into, we have a number of themes that we rely on. First and foremost is what we call revenue enhancement, and basically what that says is that we want to make sure that the city, that the District of Columbia takes advantage of all the revenue sources that similar en-

tities have, and then next to make sure that money is spent efficiently and effectively.

I like to say that money is very important because you cannot do anything without money. So I want to make sure that the city receives all the money it is supposed to receive, and then with that money it delivers the basic services and the services that it is intended to. And so that is why Medicaid is very important to us, because I believe the city is not taking full advantage of that.

I believe that if we do those things, if we keep in the forefront making sure that the city receives the monies that it is supposed to be receiving and that the money is spent effectively, we will be going a long way toward achieving our eventual goal of having an effective and efficient government. And the way I can expect to help Dr. Gandhi and other agency heads is to continue what we have been doing, being accessible, working with them as much as we can within the confines of what an IG has the responsibility of doing, and just doing what we have been doing, I guess. That is my answer.

Senator AKAKA. Thank you very much, Mr. Willoughby.

Mr. WILLOUGHBY. Thank you.

Senator AKAKA. I want to thank both of you for testifying today. Your responses have been great. Based on your testimony, we have learned a great deal about problems with the District's financial management as well as the progress that has been made.

I believe government functions best when all of its members work together, and I am pleased to see the D.C. Inspector General taking such an active role in advising and working with OCFO. I know that you are working together to exercise good financial management and to safeguard District taxpayer dollars.

I hope you will redouble your efforts to make sure that good internal controls are in place throughout the District Government and to address chronic problems in the Medicaid program. It is my hope that recommendations from this hearing and continued input from the D.C. Inspector General and GAO as well will help D.C. stay on a path to financial recovery.

This hearing record will remain open for one week during which time Members of the Subcommittee may submit additional written questions.

So thank you very much, again, for your presence here, your testimony, and your responses.

Mr. GANDHI. Thank you, Mr. Chairman. Thank you for your leadership.

Mr. WILLOUGHBY. Thank you very much.

Senator AKAKA. Thank you. This hearing is adjourned.

[Whereupon, at 11:31 a.m., the Subcommittee was adjourned.]

# A P P E N D I X

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## HEARING

On

### A REVIEW OF THE OFFICE OF THE CHIEF FINANCIAL OFFICER

Before the

**Subcommittee on Oversight of Government Management, the Federal  
Workforce and the District of Columbia  
Committee on Homeland Security and Governmental Affairs  
U.S. Senate**

**The Honorable Daniel K. Akaka, Chairman**

**March 31, 2009, 10:00 a.m.  
Room 342, Dirksen Senate Office Building**



**Testimony of  
Natwar M. Gandhi  
Chief Financial Officer  
Government of the District of Columbia**

Good morning, Chairman Akaka, Senator Voinovich and members of the subcommittee. I am Natwar M. Gandhi, Chief Financial Officer for the District of Columbia. I am here to offer remarks about the progress the OCFO has made in financial management; how we respond to outside entities' recommendations; financial management challenges in the years ahead; and interagency cooperation with the Mayor's office and the Office of the Inspector General (OIG) to achieve efficiency and improve accountability.

**Progress and Stability in Financial Management**

Mr. Chairman, since Congress created the independent CFO to work with the Mayor and the Council in 1995, the District has completed 12 consecutive balanced budgets, turned a cumulative \$550 million deficit into an impressive \$1.2 billion fund balance, and received a string of clean audit opinions from external auditors, and transformed a municipality with junk bond ratings into a financially credible jurisdiction with strong ratings.

Attachment 1 to my testimony is a chart showing a history of the annual budgetary surpluses and total General Fund balance since 1992. It tells the story of the District's successful return to fiscal solvency during the Control Board period, and later to a sound financial position evidenced by a General Fund balance of more than a billion dollars.

This turnaround did not happen accidentally, but rather it is a case study in a commitment to improve financial management and practices. Our General Obligation (GO) bond ratings have increased steadily, at what the rating agencies tell us was nearly unprecedented speed. They now stand at the A+ and A1 levels from all three rating agencies. These ratings are a clear indication to investors in

our bonds that the District of Columbia has indeed returned to a position of fiscal strength.

In addition, as you know, we were recently assigned ratings of AAA from Standard & Poor's and AA from Moody's Investors Service and Fitch Ratings on our inaugural issuance of Income Tax Secured Revenue Bonds. Had we not been carrying the strong A+/A1 GO ratings, it is questionable as to whether we would have been able to achieve the gilt-edged AAA rating from S&P, and the AA ratings from the other two agencies. These ratings enabled these bonds to be sold at such favorable interest rates that we expect the use of these bonds instead of GO bonds will lower the cost of borrowing by \$28 million over four years.

A significant area of financial improvement has been in the management of the debt burden. The Home Rule Act controls our GO borrowing by limiting GO debt service to 17 percent of revenues. However, bond rating agencies judge a municipality's creditworthiness by the amount of all its tax-supported debt, not just GO debt. Because bond rating agencies consider a tax-supported debt ratio in the 10-12 percent range to be high, in June 2007, I recommended to the Mayor and the Council that a hard cap of 12 percent be put into law. District law now contains this 12 percent cap, and the borrowing program in the Mayor's proposed FY 2010 budget and financial plan would stay within the new cap. Attachment 2 shows the District's debt burden since 1992.

#### **Response to Tax Fraud**

On the morning of November 7, 2007 federal agents arrested two employees of the Office of Tax and Revenue (OTR); each was charged with ten felony counts of conspiracy and fraud. The employees worked in the division responsible for

issuing property tax refunds, an area that had not yet been upgraded to an automated system. The scheme involved persons both internal and external to OTR. These individuals were alleged to have conspired to defraud the District government through creating fraudulent real property tax adjustment refunds and directing them to “dummy” corporations. Inconsistent with best practices, these refunds were approved only by the manager of the tax office unit where they were initiated, regardless of the size of the check. This practice dated to the late 1980s and was in direct violation of directives.

This criminal enterprise was able to thrive over 20 years because of a failure of management oversight and internal controls at OTR. Not only were the correct processes not followed, but managers and others were not alert to behavior that might have provided signs of wrongdoing – such as overt displays of wealth and extravagant gift-giving. Internal controls rest on three legs – people, processes, and systems. We had to focus immediately on all three legs to ensure that no further fraud could be perpetrated.

Immediately following the discovery of the fraud:

- We strengthened both the automated and manual controls over the refund process at all levels.
- We removed the previous tax office management under whose supervision the fraud occurred.
- We removed employees who benefited from the fraud and failed to report suspicious activities.
- We established an independent audit committee comprised of distinguished professionals to provide financial advice and review the financial management and internal controls of the OCFO.



- We hired Stephen Cordi, a distinguished tax administrator, as Deputy Chief Financial Officer for the OTR, as well as other experienced and capable managers to oversee OTR's Real Property Tax and Revenue Accounting Administrations. Steve Cordi has been with us for over a year now, and has made significant progress in instituting change in OTR.

The District's independent auditors, BDO Seidman, LLP delayed the release of the Comprehensive Annual Financial Report (CAFR) for Fiscal Year 2007 in order to allow additional time to review internal controls and determine the areas of weakness that allowed the tax fraud to occur. In the audit released March 31, 2008, the auditors gave us a "clean" audit opinion, but they found the manual refund process in OTR to be a material weakness. These findings were helpful in guiding our actions over the past year to improve internal controls. In the just-released CAFR for FY 2008, BDO Seidman reduced the severity of the finding on OTR from "material weakness" to "significant deficiency," and again gave us a "clean" audit opinion. Further, we continue to improve that record in FY 2009.

Other outside parties also reviewed the processes at the tax office. The Council of the District of Columbia authorized the WilmerHale law firm to conduct a special investigation of the real property tax fraud. WilmerHale, with the assistance of PricewaterhouseCoopers, conducted a year-long investigation into this matter. Both organizations donated their services on a pro bono basis to the District. The results of this inquiry are contained in a Report of Investigation that was released on December 15, 2008, and we are working diligently to fully implement its recommendations. In collaboration with our independent audit committee, we have engaged the services of Deloitte Financial Advisory Services to assist us in completing this work.

In sum, notwithstanding the difficulties we faced in the wake of the tax fraud, we emerged from this episode as a stronger and more resilient organization. We are maintaining our vigilant efforts to improve our internal controls and financial management review processes. One important measure of the strength of the District's financial operations is the esteem with which we are held on Wall Street – not only did we not suffer a downgrade of our bond issues, but Standard & Poor's gave our recent income tax revenue bond issue a AAA rating, the highest in the District's history. Finally, I strongly believe that our success in crisis management, reflected in the significant improvements we have made to our internal controls and financial management, is as important as the crisis itself.

**OCFO Relations with Auditors and OCFO Efforts with Mayor's Office and  
OIG to Achieve Efficiency and Improve Accountability**

As demonstrated by our response to the tax fraud, we welcome the review by outside entities of our policies and practices, and we take their recommendations seriously.

*Government Accountability Office (GAO)*

Only two weeks ago, my staff and I met with representatives of the GAO regarding how we will track and report the District's participation in the federal Stimulus Plan. The District has been chosen by GAO along with 16 states they will track as to how the stimulus funds are being used. We will work closely with them to ensure that they are receiving complete and accurate reporting on the way funds are spent. In order to facilitate the accountability for and transparency in financial reporting of the stimulus funds, we have established special stimulus budget and accounting codes to track the use of these funds.

*External auditors*

Each year the OIG contracts with an external auditor to audit the District's financial statements and internal controls. The annual Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters, commonly known as the "Yellow Book," contains detailed analyses of areas of financial management that need improvement, both within the OCFO and in various agencies of the District government such as the Medicaid program. Attachment 3 shows the history of the findings in these Yellow Book reports.

The FY 2006 report highlighted the DCPS as a material weakness. In response, we worked with the school administration to take remedial action. We assembled a multi-agency task force to focus on deficiencies found in human resources, procurement, and Medicaid cost reporting within DCPS. DCPS remained a material weakness in FY 2007 because of additional findings, but the severity was reduced to significant deficiency in the FY 2008 report.

In FY 2007 the number of material weaknesses and significant deficiencies increased to three material weaknesses and six significant deficiencies, as a result of the additional review of the tax fraud as well as more stringent auditing standards that were being instituted nationwide. In the just-released CAFR for FY 2008, the number of findings was reduced to two material weaknesses and four significant deficiencies. An audit today would find one of the material weaknesses (Treasury functions) eliminated.

We are committed to reducing the number of findings in the FY 2008 Yellow Book by correcting our practices in those areas. Some areas identified in the FY

2008 report are currently being fixed, while other problem areas may take additional time to address completely. We will continue to work with the City Administrator's office and agency directors, the OIG, and our independent auditors to identify reasonable approaches to each problem, and see that they are implemented effectively.

*The Office of the Inspector General (OIG)*

We work closely with the Inspector General. The contract for the annual audit of the CAFR is managed by IG, so we work closely with his office on that process all year long. The various IG audits and reports have findings and recommendations that pertain to the executive or our office or both. We take each finding and recommendation that pertains to our office very seriously, respond fully, and if we concur with the recommendation we implement corrective action.

**OCFO Internal Reviews and Permanent Improvements in Controls**

We value the perspectives of external entities, but we have never waited for their reviews to make improvements. When I joined the District government in 1997 I established an internal audit function at the tax office. That function was expanded to cover all of the OCFO when I became CFO in 2000. Over the years we have instituted improvements such as:

- Background checks of all new employees,
- Integrity probes of the various OCFO operating areas,
- A comprehensive written code of conduct, and
- The elimination of "dummy accounts" in the integrated tax system.

These improvements have all served the District well, and I am proud of them. But the uncovering of the tax fraud in 2007, as painful as it was, led us to make deeper

improvements. In December 2007, I established the OCFO Audit Committee to Review Financial Management and Internal Controls to advise us on how to strengthen our organization's internal controls and financial management, especially in light of the fraud. The Committee is composed of leading figures in accounting, public finance and the law. The Committee, which met regularly throughout FY 2008, is chaired by Sheldon Cohen, former Commissioner of the U.S. Internal Revenue Service.

During 2008, the internal controls of two areas of the OCFO – the tax office and the treasurer's office – were reviewed by outside firms that generously provided their services on a pro bono basis. Kroll Associates reviewed the tax office, and Deloitte Financial Advisory Services and Ernst & Young facilitated a fraud risk assessment of specific business processes within the Office of Finance and Treasury. The assessments in both these areas were important proactive steps in enhancing and promoting a culture of fraud prevention, detection, and deterrence and should serve as a model for use throughout the District.

As mentioned earlier, in 2008, we engaged the services of Deloitte Financial Advisory Services to assist us in completing this work. So far we have:

- Conducted OCFO-wide risk assessments, and based on those findings are drilling down to address potential exposures within the OCFO divisions, including the tax office, the treasurer's office, and the comptroller's office.
- Made significant progress in the development, implementation, and documentation of an internal controls system that is consistent with OMB Circular 123/Sarbanes Oxley.
- Established the position of Chief Risk Officer within the OCFO and are actively recruiting to fill it. See our organization chart in Attachment 4,

including this position, which reports directly to me and is responsible for identifying, reporting and mitigating risks throughout the OCFO agency.

- Enhanced the existing integrated tax system (ITS) to strengthen internal controls by limiting user profiles and appropriately segregating duties, and
- Assigned four of our internal auditors to conduct audits on-site in the tax office.

In addition:

- We are gathering the requirements for the procurement of both a new ITS and Real Property Tax System that will automate manual processes, provide greater security, and further guard against fraud, and
- We are changing the work environment throughout the agency through:
  - Promoting a culture that has “zero tolerance” for fraud and misconduct,
  - Enhancing integrity/accountability training,
  - Instituting periodic background investigations for all employees,
  - Establishing a 24-hour hotline operated by an independent third party so that employees may report fraud and mismanagement without fear of retribution,
  - Conducting periodic surprise cash-counts at our various locations where our cashiers conduct transactions, and
  - Increasing communication and coordination between administrations.

While we have made significant progress in these areas, much work remains. The OCFO has committed its full attention and available resources to successfully completing this most important project.

**Financial Management Challenges in the Years Ahead**

You have also asked that we address the District's projected revenue shortfalls, and the steps the OCFO plans to take to address those challenges. Like most other states, the District of Columbia has felt the effects of the current recession in the form of falling revenues. Certainly the biggest challenge facing the District today is the drop in projected revenues. Attachment 5 shows the dramatic reduction in the revenue estimates since last June.

As you know, the primary tool that the OCFO has to ensure balanced fiscal operations is to provide conservative revenue estimates. Over the years, this has proved to be key to protecting the District's hard-earned financial recovery. I will continue to exercise sound, well researched and conservative revenue estimating policies in order to retain our solid financial standing throughout this very challenging economic period.

The economic outlook for the District of Columbia has changed dramatically from that of a year ago when the previous budget was submitted to the Council. The current forecasts assume that economic conditions will continue to deteriorate as employment and wages edge downward, commercial property vacancies rise, real property transfers slow further, and construction projects are delayed. Even with this grim outlook, we are in relatively better fiscal shape than other states and cities that are projecting deficits into the billions.

On the negative side, a significant portion of our population is not well educated or trained to fill jobs in the growing employment areas and the services they will need and that we must provide will continue to tax our resources at increasing levels. On the plus side, we are fortunate to be a center for three growth areas –

government, education and health. And, even though our revenues are shrinking, the diversity of our tax base will help us to pull through these times in better shape than many other states and localities.

The Mayor has taken the opportunity of the current economic crisis to re-think how the government does business. In previous years, the District looked for ways to spend rising revenues creatively and effectively. This year the job is to provide the services our people need at the levels of quality they have come to expect. Mayor Fenty and City Administrator Tangherlini should be commended for their work to produce a balanced, workable budget and financial plan that bends the curve.

In addition, we have maintained a “rainy day fund” – the emergency and contingency cash reserves -- of at least \$360 million throughout the four year plan. And in our capital budget, we have been prudent in our borrowing by observing our debt cap limits.

Looking ahead, we must continue the sound fiscal policies that have produced balanced budgets that provide quality services to all of our people. I am often accused of being overly pessimistic, but at this time I believe that the record we have established gives us the right to be optimistic that we will come through this period with a record of responsibility and service that will be a point of pride for all of us.

### **Conclusion**

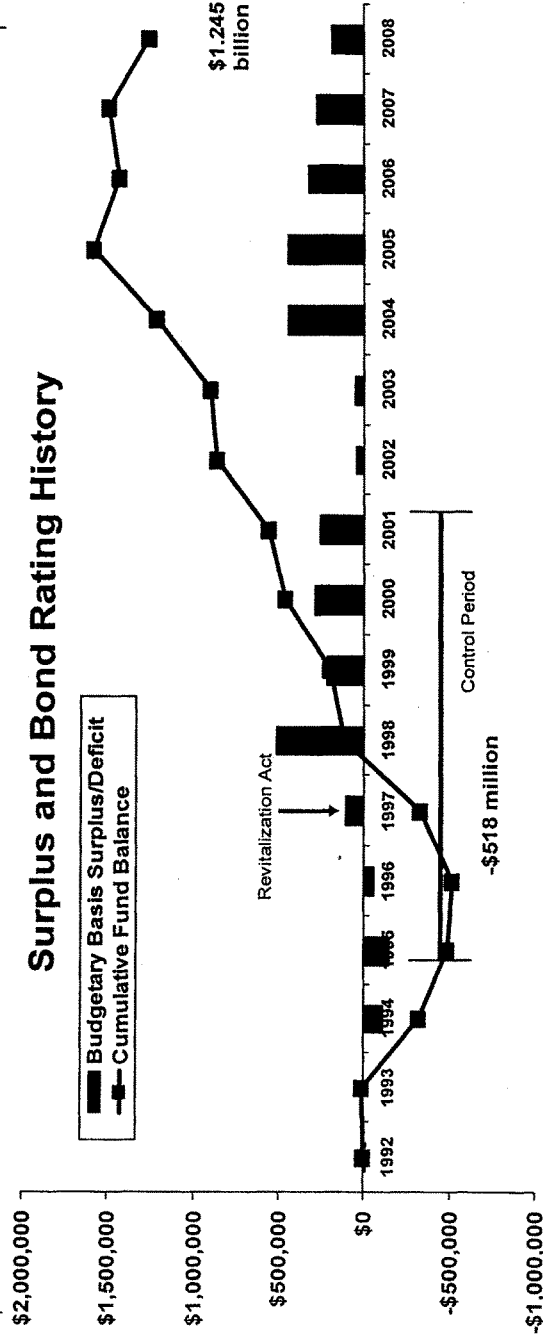
In summary, the District has accomplished much – some might even say miracles - - in the last decade, its fiscal condition is sound, and the elected leadership possesses a steadfast commitment to fiscal responsibility that has become widely



recognized. I assure you that the District will continue to balance its budgets and that the OCFO will strive to follow 'best practices' in all areas of financial management and practice. We will continue to seek ways to do the business of government better, smarter and more efficiently than any jurisdiction in the country. It is what all citizens should expect of their governments, and certainly what we expect of our Nation's Capital.

This concludes my remarks and I will be happy to answer any questions you may have.

### District of Columbia Surplus and Bond Rating History



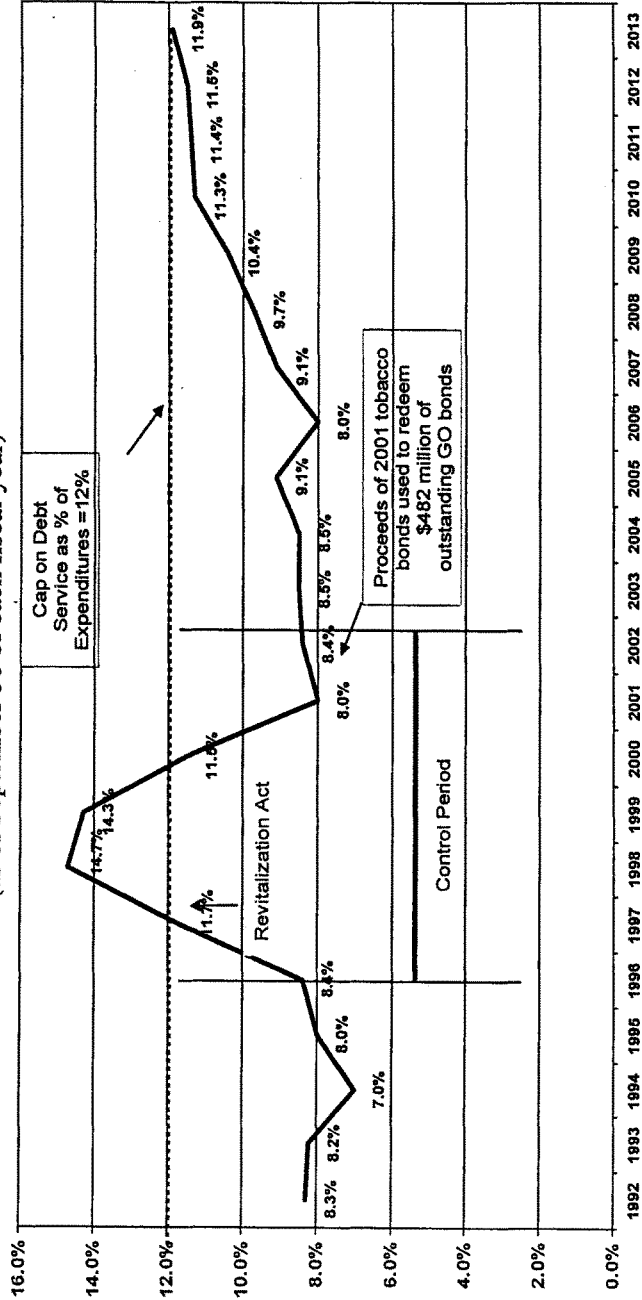
#### General Obligation Bond Ratings

S&P:	Moody's:	Fitch:
A-	A-	A-
Baa	Baa	Baa
A-	BBB+	A-
Ba2	Ba	Ba
Ba1	Ba	Ba
Ba2	Ba1	Ba1
Ba3	Ba3	Ba3
Ba1	Ba3	Ba3
BB+	BB+	BB+
BB	BB	BB
B	BBB-	B
BBB-	BBB-	BBB-
BBB+	BBB+	BBB+
BBB	BBB	BBB
BBB+	BBB+	BBB+
A-	A-	A-
A2	A2	A2
A2	A2	A2
A+	A+	A+
A+	A+	A+
A+	A+	A+
A+	A+	A+

2009 Income Tax Secured Revenue Bonds: S&P: AAA Moody's: Aa Fitch: AA

# Debt Burden

Debt Service as % of Expenditures  
(as of September 30 of each fiscal year)



YELLOW BOOK FINDINGS FY 2001 - FY 2008		
	Material Weaknesses	Reportable Conditions/Significant Deficiencies*
FY 2001	DCPS Accounting & Fin Reporting UDC Accounting & Fin Reporting Medicaid Provider Accounting	Cash/Bank Reconciliation Human Resource/Payroll Process Mgmt Accounting of Non-Routine Transactions Monitoring of Exp Against Open Procurements Disability Comp Claims Mgmt Reporting of Budgetary Revisions
FY 2002	Health Care Safety Net Contract Mgmt Medicaid Provider Accounting	Human Resource/Payroll Process Mgmt Monitoring of Exp Against Open Procurements Disability Comp Claims Mgmt
FY 2003	Health Care Safety Net Contract Mgmt Medicaid Provider Accounting	Human Resource/Payroll Process Mgmt Unemployment Comp Claimant File Mgmt
FY 2004	NONE	Unemployment Comp Claimant File Mgmt Management of Disability Comp Program
FY 2005	NONE	Management of Disability Comp Program Management of Unemployment Comp Trust Fund
FY 2006	District of Columbia Public Schools	Management of the Medicaid Program
FY 2007	Office of Tax and Revenue - Refund Process Management of the Medicaid Program District of Columbia Public Schools	Investment Reconciliations and Activities NCRC and the AWC Management of Grants Compensation Management of Disability Compensation Program Management of Unemployment Comp. Program
FY 2008	Treasury Functions Management of the Medicaid Program	Compensation Office of Tax and Revenue District of Columbia Public Schools Management of the Postretirement Health and Life Insurance Trust

\* "Significant Deficiency" used starting FY 2007

**Reportable Condition/Significant Deficiency**

FY 2006

FY 2008

FY 2001, FY 2002, FY 2003, FY 2007, FY 2008

Compensation

Medicaid

DCPS

District of Columbia Public Schools

Office of Tax and Revenue

Unemployment Comp Trust Fund

Management of the Medicaid Program

Investment Reconciliations and Activities

NCRC and the AWC

Management of Grants

Compensation

Management of Disability Compensation Program

Management of Unemployment Comp. Program

Human Resource/Payroll Process Mgmt

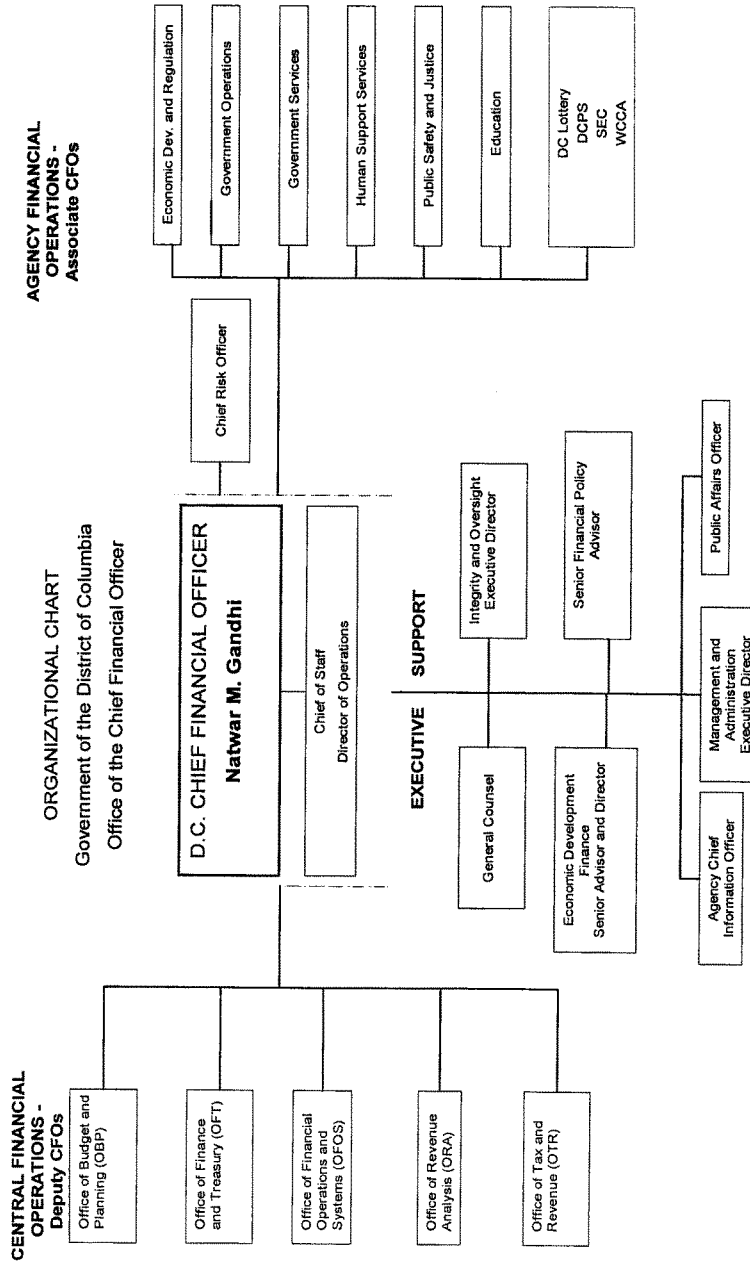
Monitoring of Exp Against Open Procurements

Disability Comp Claims Mgmt

Reporting of Budgetary Revisions

Accounting of Non-Routine Transactions

Cash/Bank Reconciliation



## Revenue Estimates for FY 2009 – 2013

Revenue Estimates: Original and Revised

Local Source, General Fund Revenue Estimate (\$ millions)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
1 Revenue estimate included in June budget (Original)	5,562.9	5,831.7	6,099.2	6,402.5	
2 Change in the estimate (September 2008)	(130.7)	(151.9)	(148.5)	(162.3)	
3 Revenue estimate of September 2008	5,432.2	5,679.7	5,950.7	6,240.2	
4 Change in the estimate December 2008)	(127.1)	(303.8)	(330.4)	(327.5)	
5 Revenue estimate of December 2008	5,305.1	5,375.9	5,620.3	5,912.7	6,216.9
6 Change in the estimate (February 2009)	(135.7)	(346.3)	(488.3)	(613.8)	(676.9)
7 Revenue estimate of February 2009	5,169.4	5,029.5	5,132.0	5,298.8	5,540.0
8 Dollar Change in General Fund revenues compared to prior year		-139.9	102.4	166.9	241.2
9 Percent Change in General Fund revenue compared to prior year		-2.7%	2.0%	3.3%	4.6%
10 Change in the estimate since June budget	(393.5)	(802.1)	(967.3)	(1,103.7)	n/a
11 Loss sustained compared to June budget	-7.1%	-13.8%	-15.9%	-17.2%	n/a

**TESTIMONY OF CHARLES J. WILLOUGHBY  
INSPECTOR GENERAL, DISTRICT OF COLUMBIA**

**BEFORE**

**THE SENATE SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT  
MANAGEMENT, THE FEDERAL WORKFORCE,  
AND THE DISTRICT OF COLUMBIA**

**MARCH 31, 2009**

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GOOD MORNING CHAIRMAN AKAKA, SENATOR VOINOVICH, AND MEMBERS OF THE SUBCOMMITTEE. I AM CHARLES J. WILLOUGHBY, AND I AM PLEASED TO SPEAK BEFORE YOU THIS MORNING AT YOUR HEARING ENTITLED, "STABILITY THROUGH SCANDAL: A REVIEW OF THE OFFICE OF THE CHIEF FINANCIAL OFFICER" (OCFO).

YOU ASKED ME TO ADDRESS SPECIFICALLY (1) THE INDEPENDENT AUDITOR'S REPORT RELATIVE TO MATERIAL WEAKNESSES IDENTIFIED IN THE COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR), (2) PROGRESS THAT THE CHIEF FINANCIAL OFFICER (CFO) HAS MADE IN RESPONDING TO RECOMMENDATIONS FROM THE OFFICE OF THE INSPECTOR GENERAL (OIG), (3) COOPERATION BETWEEN THE OIG AND OCFO TO ACHIEVE EFFICIENCY AND IMPROVE ACCOUNTABILITY, AND (4) WAYS THAT THE OCFO CAN IMPROVE ITS FINANCIAL MANAGEMENT.

WILLIAM J. DIVELLO, THE D.C. OIG ASSISTANT INSPECTOR GENERAL FOR AUDIT, IS ACCOMPANYING ME TODAY. AFTER MY REMARKS, WE WOULD BE HAPPY TO ADDRESS ANY QUESTIONS YOU MAY HAVE.

BY LAW, THE INSPECTOR GENERAL MUST ENTER INTO A CONTRACT WITH AN INDEPENDENT AUDITING FIRM TO AUDIT THE CITY'S FINANCIAL STATEMENTS. ON JANUARY 30, 2009, THE DISTRICT OF COLUMBIA RECEIVED AN UNQUALIFIED OPINION ON ITS FINANCIAL STATEMENTS FOR FISCAL YEAR (FY) 2008 FROM ITS INDEPENDENT AUDITORS, BDO SEIDMAN, LLP. IT IS NOTEWORTHY TO MENTION THAT THIS IS THE 12<sup>TH</sup> CONSECUTIVE YEAR IN WHICH THE DISTRICT HAS RECEIVED A "CLEAN" OPINION ON ITS FINANCIAL STATEMENTS FROM THE INDEPENDENT AUDITORS. WHILE AN UNQUALIFIED OPINION PROVIDES THAT THE FINANCIAL STATEMENTS WERE PRESENTED FAIRLY IN ALL MATERIAL ASPECTS, THE INDEPENDENT AUDITORS ALSO ISSUED A REPORT ON INTERNAL CONTROL AND COMPLIANCE OVER FINANCIAL REPORTING, COMMONLY REFERRED TO AS THE "YELLOW BOOK" REPORT. THE YELLOW BOOK REPORT NOTED A CONTINUING NEED TO ADDRESS SIGNIFICANT INTERNAL CONTROL DEFICIENCIES AND MATERIAL WEAKNESSES. THE GOOD NEWS FOR FY 2008 WAS THAT THERE WERE FEWER SIGNIFICANT DEFICIENCIES AND MATERIAL WEAKNESSES REPORTED THAN IN THE PRIOR YEAR (3 IN FY 2007 VERSUS 2 IN FY 2008). HOWEVER, THE AUDITOR'S REPORT SHOWS THAT PROBLEMS REMAIN IN SOME AREAS THAT REQUIRE MANAGEMENT'S ATTENTION AND ACTION.



**FISCAL YEAR 2008 MATERIAL WEAKNESSES AND THE CFO'S RESPONSE**

THE FY 2008 YELLOW BOOK REPORT CITED TWO MATERIAL WEAKNESSES: THE FIRST WAS THE OFFICE OF THE CHIEF FINANCIAL OFFICER'S TREASURY FUNCTIONS PERFORMED BY THE DISTRICT'S OFFICE OF FINANCE AND TREASURY; THE SECOND WAS THE MANAGEMENT OF THE MEDICAID PROGRAM, A MULTI-AGENCY PROGRAM PREVIOUSLY MANAGED BY THE DISTRICT'S DEPARTMENT OF HEALTH, AND NOW BY THE DEPARTMENT OF HEALTH CARE FINANCE.

FOR FY 2008, THE TREASURY FUNCTIONS CONTRIBUTING TO THE MATERIAL WEAKNESS INVOLVED THE FAILURE TO RECONCILE CASH AND INVESTMENT ACCOUNT ACTIVITIES. THE INDEPENDENT AUDITORS FOUND THAT THE DISTRICT WAS NOT ACCOUNTING FOR ALL OF ITS CASH AND INVESTMENT ACTIVITY APPROPRIATELY IN THE DISTRICT'S ACCOUNTING SYSTEM OF RECORD (SOAR) ON A TIMELY BASIS. THE AUDITORS ALSO IDENTIFIED NUMEROUS UNIDENTIFIED AND UNRECORDED TRANSACTIONS AND FOUND THAT BANK RECONCILIATIONS OF CASH ACCOUNTS WERE UNTIMELY OR INACCURATE. THE AUDITORS ALSO HAD DIFFICULTY CONFIRMING CERTAIN INVESTMENT BALANCES.

THE OFFICE OF THE CHIEF FINANCIAL OFFICER GENERALLY RESPONDED POSITIVELY TO THESE FINDINGS, PROVIDING DETAILED ACTIONS TO RECONCILE

ALL ACCOUNTS ON A MONTHLY BASIS AND PROVIDING TIMELY INPUT OF SOAR DATA TO ACCOUNTS. GIVEN THE SERIOUSNESS OF THESE MATTERS, THE DISTRICT OF COLUMBIA CITY COUNCIL COMMITTEE ON FINANCE AND REVENUE, CHAIRED BY COUNCILMEMBER JACK EVANS, IS MONITORING THE OCFO'S PROGRESS TO BRING ALL BANK ACCOUNT RECONCILIATIONS UP TO DATE AND TO TAKE ACTION TO ADDRESS ALL CASH AND INVESTMENT ACCOUNT IRREGULARITIES. WE HAVE BEEN INFORMED THAT ALL ACCOUNTS HAVE BEEN RECONCILED THROUGH DECEMBER 31, 2008 (FY 2009) AND THAT EFFORTS WILL CONTINUE TO KEEP CURRENT ALL CASH ACCOUNT RECONCILIATIONS AND CASH AND INVESTMENT ACCOUNT ACTIVITY. THE INDEPENDENT AUDITORS, UNDER THE AUSPICES OF MY OFFICE, WILL ALSO BE PERFORMING A REVIEW OF CASH ACCOUNT RECONCILIATIONS TO ASSURE DISTRICT OFFICIALS THAT THE OCFO IS PROPERLY RECONCILING AND RECORDING ALL CASH AND INVESTMENT ACCOUNT ACTIVITY.

THE SECOND MATERIAL WEAKNESS INVOLVED MANAGEMENT OF THE MEDICAID PROGRAM, WHICH HAS BEEN A LONG-STANDING PROBLEM FOR THE DISTRICT, HAVING BEEN REPORTED AS A REPORTABLE CONDITION IN PRIOR CAFR YEARS AND A MATERIAL WEAKNESS FOR FYS 2007 AND 2008. IN CATEGORIZING THE MEDICAID PROGRAM AS A MATERIAL WEAKNESS, THE INDEPENDENT AUDITORS RELIED HEAVILY ON RECENT OIG MEDICAID AUDITS AT THE DEPARTMENT OF MENTAL HEALTH AND THE MEDICAID ASSISTANCE ADMINISTRATION, AND ON TESTS OF CLAIMS DISALLOWANCES AND ACCOUNTS

RECEIVABLE WRITE-OFFS. THE OIG HAS LONG RECOGNIZED THAT THE DISTRICT'S MEDICAID PROGRAM, APPROXIMATING \$1.5 BILLION IN EXPENDITURES ANNUALLY, HAS HIGH FINANCIAL RISKS. RECOGNITION OF THESE RISKS HAS BEEN JUSTIFIED BY THE FACT THAT THE DISTRICT HAS HAD TO "WRITE-OFF" OR ABSORB HUNDREDS OF MILLIONS OF DOLLARS IN OTHERWISE FEDERALLY FUNDED MEDICAID COSTS OVER THE PAST SEVERAL YEARS. RECOGNIZING THAT MANY OF THE CITY'S MEDICAID PROBLEMS RESIDE IN BILLING AND ACCOUNTABILITY, THE DISTRICT CREATED THE DEPARTMENT OF HEALTH CARE FINANCE WHICH, AMONG ITS NUMEROUS RESPONSIBILITIES, NOW REQUIRES HEALTHCARE PROVIDERS TO THOROUGHLY DOCUMENT MEDICAID DELIVERABLE SERVICES PRIOR TO AUTHORIZING PAYMENT. WE ANTICIPATE THAT WELL SUPPORTED AND DOCUMENTED MEDICAID SERVICES LIKELY WILL SIGNIFICANTLY REDUCE UNSUPPORTED MEDICAID COSTS AND THE RESULTANT MEDICAID COST DISALLOWANCES THAT HAVE CONTRIBUTED TO PAST ACCOUNTS RECEIVABLE WRITE-OFFS. THESE ACTIONS SHOULD HELP MITIGATE SOME OF THE RISKS ASSOCIATED WITH THE DISTRICT'S MEDICAID PROGRAM.

**FISCAL YEAR 2007 MATERIAL WEAKNESSES AND THE CFO'S RESPONSE**

IN THE FY 2007 CAFR YELLOW BOOK REPORT, THE INDEPENDENT AUDITORS CITED CONDITIONS AT THE DISTRICT'S OFFICE OF TAX AND REVENUE (OTR) AS A MATERIAL WEAKNESS THAT CONTRIBUTED TO A \$50 MILLION FRAUD

PERPETRATED BY AN OTR MANAGER WORKING COLLUSIVELY WITH SEVERAL OTHER INDIVIDUALS. IN RESPONSE TO THIS FRAUD, THE INDEPENDENT AUDITORS CONDUCTED A SIGNIFICANT AMOUNT OF TESTING AND FORENSIC AUDITING TO ASSURE THAT THE CONDITIONS THAT LED TO THE FRAUD WERE LIMITED TO THE PROPERTY TAX REFUND AREA AND NOT SYSTEMIC TO OTHER OTR BUSINESS PROCESSES. CONSEQUENTLY, THE CITY DID GET A CLEAN OPINION FOR ITS FY 2007 FINANCIAL STATEMENTS, BUT THE CFO'S TAX AND REVENUE OPERATIONS WERE CONSIDERED A MATERIAL WEAKNESS. GIVEN THE SEVERITY OF THE FRAUD AND CONCERNS EXPRESSED BY THE INDEPENDENT AUDITORS, MANY INITIATIVES WERE UNDERTAKEN (1) TO EXPLAIN WHY AND HOW SUCH A FRAUD WAS PERPETRATED, AND (2) TO IDENTIFY THE ACTIONS NECESSARY TO PREVENT ANY FUTURE OCCURRENCE. ONE SUCH INITIATIVE OCCURRED WHEN THE DISTRICT'S CITY COUNCIL ESTABLISHED A TAX AND REVENUE INVESTIGATION SPECIAL COMMITTEE (SPECIAL COMMITTEE) TO REVIEW THE OTR FRAUD.

THE SPECIAL COMMITTEE RETAINED WILMER CUTLER PICKERING HALE AND DORR, LLP (WILMER HALE), WORKING WITH THE CPA FIRM OF PRICE WATERHOUSE COOPERS, LLP TO EXAMINE THE FACTS AND CIRCUMSTANCES SURROUNDING THE FRAUD SCHEME AND TO MAKE RECOMMENDATIONS TO PREVENT A RECURRENCE. THE RESULTING REPORT PUBLISHED BY WILMER HALE EXTENSIVELY REVIEWED OTR BUSINESS PROCESSES AND THE CONTROL CONDITIONS THAT CONTRIBUTED TO THE FRAUD. APPROXIMATELY 38

RECOMMENDATIONS WERE DIRECTED TO THE OCFO THAT ADDRESSED THE FAILURE OF INTERNAL CONTROLS, A CULTURE OF APATHY AND SILENCE, WHICH WAS PERVASIVE AMONG MANY OTR EMPLOYEES, AND THE LACK OF EFFECTIVE OVERSIGHT. AS A FOLLOW-UP TO THIS EFFORT, CITY COUNCIL CHAIRMAN VINCENT GRAY REQUESTED THAT THE OIG REVIEW OCFO ACTIONS TAKEN IN RESPONSE TO THE WILMER HALE FINDINGS AND RECOMMENDATIONS. WE RECENTLY INITIATED THAT FOLLOW-UP REVIEW IN RESPONSE TO THE CHAIRMAN'S REQUEST. MANY OF THE RECOMMENDATIONS MADE BY THE INDEPENDENT AUDITORS, THE OIG, AND WILMER HALE SHOULD IMPROVE OR HAVE ALREADY IMPROVED THE CONTROL ENVIRONMENT AT OTR. HOWEVER, ONE CASUALTY OF THE OTR SCANDAL THAT EXTENDS TO BROADER AREAS OF THE OCFO IS THE IMPACT ON PERSONNEL. MANY PEOPLE IN MID-LEVEL POSITIONS HAVE LEFT OCFO. THE OCFO NEEDS TO RECRUIT AND RETAIN MID-LEVEL PERSONNEL TO SUSTAIN AND CARRY OUT MANY OF THE CONTROL ENVIRONMENT IMPROVEMENTS THAT THE OCFO IS COMMITTED TO IMPLEMENT.

#### **OIG AUDITS AND THE CFO'S RESPONSE**

IN THE PAST SEVERAL YEARS, THE OIG HAS ISSUED NUMEROUS REPORTS THAT ADDRESSED IMPROVEMENTS IN VARIOUS OCFO AREAS. ONE IMPORTANT REPORT WAS A MANAGEMENT IMPLICATION REPORT (MIR) THAT WE ISSUED IN OCTOBER OF 2007, PRIOR TO THE DISCLOSURE OF THE FRAUD AT OTR, CONCERNING SYSTEMIC INTERNAL CONTROL DEFICIENCIES. A MIR IS A REPORT

THAT NOTIFIES AGENCY HEADS OF MATTERS THAT POSSIBLY HAVE CITYWIDE RAMIFICATIONS, REQUIRING IMMEDIATE OR PRIORITY ATTENTION. WHILE NOT SOLELY DIRECTED AT THE OCFO, THE MIR DID NOTE THAT PERFORMANCE AUDITS WE ISSUED TO THE OCFO FROM FYS 2005-2007 CONTAINED 13 INTERNAL CONTROL DEFICIENCIES. THESE DEFICIENCIES ADDRESSED SUCH ISSUES AS INEFFECTIVE POLICIES AND PROCEDURES, INEFFECTIVE CONTROLS TO PREVENT OR DETECT FRAUD, LACK OF DOCUMENTATION, AND INEFFECTIVE MANAGEMENT OVERSIGHT; ALL OF WHICH ARE ISSUES OR AREAS DIRECTLY RELATED TO THE OTR FRAUD MATTER. WE ALSO EVALUATED INTERNAL CONTROL WEAKNESSES FOUND IN FINANCIAL REPORTS, FINDING THAT FOR FYS 2004-2006 THERE WERE 6 INTERNAL CONTROL DEFICIENCIES AT THE OCFO AND 1 INTERNAL CONTROL DEFICIENCY INVOLVING INEFFECTIVE MANAGEMENT OVERSIGHT AT OTR. THE PURPOSE OF THE MIR WAS TO ENCOURAGE AGENCY MANAGEMENT TO LOOK AT THEIR OWN CONTROL ENVIRONMENT WITH A VIEW TOWARD IMPLEMENTING MANAGEMENT CONTROLS TO PREVENT, DETECT, AND CORRECT CONDITIONS REPORTED IN OIG AUDIT REPORTS.

IN ANOTHER MIR ISSUED IN JANUARY 2009, THE OIG FOCUSED ON INTERNAL CONTROL WEAKNESSES IN THE DISTRICT'S PAYMENT PROCESS. WHILE AGAIN NOT DIRECTED SOLELY AT THE OCFO, THE MIR DID ADDRESS CONTROL DEFICIENCIES IN THE DISTRICT'S PAYMENT PROCESS, OF WHICH THE OCFO IS AN INTEGRAL COMPONENT, WITH RESPECT TO THE VARIOUS PAYMENTS MADE FOR ACQUIRED GOODS AND SERVICES, PAYROLL PAYMENTS, THIRD-PARTY

PAYMENTS, TAX REFUNDS, AND OTHER AUTHORIZED PAYMENTS. SOME OF THE SAME PROBLEMS PREVIOUSLY CITED INCLUDED INSUFFICIENT MANAGEMENT OVERSIGHT, INEFFECTIVE SUPERVISION, LACK OF ADEQUATE POLICIES AND PROCEDURES, MISSING DOCUMENTATION, INADEQUATE SEGREGATION OF DUTIES, AND UNFAMILIARITY WITH STANDARDS OF CONDUCT AND WORKPLACE ETHICS.

OVERALL, THE FINDINGS AND RECOMMENDATIONS THE OIG HAS DIRECTED TO THE OCFO HAVE BEEN MET WITH APPROVAL, ACCEPTANCE, AND IMPLEMENTATION OF CORRECTIVE ACTIONS. OCFO'S MANAGEMENT HAS TAKEN PROACTIVE ACTIONS ON MANY OF THE OIG FINDINGS AND RECOMMENDATIONS.

#### **INTERAGENCY COOPERATION BETWEEN THE OIG AND OCFO**

BECAUSE THE OCFO PLAYS AN ESSENTIAL ROLE IN MAINTAINING THE INTEGRITY OF THE CITY'S FINANCES AND SERVING AS THE PRIMARY ACCOUNTANT FOR ALL FISCAL MATTERS ON A LOCAL BUDGET OF ABOUT \$8 BILLION, WE HAVE ENGAGED THE OCFO ON SEVERAL LEVELS TO IMPROVE INTERAGENCY COOPERATION AND OVERSIGHT EFFORTS. THE OCFO, WHILE NOT A VOTING MEMBER OF THE CAFR OVERSIGHT COMMITTEE CHAIRED BY THE OIG, ENJOYS A TENURED ROLE AS AN ACTIVE PARTICIPANT IN REGULARLY SCHEDULED CAFR MEETINGS. CAFR COMMITTEE MEETINGS SERVE AN

EXTREMELY IMPORTANT FUNCTION IN GETTING MANAGEMENT OF DISTRICT AGENCIES AND INDEPENDENT COMPONENTS, ALONG WITH THE OCFO, TO COOPERATE AND TO COORDINATE EFFORTS TO PERMIT TIMELY COMPLETION OF THE INDEPENDENT AUDITORS' FINANCIAL STATEMENT AUDIT. THROUGHOUT THE YEAR, THE OIG, WORKING WITH THE OCFO, CITY COUNCIL, AND THE MAYOR'S OFFICE, INVITES AGENCIES TO CAFR COMMITTEE MEETINGS TO ADDRESS SIGNIFICANT DEFICIENCIES AND MATERIAL WEAKNESSES, AND CHALLENGING AGENCIES TO PROVIDE SOLUTIONS TO THOSE REPORTED PROBLEMS. FOLLOW-UP CAFR MEETINGS ARE HELD TO TRACK PROGRESS ON CORRECTIVE ACTIONS. WE BELIEVE THESE PROACTIVE EFFORTS MAY HAVE CONTRIBUTED, IN PART, TO THE REDUCTION IN THE NUMBER OF SIGNIFICANT DEFICIENCIES REPORTED IN FY 2008.

#### **WAYS THE OCFO CAN IMPROVE ITS FINANCIAL MANAGEMENT**

WHILE THE OCFO HAS TAKEN MANY CORRECTIVE ACTIONS RELATIVE TO ITS OPERATIONS, WE BELIEVE THERE ARE SEVERAL AREAS WHERE ADDITIONAL MANAGEMENT ACTIONS SHOULD BE TAKEN TO IMPROVE OCFO OPERATIONS:

- GIVEN THE IMPACT THAT SOUND INTERNAL CONTROL HAS ON ACCOUNTABILITY AND EFFECTIVE AND EFFICIENT GOVERNMENT OPERATIONS, THE OCFO SHOULD ISSUE A CITYWIDE DIRECTIVE REQUIRING MANAGERS TO ESTABLISH, ASSESS, CORRECT, AND REPORT



ON INTERNAL CONTROLS. THE GUIDANCE COULD BE PATTERNED, FOR EXAMPLE, AFTER THE FEDERAL MANAGERS' FINANCIAL INTEGRITY ACT (FMFIA) OF 1982 AND THE OFFICE OF MANAGEMENT AND BUDGET (OMB) CIRCULAR A-123, MANAGEMENT'S RESPONSIBILITY FOR INTERNAL CONTROL. IN OUR VIEW, DISTRICT MANAGEMENT NEEDS TO CREATE A CLIMATE WHERE INTERNAL CONTROLS CAN DEVELOP AND FLOURISH TO PROTECT THE PUBLIC TRUST.

- REGARDING THE PAYMENT PROCESS, THE OCFO NEEDS TO ASSIGN ACCOUNTS PAYABLE OFFICIALS MORE ACCOUNTABILITY BY DEVELOPING WRITTEN POLICIES AND PROCEDURES THAT REQUIRE DUE DILIGENCE PRIOR TO THE PAYMENT OF INVOICES. FOR EXAMPLE, STEPS MUST BE TAKEN TO ENSURE THAT THE PAYMENT OF CONTRACTORS' INVOICES IS MADE ONLY PURSUANT TO THE APPROVAL OF AUTHORIZED AGENCY PERSONNEL.
- RECENT FRAUDS PERPETRATED AGAINST THE DISTRICT DISCLOSED A NEED FOR AN INTENSIFIED ANTI-FRAUD PROGRAM. BY INTENSIFYING ITS ANTI-FRAUD PREVENTIVE AND DETECTIVE CONTROLS, THE OCFO CAN BETTER CREATE A CULTURE OF ETHICAL BEHAVIOR IN THE WORKPLACE.
- THE OCFO NEEDS TO RECRUIT AND RETAIN QUALIFIED PERSONNEL, THEN PROPERLY SUPERVISE ITS STAFF, TO INCLUDE MANAGEMENT REVIEW OF TRANSACTIONS AND PROCESSES, AND TIMELY AND ACCURATE EMPLOYEE EVALUATIONS.

**CONCLUSION**

IN SUMMARY, MY OFFICE WILL CONTINUE TO PROVIDE AN INDEPENDENT ASSESSMENT OF THE OCFO TO HELP MAINTAIN THE HIGHEST STANDARD OF CONDUCT, INTEGRITY, AND EFFICIENT AND EFFECTIVE GOVERNMENT OPERATIONS.

MR. CHAIRMAN, MY STAFF AND I WILL BE HAPPY TO ANSWER ANY QUESTIONS THAT YOU MAY HAVE.

BACKGROUND  
STABILITY THROUGH SCANDAL: A REVIEW OF THE OFFICE OF THE CHIEF  
FINANCIAL OFFICER  
March 31, 2009

**Background**

In the 1990s, the District of Columbia faced a major fiscal crisis due to mismanagement of District funds and a systemic lack of accountability. The crisis led to the passage of the District of Columbia Financial Responsibility and Management Assistance Act of 1995 (P.L. 104-8), which sought to eliminate budget deficits and set the District on the path to financial recovery.<sup>1</sup> This legislation also created the District of Columbia Financial Responsibility and Management Assistance Authority (Control Board), the District Office of the Chief Financial Officer, and enhanced the powers of the Office of the Inspector General (OIG).<sup>2</sup>

The Control Board was a five-member entity appointed by President Clinton, which assumed full power over District finances, including the power to override financial decisions made by the DC City Council and Mayor. The Act specified that the activities of the Control Board would be suspended only after the District fulfilled four criteria: (1) obligations of the Control Board must be discharged; (2) all borrowings from the U.S. Treasury on behalf of the District must be repaid; (3) the District must establish sufficient access to short and long-term creditors; and (4) four consecutive balanced budgets must be achieved.<sup>3</sup>

**Hearings**

In March 1997, the Homeland Security and Governmental Affairs Subcommittee charged with oversight of the District of Columbia held a series of hearings to examine the financial state of the District since the Control Board assumed control a couple years earlier.<sup>4</sup> These hearings examined factors that led to DC's financial collapse, as well as reforms that were being undertaken in other cities facing financial and social hardship.<sup>5</sup> Recommendations such as reducing crime, reaching out to community and institutional stakeholders, and effective management of Federal funds were proposed as starting-points for DC's recovery.<sup>6</sup>

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<sup>1</sup> District of Columbia Financial Responsibility Act of 1995, P.L. 104-8, (1995).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia hearing on *The Financial Crisis Facing the District of Columbia Today*, Mar. 11, 1997.

<sup>5</sup> Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia hearing on *The President's Proposal and Alternative Approaches for the District of Columbia*, May 13, 1997.

<sup>6</sup> Subcommittee on the District of Columbia, *supra* note 4.

While the Subcommittee held a hearing in 2006 to address general challenges facing D.C., the last hearing to focus exclusively on the District's financial condition was held in 2000.<sup>7</sup> At that hearing, then-Mayor Anthony Williams described the actions he had undertaken to improve the District's performance management system and reverse a District government culture that was resistant to change. Four efforts were highlighted: first, the creation of a citywide performance plan helped agencies and the Mayor's office remain focused on the same goals for budget and performance; second, the Mayor increased agency data collection efforts to monitor performance goals; third, management supervision and training efforts were increased to address human capital shortfalls; finally, bench-marking based on the agency data and outreach to stakeholders helped the Mayor determine the "right size" for DC government.<sup>8</sup>

### **Regaining Financial Independence: the Emergence of the OCFO**

As a result of reform efforts and better financial management, the District achieved all four preconditions in February 2001 and activities of the Control Board were suspended on September 30, 2001. After Control Board functions were suspended, the District resumed control over its finances under the direction of the OCFO, whose mission is to enhance fiscal and financial stability, and to increase accountability and integrity.<sup>9</sup> The OCFO has posted twelve consecutive balanced budgets thanks largely to improvements in financial reporting and improved financial management strategy.<sup>10</sup>

Dr. Natwar M. Gandhi is currently the Chief Financial Officer (CFO) in the OCFO, which is composed of four main parts: Executive Support, Central Financial Operations, Agency Financial Operations, and the Chief Financial Officers for Independent Agencies.<sup>11</sup>

- **Executive Support**: provides support to the OCFO as an agency and is comprised of the following units:
  - Agency Chief Information Officer
  - General Counsel
  - Office of Integrity and Oversight (OIO)
  - Management and Administration
  - Public Affairs
  - Senior Advisor for Economic Development
- **Central Financial Operations**: handles many of the critical operations for budget analysis and financial operations, and are managed by Deputy Chief Financial Officers who report directly to the District's CFO:
  - Budget and Planning

<sup>7</sup> Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia on Performance Management in the District of Columbia: *A Progress Report*, May 9, 2000.

<sup>8</sup> *Id.*

<sup>9</sup> <http://cfo.dc.gov>

<sup>10</sup> Adrian Fenty and Natwar Gandhi, *Government of the District of Columbia Comprehensive Annual Financial Report Year Ended September 30, 2008*, (Jan. 30, 2009).

<sup>11</sup> D.C. Office of the Chief Financial Officer, *supra* note 9.

- Finance and Treasury
- Financial Operations and Systems
- Revenue Analysis
- Office of Tax and Revenue
- **Agency Financial Operations**: manages the financial operations and program priorities of agencies under the DC Mayor's Office. The following units make up the Central Financial Operations branch and are managed by Associate Chief Financial Officers who report directly to the District's CFO:
  - Economic Development and Regulations
  - Government Operations
  - Government Services
  - Human Support Services
  - Public Safety and Justice
  - Education
- **Independent Agencies**: a collection of four chief financial officers who, like the Associate CFOs and Deputy CFOs, report directly to the District's CFO and oversee:
  - DC Lottery
  - DC Public Schools
  - DC Sports and Entertainment Commission
  - Washington Convention Center Authority

Data from these branches are compiled by the OCFO and summarized in an annual report, the Comprehensive Annual Financial Report (CAFR). The CAFR provides a comprehensive compilation of the financial activity of the District in a given year, and is audited annually by the OIG. Copies of the CAFR are also provided to Congress, the DC City Council, Mayor's Office, and made available for public inspection. The widespread dissemination of the CAFR is part of the OCFO's efforts to increase transparency and accountability in the District's financial management system.<sup>12</sup>

#### **SYSTEM WEAKNESSES, SCANDALS, AND RESPONSES**

Although notable progress has been made by the OCFO, both the Government Accountability Office (GAO) and the OIG have identified weaknesses in the OCFO and recommended courses of action be taken to remedy those weaknesses. Scandals have also continued to plague the OCFO and District, notably the 2007 property tax refund scandal that resulted in the arrests of two OCFO employees and millions of dollars lost by the District. To its credit, the OCFO has taken steps to mitigate system weaknesses identified by the GAO and OIG.

#### **Problems Identified by the GAO and the OCFO's Responses**

In January 2007, the GAO conducted a review of the District's procurement system and found several weaknesses, including the policies setting high dollar thresholds before internal controls

<sup>12</sup> Telephone Conversation with Stephanie Royal, Assistant General Counsel, Office of the Chief Financial Officer (Mar. 26, 2009).

identified a problem.<sup>13</sup> Specifically, the OCFO was advised to: (1) eliminate the use of direct voucher payments for emergency procurements; and (2) work with the Mayor's Contracting and Procurement Officer to (a) reduce contract ratifications by unauthorized personnel, (b) process unauthorized commitments that aren't ratified using appropriate claim procedures, and (c) track the use of direct voucher payments to draw managerial attention to unauthorized claims.<sup>14</sup>

The OCFO disagreed with a number of issues identified in the GAO report, citing the fact it has no direct authority over employees of the Chief Procurement Officer (CPO) because those employees fall under the Mayor's purview.<sup>15</sup> While true, the GAO countered that the OCFO should develop stronger controls and better monitoring practices.<sup>16</sup> The OCFO acknowledged procurement deficiencies that needed to be remedied and implemented changes in its emergency voucher payment system and increased the use of administrative claim procedures to remedy unauthorized, unratified commitments.<sup>17</sup>

### **Problems Identified by the OIG and the OCFO's Responses**

#### **Internal Control Deficiencies**

In its audits, the OIG has identified "internal control deficiencies" as a pervasive problem not only within the OCFO, but also in the District government.<sup>18</sup> Internal control deficiencies are break-downs in management controls meant to prevent, detect, and deter fraud and misappropriation.<sup>19</sup> The effects of weak or non-existent internal controls have manifested themselves in every agency, including the OCFO, resulting in the mismanagement and sometimes the misappropriation of District funds.<sup>20</sup> Internal controls can be broken down into four categories:

- *Lack of documentation*: absence of documents to support a transaction, as well as documentation that is incomplete or otherwise insufficient;
- *Ineffective Policies and Procedures*: absence or insufficient policies and procedures to track funds;

<sup>13</sup> Government Accountability Office, *District of Columbia Procurement System Needs Major Reform*, GAO-07-159 (2007).

<sup>14</sup> *Id.* at 45.

<sup>15</sup> *Id.* at 59.

<sup>16</sup> Meeting with Carolyn Kirby, Government Accountability Office (Mar. 13, 2009).

<sup>17</sup> *Id.*

<sup>18</sup> Memorandum from Charles J. Willoughby, Inspector General, District of Columbia Office of the Inspector General, to Mayor Adrian Fenty, Mayor, District of Columbia (Oct. 19, 2007) (on file with author).

<sup>19</sup> *Id.*

<sup>20</sup> District of Columbia Office of the Inspector General, *Independent Auditors' Report on Internal Control and Compliance Over Financial Reporting Fiscal Year Ended September 30, 2008*, OIG No. 09-1-10MA, Feb. 4, 2009.

- *Ineffective Management Oversight*: ineffective leadership due to high turnover at key positions or ineffective monitoring of policies; and
- *Ineffective Controls to Prevent or Detect Fraud*: ineffective segregation of duties, improper authorization for transactions.<sup>21</sup>

#### FY07 and FY08 CAFR Audits

As mentioned above, the OIG conducts annual audits of the OCFO CAFR. The CAFR weaknesses are all consequential because they contribute to the inaccurate reporting of data, which in turn leads to millions of dollars in loss for the District.

An audit of the CAFR for FY08 recently was completed, and it identified two material weaknesses: management of the Medicaid Program and Account Reconciliation.<sup>22</sup> The first problem, Medicaid management, has been a chronic problem for the District.<sup>23</sup> Audits of DC's Department of Mental Health Program found that a process for reworking and resubmitting denied Medicaid claims was non-existent.<sup>24</sup> Audits also uncovered a "lack of documentation" internal control failure, whereby the District was losing millions of dollars because incomplete documentation was preventing federal reimbursement for Medicaid claims.<sup>25</sup> The second problem, Account Reconciliation, had to do largely with the District improperly accounting for its cash and investment activity by not entering it into the District's System of Accounting and Records (SOAR).<sup>26</sup> This left the District with inaccurate data on its investment activity and an inability to accurately assess how much money it had in its investment accounts.<sup>27</sup>

The OCFO indicated that they were aware of the Medicaid and Account Reconciliation weaknesses identified in the OIG FY08 CAFR audit and are working to remedy them.<sup>28</sup> They noted the audit was released in early February and as such, it would take some time before new procedures and policies were implemented.<sup>29</sup>

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<sup>21</sup> Willoughby, *supra* note 15, at 2.

<sup>22</sup> DC Inspector General, *supra* note 17, at 2.

<sup>23</sup> District of Columbia Office of the Inspector General, *Independent Auditors' Report on Internal Control and Compliance Over Financial Reporting Fiscal Year Ended September 30, 2007*, OIG No. 08-1-08MA, Apr. 9, 2008.

<sup>24</sup> District of Columbia Office of the Inspector General, *Report on Activities Fiscal Year 2008*, (2008).

<sup>25</sup> DC Inspector General, *supra* note 20, at 22-33.

<sup>26</sup> *Id.* at 3.

<sup>27</sup> *Id.*

<sup>28</sup> Meeting with David Tseng and Stephanie Royal, Office of General Counsel for the D.C. Office of the Chief Financial Officer (Mar. 12, 2009).

<sup>29</sup> *Id.*

The OIG audit of the CAFR for FY07 uncovered three material weaknesses: (1) Medicaid management, (2) the Office of Tax and Revenue (OTR) Refund Process, and (3) DC Public School (DCPS) Finances.<sup>30</sup> The first issue of Medicaid management was similar to the problems uncovered in the audit for CAFR FY08.<sup>31</sup> The second issue of OTR refunds stems largely from the manual tax refund system that lacked sufficient authorization and approval procedures, an example of an internal control failure.<sup>32</sup> The OIG recommended the implementation of automated tax refunds and stronger internal controls to deter fraud.<sup>33</sup> Finally, the DCPS was identified as “high risk” because of systemic deficiencies in payroll, untimely submission of audits, and inadequate monitoring of federal funds.<sup>34</sup>

While Medicaid management continues to be a chronic problem, the OCFO, partly in response to the FY07 CAFR, has increased internal controls in the OTR where the tax refund system is now largely automated, the issuable dollar amount for each check has been lowered, and multiple employees must verify the authenticity of refund data.<sup>35</sup> In response to financial management issues within the DCPS, the OCFO and U.S. Department of Education implemented a corrective action plan to ensure adequate monitoring of federal funds.<sup>36</sup> Automated processes were also expanded in DCPS payroll and disbursements.<sup>37</sup>

### **Scandals**

On November 7, 2007, the risks caused by the material weakness identified by the OIG in the OTR became clear when two OTR employees were arrested on a number of fraud counts, including fraudulently issuing and approving property tax refund checks.<sup>38</sup> In response to the OTR scandal, the CFO directed the OIO to take immediate action to identify management control failures and work with the OIG to conduct a broad review of OTR internal controls.<sup>39</sup>

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<sup>30</sup> DC Inspector General, *supra* note 23, at 2.

<sup>31</sup> *Id.* at 21-39.

<sup>32</sup> *Id.* at 3-4.

<sup>33</sup> *Id.*

<sup>34</sup> *Id.* at 40-45.

<sup>35</sup> Tseng and Royal, *supra* note 28.

<sup>36</sup> DC Inspector General, *supra* note 23, at 40.

<sup>37</sup> DC Inspector General, *supra* note 20, at 70-71.

<sup>38</sup> Press Release, District of Columbia Office of the Chief Financial Officer, CFO Issues Statement on Arrests in DC Property Tax Refund Scheme (Nov. 7, 2007) (on file with author).

<sup>39</sup> *Id.*



Investigation revealed that starting in 2006, an OTR officer circumvented the computerized tax systems by manually entering fictitious tax returns to obtain tax refund checks.<sup>40</sup> At the time, there was no internal control established in the OTR to prevent this fraud from happening; multiple employees were not required to review refund data before refund tax refund checks were issued.<sup>41</sup> As a result, the OTR officer issued over 40 fraudulent checks averaging over \$388,000 each.<sup>42</sup>

The fraud scheme of the OTR officer came undone in 2007 after the OCFO had implemented new internal controls to automatically flag tax refund checks for over a certain dollar amount.<sup>43</sup> When the OTR officer tried to issue a refund check for \$41,000, the new refund system attached a warning to the file and the employee was later caught.<sup>44</sup>

Fortunately the fraud was restricted to property tax refunds and the OTR, but it resulted in the loss of tens of millions of dollars for the District, and increased scrutiny on the OCFO.<sup>45</sup> In the months and years that followed, hearings were held by the DC City Council, internal controls were strengthened further and actions were taken by Dr. Gandhi against OTR employees who received checks as part of the property tax fraud scheme.<sup>46</sup>

The District continues to be plagued by scandals due to insufficient internal controls. Earlier this month, an official in the DC Office of the Chief Technology Officer (CTO) was arrested for bribery and money laundering.<sup>47</sup> The arrested CTO officer allegedly approved fraudulent time sheets for non-existent employees and worked with an outside vendor to defraud the District by charging it for software products that were never actually ordered.<sup>48</sup>

Although the arrested official was a member of the Mayor's office, not of the OCFO as was the case in the OTR scandal, the fraud highlights systemic problems in the procurement that were

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<sup>40</sup> Memorandum from William DiVello, DC Office of the Inspector General, to staff on the Oversight of Government Management, the Federal Workforce, and the District of Columbia, (Mar. 11, 2009) (on file with author).

<sup>41</sup> Meeting with William DiVello, Cheryl Ferrara, and Salvatore Guli, DC Office of the Inspector General (Mar. 11, 2009)

<sup>42</sup> Press Release, U.S. Department of Justice, Federal and local law enforcement officials announce arrests and raids in multimillion-dollar D.C. property tax refund fraud scheme (Nov. 7, 2007) (on file with the author).

<sup>43</sup> *Id.*

<sup>44</sup> DiVello, *supra* note 40.

<sup>45</sup> U.S. Department of Justice, *supra* note 42.

<sup>46</sup> David Nakamura and Nikita Stewart, *Gandhi Moving to Oust 14 Who Received Checks*, Washington Post, Oct. 22, 2008 at B4.

<sup>47</sup> Del Wilber and Nikita Stewart, *D.C. Tech Official Is Accused of Bribery*, Washington Post, Mar. 13, 2009 at B1.

<sup>48</sup> *Id.*

identified in the GAO report on procurement discussed above, such as high dollar thresholds for individual contracts and insufficient tracking of direct voucher payments.<sup>49</sup>

### **Conclusion**

Progress has certainly been made in the years since the District's financial collapse in the mid-90s. As mentioned earlier, the OCFO has helped DC post twelve consecutive balanced budgets. In the CAFR for FY08, the OCFO announced a \$191 million budgetary surplus going into FY09, which stands in contrast with the surrounding jurisdictions of the State of Maryland and the Commonwealth of Virginia, which are running greater than 10% deficits in their general funds.<sup>50</sup> Additionally, the OCFO has worked to incorporate audit feedback into its financial management scheme.

Despite this progress, the CFO projects revenue shortfalls in the coming fiscal years. Internal controls and Medicaid management also continue to be major challenges to the financial health of the District.

In the coming months, the District will be receiving large amounts of stimulus money. Recommendations from this hearing and continued input from the OIG should help DC stay on the path to financial recovery.

### **Key Questions**

- What progress has the OCFO made in financial management, including practices that achieved consecutive balanced budgets?
- How has the OCFO responded to recommendations from the OIG, the GAO, and others?
- What financial management challenges lay ahead and what steps is the OCFO taking to address those challenges?
- What sort of interagency cooperation exists between the OCFO, Mayor's Office, and OIG to achieve efficiency and improve accountability?

### **Key Legislation**

- District of Columbia Financial Responsibility Act of 1995, P.L. 104-8.

### **RESOURCES:**

#### **Hearings**

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<sup>49</sup> Kirby, *supra* note 16.

<sup>50</sup> Fenty and Gandhi, *supra* note 10.

- Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia hearing on *The Financial Crisis Facing the District of Columbia Today*, Mar. 11, 1997.
- Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia hearing on *The President's Proposal and Alternative Approaches for the District of Columbia*, May 13, 1997.
- Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia on Performance Management in the District of Columbia: *A Progress Report*, May 9, 2000.

#### **Reports and Memoranda**

- Government Accountability Office, *District of Columbia Procurement System Needs Major Reform*, GAO-07-159 (2007)
- Adrian Fenty and Natwar Gandhi, *Government of the District of Columbia Comprehensive Annual Financial Report Year Ended September 30, 2008*, (Jan. 30, 2009)
- District of Columbia Office of the Inspector General, *Independent Auditors' Report on Internal Control and Compliance Over Financial Reporting Fiscal Year Ended September 30, 2008*, OIG No. 09-1-10MA, Feb. 4, 2009
- District of Columbia Office of the Inspector General, *Independent Auditors' Report on Internal Control and Compliance Over Financial Reporting Fiscal Year Ended September 30, 2007*, OIG No. 08-1-08MA, Apr. 9, 2008
- Memorandum from Charles J. Willoughby, Inspector General, District of Columbia Office of the Inspector General, to Mayor Adrian Fenty, Mayor, District of Columbia (Oct. 19, 2007) (on file with author).
- District of Columbia Office of the Inspector General, *Report on Activities Fiscal Year 2008*, (2008)
- Council of the District of Columbia and Office of Tax and Revenue Investigation Special Committee, *Report of Investigation*, (2008) (explaining the OTR property tax scandal and commonly referred to as the "Wilmer Hale Report").

#### **Articles and Press Releases**

- Press Release, District of Columbia Office of the Chief Financial Officer, CFO Issues Statement on Arrests in DC Property Tax Refund Scheme (Nov. 7, 2007) (on file with author).

- Press Release, U.S. Department of Justice, Federal and local law enforcement officials announce arrests and raids in multimillion-dollar D.C. property tax refund fraud scheme (Nov. 7, 2007) (on file with the author).
- David Nakamura and Nikita Stewart, *Gandhi Moving to Oust 14 Who Received Checks*, Washington Post, Oct. 22, 2008 at B4.
- Del Wilber and Nikita Stewart, *D.C. Tech Official Is Accused of Bribery*, Washington Post, Mar. 13, 2009 at B1.

**Government of the District of Columbia  
Office of the Chief Financial Officer**



**Natwar M. Gandhi**  
Chief Financial Officer

October 1, 2009

The Honorable Daniel K. Akaka, Chair  
Senate Subcommittee on Oversight of Government Management,  
the Federal Workforce, and the District of Columbia  
U.S. Senate Committee on Homeland Security and Governmental Affairs  
141 Hart Senate Office Building  
Washington, DC 20510

The Honorable George V. Voinovich, Ranking Member  
Senate Subcommittee on Oversight of Government Management,  
the Federal Workforce, and the District of Columbia  
U.S. Senate Committee on Homeland Security and Governmental Affairs  
524 Hart Senate Office Building  
Washington, DC 20510

Dear Senators Akaka and Voinovich:

This letter provides a six-month status report to the Subcommittee in response to Senator Voinovich's request for same during the hearing "Stability though Scandal: A Review of the Office of the Chief Financial Officer," held in Room 342 of the Dirksen Senate Office Building on March 31, 2009.

The Office of the Chief Financial Officer (OCFO) has been working diligently to protect itself against future acts of fraud and misconduct. We have implemented the recommendations outlined in the Report of Investigation by the WilmerHale law firm, as follows:

- Deloitte and Touche LLP (Deloitte) was engaged to perform an Entity Level Risk Assessment as well as risk assessments in both the OCFO's Office of Finance and Treasury (OFT) and Office of Tax and Revenue (OTR) specifically addressing inherent fraud risk.
- The OCFO's Office of Integrity and Oversight (OIO) has developed a Fraud Awareness Program that is mandatory for all employees of the OCFO, and includes awareness of fraud "red flags" and a Fraud Hotline, which was tested and verified by Deloitte.
- A Chief Risk Officer, Kathy Crader, has been hired.
- An internal controls framework (Internal Controls Program) has been established that leverages process owners and stakeholders as subject-matter experts to ensure a comprehensive risk assessment.
- The Internal Controls Program provides for the assessment of strength of controls and on-going monitoring of controls to ensure they continue to perform as intended.

The Honorable Daniel K. Akaka  
The Honorable George V. Voinovich  
October 1, 2009  
Page 2

- The Internal Controls Program provides transparency and visibility into the control efforts being pursued, including progress updates.
- The OCFO has established a Steering Committee (SCIC) to provide continued support for the Internal Controls Program.
- The OCFO has dedicated staff to ensure policies and procedures are current and accurate. The Internal Controls Program includes regular attestations that procedures are accurate, available to the team and reflect the way work is performed.
- The Internal Controls Program provides for documentation of risks, risk assessments, controls, strength of controls, control test plans and control test results. Further, the workflows that support the program include escalation of "failed" control tests to the SCIC and a mechanism for remediation.
- Specific control opportunities highlighted in the report, as well as feedback from other sources, are being incorporated into the Internal Controls Program.
- Deloitte performed an assessment of the OCFO audit function and deemed it to be a critical function with effective leadership; afforded full authority to audit all areas; encouraged professional certifications; and has a well-defined, documented and acceptable approach for executing internal audits.
- The OCFO has also made improvements in its automated systems and controls and is currently working through the process of upgrading its major systems, SOAR and ITS. The CRO and CIO are working closely to ensure that specific control requirements are included in the process.

In conclusion, as stated above, my office continues to work diligently to uncover misconduct and fraud and to investigate allegations in order protect itself from future acts of fraud and misconduct. If you have additional questions or need additional information, please do not hesitate to contact me.

Sincerely,



Natwar M. Gandhi

cc: Mr. Benjamin Rhodeside - Chief Clerk,  
Subcommittee on Oversight of Government Management,  
the Federal Workforce, and the District of Columbia

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Testimony of

**Paul Strauss**

United States Senator

District of Columbia (Shadow)

before the

**United States Senate**

Committee on Homeland Security & Governmental Affairs

Subcommittee on Oversight of Government Management, the Federal Workforce, and the  
District of Columbia

Regarding

**“Stability through Scandal: a Review of the Office of the Chief Financial Officer”**

10:00 a.m. – March 31, 2009

Dirksen Senate Office Building

Rm. 342

Chairman Akaka, Senator Voinovich, and the members of the Sub-Committee, I am Paul Strauss, an elected United States Senator for the District of Columbia. On behalf of my constituents, the citizens of the District of Columbia, I thank you for allowing me to present this statement for the record.

While I always welcome any opportunity to talk about my beloved District of Columbia, I am somewhat perplexed as to why this Sub-Committee is utilizing your limited time and resources to focus on this purely local matter, instead of focusing on national priorities. A comparison of the District of Columbia's financial health, when contrasted with that of our nation at this present time in our history, illustrates a drastic difference. While the national debt and deficit are at the highest levels in our history, the District of Columbia retains a significant budget surplus, despite an unfair structural imbalance as well as economic challenges.

D.C.'s Incumbent Chief Financial Officer Dr. Natwar Gandhi deserves a great deal of credit for the operation and maintenance of a coordinated financial budget which collects, controls, and properly accounts for more than seven billion dollars in annual operating and capital funds. As Chief Financial Officer, Dr. Gandhi is also responsible for borrowing and investing on behalf of the District, among many other duties.

During his time as Chief Financial Officer, Dr. Gandhi has continued the twelve-year trend of balanced budgets. He has also balanced the projected budgets for fiscal years 2009 and 2010. This precedent of balanced budgets has generated a fund surplus of 1.2 billion dollar which has resulted in a Standard & Poor's Triple-A designation and a Double-A rating from Moody's Investors Service and Fitch Ratings. These new ratings will save 28 million dollars in interest payments for the government of the District over the next four years.

The District of Columbia's challenge, similar to the states of Hawaii and Ohio, is operating in an era when all basic revenue generators such as tourism, private home sales, and commercial real estate have declined to detrimental levels. Despite the national economic deterioration, the District's government has continued to function at a level superior to the majority of other states or the Federal Government at large. This is also despite a well documented structural imbalance which denies the District of Columbia revenue raising opportunities that exist in the 50 other states.

The fact that the District Government's Office of Tax and Revenue was the victim of a financial crime back in 2007 makes it no more likely a candidate for federal intervention than Ohio or Hawaii, or any other state which had the sad circumstance to be the victim of a breach of the public trust. As with any corruption, what is most damaged was the reputation of the hardworking and honest civil employees.

District residents, while saddened and disappointed to find themselves the victims of that crime, continue to find themselves confident in the ability of the Chief Financial Officer, as well as in other officials such as District of Columbia Inspector General Charles Willoughby, whom you also heard from today, to investigate such crimes. Surely the Senate faces greater problems collectively that require the full attention of this Committee, leaving the status of the District's officials in the hands of the people and government of the District of Columbia.

I thank you again for the opportunity to present this statement for the record. In closing, I would like to thank Mr. Edward Nyack of my legislative staff, for his assistance in helping to prepare this statement. I would be happy to answer any questions that you or your staff's might have.



**Post-Hearing Questions for the Record  
Submitted to Dr. Natwar Gandhi  
From Senator George V. Voinovich**

**“Stability through Scandal: A Review of the Office of the Chief  
Financial Officer”  
March 31, 2009**

**1. A 2003 report by the Government Accountability Office (GAO-03-666) notes that in the District of Columbia, the cost of providing public services is greater than annual revenue to pay for such services. GAO also recommended the District improve transparency and accountability in using federal funds.**

**a) In the current economic climate, how will DC meet its budget demands?**

By law, the District of Columbia must conclude each fiscal year with a balanced budget. As the Chief Financial Officer, I am responsible for generating revenue estimates, preparing fiscal impact statements for legislative proposals, and recording into the accounting system of record the accounting transactions for the District. These accounting transactions are the result of decisions by District policy makers, who are restricted by law from exceeding the revenue estimates for each fiscal year. Over the last decade, the District of Columbia has fulfilled that obligation. In the current economic climate, District policy makers are considering all viable options to balance the budget. These options include the elimination of positions, streamlining government functions, use of fund balance, adjustments to the fee structure, and use of federal stimulus funds. So far we have been successful at balancing the budget while meeting the needs of our residents and visitors to the city. I have no doubt that District policy makers will balance its FY 2009 budget and deliver a balanced FY 2010 proposed budget to the Congress.

**b) What can be done to improve the delivery of programs and services to help counter budget challenges?**

Delivery of programs and services to District residents is the responsibility of the Mayor and his agency directors. However, as CFO, there are several areas where I can provide financial information that will impact the delivery of programs and services. The first is the funding structure of the city and the availability of funding options, including taxes, fees, grants (both federal and private), debt issuance, and federal assistance. To counter the current budget challenges, I encourage the District's leadership to consider all sources of funds.

Once they have access, we then need to maximize the use of these funds. For example, I have made a point to advise the City Administrator that improvement of the Medicaid program should be a priority. Over a ten-year period, denied claims and/or disallowances resulting from poor or no documentation of the services provided, along with outstanding liabilities associated with Medicaid, have cost the District hundreds of millions of dollars. As CFO, my role does not extend to programmatic areas; however, the administration of the District's Medicaid programs has caused the District to lose federal funding that would have otherwise allowed for greater spending of local funds on other critical services. I commend the current Mayor and City Administrator for the creation of the Department of Health Care Finance. This newly created agency will assist the District's efforts to improve the administration of Medicaid and potentially eliminate many of the Medicaid claims process deficiencies that have resulted in the loss of federal funding.

So, by obtaining revenues from all available sources and then creating a structure that efficiently uses those resources, we should be able to improve the delivery of programs and services to help counter current budget challenges.

**Post-Hearing Questions for the Record  
Submitted to Dr. Natwar Gandhi  
From Senator George V. Voinovich**

**“Stability through Scandal: A Review of the Office of the Chief  
Financial Officer”  
March 31, 2009**

2. **Mr. Willoughby’s testimony discusses the 38 recommendations made to the Office of Tax and Revenue by the WilmerHale report to strengthen your office. How would you rate your responsiveness to the report? Do you agree with the recommendations? Do you have a strategic plan for assessing and implementing them?**

The Office of the Chief Financial Officer fully concurs with the findings of the WilmerHale report and has moved swiftly to implement its recommendations. The report, published in December 2008, has become a significant part of the OCFO’s comprehensive effort to develop and implement an organizational system of internal controls that are consistent with OMB Circular 123 and Sarbanes Oxley (where applicable). With the assistance of Deloitte Consulting, we have assessed each recommendation and determined the level of effort and resources required for its effective implementation, along with a project timeline. To date, we have made significant progress in implementing the report’s 38 recommendations and anticipate that most if not all will be implemented by the end of this fiscal year.

3. **The WilmerHale report recommended you appoint a Chief Risk Officer to assess and mitigate any operational and financial hazards. Has this position been created? If not, who conducts regular risk assessment within your office?**

The position of Risk Officer was established within the OCFO in January 2009. A nation-wide search was undertaken to identify candidates with the requisite qualifications and experience, and finalists for this position have been interviewed by OCFO senior management. A permanent selection for the position will be made by June 1, 2009. Until such time as the risk officer comes on-board, our Office of Integrity and Oversight will continue to routinely conduct risk assessments of the various business units within the OCFO.

**Response to Post-Hearing Questions for the Record  
Submitted to Senator George V. Voinovich  
From Charles J. Willoughby, Inspector General**

**“Stability through Scandal: A Review of the Office of the Chief Financial Officer”  
March 31, 2009**

1. A 2003 report by the Government Accountability Office (GAO-03-666) notes that in the District of Columbia, the cost of providing public services is greater than annual revenue to pay for such services.

GAO also recommended the District improve transparency and accountability in using federal funds. What, in the way of financial management improvements, can be done to facilitate the delivery of programs and services to help counter budget challenges? What challenges continue to exist in the way of inefficiencies?

**Response:**

The District of Columbia and the city’s leadership are faced with significant fiscal challenges that we believe will continue into the foreseeable future, given the national downturn in the economy. In the current situation, our goals remain focused on devoting our resources to audits of programs that pose serious fiscal and service delivery challenges for District executives, managers, citizens, and stakeholders.

Accordingly, we have identified the following areas as highly vulnerable:

1. Public Education Programs
2. Medicaid Program
3. Vulnerable populations
4. Procurement and contracting
5. Citizen safety and protection
6. Workforce Administration
7. Payment Process

While there is not one specific fix for these highly vulnerable areas, there are overarching management actions that can be taken on systemic issues that impact every program in the District. We believe the recommendations made in our audit reports have helped create program efficiencies, which in some small measure, facilitate service delivery programs. However, budget and programmatic challenges remain because of system deficiencies including:

- *Lack of Documentation* - This category includes no documents to support a given event or transaction, missing documents/incomplete files, and incomplete documents.
  - *Ineffective Policies and Procedures* - This category includes no policies and procedures, incomplete policies and procedures, and insufficient policies and procedures.
  - *Ineffective Management Oversight* - This category includes the absence of a control environment, ineffective supervision and leadership, high turnover in the top management positions, lack of management review for transactions and processes, and ineffective monitoring of internal control procedures.
  - *Ineffective Controls to Prevent or Detect Fraud* - This category includes ineffective safeguarding of assets, ineffective segregation of duties, delay in processing transactions, and improper authorization for transactions.
2. Mr. Willoughby, your testimony discusses the 38 recommendations made to the Office of Tax and Revenue in the Wilmer Hale report to strengthen the OCFO.

How would you rate the responsiveness of the OCFO to the report? Are you aware of a strategic plan for assessing and implementing them? What is your assessment of action already taken?

**Response:**

The OCFO has positively accepted the Wilmer Hale report and has agreed to address the report recommendations. With that said, we are currently conducting a follow-up audit of the recommendations contained in the Wilmer Hale report. The overall objective of this audit is to determine whether the OCFO has implemented the recommendations, specifically those recommendations intended to correct reported deficiencies at OTR. We will provide the Committee, as requested, during the March 31, 2009, hearing, a copy of our final report by September 2009.