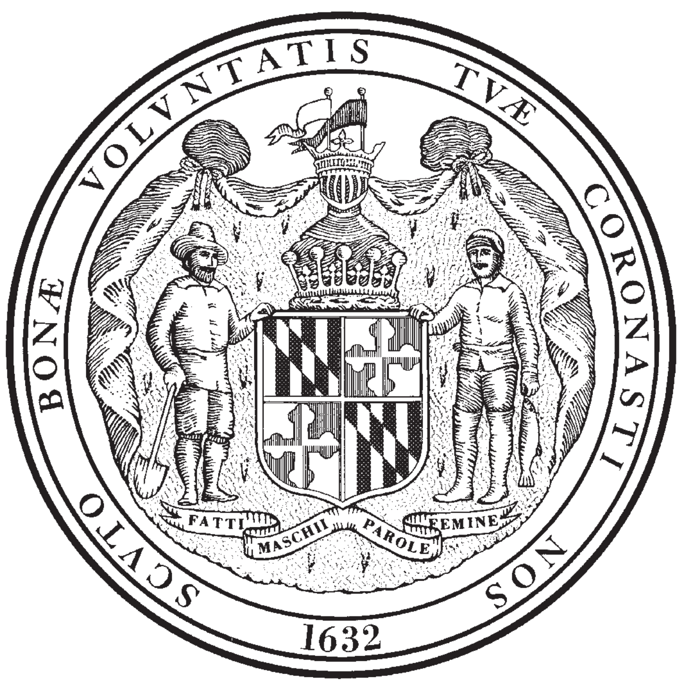
SPENDING AFFORDABILITY COMMITTEE

2004 Interim Report



ANNAPOLIS, MARYLAND
DECEMBER 2004

For further information concerning this document contact:

Library and Information Services
Office of Policy Analysis
Department of Legislative Services
90 State Circle
Annapolis, Maryland 21401

Baltimore Area: 410-946-5400 ● Washington Area: 301-970-5400
Other Areas: 1-800-492-7122, Extension 5400
TDD: 410-946-5401 ● 301-970-5401
Maryland Relay Service: 1-800-735-2258
E-mail: libr@mlis.state.md.us
Home Page: http://mlis.state.md.us

MARYLAND GENERAL ASSEMBLY
SPENDING AFFORDABILITY COMMITTEE

December 9, 2004

The Honorable Robert L. Ehrlich, Jr.
Governor, State of Maryland
State House
Annapolis, Maryland 21401

Dear Governor Ehrlich:

We are pleased to submit the fiscal policy recommendations of the Spending Affordability Committee made during the 2004 interim. These recommendations were adopted by the committee at its meeting on December 9, 2004. The committee reviewed data concerning the economic condition of the State, revenue and expenditure trends during the past several years, personnel data, the Transportation Trust Fund, and the results of the Capital Debt Affordability Committee report.

Recommendations were made concerning the fiscal 2006 spending limit, future budget sustainability, reserve fund balances, capital debt, transportation debt, and State positions.

The Spending Affordability Committee has completed its assigned tasks. As required by law, the recommendations of the committee have been submitted to the Governor and the Legislative Policy Committee.

We are most appreciative of the time and effort expended by each member of the committee. A special note of thanks and appreciation is extended to the members of the Citizens Advisory Committee for their valuable assistance and input.

Sincerely,

Delegate Michael R. Gordon
Presiding Chairman

Senator Edward J. Kasemeyer
Senate Chairman

Legislative Services Building • 90 State Circle • Annapolis, Maryland 21401-1991
410-946-5530 • FAX 410-946-5555 • TDD 410-946-5401
301-970-5530 • FAX 301-970-5555 • TDD 301-970-5401

MARYLAND GENERAL ASSEMBLY
SPENDING AFFORDABILITY COMMITTEE

December 9, 2004

The Honorable Thomas V. Mike Miller, Jr., Co-Chairman
The Honorable Michael E. Busch, Co-Chairman
Members of the Legislative Policy Committee

Ladies and Gentlemen:

We are pleased to submit the fiscal policy recommendations of the Spending Affordability Committee made during the 2004 interim. These recommendations were adopted by the committee at its meeting on December 9, 2004. The committee reviewed data concerning the economic condition of the State, revenue and expenditure trends during the past several years, personal data, the Transportation Trust Fund, and the results of the Capital Debt Affordability Committee report.

Recommendations were made concerning the fiscal 2006 spending limit, future budget sustainability, reserve fund balances, capital debt, transportation debt, and State positions.

The Spending Affordability Committee has completed its assigned tasks. As required by law, the recommendations of the committee have been submitted to the Governor and the Legislative Policy Committee.

We are most appreciative of the time and effort expended by each member of the committee. A special note of thanks and appreciation is extended to the members of the Citizens Advisory Committee for their valuable assistance and input.

Sincerely,

Michael Gordon

Delegate Michael R. Gordon
President Chairman

Edward J Kasemeyer

Senator Edward J. Kasemeyer
Senate Chairman

Legislative Services Building • 90 State Circle • Annapolis, Maryland 21401-1991
410-946-5530 • FAX 410-946-5555 • TDD 410-946-5401
301-970-5530 • FAX 301-970-5555 • TDD 301-970-5401

Maryland General Assembly
Spending Affordability Committee
2004 Membership Roster

Delegate Michael R. Gordon, Presiding Chairman
Senator Edward J. Kasemeyer, Senate Chairman

Senators

Ulysses Currie
James E. DeGrange, Sr.
Patrick J. Hogan
Nathaniel J. McFadden
Thomas M. Middleton
Thomas V. Mike Miller, Jr.
Donald F. Munson
Ida G. Ruben
J. Lowell Stoltzfus

Delegates

Kumar P. Barve
Talmadge Branch
Michael E. Busch
Norman H. Conway
Adelaide C. Eckardt
George C. Edwards
Anne Healey
Sheila E. Hixson
Adrienne A. Jones

Citizens Advisory Committee

H. Furlong Baldwin
Dana M. Jones
John C. Miller
Frederick W. Puddester

Staff

Christine A. Romans
David C. Romans

Contents

2004 Spending Affordability Committee Report and Recommendations to the Governor and the Legislative Policy Committee

The Spending Affordability Committee was created in 1982 (Chapter 585, Acts of 1982). The committee is composed of 20 legislative members including the presiding officers, the majority and minority leaders, the chairmen of the fiscal committees (or their designees), and other members appointed by the presiding officers. A four-member citizen advisory committee assists the committee.

The committee's primary responsibility is to recommend to the Governor and the General Assembly a level of spending for the State operating budget that is reflective of the current and prospective condition of the State's economy. Consideration is given to constraining disproportionate growth in State-funded expenditures in any fiscal year which might necessitate or "build in" unsupportable levels of spending in future years. The committee's prior recommendations and legislative action on the operating budget are reflected in the table on the following page.

The committee notes that operating spending in relation to the State's economy, as measured by the personal income statistic, is lower now than when the spending affordability process began in 1982. As illustrated in the chart on page four, throughout much of the 1980s, the ratio remained relatively stable. During the 1990 and 1991 sessions, the combination of increased spending demands and economic slowdown caused the spending ratio to increase. Following the recession, however, operating spending in relation to personal income fell acutely. With the onset of another recession in calendar 2001, spending in relation to personal income rose again. However, economic recovery, paired with spending restraint, caused the spending ratio in 2004 to dip to the lowest levels recorded.

The committee's statutory responsibility is to consider spending growth in relation to growth anticipated in the State's economy. In its review of the State's economy, the committee considered both income and wealth factors in developing a broad understanding of Maryland's economic position. In determining the spending limit, the committee has considered economic performance, revenue estimates, and budget requirements.

Spending Affordability Committee's Prior Recommendations and Legislative Action on the Operating Budget
($ in Millions)

	Committee Recommendation		Legislative Action	
Session Year	**Growth Rate**	**Amount**	**Growth Rate**	**Amount**
1983	9.00%	$428.0	5.70%	$269.8
1984	6.15%	326.7	8.38%	402.0
1985	8.00%	407.2	7.93%	404.6
1986	7.70%	421.5	7.31%	402.2
1987	7.28%	430.2	7.27%	429.9
1988	8.58%	557.5	8.54%	552.9
1989	8.79%	618.9	8.78%	618.2
1990	9.00%	691.6	8.98%	689.7
1991	5.14%	421.8	5.00%	410.0
1992	No recommendation		10.00%	823.3
1993	2.50%	216.7	2.48%	215.0
1994	5.00%	443.2	5.00%	443.2
1995	4.50%	420.1	4.50%	420.0
1996	4.25%	415.0	3.82%	372.8
1997	4.15%	419.6	4.00%	404.6
1998	4.90%	514.9	4.82%	506.6
1999	5.90%	648.8	5.82%	640.6
2000*	6.90%	803.0	6.87%	800.0
2001**	6.95%	885.3	6.94%	884.6
2002	3.95%	543.2	3.40%	468.1
2003	2.50%	358.2	0.94%	134.1
2004	4.37%	635.2	4.33%	629.0

*2000 legislative action does not reflect $266 million of Cigarette Restitution Fund (CRF) appropriations. CRF dollars were excluded because they had not previously been available to the State. The 2000 growth rate including CRF dollars was 9.16%.

**Data from the 2001 session and subsequent years reflect a revised methodology for calculating the spending affordability limit; data from the earlier years reflect the older methodology.

Economy

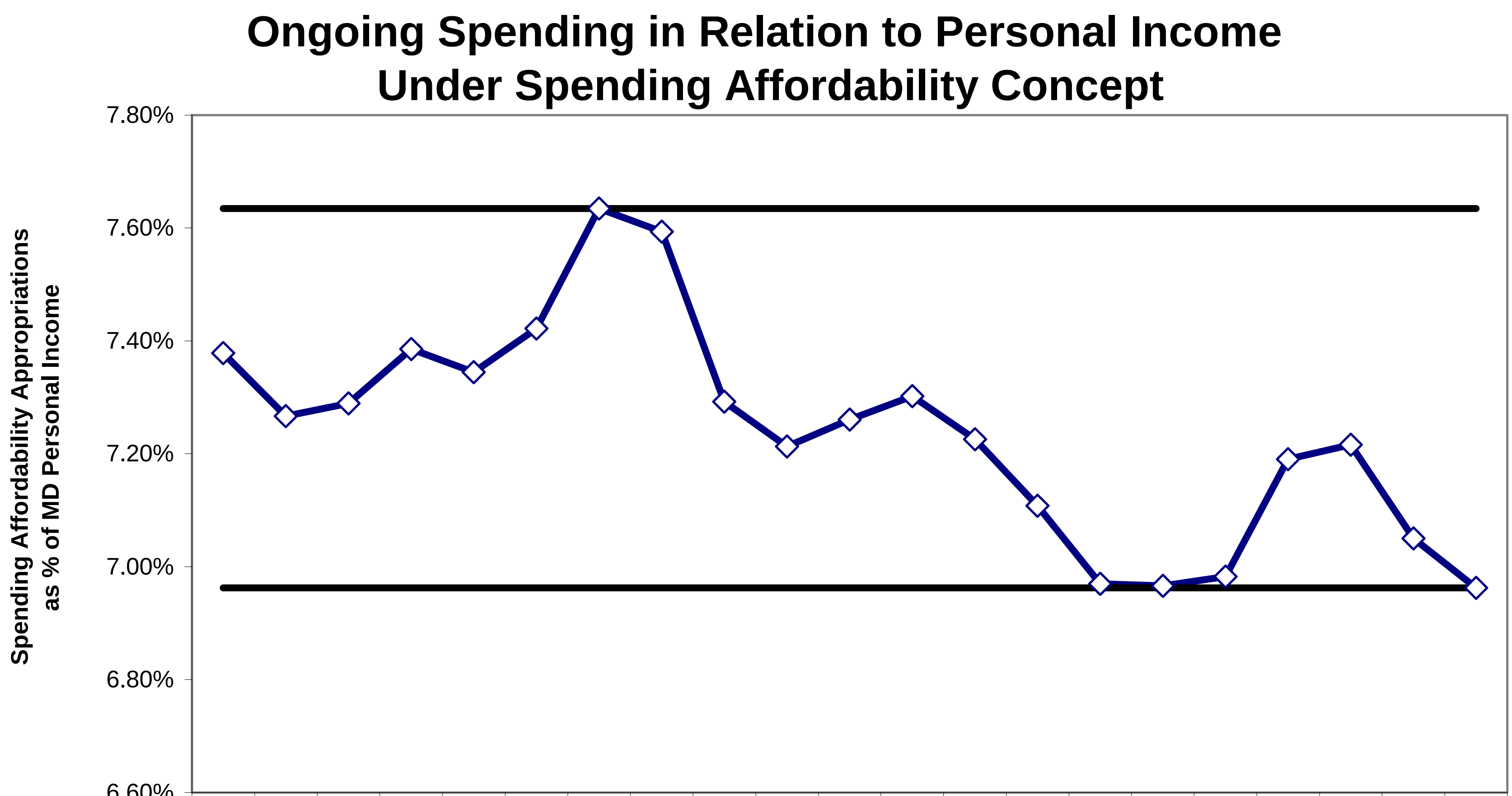
The Maryland economy has begun to experience accelerating growth after three sluggish years. Although the recession that began in March 2001 and ended in November 2001 was relatively mild in Maryland, the State did go through three years with employment growth of less than 1%. In the last two years – 2002 and 2003 – personal income growth was less than 4%. The economic situation turned decidedly more positive starting in early 2004. In the first 10 months of 2004, Maryland employment is 1.4% higher than the same period in 2003, an increase of 35,600 jobs. By comparison, employment for all of 2003 grew by just 0.2% (5,200 jobs). Personal income growth has also accelerated. For the first half of 2004, personal income in Maryland is up almost 5.8%. Wage and salary income is also up almost 5.8% over the same period last year. In 2003 both total personal income and wage and salary income grew just 3.8%.

In light of the improving employment and personal income data, the economic outlook is somewhat better than the forecast from December 2003 that was the basis of the Board of Revenue Estimates revenue projections. At that time, the board was already anticipating that the Maryland economy would improve in 2004 and over the next several years. As a result, the employment outlook today is only slightly better than the board's forecast. In terms of personal income, the outlook is more significantly improved reflecting stronger wage and salary growth and better performance from business income from partnerships and sole proprietorships.

Revenues

The improving economy, along with some other factors, pushed general fund revenues in fiscal 2004 to $10.3 billion, exceeding the estimate for the year by $261 million. Total general fund revenues grew by 9.5% over fiscal 2003. There were a number of law changes between 2003 and 2004 that boosted the increase but adjusting for those factors still results in very strong growth of 7.3% between the two years. The major economic-related revenue sources, the personal income tax, the sales tax and the corporate income tax, combined exceeded their estimates by $176 million. Other revenues sources that are not as directly tied to the economy, the lottery and estate and inheritance taxes, also did well, exceeding their estimates by $18 million and $21 million, respectively.

In October 2004 the Department of Legislative Services (DLS) projected that general fund revenue for fiscal 2005 will be about $455 million higher than the estimate upon which the current budget was based. The DLS estimate represents an increase of 7.2% over fiscal 2004. These figures include $150.6 million from payments to settle back taxes relating to the use of Delaware holding companies. Chapter 557, Acts of 2004 (Senate Bill 187) established a settlement period that ran from July 1, 2004, to November 1, 2004, for corporations that pay taxes owed from the use of Delaware holding companies for tax years 1996 to 2003. If we exclude this one-time revenue, the DLS estimate for fiscal 2005 is higher than the current estimate by $313 million and grows over fiscal 2004 by 5.9%. In fiscal 2006 DLS expects total general fund revenues to grow 3.1% over fiscal 2005 or 4.5% if we exclude the Delaware holding company settlement payments from fiscal 2005.



	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
SA as % of PI	7.38	7.27	7.29	7.39	7.34	7.42	7.63	7.59	7.29	7.21	7.26	7.30	7.23	7.11	6.97	6.97	6.98	7.19	7.22	7.05	6.96
20-year High	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63	7.63
20-year Low	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96	6.96

Budget Requirements

The committee is projecting a general fund balance of $560 million in fiscal 2005. The positive balance is attributable to continued adherence to spending limits supplemented by one-time transfers, the carry-forward of fund balance from the prior year, and one-time revenues associated with the settlement period applicable to Delaware holding companies. These actions are partially offset by potential deficiency appropriations of about $204.6 million to address specific anticipated spending shortfalls during fiscal 2005. Areas projected to require deficiency funding include Medicaid reimbursements for providers, mental health services, foster care placement costs, and expenses related to inmates confined to local jails.

Legislatively mandated increases in education aid and escalating Medicaid expenses underpin the 7.5% increase in operating spending forecast for fiscal 2006. While the forecast does not anticipate a general salary increase for State employees, employment related costs increase significantly as health insurance costs escalate, most employees qualify for increments, and a $600 deferred compensation match is restored.

If no actions are taken to decrease expenditures or generate additional revenue, fiscal 2006 expenditures could exceed revenues by $311 million. Factors contributing to the potential shortfall include a $303 million decline (compared to fiscal 2005) in the availability of one-time transfers and temporary revenues to support spending, mandated increases in education aid, and continued growth in Medicaid spending. With general fund revenues forecast to grow slower than operating expenditures in fiscal 2006, the fiscal 2006 estimate brings the imbalance between ongoing revenues and ongoing operating costs to $780 million. The outlook for future years is no better as spending pressure will exceed the normal growth of revenues through fiscal 2008 under current law.

Recommendations

In light of the considerations discussed above, the committee proposes the following recommendations for the 2005 session:

1. Adjustments to Spending Affordability Calculation

A. Base Adjustments

The 2004 session spending calculation, which serves as the base for the 2005 spending limit, has been adjusted. Adjustments are made to exclude appropriations inadvertently included within the limit at the 2004 session, stabilize the base by recognizing temporary fund shifts, and recognize transportation revenue enhancements approved at the 2004 session.

The final 2004 calculation did not include $13 million in exclusions attributable to special fund capital appropriations in the Department of Agriculture. Reducing the base correspondingly reflects this exclusion. Spending appropriated in the 2004 session but excluded from the spending affordability calculation includes $169 million in temporary federal funds supporting ongoing operating budget activities associated with Medicaid and the Maryland State Police. The base is increased correspondingly to recognize that the federal funds substituted for State funds on a one-time basis. The base is also increased to reflect the Transportation Trust Fund (TTF) revenue enhancement (Chapter 9, Acts of 2004). The legislation increases spending by $166 million. Consistent with actions taken by the Spending Affordability Committee in 1982 after TTF revenue enhancements, the spending calculation is adjusted to reflect the law change.

B. Operating Maintenance Exclusion

For the last four years, operating spending by the Department of General Services (DGS) on facilities maintenance projects above a base funding level of $2 million has been excluded from the spending affordability calculation. The exclusion was initially authorized in the committee's December 2000 report which noted a backlog of operating maintenance projects at State facilities in the magnitude of $47 million. Left unaddressed, the committee recognized that this could lead to further deterioration of the State's infrastructure and lead to higher costs in the long run.

Despite the exclusion, DGS reported in August 2004 that it currently has a $39.8 million backlog of deferred maintenance and repair work and that $26.9 million is rated as a high or medium priority (defined as either posing a high legal or operational risk) or posing a high economic risk (possible damage to other assets). The DGS report includes a plan to eventually eliminate the backlog by increasing the annual deferred maintenance appropriation to $5 million. DGS projects that an annual appropriation of $5 million would eliminate the high and medium priority backlog by fiscal 2015 and the entire backlog by fiscal 2019. These projections assume that new projects accumulate at the historical annual average of $2.4 million a year. **In an effort to reduce the backlog, the committee continues to support the exclusion from the spending affordability calculation of operating maintenance spending by DGS above the historical spending level of $2 million.**

C. Medical Malpractice Exclusion

Medical malpractice insurance rates for most Maryland doctors are scheduled to increase by 33% in January 2005. The State is currently searching for solutions that will moderate the growth in rates and prevent an exodus of physicians. The State's response to the problem may well include an immediate financial commitment that provides temporary relief for physicians while long-term remedies are developed.

If the General Assembly establishes a fund or program supported by adequate revenues to address the increase in malpractice insurance rates, the spending should be excluded from the calculation of the spending affordability limit for the 2005 session.

2. Operating Budget

A. Spending Limit and Sustainability

Appropriations subject to the spending affordability limit shall be limited to growth of no greater than 5.70 % over those approved at the 2004 session. This limit would provide for a $882.6 million increase in appropriations at the 2005 session, allowing for total expenditures subject to spending affordability of $16,367.4 million.

In recognition of the continued structural imbalance in State finances, this limit will require reductions in spending to levels below that estimated to be required to support current services. Budget reductions cannot comprise the whole solution to the State's structural problem; however, even as we limit spending growth to "affordable" levels in economic terms, the committee notes that the existing revenue base of the State is insufficient to support the remaining programs.

The committee, therefore, calls on the Governor and the General Assembly to take the actions necessary to find the revenues required to pay for the cost of government services provided and promised in the future. **Accordingly, the committee recommends that future sustainability be a primary consideration in the development of the fiscal 2006 general fund budget and that the imbalance between revenues and expenditures be erased entirely by fiscal 2007.**

3. State Reserve Fund

A. Rainy Day Fund

In addition to its general fund recommendations, the committee also recommends a prudent use of the Revenue Stabilization Account ("Rainy Day Fund") to address general fund needs. Section 7-311 of the State Finance and Procurement Article establishes the Rainy Day Fund to retain revenues for future needs and guard against future tax increases. The section requires that the fund have at least 5% of the estimated general fund revenues. The statute allows for the withdrawal of funds.

Because the Rainy Day Fund balance is a conspicuous feature of State finance and is relied upon by bond rating agencies and others as a measure of State financial health and management, the committee expects that the fund be managed prudently. The rating agencies advise that use of the Rainy Day Fund during an economic downturn will not impact the State's AAA bond rating. However, they will look closely at the State's plan to restore structural balance between revenues and spending.

Because the Rainy Day Fund balance is projected to exceed 5% of the estimated general fund revenue, the committee supports the withdrawal of funds so long as the closing fund balance exceeds 5%. The committee recommends the State reduce the Rainy Day Fund balance below 5% only if all other available cash balances are exhausted and other options have been fully explored.

B. Repayment of the Transportation Trust Fund

The Budget Reconciliation and Financing Act of 2003 transferred $314.9 million from the TTF to the general fund. Concerned about the sufficiency of funding for future transportation projects, the General Assembly included a provision in the Budget Reconciliation and Financing Act of 2004 instituting a process by which a portion of unappropriated general fund surpluses will reimburse the TTF. The Act requires the annual transfer of any unappropriated general fund surpluses between $10 million and $60 million to the TTF until the entire $314.9 million is repaid. Since the general fund closed fiscal 2004 with a substantial unappropriated fund balance, a $50 million transfer to the TTF is required in fiscal 2006.

In light of the moderate revenue increase available to support the State's transportation needs, the committee recommends that the General Assembly make every effort to approve the $50 million transfer to the TTF in fiscal 2006 and encourages the budget committees to leave a fund balance sufficient to ensure a similar transfer in fiscal 2007.

4. Capital Budget

A. General Obligation Debt

The committee concurs with the recommendation of the Capital Debt Affordability Committee (CDAC) that $670 million in general obligation bonds may be authorized at the 2005 session. This level allows for a $15 million increase in spending over the 2004 session authorization. The recommendation is consistent with the spending plan proposed by the CDAC in the 2003 interim. The $670 million debt authorization includes $5 million to the Tobacco Transition Program. The bond funding may include the issuance of both taxable and tax-exempt debt.

Accordingly, the committee concurs in the recommendation of the Capital Debt Affordability Committee that $670 million in new general obligation bonds may be authorized at the 2005 session. This authorization allows for the use of taxable and tax-exempt bonds and gives the Governor and the legislature considerable flexibility to structure capital financing in the context of the total budget needs of the State.

B. Public School Construction

Chapter 307, Acts of 2004, also referred to as the Public School Facilities Act of 2004, established a State goal to fully fund school construction projects by fiscal 2013 to meet all minimum required standards as of July 2003. The Act was a response to the November 2003 survey results of the Task Force to Study Public School Facilities. The task force concluded that many Maryland public schools were deficient in some capacity and that the cost to bring schools up to standard would be $3.85 billion. Through the Public School Facilities Act, the State would provide $2 billion of the $3.85 billion over the next eight fiscal years, with the remaining balance funded by local governments. The State has currently committed to $800 million ($100 million annually) in the Department of Budget and Management's *Capital Improvement Program*, leaving a $1.2 billion shortfall. Authorizing $150 million annually for eight years would fund the shortfall.

The Act required that CDAC review public school construction needs and make a funding recommendation annually. CDAC recommended to the General Assembly that the State continue to authorize $100 million in public school construction and also analyzed the effect of authorizing an additional $1.2 billion for public school construction. The committee concluded that authorizing this additional debt would not exceed debt capacity as currently defined, yet the committee warned that such a task would limit the State's ability to issue debt for other programs and that changes in personal income could breach affordability measures. CDAC concluded that:

> *"[g]iven the magnitude of the proposed additional funding for school construction, however, the committee recommends fully exploring alternative funding mechanisms, new revenue streams, or shifting other capital projects before considering an additional $1.2 billion in general obligation bond authorizations."*

The committee is concerned about the adequacy of public school construction funding and notes that additional spending for public school construction is affordable, based on CDAC criteria. The committee notes, however, that current general obligation bond debt service expenditure projections will put additional pressure on the general fund in the future. The committee recommends that the General Assembly evaluate the proposed fiscal 2006 capital budget and the progress made toward meeting the funding goal established by the Governor and General Assembly in the Public School Facilities Act of 2004 and consider appropriate action to meet the funding goal.

C. Higher Education Debt

For fiscal 2006 the University System of Maryland intends to issue up to $50 million in auxiliary debt and $25 million in academic debt. This level of issuance will result in a debt service ratio below the 5.5% of current unrestricted funds and mandatory transfers recommended by the system's financial advisers. Morgan State University plans on issuing $10 million in auxiliary debt. St. Mary's College and Baltimore City Community College do not plan on issuing any debt in fiscal 2006.

The committee concurs in the recommendation of the Capital Debt Affordability Committee that $25 million in new academic revenue bonds may be authorized for the University System of Maryland at the 2005 session.

D. Transportation Debt

The Maryland Department of Transportation (MDOT) competes with other State capital projects within debt affordability limits. Transportation debt capacity is limited by the constraints on debt outstanding, debt service coverage, the cash flow needs for projects in the capital program, and overall State debt affordability limits.

The committee recommends that the General Assembly continue to set an annual limit on the level of State transportation debt so as to maintain debt outstanding within the 3.2% of personal income debt affordability criterion and debt service within the 8.0% of revenues debt affordability criterion.

5. Transportation

A. Traditional Debt: Consolidated Transportation Bonds

The 2004 draft *Consolidated Transportation Program* anticipates the issuance of debt by MDOT through fiscal 2010 totaling $1,105 million. Chapter 9, Acts of 2004 raised the maximum outstanding debt limit to $2 billion (from $1.5 billion) concomitant with the adoption of provisions that increased vehicle registration fees. Debt outstanding is projected to reach $1,760 million by fiscal 2010.

To the extent that transportation revenues exceed those projected by MDOT, the committee finds that additional funds should be used to reduce the amount of bonds sold.

B. Financing of the InterCounty Connector

During the 2004 legislative session, MDOT estimated the cost of constructing the InterCounty Connector (ICC) to be approximately $1.7 billion. Based on the findings of the Draft Environmental Impact Statement, the cost of constructing the ICC is now projected to be approximately $2.1 billion, and inflation could add approximately $100 million to that total each year. To meet the increased cost of the ICC, MDOT proposes that the amount of bonds issued by the Maryland Transportation Authority (MdTA) and backed by tolls from extant facilities increase to between $600 and $800 million (from the range of $100 million to $350 million proposed in the draft conceptual financing plan proposed by MDOT during the 2004 session).

MDOT also proposes that approximately $1 billion in grant anticipation revenue vehicles (GARVEE) bonds be issued by MdTA. Under a provision adopted in the Budget Reconciliation and Financing Act of 2004, the maturity of any GARVEE issued by either MDOT or MdTA may not exceed 15 years, while the annual payments for principal and interest on these bonds may not exceed 13% of the State's average annual authorization level in the current federal authorization act for highway aid. These restrictions would allow for the issuance of between $600 million and $700 million in GARVEE bonds, contingent on federal aid receipts. To obtain the statutory authorization needed to issue $1 billion in GARVEEs, MDOT is expected to ask that existing law be modified to allow up to 20% of annual federal highway aid to be utilized to meet the debt service on a GARVEE bond.

In addition to these two types of bonds, MDOT proposes that the remaining financing needed for the ICC be obtained through the issuance of between $400 million and $600 million in MdTA bonds backed by tolls assessed on the ICC, as well as the utilization of between $50 million and $300 million in PAYGO capital from the TTF, and the utilization of a special federal earmark for the project estimated to range between $10 million and $50 million. Under this proposed financing scheme, between 80% and 90% of the entire cost of the project will come from debt issuances.

The committee recommends that the budget committees explore all options available for providing funding for the ICC to determine which combination of options would provide the most prudent and economical financing for the project.

6. Cigarette Restitution Fund

A provision in the Budget Reconciliation and Financing Act of 2002 requires a minimum of 25% of appropriations from the Cigarette Restitution Fund (CRF) to be dedicated to Medicaid through fiscal 2006. With the expiration of this provision, future appropriations to the Medicaid program from the CRF are uncertain. Medicaid costs are currently projected to grow at a rate of more than 8% per year over the next five years; faster than the expected growth in general fund revenues. In light of escalating health care expenses, consistency in CRF support is critical to maintaining an adequate level of support for the Medicaid program. **The committee recommends that the appropriate committees consider legislation to extend for five years the requirement directing a minimum of 25% of CRF appropriations to the Medicaid program.**

7. State Employment

A. Position Ceiling

Given current financial conditions, the prudent allocation of personnel resources is critical. Personnel costs comprise approximately a quarter of the State operating budget, and any effort to permanently reduce personnel spending through position ceilings or other means will help resolve the structural budget gap. Position ceilings imposed by the General Assembly for fiscal 2003, 2004, and 2005 have resulted in a decline in the size of the State's regular workforce from 82,087 full-time equivalent positions in fiscal 2002 to 78,095 in fiscal 2005.

The committee anticipates additional workforce needs in fiscal 2006 to address the Department of Juvenile Services takeover of a previously privatized facility and an ongoing caseload to staff initiative at the Office of the Public Defender. However, the committee notes that exclusive of higher education there are currently almost 4,000 vacant executive branch positions.

The committee recognizes the continuing necessity of limiting the addition of nonessential positions and recommends an Executive Branch position ceiling (excluding higher education) of 52,917 positions, the number of positions currently authorized.

B. Limit on Positions Created

To further constrain the growth in State spending, the committee recommends that the addition of new positions in fiscal 2006 should be limited to:

- **critical public safety and homeland security needs;**
- **facilities scheduled to open in fiscal 2006; and**
- **addressing workload increases and essential services at 24-hour facilities.**

If the Governor finds it necessary to add positions, these additions should be offset with abolitions elsewhere in the State budget. There are currently 3,899 positions vacant in the Executive Branch outside of higher education.

C. Workforce Planning

The recommended position limit should be regarded as a ceiling and not a goal. We expect the Governor and the budget committees to undertake as part of their normal process a critical examination of the necessity of each position to the mission of their agencies and of State Government. In particular, we request that special attention be paid

to the adequacy or excess of positions allocated to particular agencies, and, within agencies, to the proper relationship of positions allocated to overhead and central office functions as opposed to those providing direct services to citizens.

D. Health Insurance

The cost of providing health insurance to State employees and retirees is projected to rise approximately 11% in fiscal 2006, 17% compared to the underfunded fiscal 2005 budget. Cost containment strategies under consideration by the State generally focus on cost shifts from the State to the employees and retirees.

While cost shifting to the employees/retirees is one strategy to consider, the State should also examine innovative case management and joint purchasing initiatives that constrain the growth in overall program costs and thus benefit both the State and the employees/retirees. Any decisions concerning changes to the State's health benefits programs should be arrived at through a collaborative process that includes the Governor, the General Assembly, and the exclusive representatives of the State employees.

Part 1

Economic Outlook

U.S. Employment

- The recession that began in March 2001 officially ended in November of that year, but employment continued to fall until August 2003. Peak to trough, employment fell 2.1%, or about 2.7 million jobs over the course of those 29 months.

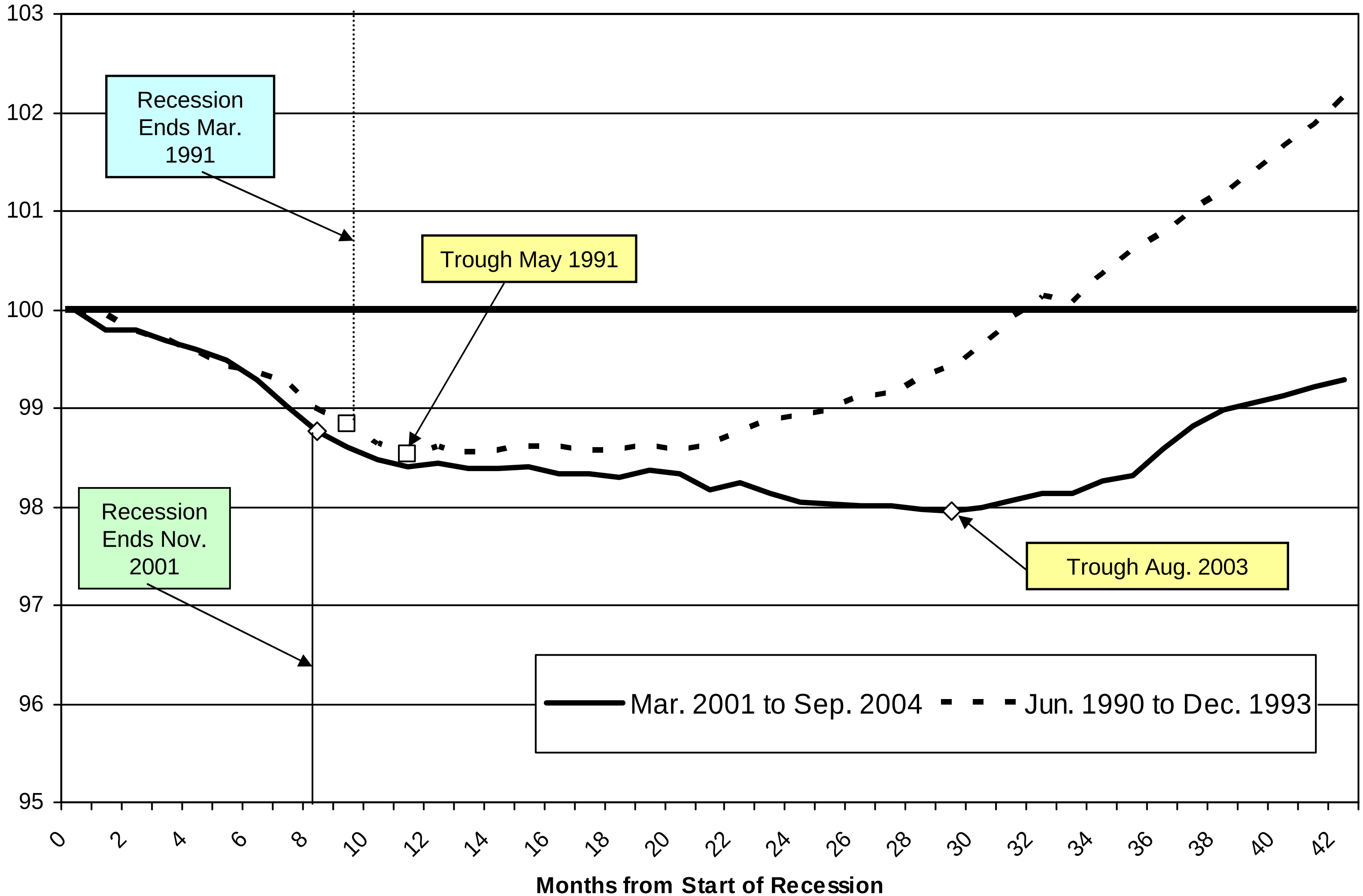
- Since August the U.S. economy has added 1.8 million jobs, an increase of 1.4%. Despite that progress, total employment as of September was below the peak reached in March 2001 by 0.9 million jobs, 42 months after the recession began.

- The recession of the early 1990s officially began in July 1990 (employment peaked in June 1990) and ended in March 1991. Employment bottomed out 11 months later in May 1991 with a peak to trough decline of 1.5%.

- In February 1993 U.S. employment reached a level above the June 1990 peak for the first time, 32 months after the recession began.

- At a similar point in time as we are today, 42 months from the start of the recession, employment in the early 1990s was up 2.2% (December 1993 compared to June 1990).

U.S. Employment – Indexed to Start of Recession



Maryland Employment

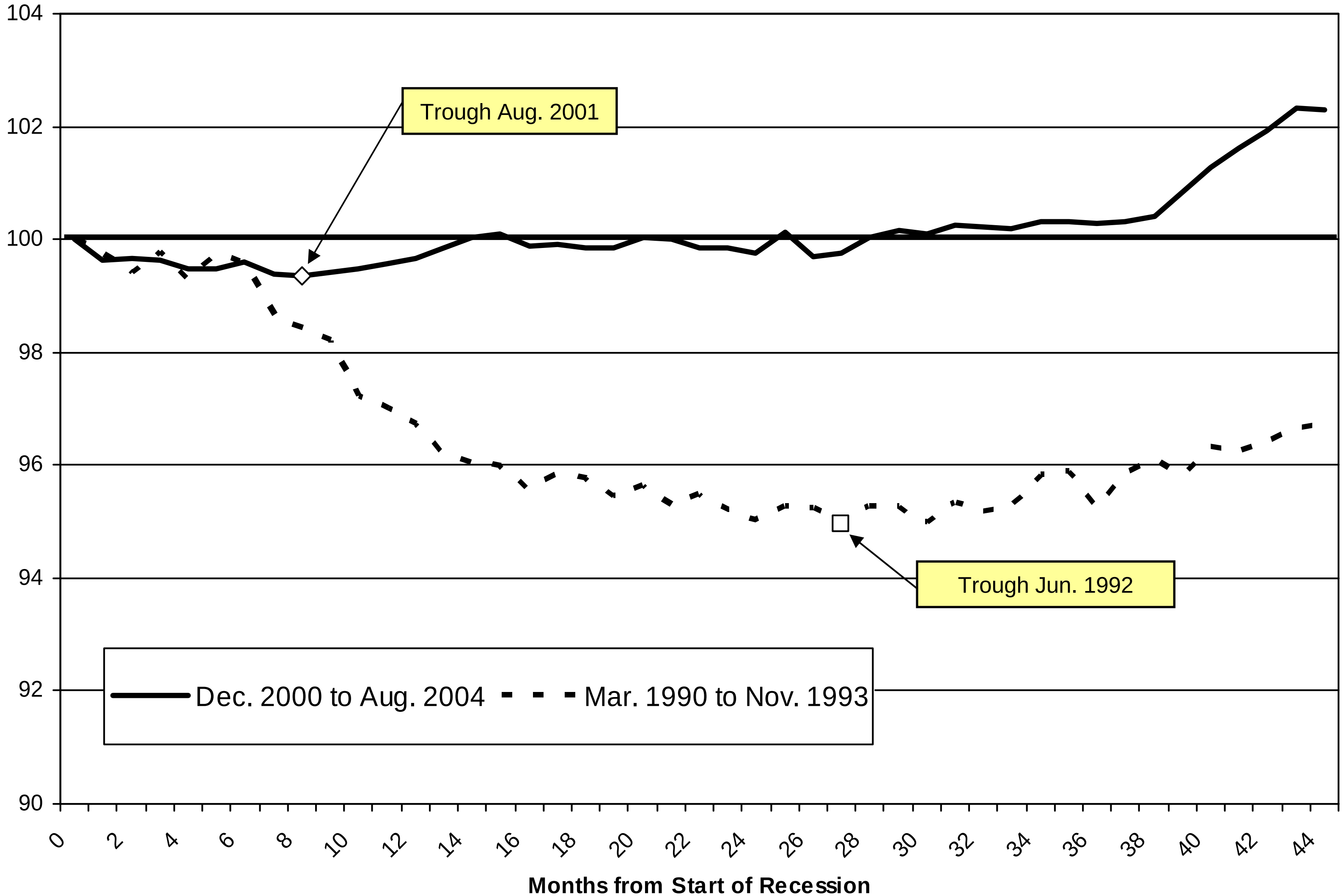
- Employment in Maryland peaked in December 2000 and bottomed out eight months later in August 2001. The total peak to trough decline was 0.7%, or 16,000 jobs. While certain sectors like manufacturing and telecommunications continued to lose substantial numbers of jobs after August 2001, those losses were offset by gains in other areas.

- In February 2002 Maryland employment exceeded the level of December 2000 for the first time. The entire cycle encompassed 14 months.

- The Maryland experience in the recession of the early 1990s was very different. Maryland employment peaked in March 1990 and hit bottom 27 months later in June 1992 with a peak to trough decline of 5.0%. It was not until August 1995, 65 months after the recession began, that employment reached a level above the March 1990 peak.

- At a similar point in time as we are today, 44 months from the start of the recession, employment in the Maryland in the early 1990s was still down by 3.3% (November 1993 compared to March 1990).

Maryland Employment
Indexed to Start of Recession



Change in Maryland Payroll Employment*

	Mar. 1990 to Nov. 1993		Dec. 2000 to Aug. 2004	
	Number	**Percent**	**Number**	**Percent**
Government	200	0.0%	14,700	3.3%
Federal	418	0.3%	1,489	1.2%
State	-2,428	-2.5%	1,424	1.3%
Local	2,211	1.2%	11,787	5.4%
Manufacturing	-26,200	-13.0%	-28,900	-16.7%
Construction & Mining	-41,200	-24.5%	13,200	8.0%
Trade, Transportation, and Utilities	-34,200	-7.5%	-13,200	-2.8%
Transportation and Utilities	-87	-0.1%	-6,011	-7.5%
Trade	-34,113	-8.9%	-7,189	-1.8%
• Wholesale	-9,347	-10.1%	-3,274	-3.5%
• Retail	-24,766	-8.5%	-3,916	-1.3%
Information	-9,200	-17.2%	-11,900	-19.2%
Financial Activities	-5,100	-3.6%	9,500	6.4%
Professional and Business Services	14,500	5.8%	11,600	3.2%
Education and Health Services	35,400	16.0%	34,900	11.1%
Leisure and Hospitality	-2,700	-1.5%	28,000	13.4%
Other Services	-2,800	-2.9%	2,100	1.8%
Total	**-71,300**	**-3.3%**	**57,100**	**2.3%**

* Seasonally adjusted; detail may not add to the total.

Sources: U.S. Department of Labor and Economy.com, Inc.

Maryland Economic Forecasts
December 2003 Compared to September 2004

Year-over-year Percent Change

Calendar	Employment		Personal Income	
Year	**Dec. 2003**	**Sep. 2004**	**Dec. 2003**	**Sep. 2004**
2001	0.7%	0.7%	5.0%	5.1%
2002	0.2%	0.4%	3.8%	3.8%
2003	0.4% *	0.2%	3.1% *	3.8%
2004E	1.3%	1.5%	4.6%	5.6%
2005E	1.9%	2.1%	5.5%	5.7%
2006E	1.9%	2.0%	5.3%	5.9%
2007E	1.7%	1.8%	4.8%	5.5%

* Estimates

Source: Board of Revenue Estimates; Department of Legislative Services

Part 2

General Fund Revenues

Fiscal 2004 General Fund Revenues
($ in Millions)

Source	Actual FY 2003	Fiscal 2004 Estimate*	Fiscal 2004 Actual	Fiscal 2004 Difference	Percent Change FY 2003-2004
Personal Income Tax	$4,703.7	$4,988.7	$5,077.6	$88.9	7.9%
Sales and Use Tax	2,697.1	2,865.4	2,921.8	56.4	8.3%
State Lottery	422.9	418.8	436.4	17.6	3.2%
Corporate Income Tax	288.3	297.9	328.6	30.7	14.0%
Business Franchise Taxes (1)	143.4	188.2	190.6	2.4	33.0%
Insurance Premiums Tax	228.5	246.7	260.0	13.4	13.8%
Estate & Inheritance Taxes	142.3	132.8	153.8	21.0	8.1%
Tobacco Tax (2)	199.2	269.1	272.4	3.3	36.8%
Alcohol Beverages Tax	25.7	26.4	26.9	0.4	4.7%
Motor Vehicle Fuel Tax	12.5	12.8	13.0	0.3	4.0%
District Courts	71.6	81.1	84.4	3.3	17.9%
Clerks of the Court	51.6	54.0	56.8	2.8	10.2%
Hospital Patient Recoveries (3)	73.7	78.4	90.9	12.4	23.3%
Interest on Investments	31.9	27.1	26.6	-0.5	-16.6%
Miscellaneous (4)	224.8	292.7	301.0	8.2	33.9%
Total Current Revenues	**$9,317.0**	**$9,980.1**	**$10,240.7**	**$260.6**	**9.9%**
Delaware Holding Co. Settlements (5)		11.5	11.5	0.0	n/a
Temporary Federal Medicaid Aid	33.4				
Miscellaneous Transfers	12.1	2.5	2.5		
Grand Total	**$9,362.5**	**$9,994.2**	**$10,254.7**	**$260.6**	**9.5%**

* From the Board of Revenue Estimates, March 2004 with adjustments for action at the 2004 legislative session.

(1) Fiscal 2004 reflects the increase in corporate filing fees authorized by the Budget Reconciliation and Financing Act of 2003. The Board of Revenues Estimates expected filing fee revenue to total $49.7 million in fiscal 2004. Actual filing fees in fiscal 2004 were $52.3 million compared to $14.4 million in fiscal 2003.

(2) In fiscal 2003, $79.7 million of tobacco tax revenue was placed in a special fund for local education aid. In fiscal 2004 all tobacco tax revenue was once again in the general fund, accounting for the large increase.

(3) SB 323 (2002 session) stipulated that $14.0 million of disproportionate share payments in fiscal 2003 be put in a special fund used for the State's mental hygiene deficit. In fiscal 2004 all disproportionate share payments were once again in the general fund.

(4) SB 323 (2002 session) reduced the time period for property to be declared abandoned from five years to four in fiscal 2003 and from four years to three in fiscal 2004. Beginning in fiscal 2004, local reimbursements for teachers' retirement costs associated with federally funded positions moved back into the general fund.

(5) A total of $15.2 million in corporate income tax payments were received under the Comptroller's settlement offer relating to the use of Delaware holding companies. Of that amount, $11.5 million went to the general fund and $3.7 million went to the Transportation Trust Fund. Because the revenue is of a one-time nature, it is not included with the corporate income tax.

Fiscal 2005 General Fund Revenues
($ in Millions)

Source	FY 2004	FY 2005	$ Difference	% Difference
	Fiscal Year through September			
Personal Income Tax [(1)]	$817.6	$1,055.6	$238.0	29.1%
Sales and Use Tax	464.7	496.3	31.7	6.8%
State Lottery	100.0	100.8	0.9	0.9%
Corporate Income Tax	73.0	105.5	32.5	44.5%
Business Franchise Taxes	33.8	38.8	5.0	14.8%
Insurance Premiums Tax	57.0	62.0	5.0	8.8%
Estate and Inheritance Taxes	29.9	58.9	28.9	96.8%
Tobacco Tax	54.0	58.2	4.2	7.9%
Alcohol Beverages Tax	4.4	4.6	0.2	4.0%
Motor Vehicle Fuel Tax	1.1	1.1	0.0	1.7%
District Courts	19.5	22.0	2.5	13.0%
Clerks of the Court	13.7	16.9	3.2	23.0%
Hospital Patient Recoveries [(2)]	3.1	1.3	-1.9	-58.9%
Interest on Investments	2.7	2.7	0.1	2.3%
Miscellaneous	$27.832	29.1	1.3	4.6%
Current Revenues	**$1,702.3**	**$2,054.0**	**$351.6**	**20.7%**
Delaware Holding Co. Settlements [(3)]		$45.4		
Total Revenues	**$1,702.3**	**$2,099.4**	**$397.0**	**23.3%**

(1) Fiscal 2005 collections reflect certain law changes that were not in effect at this time last year. Specifically, these law changes include flat withholding, an accelerated schedule for paying withholding and increasing the safe harbor for estimated payments from 100% of the prior year's liability to 110%. All of these provisions have the effect of artificially inflating current collections relative to last year but it is not possible to quantify the effect.

(2) Includes revenues from Medicare, insurance, and sponsors only.

(3) SB 187 established a settlement period applicable to corporate income tax that has been or may be assessed by the Comptroller relating to the use of Delaware holding companies. The settlement period runs from July 1, 2004, to November 1, 2004. Through September, $59.7 million in net collections have been received, 76% of which is credited to the general fund.

General Fund Revenue Projections

($ in Millions)

Source	FY 2004 Actual	---- FY 2005 Estimate ---- May*	October	$ Diff.	% Change FY04-05	FY 2006 Estimate	% Change FY05-06
Personal Income Tax [1]	$5,077.6	$5,350.9	$5,388.1	$37.2	6.1%	$5,702.3	5.8%
Sales and Use Tax	2,921.8	2,971.1	3,104.4	133.3	6.2%	3,254.8	4.8%
State Lottery	436.4	441.4	441.4	-0.1	1.1%	457.8	3.7%
Corporate Income Tax [2]	328.6	376.3	395.1	18.7	20.3%	451.7	14.3%
Business Franchise Taxes	190.6	193.8	190.5	-3.4	-0.1%	193.6	1.6%
Insurance Premiums Tax	260.0	254.1	275.6	21.6	6.0%	289.9	5.2%
Estate and Inheritance Taxes	153.8	139.8	154.0	14.2	0.1%	152.5	-1.0%
Tobacco Tax	272.4	264.3	268.9	4.7	-1.3%	263.6	-2.0%
Alcohol Beverages Tax	26.9	26.7	27.4	0.6	1.9%	27.8	1.5%
Motor Vehicle Fuel Tax	13.0	13.1	13.3	0.2	1.8%	13.4	1.4%
District Courts	84.4	79.4	85.8	6.4	1.6%	87.1	1.6%
Clerks of the Court	56.8	43.7	53.7	10.1	-5.4%	49.8	-7.3%
Hospital Patient Recoveries	90.9	79.0	83.4	4.5	-8.2%	83.1	-0.4%
Interest on Investments	26.6	48.4	76.7	28.3	188.2%	69.5	-9.3%
Miscellaneous [3]	301.0	251.7	288.1	36.4	-4.3%	240.7	-16.4%
Total Current Revenues	**$10,240.7**	**$10,533.6**	**$10,846.2**	**$312.6**	**5.9%**	**$11,337.9**	**4.5%**
Delaware Holding Co. Settlements [4]	11.5	8.3	151.0	142.8	n/a	0.0	n/a
Miscellaneous Transfers	2.5	0.0	0.0	0.0	n/a	0.0	n/a
Grand Total	**$10,254.7**	**$10,541.9**	**$10,997.3**	**$455.4**	**7.2%**	**$11,337.9**	**3.1%**

* From the Board of Revenue Estimates, March 2004, with adjustments for legislative action at the 2004 session.

Footnotes for General Fund Revenue Projections

(1) Fiscal 2005 and 2006 reflect the impact of provisions from the Budget Reconciliation and Financing Act of 2004 which imposed a tax equal to the lowest county income tax on nonresidents and decoupled the Maryland tax from the Federal depreciation deduction for large sport utility vehicles used for business purposes.

(2) Fiscal 2005 and 2006 reflect the impact of HB 297 (2004 session) which prevents corporations from avoiding Maryland tax by shifting income away from the State through the use of a Delaware holding company and other tax avoidance techniques. Also included is the impact of the Budget Reconciliation and Financing Act of 2004 provision that decoupled from the Federal depreciation deduction for large sport utility vehicles.

(3) In fiscal 2005 revenues from abandoned property are expected to be around $97 million reflecting the demutualization of several insurance companies. In March 2004 the Board of Revenue Estimates increased the miscellaneous estimate by $30 million in fiscal 2004 and $23 million in fiscal 2005 to reflect this additional abandoned property. However, the revenue was not received in fiscal 2004 so the entire amount is now expected in fiscal 2005. In fiscal 2006 abandoned property revenues are expected to fall to an average level (around $45 million) accounting for much of the drop in miscellaneous revenues.

(4) SB 187 established a settlement period applicable to corporate income tax that has been or may be assessed by the Comptroller relating to the use of Delaware holding companies. The settlement period runs from July 1, 2004, to November 1, 2004. Through September, $59.7 million in net collections have been received, 76% of which is credited to the general fund. The estimate assumes the general fund will receive an additional $25 million in net payments between now and the end of the settlement period.

Part 3

General Fund Budget

Executive Summary

- Economic and general fund revenue performance have improved materially since the 2005 budget was passed.

- The effect of better revenues is offset, however, by big budget deficiencies in fiscal 2005 and pressure for spending growth in excess of revenue growth in fiscal 2006.

- Although the structural shortfall narrowed considerably in fiscal 2004 and 2005, under current policies the structural gap will widen in fiscal 2006.

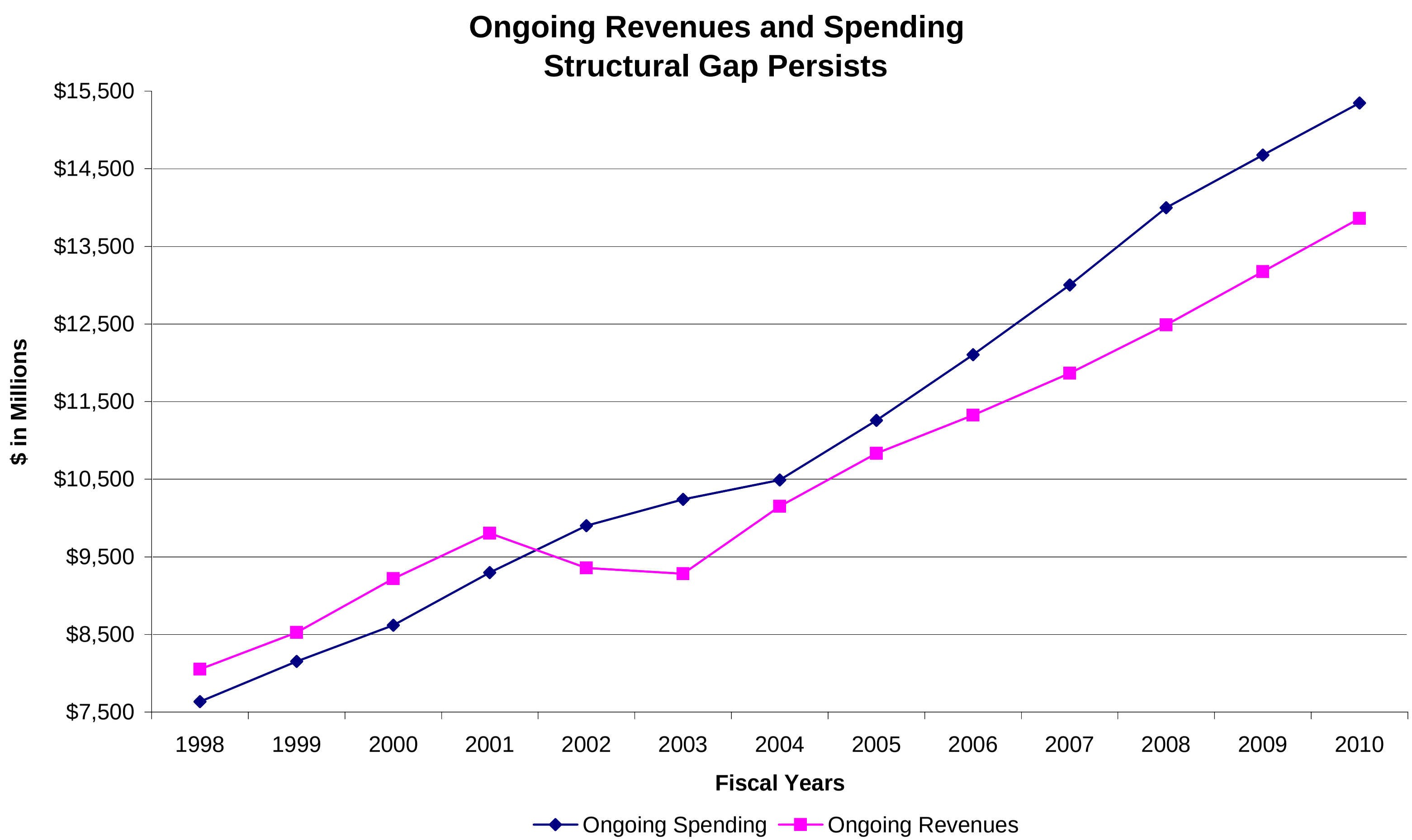
General Fund: Recent History and Outlook

Fiscal 2003 – 2006
($ in Millions)

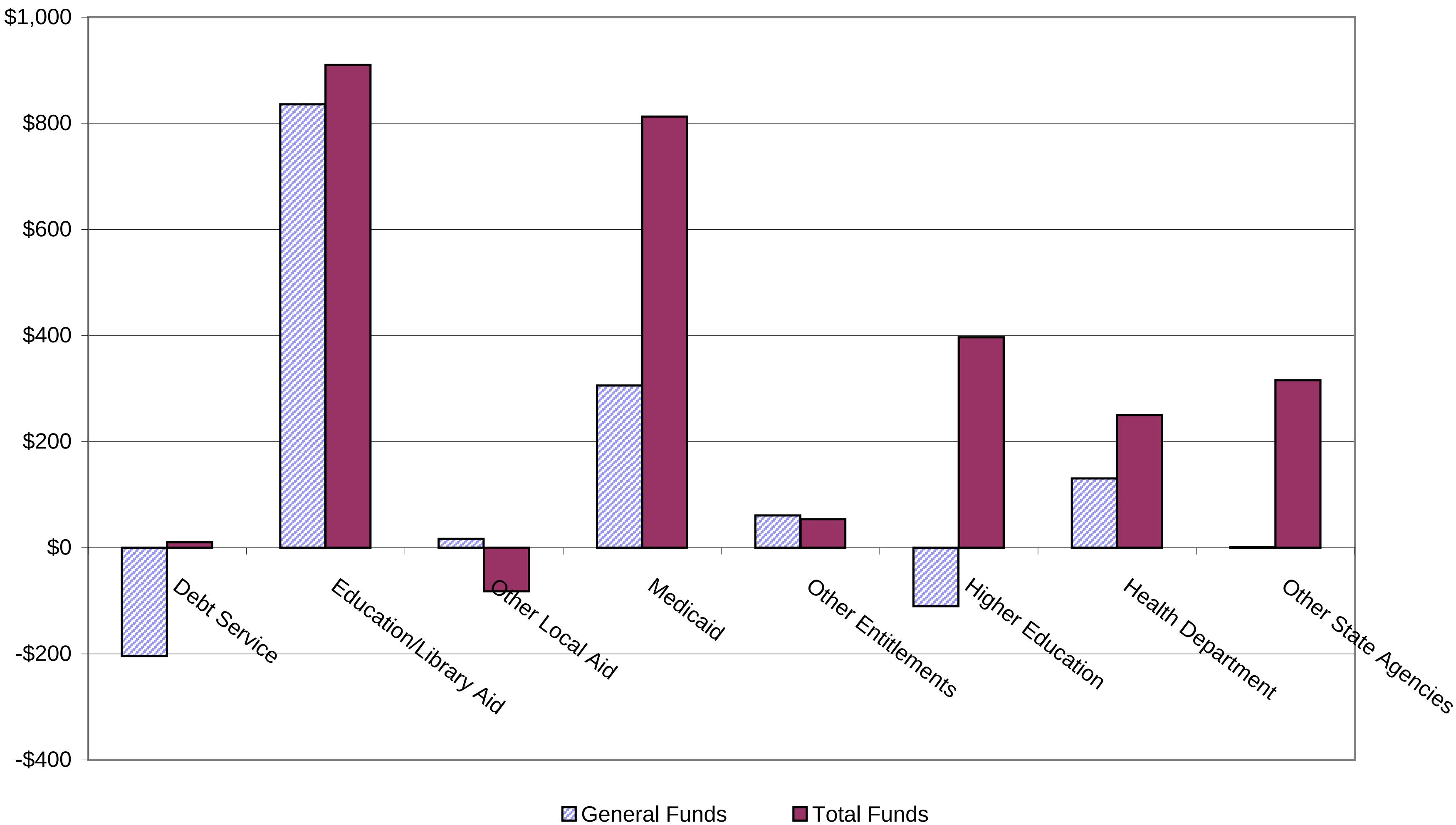
	Actual		Forecast	
	FY 2003	FY 2004	FY 2005	FY 2006
Funds Available				
Ongoing Revenues	$9,281	$10,151	$10,831	$11,325
Balances and Transfers	1,124	469	927	779
One-time Federal Aid	123	227	0	0
Short-term Revenues	48	103	166	13
Subtotal Funds Available	**$10,577**	**$10,951**	**$11,924**	**$12,116**
Appropriations, Deficiencies, and Cost Containment				
Ongoing Operating Costs and Deficiencies	$10,240	$10,488	$11,256	$12,105
Prior Year Withdrawn Appropriations/Reversions	2	0	0	0
Capital	31	1	1	3
Appropriations to Reserve Fund/Heritage Tax	181	10	107	320
Subtotal Spending	**$10,454**	**$10,498**	**$11,364**	**$12,427**
Cash Balance/Shortfall	**$123**	**$453**	**$560**	**-$311**
Structural				
Balance (Ongoing revenues less operating costs)	**-$958**	**-$337**	**-$425**	**-$780**
Ratio (Ongoing revenues/operating costs)	**91%**	**97%**	**96%**	**94%**
Reserve Fund Activity				
Appropriations to Rainy Day Fund	$181	$0	$104	$250
Transfers to General Fund	-249	0	-91	-218
Net Change	**-$68**	**$0**	**$13**	**$31**
Estimated Rainy Day Fund Balance – June 30	**$490**	**$497**	**$519**	**$567**

The Shrinking Budget Gap
What a Difference Several Months Make
($ in Millions)

FY 2006 Budget Gap (June 2004)	**-$1,062**
Actual Fiscal 2004 Spending Lower Than Budgeted	12
Actual Fiscal 2004 Revenues Higher Than Estimated	261
Transfers to Accounting Reserves	-50
Revised Fiscal 2005 Revenue Forecast	376
Estimated Fiscal 2005 Deficiencies	-205
Revised Fiscal 2006 Revenue Forecast	401
Revised Fiscal 2006 Expenditure Forecast	-121
FY 2006 Estimated Budget Gap (DLS – October 2004)	**-$388**


Ongoing Revenues and Spending
Structural Gap Persists
$ in Millions
$15,500
$14,500
$13,500
$12,500
$11,500
$10,500
$9,500
$8,500
$7,500
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
Fiscal Years
Ongoing Spending
Ongoing Revenues

Changes in General and Total Fund Spending
Fiscal 2002 – 2005
($ in Millions)



2006 Baseline Budget Forecast Assumptions

Baseline Budget Concepts

- Current laws, policies, and practices are continued.
- Inflationary increases are recognized.
- Large one-time purchases and nonrecurring PAYGO expenditures are removed.
- Anticipated deficiencies are identified.
- Federal mandates and multi-year commitments are observed.
- Legislation adopted at the prior session is funded.
- Nondiscretionary changes in workload are recognized.
- Full year costs of programs started during the previous year are included.
- Positions and operating expenses associated with new facilities are recognized.
- Employee turnover is adjusted to reflect recent experience.

Caseload Assumptions

	FY 2004	FY 2005	FY 2006	Percent Change FY 05-06
Pupil Enrollment *	821,984	828,961	835,653	0.8%
Medicaid	502,910	515,052	523,533	1.6%
Children's Health	97,564	102,442	107,564	5.0%
Temporary Cash Asst.	71,179	68,469	68,469	0.0%
Foster Care/Adoption	14,531	14,854	15,278	2.9%

* Data for 2004, 2005, and 2006 reflect 9/02, 9/03, and 9/04 (est.) full-time equivalent enrollments.

2006 Baseline Budget Forecast Assumptions (Cont.)

Inflation Assumptions

- Employee Health Insurance (10% annual inflation since fiscal 2004. Fiscal 2005 and 2006 costs reflect contracts approved by the Board of Public Works in September 2004).
- Medical Contracts and Supplies (5%).
- Prescription Drugs for State Facilities (9%).
- Utilities (20%).
- Food (6%).

Employee Compensation

- Merit increases of 2% and 4% based on salary plan.
- Fully fund deferred compensation program.
- No general salary increase for fiscal 2006. (1% equals $20 million in general funds.)

Other Assumptions

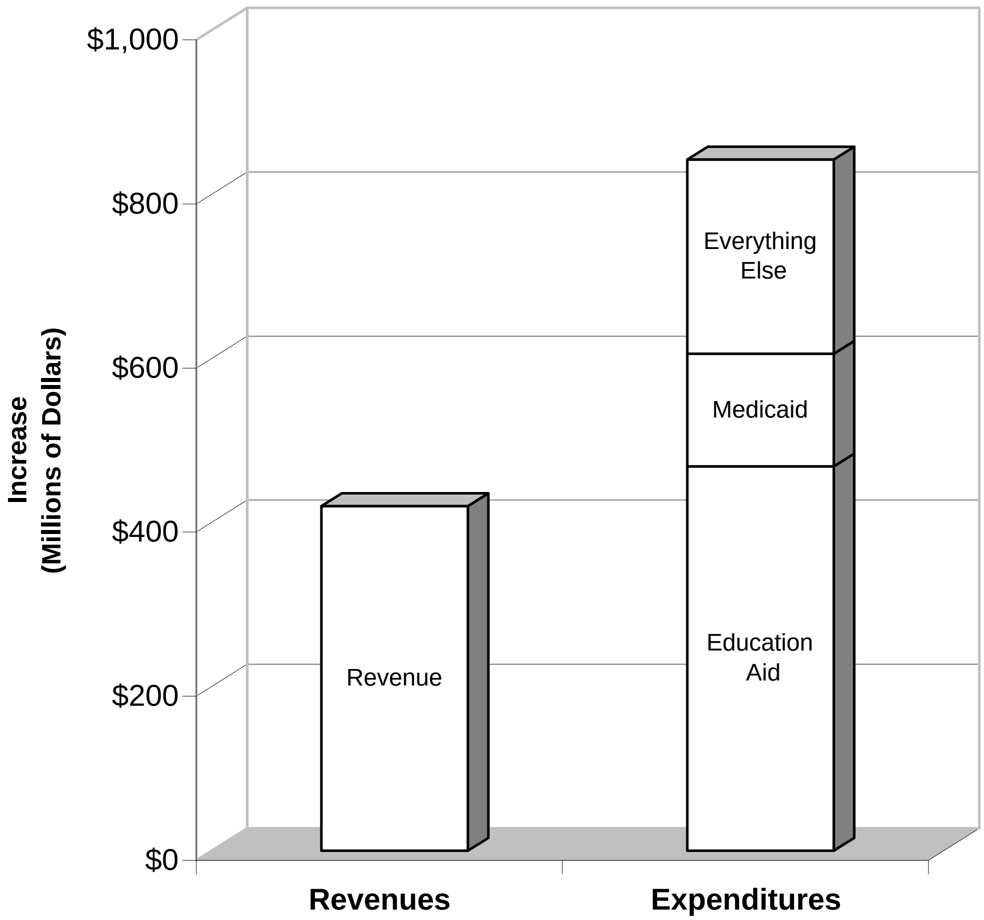
- Cost increases for the University System of Maryland and Morgan State University are allocated between general funds and tuition and fees based on the current ratio of general funds to tuition and fees.
- No fiscal impact from Congressional re-authorization of Temporary Assistance for Needy Families (TANF) funding is assumed.
- $25 million TANF bonus payment for reduction in out-of-wedlock births offsets $18 million of inappropriate charges to federal funds by the Department of Human Resources at fiscal 2003 closeout and substitutes for $7 million of general funds in fiscal 2006.
- Insufficient Cigarette Restitution Funds (CRF) exist to maintain fiscal 2005 spending level and restore the tobacco program to the statutorily mandated level. The baseline assumes full funding of the tobacco program with CRF dollars and substitutes general funds for CRF to fully fund Medicaid.

Potential Fiscal 2005 General Fund Deficiencies
($ in Millions)

Explanation	General Funds
Medicaid: Fiscal 2005 budget developed on underfunded fiscal 2004 base ($25 million), unbudgeted calendar 2005 MCO rate increase ($23 million), and unfavorable trends in utilization/inflation ($22 million).	$70.0
Medicaid/Mental Health: Pay prior year bills with fiscal 2005 dollars.	44.1
Foster Care: Caseload growth and underattainment of federal funds.	38.7
Mental Health: Uncollectible federal fund receivables.	15.0
Local Jail Reimbursement Payments: Reimburse local jails for all prior year costs as required by Budget Reconciliation and Financing Act of 2004.	14.6
Maryland State Department of Education: Loss of federal Medicaid dollars to cover 50% of certain day services for children with autism and underfunding of nonpublic placements.	13.5
Juvenile Services:	
Fiscal 2005 per diem placement costs exceed budget.	3.1
Prior year per diem placement costs.	1.3
Maryland Stadium Authority: State share of Baltimore City Convention Center deficit exceeds appropriation.	2.0
DPSCS: Operating costs related to medical contract and utilities.	1.6
Other: Maryland State Police, State Treasurer, and Canal Place.	0.6
Total General Fund Deficiencies	**$204.6**

DPSCS = Department of Public Safety and Correctional Services

Baseline Expenditure Increase Twice the Increase in General Fund Revenues
Fiscal 2006



State Expenditures – General Funds
($ in Millions)

Category	Work. Appr. FY 2004	Leg. Appr. FY 2005	Baseline FY 2006	$ Diff. 05 to 06	% Diff. 05 to 06
Debt Service	$0.0	$0.0	$0.0	$0.0	n/a
Aid to Local Governments					
General Government	206.0	208.3	213.1	4.9	2.3%
Community Colleges	174.9	184.0	193.5	9.5	5.1%
Education/Libraries	3,369.4	3,683.2	4,164.8	481.6	13.1%
Health	60.4	60.9	63.1	2.2	3.6%
	$3,810.7	**$4,136.4**	**$4,634.6**	**$498.2**	**12.0%**
Entitlements					
Foster Care Payments	169.3	172.5	224.7	52.1	30.2%
Assistance Payments	86.6	75.6	74.2	-1.4	-1.8%
Medical Assistance	1,624.4	1,848.8	2,081.1	232.3	12.6%
Property Tax Credits	48.9	47.7	47.8	0.1	0.2%
	$1,929.1	**$2,144.6**	**$2,427.8**	**$283.2**	**13.2%**
State Agencies					
Health	1,183.7	1,223.8	1,258.4	34.6	2.8%
Human Resources	294.5	318.0	317.9	-0.1	0.0%
Systems Reform Initiative	26.9	36.0	36.0	0.0	0.0%
Juvenile Services	169.3	173.5	183.4	9.9	5.7%
Public Safety/Police	842.6	953.0	1,043.7	90.6	9.5%
Higher Education	837.5	851.0	906.4	55.5	6.5%
Other Education	262.3	283.7	301.0	17.2	6.1%
Agric./Natl. Res./Environment	135.6	130.2	135.4	5.2	4.0%
Other Executive Agencies	461.8	495.5	546.0	50.5	10.2%
Judicial/Legislative	334.9	341.9	349.4	7.5	2.2%
	$4,549.0	**$4,806.5**	**$5,077.4**	**$270.9**	**5.6%**
Deficiencies	0.0	204.6	0.0	-204.6	-100.0%
Subtotal	**$10,288.8**	**$11,292.2**	**$12,139.8**	**$847.6**	**7.5%**
Capital	0.7	1.2	3.0	1.8	150.0%
Heritage Reserve Fund	0.0	0.0	20.0	20.0	n/a
Reserve Fund	10.0	106.7	299.7	193.0	181.0%
Appropriations	**$10,299.5**	**$11,400.0**	**$12,462.5**	**$1,062.4**	**9.3%**
Reversions	-37.2	-36.0	-35.0	1.0	-2.8%
Grand Total	**$10,262.3**	**$11,364.0**	**$12,427.5**	**$1,063.4**	**9.4%**

Components of Budget Change
($ in Millions)

Summary of Budget Change	Dollars	Share of Growth
Ongoing Requirements/Entitlements	$756.8	71%
Legislation	79.4	7%
Commitments	24.9	2%
State Agency Costs	211.0	20%
Subtotal Operating Budget	**$1,072.2**	**100%**
PAYGO	1.8	
Appropriation to Reserve Fund	193.0	
Total Baseline Increase in State Expenditures	**$1,267.00**	
Less Deficiency Appropriations	-204.6	
Total	**$1,062.4**	

Detail on Components
($ in Millions)

Ongoing Requirements/Entitlements		**$756.8**
Education Formulas	$405.0	
Medical Assistance – Enrollment, Inflation, MCO Rates, and Prior Underfunding	225.1	
Foster Care − Caseload and Lower Federal Fund Attainment	52.1	
Higher Education (St. Mary's College, Community Colleges, BCCC, Sellinger Formula)	23.2	
Special Education – No Federal Funds for Day Habilitation Services for Children with Autism and Growth in Nonpublic Placement Costs	13.5	
Wage Initiative for Providers Serving Developmentally Disabled − Chapter 722, Acts of 2001	11.2	
Mental Hygiene − Inflation and Utilization	8.4	
Per Diem Reimbursements for Inmates in Local Facilities	6.3	
Disparity Grant for Low Wealth Counties	3.5	
Formula Aid to Local Governments for Police Protection and Health	3.5	
Formulas for Maryland School for the Deaf & Maryland School for the Blind	2.5	
Private Donation Incentive Program – Fund Deferrals	1.6	
Library Formula Aid and Retirement	0.5	
Mandated Salary Increases for Constitutional Officers/General Assembly	0.6	
Mandated Funding for Operating Deficits at Baltimore City Convention Center	0.5	
Mandated Increase for Maryland State Arts Council	0.4	
Maryland Tourism Board	0.1	
Other Local Aid	0.1	
Temporary Cash Assistance – Modest Caseload Decline	-1.4	

Detail on Components (Continued)
($ in Millions)

Legislation		**$79.4**
Geographic Cost of Education Index	$54.2	
Heritage Tax Credit Reserve Fund – Chapter 76, Acts of 2004	20.0	
Hold Harmless Provision for Aging Schools Funding	1.7	
Other Legislation with Impact Less Than $1 Million	3.5	
Commitments		**$24.9**
Major Information Technology Projects per DBM Schedule	10.9	
Lease Payments for Wiring Schools for Technology Project	6.6	
Increase Staffing Levels at Office of the Public Defender	4.4	
Annualize Fiscal 2005 Cost of New Community Placements of Developmentally Disabled	2.0	
New Facilities/Facility Expansions (Crime Laboratory, Police Barrack, Etc.)	1.0	
State Agency Costs		**$211.0**
Employee Health Insurance	57.0	
Employee Increments	48.0	
University System of Maryland and Morgan State University	47.9	
Public Safety's Inmate Medical Contract	31.0	
Increase in Retirement Rates	20.4	
Restore $600 Deferred Compensation Match	9.0	
Shift Medicaid Expenses from CRF to General Funds	6.5	
Dept. of Juvenile Services − Residential Placement Costs Rise Due to Underfunding and Caseload Increases	4.4	
Child Care Subsidies − Caseload Increases	4.0	
Workers' Compensation Charges	3.9	
Other Changes	-4.3	
Federal Bonus for Reducing Out-of-wedlock Births Reduces Need for General Funds	-7.0	
Vacancy Rate Adjusted to Reflect Current Experience of More Than 5%	-9.8	
PAYGO		**$1.8**
State Reserve Fund		**$193.0**
Sweeper: Unappropriated Fund Balance from Fiscal 2004 to State Reserve Fund	146.0	
Dedicated Purpose Fund to Receive First $50 Million of Unappropriated Fund Balance for Repayment of Transportation Trust Fund	50.0	
Remove One-time Hurricane Isabel Funds	-3.0	

State Expenditures – General Funds
($ in Millions)

Category	Actual FY 2002	Leg. Appr. FY 2005	$ Diff. 02 to 05	% Diff. 02 to 05
Debt Service	$204.0	$0.0	-$204.0	-100.0%
Aid to Local Governments				
General Government	200.5	208.3	7.8	3.9%
Community Colleges	178.6	184.0	5.4	3.0%
Education/Libraries	2,847.4	3,683.2	835.8	29.4%
Health	57.3	60.9	3.5	6.2%
	$3,283.9	**$4,136.4**	**$852.5**	**26.0%**
Entitlements				
Foster Care Payments	117.7	172.5	54.8	46.6%
Assistance Payments	65.2	75.6	10.3	15.9%
Medical Assistance	1,543.1	1,848.8	305.7	19.8%
Property Tax Credits	52.0	47.7	-4.4	-8.4%
	$1,778.1	**$2,144.6**	**$366.5**	**20.6%**
State Agencies				
Health	1,093.1	1,223.8	130.7	12.0%
Human Resources	299.8	318.0	18.2	6.1%
Systems Reform Initiative	40.1	36.0	-4.2	-10.4%
Juvenile Services	161.3	173.5	12.3	7.6%
Public Safety/Police	921.0	953.0	32.0	3.5%
Higher Education	961.3	851.0	-110.3	-11.5%
Other Education	276.0	283.7	7.7	2.8%
Agric./Natl. Res./Environment	147.3	130.2	-17.1	-11.6%
Other Executive Agencies	570.9	495.5	-75.5	-13.2%
Judicial/Legislative	314.8	341.9	27.0	8.6%
	$4,785.6	**$4,806.5**	**$20.9**	**0.4%**
Deficiencies	0.0	204.6	204.6	n/a
Subtotal	**$10,051.6**	**$11,292.2**	**$1,240.6**	**12.3%**
Capital	299.0	1.2	-297.8	-99.6%
Reserve Fund	221.8	106.7	-115.1	-51.9%
Appropriations	**$10,572.3**	**$11,400.0**	**$827.7**	**7.8%**
Reversions	0.0	-36.0	-36.0	n/a
Grand Total	**$10,572.3**	**$11,364.0**	**$791.7**	**7.5%**

Part 4

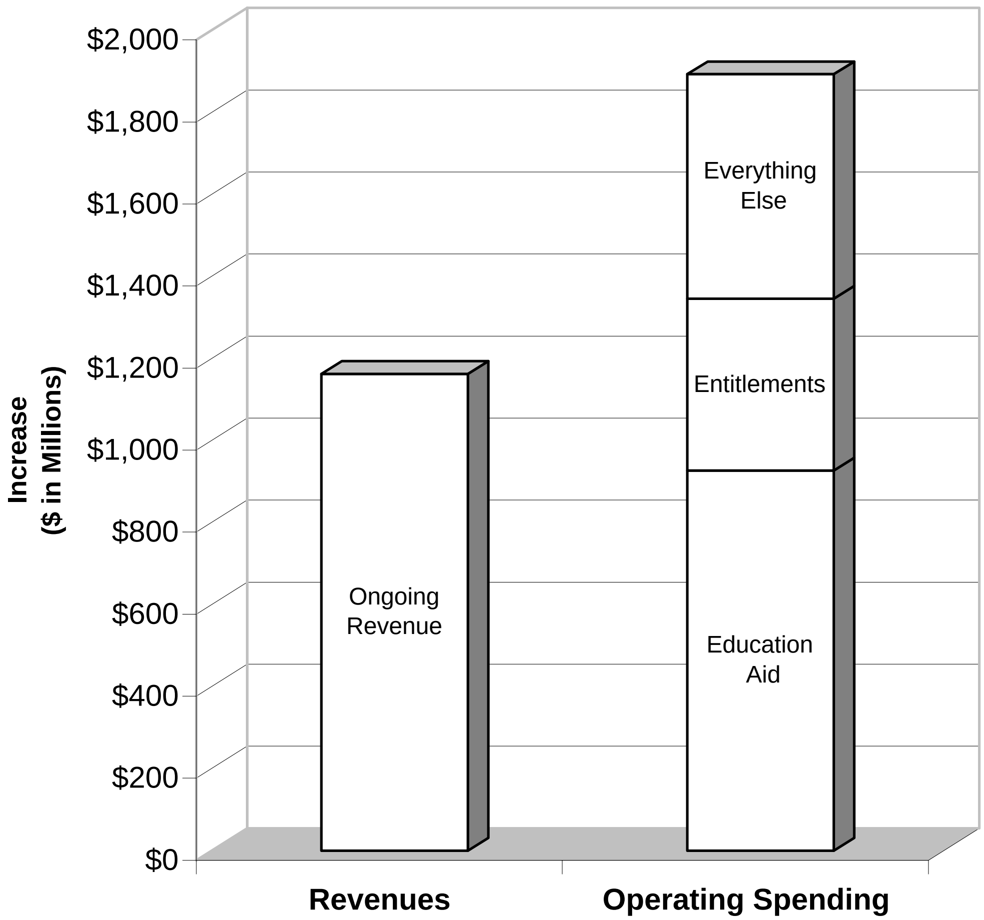
General Fund Forecast

General Fund Projections
Fiscal 2005 – 2010

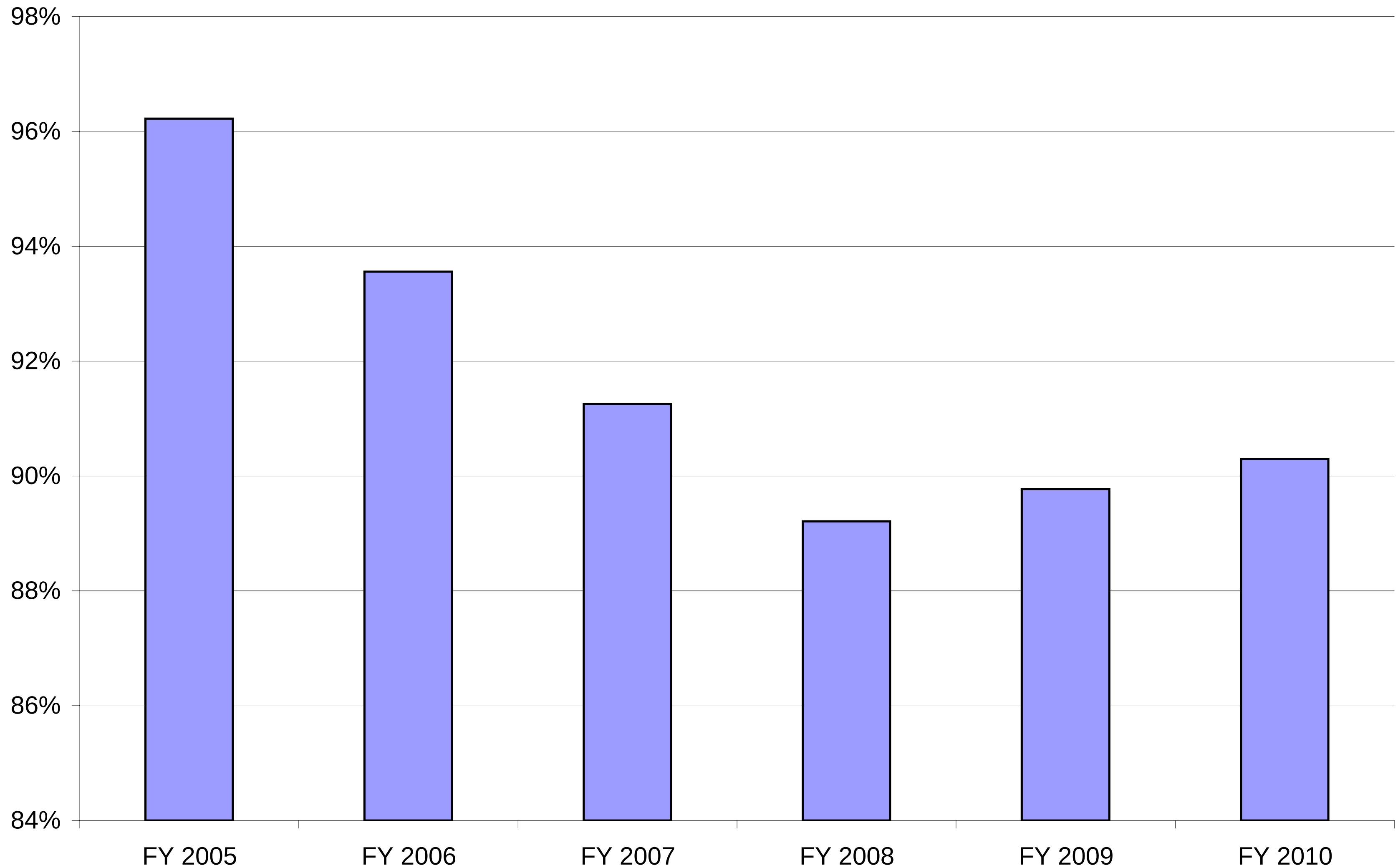
	Leg. Approp. FY 2005	Baseline FY 2006	FY 2007	FY 2008	FY 2009	FY 2010	Annual Growth Rate FY 06-08	Avg. Annual Growth Rate FY 08-10
Revenues – October 2004 DLS Estimate								
Individual Income	$5,388	$5,702	$6,059	$6,449	$6,862	$7,305	6.3%	6.4%
Sales and Use	3,104	3,255	3,408	3,592	3,786	3,980	5.1%	5.3%
Lottery	441	458	470	482	496	511	2.7%	2.9%
Other	1,897	1,910	1,931	1,964	2,030	2,063	1.4%	2.5%
Subtotal	**$10,831**	**$11,325**	**$11,867**	**$12,487**	**$13,174**	**$13,860**	**5.0%**	**5.4%**
Adjustments								
Balance	$453	$561	$0	$0	$0	$0		
Short-term Revenues	166	13	0	0	0	0		
Rainy Day Fund Transfer	91	218	0	0	0	0		
BRFA of 2004 and Other Fund Transfers	384	0	0	0	0	0		
Total Revenues	**$11,924**	**$12,117**	**$11,867**	**$12,487**	**$13,174**	**$13,860**	**1.5%**	**5.4%**
Expenditures								
Debt Service	$0	$0	$0	$13	$63	$72	n/a	134.8%
Local Aid – Education\Libraries	3,683	4,165	4,592	5,092	5,249	5,417	10.6%	3.1%
Local Aid – Other	453	470	486	504	524	542	3.6%	3.6%
Entitlements	2,145	2,428	2,615	2,847	3,059	3,288	8.3%	7.5%
State Operations	4,807	5,077	5,346	5,576	5,814	6,065	4.8%	4.3%
Reversions	-36	-35	-35	-35	-35	-35	0.0%	0.0%
Deficiencies	205	0	0	0	0	0		
Subtotal	**$11,256**	**$12,105**	**$13,004**	**$13,998**	**$14,675**	**$15,349**	**7.5%**	**4.7%**
Capital	$1	$23	$33	$33	$2	$2	19.8%	-75.4%
Reserve Fund	107	300	8	10	10	9	-82.1%	-4.3%
Total Expenditures	**$11,364**	**$12,427**	**$13,044**	**$14,040**	**$14,687**	**$15,360**	**9.4%**	**4.6%**
Surplus (Shortfall)	**$561**	**-$311**	**-$1,177**	**-$1,553**	**-$1,513**	**-$1,500**		
Annual Change		-871	-867	-376	40	13		
Ongoing Revenues vs. Operating Expenses		**-$780**	**-$1,137**	**-$1,511**	**-$1,501**	**-$1,489**		
Revenue Stabilization Fund								
Ending Balance	$519	$567	$593	$624	$659	$693		
As a Percent of Revenues	4.8%	5.0%	5.0%	5.0%	5.0%	5.0%		
Ratio of Operating Revenues to Expenditures	0.96	0.94	0.91	0.89	0.90	0.90		

Expenditure Increase Exceeds the Increase in General Fund Revenues

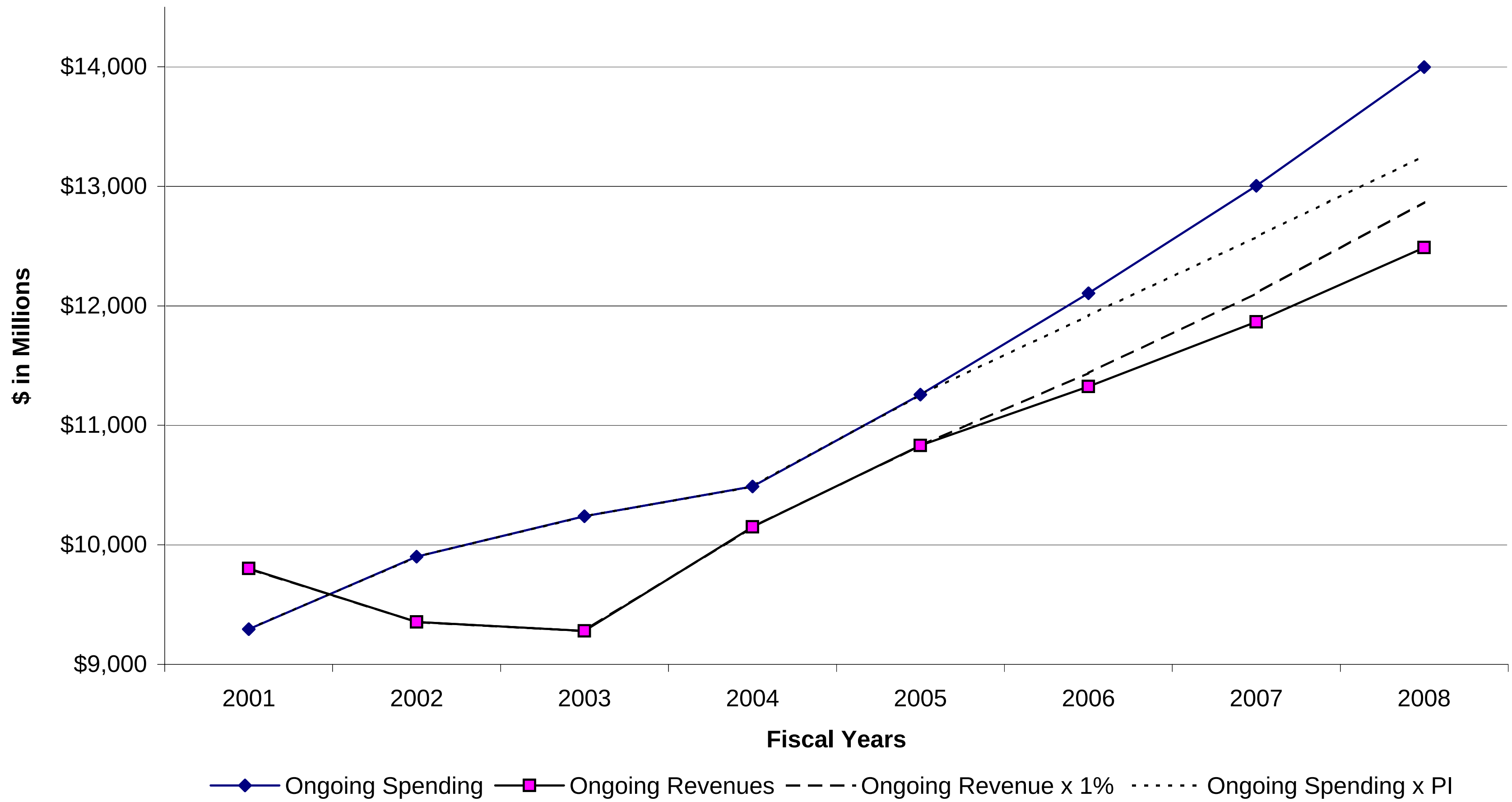
Fiscal 2006 – 2008



Ongoing Revenues as Percent of Operating Spending



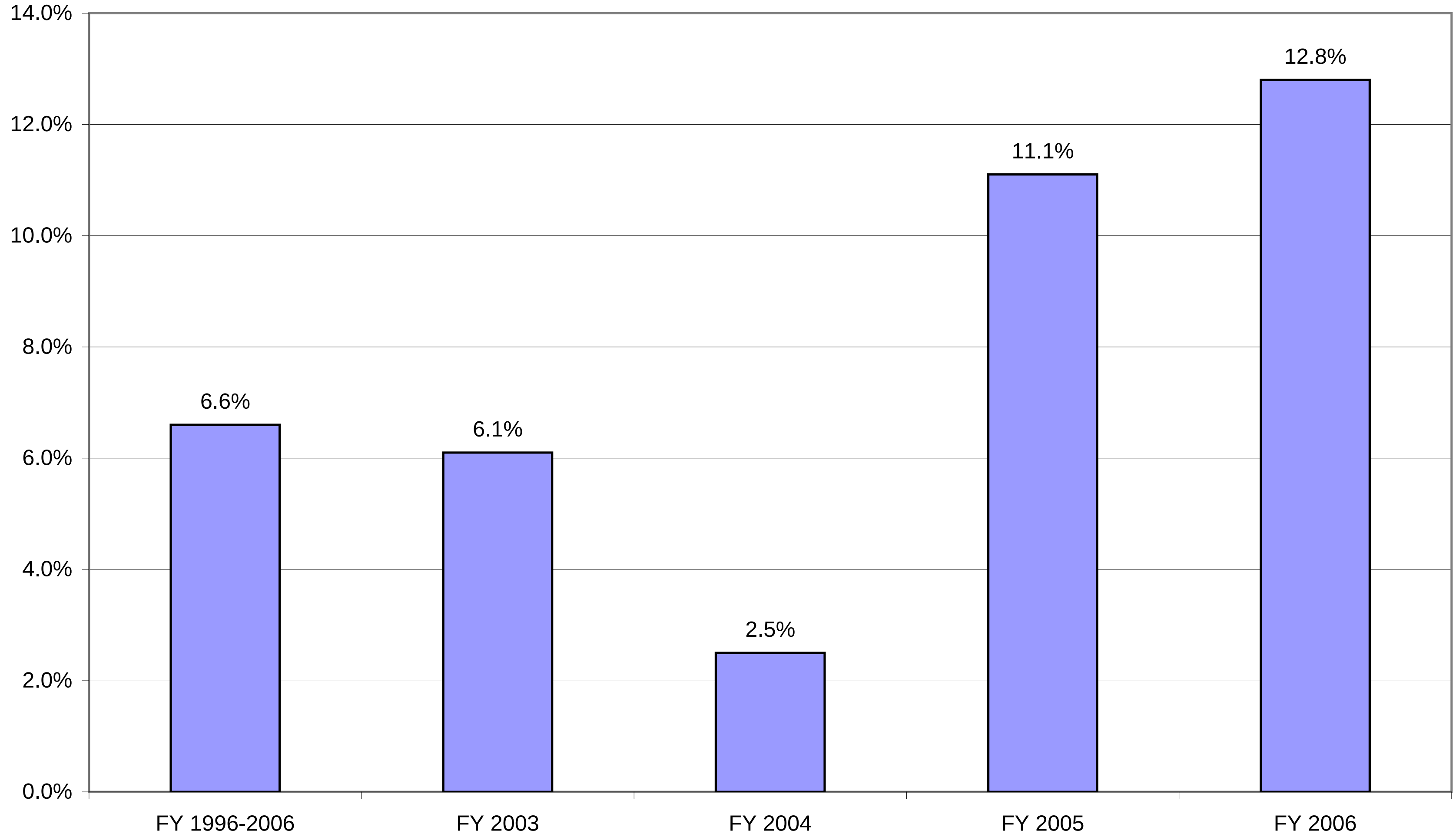
Normal Budget Cuts and Good Luck Will Not Close the Budget Gap



Part 5

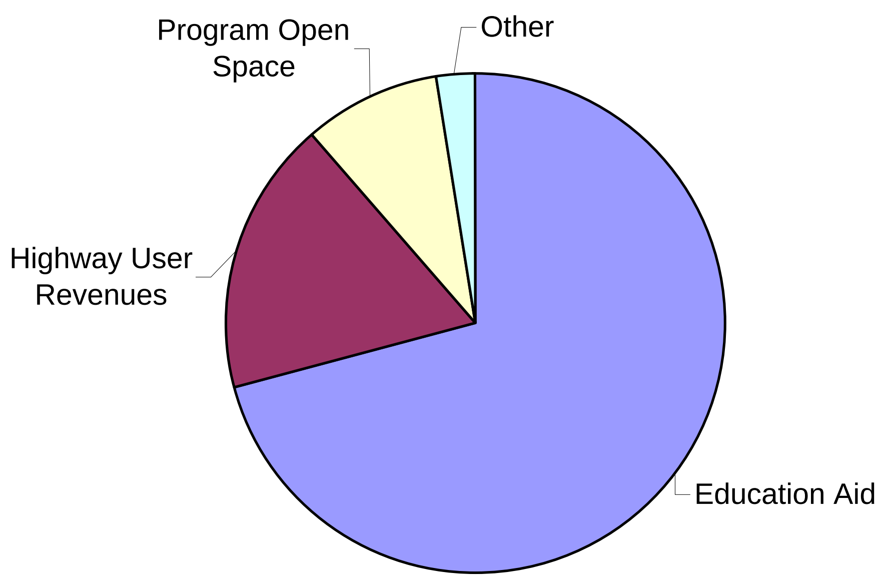
Local Government Assistance

Annual Growth in State Aid to Local Governments General and Special Funds



Programs Driving State Aid Increase in Fiscal 2006
State Funds
($ in Millions)

	State Aid Increase	Percent of Increase
Education Aid	$482.1	70.7%
Highway User Revenues	121.4	17.8%
Program Open Space	61.1	9.0%
Other State Aid	17.2	2.5%
Subtotal	**$681.7**	**100.0%**
Unclaimed Income Tax Payment	-81.0	
Total State Aid Increase	**$600.7**	



State Aid by Governmental Entity

Amount and Percent of Total
State Funds
($ in Millions)

	FY 2006 State Aid Amount	Percent of Total
Public Schools	$4,115.8	77.8%
County/Municipal	864.5	16.3%
Community Colleges	193.5	3.7%
Local Health	63.1	1.2%
Libraries	50.9	1.0%
Total	**$5,287.8**	**100.0%**

Increase in State Aid by Governmental Entity

State Funds
($ in Millions)

	FY 2006 Aid Increase	Percent of Increase
Public Schools	$482.1	80.3%
County/Municipal	106.3	17.7%
Community Colleges	9.5	1.6%
Local Health	2.2	0.4%
Libraries	0.5	0.1%
Total	**$600.7**	**100.0%**

State Aid by Major Programs
Fiscal 2004 – 2006
State Funds
($ in Millions)

	FY 2004	FY 2005	Baseline FY 2006	Difference	Percent Difference
Public Schools					
Foundation Program	$2,013.4	$2,114.6	$2,322.1	$207.5	9.8%
Compensatory Aid	350.8	487.5	598.1	110.6	22.7%
Student Transportation	167.0	175.5	185.2	9.7	5.5%
Special Education – Formula	116.2	157.2	191.7	34.5	21.9%
Special Education – Nonpublic	104.0	108.8	133.9	25.1	23.1%
Limited English Proficiency	38.9	51.3	67.0	15.7	30.6%
Guaranteed Tax Base	0.0	19.1	38.8	19.7	102.8%
Geographic Cost Index	0.0	0.0	54.2	54.2	
Other Education Programs	139.5	116.5	117.8	1.3	1.2%
Subtotal Direct Aid	**$2,929.8**	**$3,230.5**	**$3,708.9**	**$478.4**	**14.8%**
Retirement Payments	383.6	403.2	406.9	3.7	0.9%
Total Public School Aid	**$3,313.4**	**$3,633.7**	**$4,115.8**	**$482.1**	**13.3%**
Libraries					
Library Aid Formula	$27.3	$27.8	$28.1	$0.3	1.1%
State Library Network	13.9	14.2	14.3	0.2	1.2%
Subtotal Direct Aid	**$41.2**	**$41.9**	**$42.4**	**$0.5**	**1.1%**
Retirement Payments	8.0	8.4	8.5	0.1	0.8%
Total Library Aid	**$49.2**	**$50.4**	**$50.9**	**$0.5**	**1.1%**
Community Colleges					
Community College Formula	$142.7	$146.6	$154.1	$7.6	5.2%
Other Programs	17.0	21.4	23.6	2.2	10.5%
Subtotal Direct Aid	**$159.7**	**$167.9**	**$177.8**	**$9.8**	**5.9%**
Retirement Payments	15.2	16.0	15.7	-0.3	-1.9%
Total Community College Aid	**$174.9**	**$184.0**	**$193.5**	**$9.5**	**5.2%**
Local Health Grants	**$60.4**	**$60.9**	**$63.1**	**$2.2**	**3.6%**
County/Municipal Aid					
Transportation	$373.2	$433.8	$555.1	$121.4	28.0%
Public Safety	91.0	91.8	93.1	1.3	1.4%
Program Open Space/Recreation	21.4	15.8	76.9	61.1	386.6%
Disparity Grant	105.8	93.1	96.6	3.5	3.7%
Utility Restructuring Grant	26.2	30.6	30.6	0.0	0.0%
Other Grants	0.7	91.5	10.6	-80.9	-88.5%
Subtotal Direct Aid	**$618.3**	**$756.6**	**$862.9**	**$106.3**	**14.0%**
Retirement Payments	1.6	1.6	1.6	0.0	2.0%
Total County/Municipal Aid	**$619.9**	**$758.2**	**$864.5**	**$106.3**	**14.0%**
Total State Aid	**$4,217.9**	**$4,687.1**	**$5,287.8**	**$600.7**	**12.8%**

Source: Department of Legislative Services, November 2004

County Tax Changes in Fiscal 2005

County	Tax Action
Allegany	Increased real property and hotel/motel taxes.
Anne Arundel	Decreased real property tax.
Baltimore City	Increased recordation, energy, and telecommunications taxes.
Baltimore	Increased 911 fee.
Caroline	Imposed a hotel/motel tax, and increased the cable franchise tax.
Charles	Increased real property tax.
Frederick	Imposed a hotel/motel tax, and increased 911 fee.
Kent	Increased local income tax.
Montgomery	Decreased real property tax. Increased energy and transit taxes.
Prince George's	Increased 911 fee.
Queen Anne's	Decreased real property tax.
St. Mary's	Decreased real property and local income taxes.
Somerset	Increased hotel/motel tax.
Talbot	Decreased real property tax and increased hotel/motel tax.
Wicomico	Decreased real property tax.

Fifteen jurisdictions made changes to their local taxes and fees in fiscal 2005, with nine jurisdictions increasing local taxes/fees, four jurisdictions reducing local taxes/fees, and two jurisdictions increasing and reducing local taxes/fees. Property taxes were increased in two jurisdictions and reduced in six jurisdictions, while the income tax was increased in one jurisdiction and reduced in one jurisdiction. The recordation tax was increased in one jurisdiction and the hotel/motel tax was increased in five jurisdictions.

Number of Counties Changing Local Tax Rates

Fiscal 2001 – 2005

	FY 2001		FY 2002		FY 2003		FY 2004		FY 2005	
	▲	▼	▲	▼	▲	▼	▲	▼	▲	▼
Property	9	2	5	3	1	5	4	1	2	6
Income	7	1	4	0	0	0	6	0	1	1
Recordation	1	0	1	0	2	0	5	0	1	0
Transfer	0	0	0	0	0	0	1	1	0	0
Admissions/Amusement	2	0	0	0	1	0	2	0	0	0
Hotel/Motel	3	0	0	0	0	0	1	0	5	0

Note: ▲ Represents Increase ▼ Represents Decrease

Local Government Salary Actions in Fiscal 2005

County	County Government COLA	County Government Step	School Teachers COLA	School Teachers Step
Allegany	2.50%	No	4.00%	Yes
Anne Arundel[1]	2.00%	Yes	3.00%	Yes
Baltimore City[2]	Varies	Varies	0.00%	Yes
Baltimore[3]	2.25%	Yes	4.00%	Yes
Calvert[4]	2.00%	Yes	n/a	Yes
Caroline	4.00%	Yes	4.00%	Yes
Carroll	2.10%	Yes	2.00%	Yes
Cecil	0.00%	Yes	4.00%	Yes
Charles	2.00%	Yes	3.00%	Yes
Dorchester[4]	$752	Yes	n/a	n/a
Frederick[5]	1.50%	No	2.00%	No
Garrett	2.00%	Yes	4.00%	Yes
Harford	1.00%	Yes	2.00%	Yes
Howard	3.00%	Yes	6.00%	Yes
Kent	$500	Yes	2.00%	Yes
Montgomery[6]	2.00%	Yes	2.00%	Yes
Prince George's[7]	1.50%	Yes	3.00%	Yes
Queen Anne's[8]	2.00%	Yes	2.75%	Yes
St. Mary's[9]	2.50%	Yes	3.70%	Yes
Somerset	0.00%	Yes	2.00%	Yes
Talbot	0.00%	Yes	1.00%	Yes
Washington	3.00%	No	3.50%	Yes
Wicomico	3.00%	No	4.00%	Yes
Worcester	2.00%	Yes	2.00%	Yes
Number Granting	21	20	21	22

Source: Department of Legislative Services

Comments

1 In Anne Arundel County, police officers received a 3% cost-of-living adjustment (COLA), everyone else received a 2% COLA.

2 In Baltimore City, firefighters received a flat 3% raise, and there was no step increase. City Union of Baltimore received a 2% COLA and a step increase. County managerial employees received neither a raise nor a step increase. Salary actions for the police department and other employee unions have yet to be decided.

3 In Baltimore County, firefighters received a COLA of $2,300, police officers received a COLA of $2,500, and all other county employees received a COLA of 2.25%.

4 In Calvert and Dorchester counties, salary action for teachers for fiscal 2005 remain in arbitration. Calvert County school administrators received a 3% COLA.

5 In Frederick County, the COLA also included a $200 adjustment for part-time employees and a $400 adjustment for full-time employees. In addition, no step increase was issued by the board of education; however, a new pay scale was implemented with revised step placement.

6 In Montgomery County, firefighters received a COLA of 3.5%, fire management received a COLA of 7%, and all other county government employees received a COLA of 2%.

7 In Prince George’s County, general salary schedule employees received a COLA of 1.5%. A 2% COLA was issued for police officers, firefighters, and correctional officers.

8 In Queen Anne’s County, teachers received a COLA of 2.75% and school administrators received a 4.29% COLA.

9 In St. Mary’s County, for both teachers and school administration, the COLAs were 3.5% for 12-month employees, 3.6% for 11-month employees, 3.7% for 10-month employees, and 3% for classified positions.

Part 6

Debt Management

General Obligation Bonds

2004 Capital Debt Affordability Committee Recommendations

- The committee recommends that the General Assembly authorize up to $670 million in general obligation (GO) bonds in the 2005 legislative session.

- This is consistent with the authorization levels proposed by Capital Debt Affordability Committee (CDAC) in its last report released in the fall of 2003.

- This provides a $15 million increase over the authorization in the 2004 legislative session.

Proposed Debt Levels Meet Current CDAC Criterion

- The CDAC criteria are that:

  - tax-supported debt outstanding should not exceed 3.2 percent of Maryland personal income; and

  - tax-supported debt service payments should not exceed 8 percent of State revenues.

- The table below shows the committee's projections based on authorizing $670 million in fiscal 2006. The proposed authorization meets the affordability criteria:

Fiscal Year	Debt Outstanding as a Percent of Personal Income	Debt Service as a Percent of Revenues
2005	2.81%	6.18%
2006	2.84%	6.22%
2007	2.82%	6.02%
2008	2.81%	6.12%
2009	2.85%	6.30%
2010	2.89%	6.48%

Source: Report of the Capital Debt Affordability Committee, September 2004

General Obligation Bonds

Annuity Bond Fund – Projected Cash Flow
State Property Taxes Are Less Than Debt Service Costs
Fiscal 2005 – 2010
($ in Millions)

	FY 05	FY 06	FY 07	FY 08	FY 09	FY 10
Property Tax Receipts	$514	$568	$607	$654	$687	$719
Bond Sale Premiums	19	0	0	0	0	0
Other Revenues	4	3	3	3	3	3
ABF Fund Balance Transferred from Prior Year	130	113	72	44	29	0
Total Special Fund Revenues Available	**$667**	**$684**	**$682**	**$701**	**$719**	**$722**
ABF Fund Balance Transferred to Next Year	113	72	44	29	0	0
Subtotal Special Fund Appropriation	**$554**	**$612**	**$638**	**$671**	**$719**	**$722**
Projected Debt Service Expenditures	**$554**	**$612**	**$638**	**$671**	**$721**	**$755**
Annual Special Fund Revenue Shortfall	**$0**	**$0**	**$0**	**$0**	**$1**	**$33**
State Property Tax Rate per $100 of Assessable Base	0.132	0.132	0.132	0.132	0.132	0.132
Property Tax Rate Increase Required to Support Debt Service	0.000	0.000	0.000	0.000	0.000	0.007

General Obligation Bonds

State Property Taxes Are Less Than Debt Service Costs

- GO bond debt service is supported by the Annuity Bond Fund (ABF). State property taxes, bond sale proceeds, and other revenues are deposited into the fund. The end-of-year fund balances are carried forward and may be appropriated in the next year.

- GO bond debt service costs exceed State property tax receipts in each year between fiscal 2005 and 2010.

- Through fiscal 2008, proceeds from bond sale premiums supplement property tax receipts so that the ABF does not require additional appropriations.

- If interest rates for Maryland's AAA-rated GO bonds rise above 5 percent, the State is unlikely to generate additional proceeds from bond sale premiums. Most interest rate forecasts project that interest rates will rise. This forecast does not assume any proceeds from bond sales beyond fiscal 2005.

- In fiscal 2009, proceeds are depleted and other revenues will need to supplement the ABF.

- By fiscal 2010 the gap requires either $33 million in general funds or a State property tax rate increase totaling $0.007 per $100 of assessable base. This would increase the State property tax rate to $0.139 per $100 of assessable base.

General Obligation Bonds

Legislation Establishes Goal to Provide Additional Resources for Public School Capital Projects

- Chapters 306 and 307, Acts of 2004 (Public School Facilities Act of 2004) established the goal that State and local governments provide $3.85 billion to support public school capital projects. The Act recommended that the State provide $2 billion of the $3.85 billion.

- The Act also requires that the CDAC review additional school construction needs. As previously mentioned the CDAC did not recommend expanding the program, and instead recommended that the State first explore:

    - ***Alternative Funding Mechanisms:*** Chapters 306 and 307, Acts of 2004 authorize the use of alternative financing methods, such as leasing arrangements with contractors, and allow all counties to issue bonds for public school construction;

    - ***New Revenue Streams:*** Possible revenue sources include video lottery terminals or increasing State property tax rates; or

    - ***Shifting Other Capital Projects:*** This could be achieved by amending the Department of Budget and Management's Capital Improvement Program to delay or delete capital projects.

- With respect to the GO bond program, the costs of three options are examined:

    - ***Authorizing $150 Million Annually:*** This approach is consistent with the goal set by the legislation and relies totally on GO debt to fund the initiative. The entire $1.2 billion would be authorized in eight years;

    - ***Authorizing $100 Million Annually:*** This could be achieved by implementing the program more slowly or supplementing the GO bonds with options noted in the CDAC report; and

    - ***Authorizing $50 Million Annually:*** This could be achieved by implementing the program more slowly or supplementing the GO bonds with options noted in the CDAC report.

General Obligation Bonds

Authorizing Additional GO Bonds for Public School Capital Projects Adds to the Debt Service Revenue Shortfall

Authorizing $50 Million, $100 Million, or $150 Million Annually in GO Bonds
Additional Debt Service Costs
($ in Millions)

	FY 06	FY 07	FY 08	FY 09	FY 10
Annual Special Fund Revenue Shortfall	$0.0	$0.0	$0.0	$1.1	$33.4
$50 Million Annual Authorization					
Additional Debt Service	0.0	1.3	3.4	7.2	12.1
Total Annual Shortfall	**$0.0**	**$0.0**	**$0.0**	**$13.0**	**$45.5**
$100 Million Annual Authorization					
Additional Debt Service	0.0	2.5	6.7	14.5	24.1
Total Annual Shortfall	**$0.0**	**$0.0**	**$0.0**	**$24.8**	**$57.5**
$150 Million Annual Authorization					
Additional Debt Service	0.0	3.8	10.1	21.7	36.2
Total Annual Shortfall	**$0.0**	**$0.0**	**$0.0**	**$36.7**	**$69.6**

- In fiscal 2007 and 2008, the fund balance is sufficient to support the additional debt service. By fiscal 2009, additional debt service exceeds the fund balance, resulting in a shortfall.

- The total debt service cost is estimated to be $1.8 billion if the entire amount is funded with GO bonds. Funding two-thirds ($100 million annually for eight years) of the program results in $1.2 billion in total debt service and funding one-third ($50 million annually for eight years) of the program results in $612 million in total debt service.

- Under the most aggressive approach, authorizing $150 million annually, annual debt service costs peak in fiscal 2019 at $131 million.

- Based on current CDAC criterion, all three options are affordable through fiscal 2010. Under the most aggressive approach, Department of Legislative Services estimates debt outstanding to personal income will peak at 2.86 and debt outstanding to revenues will peak at 6.18.

- Under the most aggressive approach, there is just over $1 billion in estimated debt capacity in fiscal 2010.

Part 7

Transportation Trust Fund

Transportation Trust Fund Closeout
($ in Millions)

	Projected FY 2004	Actual FY 2004	Variance
Fund Balance			
Starting Fund Balance	$145.0	$145.0	$0.0
Ending Fund Balance	102.0	288.0	186.0
Change in Fund Balance	**-$43.0**	**$143.0**	**$186.0**
Gross Tax and Fee Revenue Summary	$1,900.0	$1,946.0	$46.0
Other Receipts and Adjustments	536.0	659.0	123.0
Bond Sale Proceeds	370.0	320.0	-50.0
Bond Premium		10.0	10.0
Total Revenues and Adjustments	**$2,806.0**	**$2,935.0**	**$129.0**
Expenditures			
Operating & Capital Fund Expenditures	2,034.0	1,969.0	-65.0
Fund Transfers & Deductions	313.0	311.0	-2.0
Highway User Revenues	366.0	377.0	11.0
Maryland Department of Transportation Debt Service	136.0	135.0	-1.0
To TTF as Changed Fund Balance	-43.0	143.0	186.0
Total Funds by Use	**$2,806.0**	**$2,935.0**	**$129.0**

Note: Totals may not sum to total due to rounding.

Source: Maryland Department of Transportation, October 2004

- Most of the increase in the closing balance is due to one-time cash receipts and does not represent ongoing increases in the Transportation Trust Fund (TTF) revenues.

- Additional non-tax revenues were generated through reimbursements received by the TTF from the (1) Washington Metropolitan Area Transit Authority for moneys advanced from the TTF to cover construction costs due to the timing of federal aid receipts and from the (2) Maryland Transportation Authority (MdTA) to cover expenses incurred by the Highway Administration for the InterCounty Connector (ICC).

- Operating and capital expenditures were approximately $65 million lower than expected, due primarily to cash flow to ongoing capital projects and offset by lower bond sales of $50 million.

Transportation Trust Fund Forecast

Fiscal 2005 – 2010

	Base Year 2004	Current Year 2005	Estimate FY 2006	Estimate FY 2007	Estimate FY 2008	Estimate FY 2009	Estimate FY 2010
Opening Fund Balance	**$145**	**$288**	**$100**	**$100**	**$100**	**$100**	**$100**
Closing Fund Balance	**$288**	**$100**	**$100**	**$100**	**$100**	**$100**	**$100**
Net Revenues							
Taxes and Fees	$1,412	$1,587	$1,591	$1,640	$1,687	$1,731	$1,771
Operating and Miscellaneous	617	538	425	428	441	454	479
Transfers between TTF and GF	-155	0	50	0	0	0	0
MdTA Transfer	43	43	43	43	0	0	0
Net Revenues Subtotal	1,917	2,168	2,109	2,111	2,128	2,185	2,250
Bonds Sold	320	275	260	85	110	190	185
Bond Premiums	10	0	0	0	0	0	0
Total Revenues	**$2,247**	**$2,443**	**$2,369**	**$2,196**	**$2,238**	**$2,375**	**$2,435**
Expenditures							
Debt Service	$135	$159	$160	$141	$150	$165	$183
Operating Budget							
State Capital	792	1,249	906	697	683	751	744
Total Expenditures	**$2,105**	**$2,630**	**$2,369**	**$2,196**	**$2,238**	**$2,375**	**$2,435**
Debt							
Debt Outstanding	$1,186	$1,345	$1,513	$1,531	$1,567	$1,672	$1,760
Debt Coverage – Net Income	3.5	4.9	4.9	4.5	3.9	3.4	3.1
Local Highway User Revenues (HUR)	**$480**	**$551**	**$548**	**$565**	**$580**	**$594**	**$607**
Transferred to General Fund	$102	$102	$0	$0	$0	$0	$0
Net HUR to Counties	**$377**	**$449**	**$548**	**$565**	**$580**	**$594**	**$607**
Capital Summary							
State Capital	$792	$1,257	$907	$696	$683	$751	$744
Total Federal Capital (Cash Flow)	589	732	758	690	640	479	476
GARVEE Bond Repayment	0	0	20	40	60	60	60
Net Federal Capital to TTF	589	732	738	650	580	419	416
Total Capital Expenditures	**$1,381**	**$1,989**	**$1,645**	**$1,346**	**$1,263**	**$1,170**	**$1,160**

Source: Department of Legislative Services

Trust Fund Forecast Assumptions and Results

Assumptions

- Forecast reflects fund transfers:

  - Forecast assumes that $50 million will be repaid to the TTF from the general fund. Chapter 430, Acts of 2004 requires that up to $50 million of an unappropriated general fund surplus must be transferred to the TTF annually until the entire amount of the money transferred from the TTF to the general fund has been repaid. The general fund finished fiscal 2004 with an unappropriated surplus of $309.7 million; as a result, the TTF forecast assumes that the first repayment of $50 million will be made from the general fund to the TTF in fiscal 2006.

  - Forecast reflects the transfer of $102 million annually from Highway User Revenues to the general fund in fiscal 2004 and 2005.

  Forecast also assumes:

  - moderate increases in the motor fuel tax, titling tax, and corporate income tax revenues – and includes $47.5 million in fiscal 2005 as the TTF's portion of the Delaware holding company settlements;

  - all additional revenues expected to be generated by the increases in the motor vehicle registration fee;

  - annual $43 million MdTA grants for transit continue through fiscal 2007 and;

  - a $100 million fund balance will be maintained and that debt coverage ratios will exceed 2.5.

Results

- Over the six-year period covered by the forecast, an additional $356 million is made available for the capital program over the amount obtained in the MDOT June forecast. This permits MDOT to maintain at least a $1.2 billion capital program through fiscal 2008.

- Total debt outstanding reaches $1.76 billion by the end of the forecast period.

- Forecast could support additional debt sales of approximately $200 million and remain within statutory debt limits.

Comparison of Proposed Capital Programs – Fiscal 2005 to 2009
As Shown in the 2004 Final CTP and the 2005 Draft CTP
($ in Millions)

	2004 Final CTP	2005 Draft CTP	Change	Percent Change
State Funds				
Special Funds	$2,562.0	$4,046.7	$1,484.7	58%
Other Funds	197.0	223.6	26.6	14%
Subtotal State Funds	2,759.0	4,280.3	1,521.3	55%
Federal Aid*	$2,433.7	$3,118.8	$685.1	28%
Total Funds	$5,192.7	$7,389.1	$2,196.4	42%

CTP = *Consolidated Transportation Program*

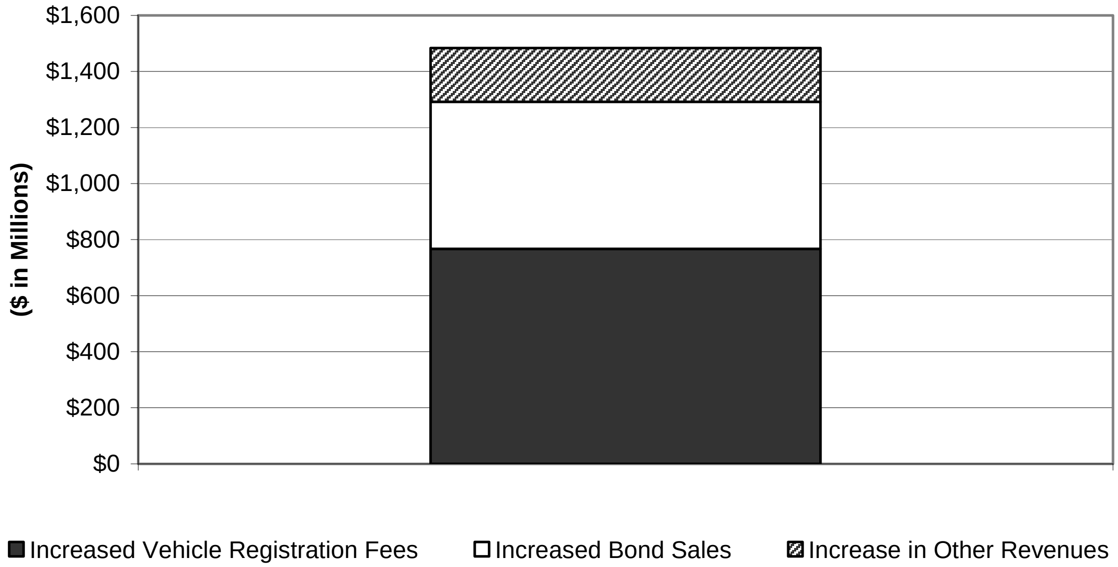
*Federal aid received directly by the Washington Metropolitan Area Transit Authority is not shown in this category. This aid totaled $480.4 million in the final 2004 CTP and totals $450.6 in the draft 2005 CTP.

- **15 Projects Added to the Construction Program:** Fifteen projects totaling $283.8 million have been added to the construction program in the draft 2005 CTP, including two transit projects (Maryland Rail Commuter vehicle and locomotive mid-life overhauls), one aviation project (an expansion of the Hagerstown airport), and 12 highway projects.

- **17 Projects Have Moved to the Construction Program from the Development and Evaluation Program:** Seventeen projects included in earlier CTPs totaling $762.5 million have moved to the Construction Program, including one transit project (Baltimore – Red Line) and 16 highway projects.

Effect of Transportation Revenue Increase

Sources of Increased Special Fund Capital Spending
(Based on Comparison of MDOT
December 2003 and June 2004 Forecasts)



Chapter 9, Acts of 2004 increased annual vehicle registration fees for all classes of vehicles and required the Motor Vehicle Administration to recover the cost of its annual capital expenditures through its miscellaneous fees; rental vehicles were subsequently exempted from the vehicle registration fee increase through a provision adopted in the Budget Reconciliation and Financing Act of 2004.

Projected Revenue from Vehicle Registration Fees
($ in Millions)

	FY 04	FY 05	FY 06	FY 07	FY 08	FY 09	Total FY 05-09
December 2003 TTF Forecast	$192	$196	$198	$201	$203	$206	$1,004
November 2004 TTF Forecast	199	345	349	355	358	364	1,771
Annual Change	7	149	151	154	155	158	767

Federal Highway Aid Assumptions

- **Reauthorization of Federal Transportation Equity Act for the 21st Century (TEA-21) Delayed:** The authorization Act for federal spending on highway and transit construction in the United States was scheduled to expire September 30, 2003; however, this existing authorization was extended six times during calendar 2004. The most recent extension was enacted on September 30, 2004, and can remain in force for up to eight months. Given the uncertainty surrounding the likely size of the next federal reauthorization, it is unclear at this time exactly how much of an increase in federal highway aid Maryland is likely to receive.

- **MDOT Assumes $530 Million in Federal Aid Authorizations Per Annum:** In the current forecast, the Maryland Department of Transportation is assuming that it will receive $530 million per year in federally authorized aid under the next reauthorization, of which it will be able to spend approximately 87 percent (approximately $460 million) in obligational authority.

  - Under TEA-21, Maryland received an annual average of $430 million in authorized aid (excluding earmarks).

  - In federal fiscal 2004, Maryland received $534 million in authorized aid.

  - In federal fiscal 2005, Maryland anticipates receipt of $580 million in authorized aid.

- **Draft 2005 CTP Withholds $240 Million in Federal Aid in Anticipation of GARVEE Repayments:** A total of $240 million is withheld from the federal aid cash flow figures shown in the draft 2005 CTP in anticipation of the repayment of Grant Anticipation Revenue Vehicles (GARVEEs) (including $20 million withheld in 2006, $40 million withheld in 2007, and $60 million withheld every year thereafter).

Projected Federal Highway Aid Cash Flow
(Minus Federal Funding Withheld in Anticipation of GARVEE Debt Service)
($ in Millions)

	FY 04	FY 05	FY 06	FY 07	FY 08	FY 09	Total FY 05-09
December 2003 TTF Forecast	$734	$634	$605	$500	$418	$277	$2,434
November 2004 TTF Forecast	622	732	738	650	580	419	3,119
Annual Change	112	98	133	150	162	142	685

Intercounty Connector (ICC)

Project Status

- The **Draft Environmental Impact Statement** is to be completed and released in **November 2004**. The timeline for other major project steps is as follows:
  - July 2005: Final Environmental Impact Statement/Record of Decision (Final Alignment Selected)
  - Fall 2006: Initiation of Construction
  - Fall 2010: Opened to Traffic

Total Cost

- During the 2004 legislative session, the Maryland Department of Transportation (MDOT) estimated the cost of constructing the ICC to be approximately $1.7 billion. Based on the findings of the Draft Environmental Impact Statement, the cost of constructing the ICC is now projected to be approximately $2.1 billion.

- Consequently, MDOT must identify an additional $400 million in financing.

Revised Conceptual Financing Plan

MDOT's Revised Conceptual Financing Plan for the ICC
November 2004

Funding Source	Amount
GARVEE Bonds (issued by MdTA/MDOT)	$900 million – $1 billion
MdTA Bonds (ICC Tolls)	$400 – $600 million
MdTA Bonds (extant bonding capacity)	$600 – $800 million
TTF Contribution	$50 – $300 million
Federal Contribution (from reauthorization)	$10 – $50 million

- **MdTA Bond Financing:** The amount of bonds projected to be issued by the Maryland Transportation Authority (MdTA) and backed by its extant bonding capacity has been increased to between $600 million and $800 million (it was between $100 million and $350 million in the earlier conceptual financing plan).

- **Federal Aid Assumptions:** At this time, the House version of the TEA-21 reauthorization legislation contains an earmark of $9 million for the ICC. The Senate version of the TEA-21 reauthorization contains no earmarks for any projects.

MDOT Will Seek Modification of GARVEE Bond Restrictions

- **Limits Imposed on the Use of GARVEE Bonds:** Under a provision adopted in the Budget Reconciliation and Financing Act of 2004, the maturity of any GARVEE issued by MDOT or MdTA may not exceed 15 years, while the annual payments for principal and interest on these bonds may not exceed 13 percent of the State's average annual authorization level in the current federal authorization act for federal highway aid. These restrictions would allow for the issuance of between $600 million and $700 million in GARVEE bonds (contingent on federal aid receipts).

- **MDOT to Request that 20 Percent of Federal Aid Be Available for Expenditure on GARVEEs:** To meet the need for additional financing for the ICC, MDOT will propose to sell a total of $1 billion in GARVEEs. Assuming that Maryland receives approximately $530 million per annum in federal highway aid authorizations under the new reauthorization, MDOT would likely need to utilize approximately 20 percent per annum of the State's total federal highway aid to meet annual debt service on a GARVEE issuance.

Issues

- **Earlier Stand Alone Issuances Are Not as Large as MDOT's Proposed Issuance:** Stand alone GARVEEs are not backed by any revenues other than federal aid. To date, five states have issued stand alone GARVEEs. No stand alone issuance has been as large as MDOT's proposed issuance.

Outstanding Issuances of Stand Alone GARVEEs
($ in Millions)

State	Amount Issued	Rating (Moody's)	Maturity	Approx. Annual Federal Aid	% of Federal Aid for Debt Service
Alabama	$200	Aa3*	2017	$550 - $600	3.2% - 3.5%
California	$625	Aa3*	2015	$2,546	3%
Michigan	$600	Aaa* (1) (2)	2009	$860 - $945	1% - 22%
Oklahoma	$48	Aa3	2018	$400 (3)	1%
Rhode Island(4)	$216.8	Aaa*	2015	$160	4% - 26%

*State utilized bond insurance.

(1) GARVEE carries a variable interest rate.
(2) Debt service on the GARVEE varies significantly from year to year due to the wide variance in the amount of principal repaid from year to year.
(3) Average federal aid received by the state during the TEA-21 period.
(4) Bonds issued by the Rhode Island Economic Development Corporation.

- **Issuances as Large as MDOT's Proposed Issuance Are Not Stand Alone:** To date, three states have each issued GARVEEs as large as MDOT's proposed issuance; none have been stand alone GARVEEs.

Largest GARVEE Issuances
($ in Millions)

State	Amount Issued	Rating (Fitch)	Maturity	Additional Recourse
Massachusetts	$1,499	AA	2015	10 cents/gallon from state's gas tax receipts
Colorado	$1,470	AA	2017	Highway Users Trust Fund; 10% of state sales tax
Virginia	$898	AA	2012	Transportation Trust Fund revenues and some additional funds

- **Increased Use of MdTA Debt Takes Its Toll:** Under the earlier financing plan, which called for MdTA to issue between $100 and $350 million in debt backed by its extant toll revenues, MdTA is projected to have more than $1 billion in total debt outstanding by 2009 (including all debt issued for its ongoing capital projects). As the level of bonds issued by MdTA for the ICC increases, its total debt outstanding increases and it becomes likely that MdTA will need to increase toll rates to meet debt service obligations.

- **Imbalance of PAYGO and Debt:** Assuming a cash contribution from the TTF of $150 million and a federal earmark of $9 million, it is likely that under the current financing plan, more than 90 percent of the entire financing for the ICC will come from debt issuances.

- **Current GARVEE Limits in Keeping with Nationwide Trends:** A number of states have recently enacted limits on GARVEE bonds that are similar to those adopted in Maryland. Chapter 793 (SB/507) enacted during California's 2004 legislative session limits GARVEE debt service to 15 percent of federal aid. Louisiana and Florida limit GARVEE debt service to 10 percent of federal aid.

Part 8

Cigarette Restitution Fund

Cigarette Restitution Funds
Fiscal 2006 Baseline Estimates
($ in Millions)

	FY 04 Actual Spending	FY 05 Working Appropriation	FY 06 Baseline Appropriation	FY 07 Estimated	FY 08 Estimated
Beginning Fund Balance[1]	$55.1	$10.5	$6.3	$0.0	$69.8
Settlement Payments	150.7	143.7	143.6	145.0	173.0
Subtotal	**$205.8**	**$154.2**	**$149.9**	**$145.0**	**$242.8**
Payment to Law Offices	-$30.0	-$30.0	-$29.9	$0.0	$0.0
From Special Reserve Fund	13.5	0.0	0.0	0.0	0.0
Total Available Revenue	**$189.3**	**$124.2**	**$120.0**	**$145.0**	**$242.8**
Health					
Tobacco	$13.8	$9.5	$18.5	$18.5	$18.5
Cancer	31.0	30.5	30.5	30.5	30.5
Substance Abuse	17.1	17.1	17.1	17.1	17.1
Medicaid[2]	108.3	51.5	44.8	0.0	0.0
Administration	0.5	0.4	0.4	0.4	0.4
Subtotal	**$170.7**	**$109.0**	**$111.3**	**$66.5**	**$66.5**
Other					
Aid to Nonpublic Schools	$3.0	$3.0	$3.0	$3.0	$3.0
Crop Conversion	5.1	5.7	5.5	5.5	5.5
Attorney General	0.0	0.2	0.2	0.2	0.2
Subtotal	**$8.1**	**$8.9**	**$8.7**	**$8.7**	**$8.7**
Total Expenses	**$178.8**	**$117.9**	**$120.0**	**$75.2**	**$75.2**
Ending Fund Balance	**$10.5**	**$6.3**	**$0.0**	**$69.8**	**$167.6**

(1) The fiscal 2004 beginning fund balance includes prior year funds not reverted until the close of fiscal 2004.

(2) 25 Percent of Cigarette Restitution Funds are required to be appropriated to Medicaid through fiscal 2006.

Settlement payments increase in fiscal 2008 with the beginning of Strategic Contribution Payments from the participating tobacco manufacturers. These payments, estimated at $28 million annually, continue through fiscal 2017.

Sources: Department of Budget and Management; Department of Legislative Services

Part 9

State Employment

Regular Full-time Equivalent Positions
Fiscal 2002 Actuals to 2005 Working Appropriation

Department/Service Area	FY 02 Actual	FY 03 Actual	FY 04 Actual	FY 05 Leg. Approp.	BPW & Other Changes	FY 05 Working Approp.	Growth Rate FY 02 - 05 Working
Legislative	730	730	730	739	0	739	1.2%
Judiciary	3,010	3,224	3,224	3,224	0	3,224	7.1%
Legal	1,381	1,397	1,445	1,511	0	1,511	9.4%
Executive and Administrative Control	1,619	1,604	1,572	1,563	3	1,566	-3.2%
Financial and Revenue Administration	2,158	2,098	2,032	2,030	5	2,035	-5.7%
Budget and Management	524	531	472	468	0	468	-10.7%
Retirement	194	185	181	179	1	180	-7.2%
General Services	793	807	728	716	-4	712	-10.2%
Transportation	9,538	9,319	9,096	9,044	0	9,044	-5.2%
Natural Resources	1,629	1,577	1,454	1,429	-1	1,428	-12.3%
Agriculture	480	460	434	430	0	430	-10.4%
Health and Mental Hygiene	8,536	8,212	7,710	7,547	1	7,548	-11.6%
Human Resources	8,273	7,729	7,379	7,281	22	7,303	-11.7%
Labor, Licensing, and Regulation	1,706	1,617	1,519	1,490	0	1,490	-12.7%
Public Safety and Correctional Services	11,663	11,563	11,231	11,195	0	11,195	-4.0%
MSDE and Other Education	1,955	2,019	1,892	1,938	0	1,938	-0.8%
Housing and Community Development	449	425	393	386	0	386	-14.1%
Business and Economic Development	324	318	299	298	1	299	-7.7%
Environment	1,028	1,032	951	943	0	943	-8.3%
Juvenile Services	2,123	1,996	1,939	1,963	0	1,963	-7.5%
Police and Fire Marshal	2,590	2,573	2,480	2,479	0	2,479	-4.3%
Subtotal	**60,701**	**59,413**	**57,159**	**56,851**	**28**	**56,879**	**-6.3%**
Higher Education	21,386	21,403	20,966	20,966	249	21,215	-0.8%
Total	**82,087**	**80,816**	**78,125**	**77,818**	**277**	**78,095**	**-4.9%**
Non-higher Education Executive Branch Total	**56,961**	**55,460**	**53,205**	**52,889**	**28**	**52,917**	**-7.1%**

Contractual Full-time Equivalent Positions

Fiscal 2002 Actuals to 2005 Working Appropriation

Department/Service Area	FY 02 Actual	FY 03 Actual	FY 04 Working Approp.	FY 05 Leg. Approp.	Growth Rate FY 02 - 05
Judiciary	371	390	390	371	0.0%
Legal	99	71	106	108	9.0%
Executive and Administrative Control	208	206	179	181	-13.0%
Financial and Revenue Administration	35	29	38	41	17.9%
Budget and Management	33	27	19	21	-37.0%
Retirement	30	24	30	30	-1.1%
General Services	35	26	28	28	-19.9%
Transportation	142	122	176	172	20.6%
Natural Resources	332	378	480	439	32.1%
Agriculture	36	44	51	41	14.1%
Health and Mental Hygiene	409	357	487	496	21.3%
Human Resources	111	73	148	135	22.0%
Labor, Licensing, and Regulation	176	114	159	179	1.3%
Public Safety and Correctional Services	298	281	480	477	60.0%
MSDE and Other Education	218	190	192	202	-7.5%
Housing and Community Development	49	50	71	62	26.4%
Business and Economic Development	49	47	42	36	-26.9%
Environment	32	23	43	43	33.1%
Juvenile Services	119	98	133	75	-37.0%
Police and Fire Marshal	46	32	59	47	2.9%
Subtotal	**2,828**	**2,582**	**3,311**	**3,182**	**12.5%**
Higher Education	6,079	5,700	5,860	6,146	1.1%
Total	**8,907**	**8,282**	**9,171**	**9,327**	**4.7%**
Non-higher Education Executive Branch Total	**2,457**	**2,192**	**2,921**	**2,811**	**14.4%**

General Salary Increases, Increments, and Other Compensation
Fiscal 1999 – 2005

Fiscal Year		State Employees: General Salary Increase	State Employees: Increments	Additional Police, Natural Resources Police, and Park Ranger Salary Increases	Maximum Deferred Compensation Match by State	Pay-for-performance Bonuses	Annual Salary Review Reclassifications	Other
1999			On time		None	Outstanding: $300		
	7/1/1998	$900		4.0%				
	1/1/1999	$375						
2000			On time		$600	Outstanding: $1,000 Exceeds standards: $500		Salary schedules expand from 6 to 16 steps on 7/1/99.[1]
	7/1/1999	$638		4.0%				
	1/1/2000	$637						
2001			On time		$600	Outstanding: $1,000 Exceeds standards: $500		Standard salary schedule expands by 4 grades on 7/1/00[2] and a new physicians' schedule is developed.
	11/15/2000	4.0%						
	1/1/2001						Yes[3]	
2002			On time		$600	Outstanding: $500 Exceeds standards: $250		Salary schedules expand from 16 to 18 steps on 7/1/01.[1]
	7/1/2001			$850			Yes[4]	
	1/1/2002	4.0%						
2003		None	None		$500	None		
2004		None	None		None	None		
2005	7/1/2004	$752	On time		None	None	Yes[5]	

[1] The executive pay plan and physicians' schedules did not expand.

[2] The standard salary schedule expanded to accommodate management service positions moved off the executive salary schedule.

[3] The following classifications were given upgrades effective January 1, 2001, most of which were in the 1 to 2 grade range: clerical workers, social workers in criminal justice and health services, computer operations and related classifications, professional fiscal and related classifications, election workers (local funds), and assistant superintendents at State hospitals.

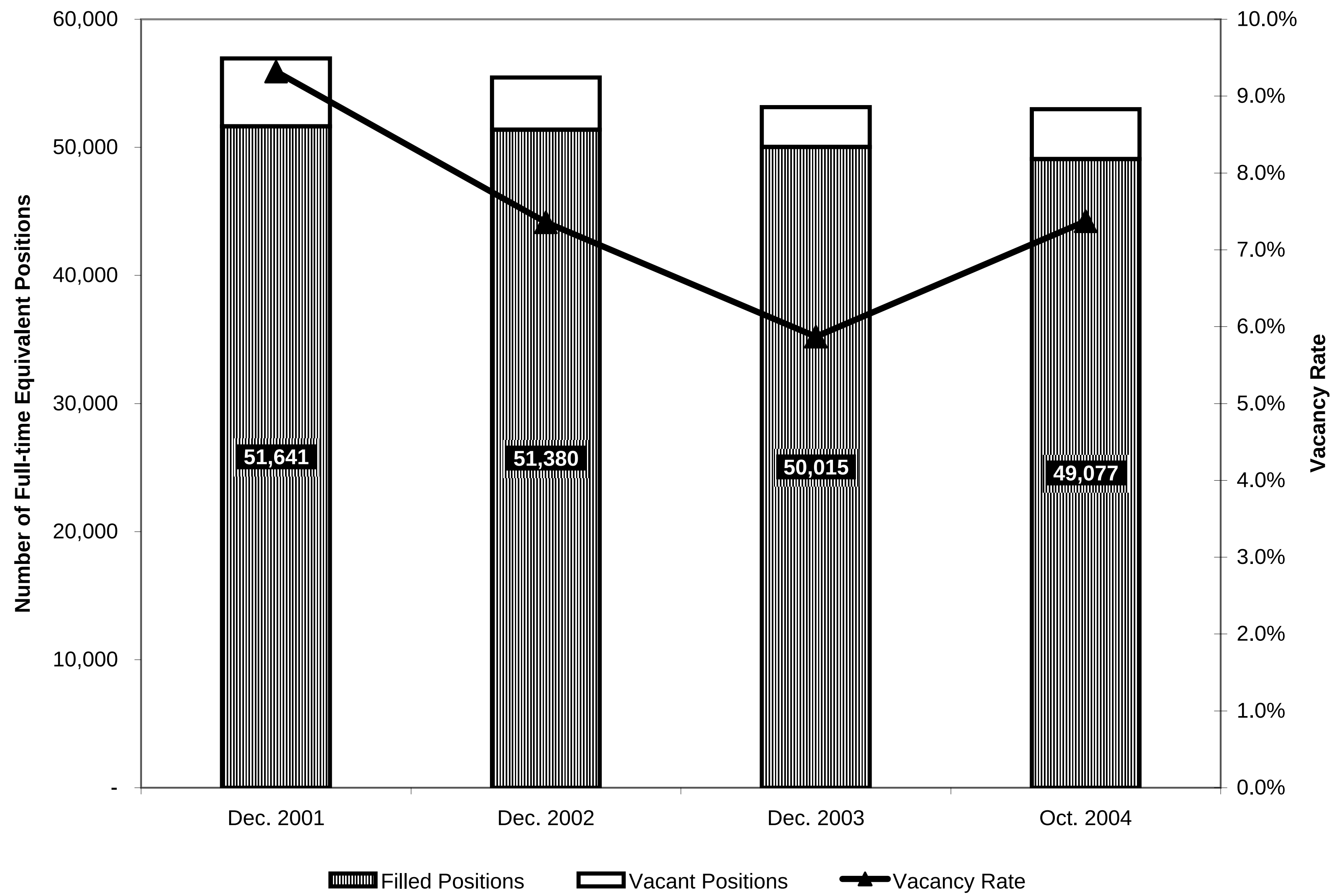
[4] Three groups of employees received reclassifications in fiscal 2002: nurses, institutional educators, and addictions counselors who work in local health departments and nonprofits. Statewide increases went to nurse classifications through two grade increases, one on July 1, 2001, and one on January 1, 2002. Institutional educators received increases through an adjustment to their pay plan.

[5] The following classifications are provided upgrades: public defenders, social services attorneys, assistant general counsels (human relations), assistant State prosecutors, direct service workers in the Department of Juvenile Services, professional assessors, agricultural lab scientists, chemists, public health lab scientists, administrative law judges, and financial examiners.

Non-higher Education Executive Branch Positions

Filled and Vacant Positions

December 2001 – October 2004



Vacant Positions, Turnover Rate, and Necessary Vacancies

Fiscal 2005 Legislative Appropriation

Department/Service Area	Oct. 2004 Vacancy Rate	Oct. 2004 Vacancies	2005 Leg. Approp. Turnover Rate	2005 Necessary Vacancies	Funded/ (Unfunded) Vacancies
Legislative	3.5%	26	1.2%	9	17
Judiciary	4.5%	145	2.5%	80	65
Legal	9.6%	145	6.0%	91	54
Executive and Administrative Control	7.5%	117	3.2%	51	66
Financial and Revenue Administration	7.5%	153	5.0%	102	51
Budget and Management	10.7%	50	2.9%	14	36
Retirement	7.8%	14	5.1%	9	5
General Services	12.4%	88	4.4%	32	56
Transportation	4.8%	430	5.2%	470	-40
Natural Resources	8.4%	120	7.7%	110	10
Agriculture	8.0%	35	6.7%	29	6
Health and Mental Hygiene	8.9%	659	6.4%	478	181
Human Resources	8.3%	606	4.6%	333	273
Labor, Licensing, and Regulation	4.6%	69	4.0%	59	9
Public Safety and Correctional Services	7.0%	783	5.1%	570	212
MSDE and Other Education	5.8%	112	5.3%	103	9
Housing and Community Development	7.0%	27	5.5%	21	6
Business and Economic Development	4.7%	14	3.6%	11	3
Environment	6.7%	63	6.5%	61	2
Juvenile Services	13.4%	263	9.7%	190	74
Police and Fire Marshal	6.1%	152	3.8%	93	59
Subtotal	**7.2%**	**4,069**	**5.1%**	**2,912**	**1,158**
Higher Education*	5.6%	1,079	3.0%	638	441
Total	**6.8%**	**5,149**	**4.4%**	**3,440**	**1,709**
Non-higher Education Executive Branch Total	**7.4%**	**3,899**	**5.3%**	**2,829**	**1,070**

* Vacancies are for the University System of Maryland only; Morgan State, St. Mary's College, and Baltimore City Community College are excluded from the vacancy rate calculation.

Job Family Composition

Change Between Fiscal 2001 and Fiscal 2005 Working Appropriation

Executive Branch Agencies[1]

Job Family	Total FY 2005 FTEs	Percent of Grand Total	Change from Fiscal 2001 FTEs	Percent Change from Fiscal 2001
Officials and Administrators	3,064	7.0%	138	4.7%
Protective Services	10,362	23.6%	112	1.1%
Professionals	18,636	42.4%	-84	-0.4%
Skilled Craft	670	1.5%	-85	-11.3%
Service/Maintenance	750	1.7%	-123	-14.0%
Paraprofessionals	3,026	6.9%	-214	-6.6%
Technicians	2,114	4.8%	-519	-19.7%
Administrative Support	5,317	12.1%	-744	-12.3%
Grand Total	**43,939**	**100.0%**	**-1,518**	**-3.3%**

[1] Excluding transportation, higher education institutions, and Historic St. Mary's City. Please note that these data include 133.3 positions scheduled to be abolished in the Department of Health and Mental Hygiene during fiscal 2005. Please also note that there are an additional 32.5 full-time equivalent positions statewide for which job family information is not available.

The State Workforce: What's Ahead in Fiscal 2006?

- **The Office of the Public Defender:** The final phase of the three-year Caseload Initiative is scheduled for fiscal 2006. In support of the initiative, 127.5 full-time equivalent (FTE) public defender, social worker, investigator, and support staff positions were added in fiscal 2004 and 2005. It is anticipated that 85 positions will be requested to complete the initiative in fiscal 2006 and to support the implementation of a restricted prohibition on juvenile waiver of counsel (Chapter 442, Acts of 2004).

- **Hickey School:** As of April 1, the Department of Juvenile Services (DJS) assumed responsibility for the operation of the Charles Hickey School (Hickey) as a temporary measure pending the award of a new contract to operate the facility. The fiscal 2005 budget bill included language providing DJS with a limited exemption to the contractual position cap for workers at Hickey.

  DJS has now decided that it will assume permanent responsibility for the operation of Hickey and is also developing new programming at Victor Cullen Academy (a facility that is currently closed) as well as Cheltenham. No detail as to spending and staffing levels for any of this programming has yet been provided to the committees. Nor has any request been made to make an exception from the fiscal 2005 regular position cap.

  In its baseline estimate, DLS assumed that DJS would need to create 280 permanent positions for the programming at Hickey. No assumption has been made for new positions at Victor Cullen or Cheltenham. That programming would require perhaps an additional 70 positions.

- **Higher Education:** Chapters 239 and 273 (Acts of 2004) have provided the University System of Maryland and Morgan State University (MSU) with the autonomy from the General Assembly to establish staffing levels absent specific legislative constraints, as did Chapter 401 (Acts of 2003) for St. Mary's College. Fiscal 2005 student enrollment is projected to increase approximately 2.0 percent over fiscal 2004 levels. By the end of October 2004, the impact of this legislation has been to add 34 FTE positions at MSU, 14 FTE positions at St. Mary's College, and 201 FTE positions at the University System of Maryland for fiscal 2005, a 1.2 percent total increase in staff over fiscal 2004. While student enrollment is also projected to increase 2.7 percent between fiscal 2005 and 2006, the impact Chapters 401, 239, and 273 will have on higher education's workforce for fiscal 2006 is indeterminate.

Department of Legislative Services
Health Insurance Baseline Forecast
Fiscal 2004 – 2006

	FY 2004	Projected FY 2005	Projected FY 2006	FY 05 - 06	% Increase FY 05 - 06
Health Maintenance Organization Premiums	$60.9	$71.3	$83.2	$11.9	16.6%
Preferred Provider Option Health Plans	207.6	224.0	234.4	10.3	4.6%
Point of Service Health Plans	159.0	174.9	185.2	10.3	5.9%
Prescription Plan	223.7	253.1	291.0	38.0	15.0%
Dental Plans	11.9	12.7	14.1	1.4	11.0%
Administration Costs	6.5	6.0	6.5	0.5	7.7%
Total Cost Projection	**$669.7**	**$736.7**	**$814.3**	**$77.7**	**10.5%**
Total Fiscal 2004 Working Appropriation, Fiscal 2005 Legislative Appropriation, and Fiscal 2006 Baseline	**$670.5**	**$694.6**	**$814.3**	**$119.7**	**17.2%**
Difference Between Projections and Budget	**$0.8**	**-$42.1**	**$0.0**		

Pension System Rates and Actuarial Funding Levels
Fiscal 2005 – 2006

Plan	FY 2005 Rate	FY 2006 Rate	FY 2006 "True Rate"	Actuarial Funding Level	Total Budget Increase ($ in Millions)
Corridor-funded Plans					
Employees	4.73%	5.76%	9.88%	89.2%	$28.9
Teachers	9.35%	9.35%	10.16%	92.8%	0.0
Non-corridor Funded Plans					
State Police	0.00%	8.22%	8.22%	107.2%	6.6
Judges	36.72%	41.12%	41.12%	80.1%	1.5
Law Enforcement Officers	37.73%	38.47%	38.47%	63.3%	0.3
Aggregate	**7.97%**	**8.46%**	**10.42%**	**91.2%**	**$37.3**

Note: Funding levels reflect State funds only and exclude any municipal contributions or funds.

Source: Milliman USA

- **Corridor Method:** Chapter 440, Acts of 2002 established what is known as the "corridor method" of pension funding. By this method, the contribution rates for the Employees' and Teachers' pension systems are frozen at 2002 levels, so long as the systems remain actuarially funded between 90 and 110 percent inclusive. Should the actuarial funding levels fall outside this "corridor," the statute calls for an adjustment of 20 percent of the difference between the prior year's contribution rate and the "true rate" (the level by which normal costs are absorbed plus a 25-year scheduled amortization component of any unfunded accrued liability).

- **State Police Rate Increase:** During the 2004 actuarial valuation by Milliman USA, it was discovered that for an unknown period of years, a segment of participants in the State Police system (and Judges' and Law Enforcement Officers' systems to a lesser degree) were being improperly "coded" in the actuarial database engine. The benefits owed to these employees were being computed on a single-life annuity basis, where they should have been coded as joint-and-survivor annuities. As a result, the State Police pension system has long been operating under an assumption that the system was inordinately over-funded. Based on a 0 percent contribution rate in fiscal 2005 and the aforementioned coding error, the State Police surplus fell from $222.8 million to $87.4 million. The contribution rate for the State Police will increase to 8.22 percent of payroll in fiscal 2006. If market investment returns approximate expectations (7 to 8 percent), then the 8.22 percent contribution will not add to the surplus, rather only slow the degradation of the surplus. This occurs because the 8.22 percent contribution does not exceed the normal cost of 25.05 percent (the present value of the cost of future benefits owed).

Part 10

Revenue Stabilization Account

State Reserve Fund Activity – Fiscal 2004 to 2006
($ in Millions)

	Rainy Day Fund	Dedicated Purpose Acct.	Catastrophic Event Acct.	Joseph Fund Acct.
Balances on Hand 6/30/03	**$490.2**	**$11.4**	**$0.2**	**$8.2**
Fiscal 2004 Appropriations	0.0	0.0	0.0	0.0
Fiscal 2004 Deficiency Appropriations			10.0	
Expenditures				
Hurricane Isabel Reconstruction			-2.9	
Child Welfare Protective Services				-8.2
TANF/Welfare Programs		-11.4		
Estimated Interest	6.4			0.0
Balances on Hand 6/30/04	**$496.6**	**$0.0**	**$7.4**	**$0.0**
Fiscal 2005 Appropriations	103.7	3.0	0.0	0.0
Expenditures				
Hurricane Isabel Reconstruction		-3.0	-4.4	
Transfers to General Fund	-91.0			
Estimated Interest	10.2			0.0
Estimated Balances 6/30/05	**$519.4**	**$0.0**	**$3.0**	**$0.0**
Fiscal 2006 Appropriations	249.7	50.0	0.0	0.0
Expenditures				
Reimburse TTF		-50.0		
Transfers to General Fund	0.0			
Estimated Interest	16.1			0.0
Estimated Balances 6/30/06	**$785.2**	**$0.0**	**$3.0**	**$0.0** [(1)]
Balance in Excess of 5% GF Revenues	**$218.3**			

Note: Totals may not sum to total due to rounding.

[(1)] Joseph Fund Account balance is projected to be $13,600 at the end of fiscal 2006.

TTF = Transportation Trust Fund

TANF = Temporary Assistance for Needy Families

Sources: Department of Budget and Management; Office of the Comptroller

Part 11

Spending Affordability Concept

State Spending Under the Spending Affordability Concept
In Relation to Maryland Personal Income
($ in Millions)

Session	Appropr. Under SA	Percent Change	CY	Personal Income	Percent Change
1983	$4,799		1983	$61,842	
1984	5,090	6.1%	1984	68,984	11.5%
1985	5,474	7.5%	1985	75,325	9.2%
1986	5,909	8.0%	1986	81,069	7.6%
1987	6,477	9.6%	1987	87,696	8.2%
1988	7,041	8.7%	1988	95,868	9.3%
1989	7,684	9.1%	1989	103,528	8.0%
1990	8,374	9.0%	1990	109,686	5.9%
1991	8,614	2.9%	1991	113,436	3.4%
1992	8,667	0.6%	1992	118,848	4.8%
1993	8,865	2.3%	1993	122,906	3.4%
1994	9,332	5.3%	1994	128,523	4.6%
1995	9,771	4.7%	1995	133,814	4.1%
1996	10,119	3.6%	1996	140,035	4.6%
1997	10,509	3.9%	1997	147,843	5.6%
1998	10,998	4.6%	1998	157,784	6.7%
1999	11,639	5.8%	1999	167,075	5.9%
2000 (1)	12,705	9.2%	2000	181,957	8.9%
2001 (2)	13,752	n.a.	2001	191,257	5.1%
2002	14,327	4.2%	2002	198,544	3.8%
2003	14,535	1.5%	2003	206,166	3.8%
2004 (3)	15,485	6.5%	2004	217,562	5.5%
2005 (3)	16,367	5.7%	2005	229,936	5.7%

Note: Appropriations reflect post-session corrections and changes in methodology and personal income reflects revisions to earlier years.

(1) This is the 2000 session SAC appropriation that includes cigarette restitution funds (CRF). Without CRF, the increase would have been 6.9 percent.

(2) This is the 2001 session SAC appropriation utilizing a revised method for calculating the SAC limit. Subsequent years also reflect the revised methodology.

(3) Personal income in 2004 and 2005 projected by the Board of Revenue Estimates (December 2004).