



**TREASURER'S REPORT TO  
LEGISLATIVE POLICY COMMITTEE**

**June 1, 2015**

**Nancy K. Kopp**

*State Treasurer*

**Section 5-104 of the State Government Article of the Annotated Code of Maryland provides that, “The Treasurer shall address the Legislative Policy Committee of the General Assembly on a semi-annual basis and as necessary on issues of legislative importance, including the activities of the Board of Public Works, bond sales, and investment and procurement initiatives.” This Report is in fulfillment of that law and covers the period since the Report of December 16, 2014. I invite and welcome further discussion with the Committee at your convenience.**

The State Treasurer’s activities and responsibilities are of particular concern to the Legislature. One of seven statewide Constitutional officers, and the only one elected by the General Assembly, the State Treasurer’s duties are multifaceted and extend throughout State government and higher education. The Treasurer’s duties include membership on the Board of Public Works and Board of Revenue Estimates and Chairmanship of the Capital Debt Affordability Committee. The Treasurer presently also serves as Chair of the Board of Trustees of the College Savings Plans of Maryland and the Board of Trustees of the State Retirement and Pension System. She is a member of the governing boards of the Teachers’ and Employees’ Supplemental Retirement Plans, the Maryland Health and Higher Education Facilities Authority, the Maryland Small Business Development Financing Authority and of the Maryland Agricultural Land Preservation Foundation. Several of these Boards work under the general oversight of legislative committees which are in periodic receipt of reports and communications from the Office, as do the two legislative budget committees.

We continue to plan and conduct our bond sales effectively, while striving to maintain Maryland’s coveted AAA bond rating. We monitor the market routinely to take advantage of savings as they become available, such as by refunding our General Obligation Bonds or issuing new types of debt such as Qualified Zone Academy Bonds. And as you know, we continue to invest State funds prudently and conservatively to minimize risk to the Maryland taxpayers.

The items set forth below detail a number of our recent achievements and we are always available to provide greater information or answer questions regarding these and other issues.

## **BOARD OF PUBLIC WORKS**

Between December 1, 2014 and May 15, 2015, the Board of Public Works (“BPW”) met 11 times to consider State procurements, expenditures of capital appropriations, the acquisition, use and transfer of State assets, issuances of licenses to dredge and fill wetlands, and the acquisition of land and easements in support of Program Open Space, the Conservation Reserve Enhancement Program, the Rural Legacy Program and the Agricultural Land Preservation Program.

During this timeframe, in addition to the State General Obligation Bond Authorizations, including Qualified Zone Academy Bond authorizations, and the Capital-Lease financings discussed in more detail in the Debt Management Section of this Report, the following items, worthy of note, were considered by the Board of Public Works:

### **State Budget**

- Approved reductions to the State’s Operating Budget for FY 2015 of \$198,655,188 in General Funds and \$7,450,000 in Special Funds (total reduction of \$206,105,188). The General Fund reductions were to be achieved by a 2% across-the-board agency reduction combined with additional agency-specific reductions. (1/7/15)
- Approved a request of the Department of Budget and Management to abolish 506 full-time equivalent (FTE) positions and reduce associated appropriations pursuant to the Voluntary Separation Program (VSP) adopted by the State. The action eliminated 458 positions held by regular employees in the Executive Branch agencies who were approved for the VSP and 48 vacant positions. These position reductions provide a savings in FY 2015 of \$2.48 million. Approval was also given to additional agency-specific FY 2015 General Fund reductions totaling \$5.02 million, for a total FY 2015 State Operating Budget reduction of \$7.5 million. (5/13/15)

### **Public School Construction**

- State School Construction – Capital Improvement Program (CIP) for FY 2016: Approved allocations totaling \$318.19 million. (05/13/15)
  - Incorporates \$187.5 million approved by the BPW on January 28, 2015.
  - Approval at the May 13, 2015 BPW meeting was given for additional projects in the amount of \$130.69 million.
  - The FY 2016 CIP includes \$280 million of new bond authorizations and \$38.19 million in reverted funds from the Statewide Contingency Account.
- Aging School Program for FY 2016: Approved allocations totaling \$7.1 million (\$6.1 million in new authorizations + \$0.997 million in reverted funds). (05/13/15)

- Qualified Zone Academy Bond Program for FY 2016: Approved allocations to thirteen school systems in the amount of \$5,515,000 (\$4,625,000 in new authorizations + \$890,000 of reallocated contingency balances). (05/13/15)

### **Baltimore City 21<sup>st</sup> Century Public School Construction Initiative**

- Frederick Elementary School: Renovation and Addition:
  - Approved a request of the Maryland Stadium Authority (MSA) to award a contract for construction manager, preconstruction services. (12/17/14)
- Ft. Worthington Elementary School: Construction of Replacement School:
  - Approved a request of MSA to award a contract for construction manager, preconstruction services. (12/17/14)
- John Eager Howard Elementary School: Renovation and Addition:
  - Approved a request of MSA to award a contract for design and engineering services. (1/28/15)
  - Approved a request of the Maryland Stadium Authority to award a contract for construction manager, preconstruction services. (2/18/15)
- Lyndhurst Elementary School: Renovation and Addition:
  - Approved a request of MSA to award a contract for design and engineering services. (1/28/15)
  - Approved a request of MSA to award a contract for construction manager, preconstruction services. (2/18/15)
- Robert Poole Middle School: Renovation and Addition:
  - Approved a request of MSA to award a contract for design and engineering services. (3/18/15)
- Arundel Elementary/Middle School: Construction of Replacement School:
  - Approved a request of MSA to award a contract for construction manager, preconstruction services. (4/15/15)
  - Approved a request of MSA to award a contract for design and engineering services. (4/15/15)

### **State Services and Facilities**

- Approved a request of the Maryland State Department of Education (MSDE) to award a contract to provide program management of all activities of the Partnership for the Assessment of Readiness for College and Career (PARCC) Consortium (12 states including Maryland), including operationalizing the PARCC assessment. (12/3/14)

- Approved a request of the Department of Public Safety and Correctional Services to award a contract to construct a Youth Detention Center facility in Baltimore City to house juvenile detainees charged as adults. The facility will include detainee housing, classrooms and educational services, administration, medical, dental and behavioral health treatment services, visitation, recreation and food services for 60 youth in a separate building that provides sight and sound separation from the pre-trial adult population. (5/13/15)
- Approved Phase II of an energy performance contract to implement energy saving measures for the Department of Juvenile Services at its Charles Hickey School, Baltimore Juvenile Justice Center, Lower Eastern Shore Children's Center, Alfred D. Noyes Children's Center, Western Maryland Children's Center, and Victor Cullen Center Facilities.
- Approved the Maryland Department of Transportation (MDOT) disposing of approximately 2.8 acres at the interchange of MD 355 and Montrose Road in Montgomery County. The property would be purchased by Montgomery County and used for a police and fire station, with a mix of senior market-rate and senior affordable housing above the station, to serve planned development in the White Flint area. (1/7/15)
- Approved the sale by Coppin State University of approximately 1.5 acres of real property, including the former Hebrew Orphan Asylum, to The Coppin Heights Community Development Corporation for private development of a community health center. (2/18/15)
- Approved the Maryland Port Administration (MPA) entering into an interagency agreement with the Maryland Environmental Service (MES) for MES to undertake the construction of the Stage 1 expansion of the Cox Creek Dredged Material Containment Facility in Anne Arundel County onto adjacent MPA-owned property. (4/1/15)
- Approved the extension of the MPA contract with MES for continuation of Phase II construction of the Masonville Dredged Material Containment Facility to increase the planned placement capacity of the facility. (4/1/15)
- Approved the transfer of 56 +/- acres located at the Springfield Hospital Center from the Department of Health and Mental Hygiene to the Maryland Military Department to provide a site for construction of a new Maryland Army National Guard Readiness Center to be known as the Freedom Readiness Center. The new facility will replace the existing Ellicott City and Catonsville Armories. (5/13/15)

### **Elections**

- Approved a request of the State Board of Elections to lease a new statewide voting system that will produce a voter-verifiable paper record of each voter's selections. The

new voting system is intended to be in place and ready for use during the 2016 Presidential Election Cycle. (12/17/14)

- Approved a request of the State Board of Elections to award a contract for operations and maintenance support for the State's election management system through the 2016 election cycle. (4/15/15)

### **BWI Marshall Airport**

- Approved a non-exclusive concession contract to operate and manage the BWI Marshall Rail Station Parking Garage and Public Automobile Parking Facilities. (12/3/14)
- Approved a request of the Maryland Aviation Administration to proceed with an expedited procurement of on-call maintenance and repair activities for a recently constructed stream restoration project that is a part of the Runway Safety Area Improvements Program. (1/28/15)
- Approved a Lease and Concession Contract with Alclear, LLC to establish and operate a Registered Traveler Security Screening Expedited Passenger Program (Registered Traveler). (2/18/15)
- Approved a Concession Contract with FlightCar, Inc. to establish and operate a non-exclusive Off-Airport Rental Car Concession, in an effort to provide airline passengers at BWI Marshall with alternative ground transportation venues other than the ground transportation services currently offered (on-Airport rental car services, scheduled ground transportation services and Airport taxicab services). (3/4/15)
- Approved a request of the Maryland Aviation Administration to award a contract for the construction of a new passenger security checkpoint and airside passenger connector between Concourses D and E. (3/4/15)
- Approved a non-exclusive concession contract to establish, operate and maintain a concierge hotel reservation service. (5/13/15)

### **State Property Tax Rate**

- Set the State Real Property Tax Rate for FY 2016 based upon the recommendation of the Commission on State Debt. The rate remained unchanged at 11.2 cents per \$100 of the full assessed value of real property other than that of public utilities and 28.0 cents per \$100 of the full assessed value of real property of public utilities. (04/29/15)

### **Bonds**

- Approved the Maryland Stadium Authority issuing \$9,585,000 in non-tax supported Revenue Bonds (Series 2014 Refunding Revenue Bonds) to repay the outstanding

principal balance on the Camden Yards Sports Complex Taxable Revenue Bond Series 2011. (12/3/14)

- Adopted resolutions authorizing the issuance and sale by MDOT of its Consolidated Transportation Bonds, Series 2015 in an amount not exceeding \$350 million. (1/7/15)
- Adopted resolutions authorizing the issuance and sale by MDOT of its Consolidated Transportation Bonds, Series 2015 (Second Issue) in an amount not exceeding \$150 million. (4/15/15)
- Adopted resolutions authorizing the issuance and sale by MDOT of its Consolidated Transportation Bonds, Refunding Series 2015 in an amount not exceeding \$400 million. (4/15/15)

### **Personnel, Procurement & Regulations**

- Personnel: “Rule of 100”: Pursuant to Section 7-236 of the State Finance & Procurement Article and Section 32 of the Budget Bill for 2015 (SB 170), the Board of Public Works is authorized to create no more than 100 additional State funded positions during FY 2015. The following actions were taken as a result of this authorization:
  - Approved the request of the Maryland Aviation Administration to establish five special-funded positions to maintain service for expanded facility operations and passenger growth at BWI Marshall Airport, as well as to meet Federal Aviation Administration staffing requirements. (1/7/15)
  - Approved the request of the Governor’s Office of Minority Affairs to add one full-time equivalent position as a contractual conversion to provide monitoring and compliance duties relating to the State’s Minority Business Enterprise (MBE) Program and the Program’s application at each of the State’s Video Lottery Terminal Facilities. (1/7/15)
  - With approval of these 2 requests during this reporting period, 56.1 positions have been created within the “Rule of 100” for FY 2015.
- Personnel: Approved the request of the Department of Business and Economic Development (DBED) to create two positions outside of the “Rule of 100” to serve as the primary contacts for coordination and management of grants related to supporting the Missions of Maryland’s military installations. The requested positions are supported entirely with federal funds and will be abolished when funds are no longer available. (12/3/14)
- Personnel: Approved the request of DHMH to create one position outside of the “Rule of 100” to serve as the Project Director for the Maryland Behavioral Health for Adolescents and Young Adults grant that supports a demonstration project to generate knowledge and new approaches to the addressing prescription opioid use and heroin overdose deaths of

youth and young adults in Maryland.. The establishment of the full-time position is a condition of the federal funding, is supported entirely with federal funds, and will be abolished when the funds are no longer available. (5/13/15)

- Adopted new regulations and amendments to existing COMAR provisions to implement changes to State Procurement Law made during the 2014 Legislative Session and to clarify the veteran-owned small business requirement. These changes: (1) implement the sunset of the individual surety law and the unsolicited proposal law; (2) clarify that a veteran-owned small business may use its own workforce to meet a VSBE goal; (3) provide for debarment from State contracting for Internal Revenue Code violations and State Living Wage and Prevailing Wage violations; and (4) update the membership and requirements of the Maryland Green Purchasing Committee. (2/18/15)
- Approved publishing for comment in the *Maryland Register* amendments to existing COMAR provisions relating to the Public School Construction Program to establish in regulation the State cost share percentage for each subdivision and the Maryland School for the Blind for FYs 2016, 2017, and 2018 and to set a maximum State cost share percentage of 98% in FY 2019 and subsequent years. (4/1/15)
- Approved publishing for comment in the *Maryland Register* amendments to existing COMAR provisions relating to the Public School Construction Program to establish relocatable classroom indoor environmental quality standards for relocatable classrooms built after July 1, 2015. (4/1/15)

### **Lottery & Gaming**

- Approved a request of the Maryland State Lottery & Gaming Control Commission to modify the State's contract with two manufacturers of Video Lottery Terminals (VLTs) to increase the VLT trade-in amounts contained in the original contract in order to accommodate the law change that removed the Commission's responsibility to own or lease the VLTs and instead requires each VLT facility, except for Ocean Downs and Rocky Gap, to acquire its own VLTs. (3/18/15)
- Approved a request of the State Lottery & Gaming Control Commission to modify the State's contract for a Video Lottery Terminal Program in order to provide services and equipment necessary to start-up and operate a sixth VLT facility in Prince George's County. (5/13/15)

### **Environmental Programs & Natural Resources**

- Approved a request of the Maryland Department of the Environment to award a contract to support the Multi-State Zero Emission Vehicle Program Implementation Task Force. (12/3/14)



- Approved a request of the Department of Natural Resources to award a contract to design and construct a stone revetment and living shoreline project to protect the southwest portion of St. Clement's Island. (12/3/14)
- Approved a request of the Department of the Environment to award a contract to support Maryland's participation in the Regional Greenhouse Gas Initiative and the implementation of regulations for Maryland's CO2 Budget Trading Program. (5/13/15)

## TREASURY MANAGEMENT DIVISION

### Banking Services Department

The primary mission of the Banking Services Department (BSD) is to manage and control relationships with vendors providing financial services for the State of Maryland, to anticipate agency banking requirements, and respond timely to agency requests.

The Department is directly responsible for managing the banking needs for all agencies of the State. BSD continues to oversee enhancements added to lockbox processing and improved reconciliation processes throughout the State. Total business process improvement at the agencies continues. Currently, the STO is leading the preparation for changes in Credit Card Processing which will take effect in June and October of 2015.

The Department procures financial products and services statewide. Twelve months ago, BSD conducted a procurement on behalf of the College Savings Plans of Maryland (CSPM) to provide services for the accounts and assets under the control of the Board, including depository, disbursements, lockbox and custodial services. The BSD is providing on site assistance in implementation of best practices for the procured services for CSPM. The Department continued the implementation process for the Agency Depository Contracts for statewide banking depository services. Almost 400 agency bank accounts have been moved to the newly designated depositories. Public Resources Advisory Group (PRAG) was awarded the Investment Advisor and Bidding Agent Contract and assisted in the 2015 First Series B bond refunding escrow. BSD participated in the RFP process for Quality Assurance Services for Electronic Benefits Transfer implementation for WIC for Maryland and U.S. Virgin Islands. The second WIC procurement for processing services is underway and BSD will lead the Evaluation Committee.

BSD continues to ensure the accurate and timely recordation of State funds and the reconciliation of the State's bank accounts to the State's R\*STARS accounting system. The Department must account for the receipt of all warranted deposits and the disbursement of all warranted payments. To meet these responsibilities, a comprehensive daily cash reconciliation is performed which allows BSD to proactively resolve agency banking issues. Even as the volume of transactions has increased, the processes and controls developed by BSD continue to result in a timely, accurate, and well documented reconciliation of the State's cash accounts. For fiscal year 2014, total cash receipts and disbursements exceeded \$181 billion. As of April 30<sup>th</sup> total cash receipts and disbursements exceeded \$174 billion for the current fiscal year. The State's General Fund bank accounts continued to be reconciled to the penny on a daily basis to the State's general ledger.

In addition to the reconciliation duties, the Department performs daily operational functions that are critical to the movement of funds into and out of the State's bank accounts and to the recordation of these transactions in R\*STARS. These include:

- Processing the drawdown of funds from federal programs and grants
- Initiating Federal Reserve wire payments
- Managing foreign currency transactions

- Processing check stop payments, cancellations and reissues
- Initiating replacement checks for failed ACH payments
- Recovering funds for fraudulent check presentments
- Providing transaction research assistance to State agencies
- Managing the Unpresented and Undeliverable Check Funds
- Recordation in R\*STARS of all bank adjustments
- Maintenance of tables to allow for accurate posting of electronic receipts

Another responsibility of the Department is to ensure protection of all State funds on deposit with financial institutions through monitoring of bank account and collateral balances. Utilizing the Treasurer's Bank Account Information System (TBAIS), BSD monitors over 1,800 agency bank accounts at 23 financial institutions. Total posted collateral as of April 30<sup>th</sup>, 2015 was \$526+ million. The annual Bank Account Survey, a verification tool used to ensure all accounts are collateralized appropriately and monitored monthly, has been completed. The results of the survey were updated in TBAIS to ensure collection of all interest owed to the General Fund.

The BSD continues to serve as the State's authority for the development, control and maintenance of statewide policies and procedures for banking products and services. We continually strive to stay at the forefront of changes in banking products and services offered in the financial industry. The Department will continue to explore new financial products and improved data delivery methods that will increase its capabilities to provide efficient, cost-saving, banking and financial services to Maryland State agencies.

## **Investment Department**

The Treasurer's conservative investment policy and practices have protected the investment portfolio through these continued unprecedented economic times. It is a true accomplishment in this environment to report that all principal is intact and a modest but continuous return has been earned on the portfolio. The par value of the General Fund investment portfolio for April 30, 2015 was \$6,305,539,049.74 as compared to April 30, 2014 when it was \$6,123,432,943.26. This is an increase of over \$182 million dollars.

On April 30, 2015 the portfolio was earning an average of 1.043%, compared to 1.059% for the same date in 2014. The return reflects the diligence of the investment staff despite the impact of the Federal Open Market Committee maintaining the Fed Funds Target rate at .25% or less since December 16, 2008. For comparison, the three month constant maturity Treasury Bill averaged 0.025% from July 2014 until the end of April 2015 as compared with 0.045% for the same time period in the previous fiscal year. The low rate environment combined with the highly conservative portfolio strategy focused on liquidity to offset unpredictable and volatile cash flows has resulted in continued moderate but positive interest earned.

The General Fund gross interest earnings received year-to-date for fiscal year 2015 are \$46,958,325 compared to \$56,353,238 received for the same time period in fiscal year 2014. The almost \$9.4 million decrease in interest received is directly attributable to reduced cash balances available for investment and the historically low-rate environment.

The following chart tracks the number of individual agency accounts that receive an interest allocation from the total interest earned on the investment portfolio. It should be remembered that as the total General Fund portfolio decreases, the proportion of Agency Funds to General Funds increases and therefore their allocated share increases.

**Total Interest Earned**  
**% of Total Interest Earned Allocated to State Agencies**

<b>Fiscal Year</b>	<b>Net General Fund</b>	<b>Allocated to State Agencies</b>	<b>Total</b>	<b>% of Total Allocated to State Agencies</b>
<b>2000</b>	121,951,720	103,173,287	225,125,007	46%
<b>2001</b>	136,981,074	144,249,899	281,230,973	51%
<b>2002</b>	82,641,807	66,399,769	149,041,576	45%
<b>2003</b>	37,205,637	42,240,523	79,446,160	53%
<b>2004</b>	25,037,345	29,053,449	54,090,794	54%
<b>2005</b>	52,886,074	54,538,463	107,424,537	51%
<b>2006</b>	149,613,238	109,222,108	258,835,346	42%
<b>2007</b>	150,798,001	205,589,917	356,387,918	58%
<b>2008</b>	155,170,184	207,179,098	362,349,282	57%
<b>2009</b>	102,768,740	142,619,087	245,387,827	58%
<b>2010</b>	44,190,425	87,921,654	132,112,079	67%
<b>2011</b>	53,178,733	87,900,159	141,078,892	62%
<b>2012</b>	23,207,535	48,647,954	71,855,489	68%
<b>2013</b>	8,646,595	40,710,863	49,357,458	83%
<b>2014</b>	19,133,149	52,602,770	71,735,919	73%
<b>APRIL 2015</b>	591,917	46,366,408	46,958,325	98%

The Securities Lending Program continues to provide additional revenue. The program has earned \$129,382.92 so far in fiscal year 2015. This compares with \$213,598.94 for the same period in fiscal year 2014. The continued fortification of Bank Balance sheets and slower economic environment has reduced borrowers' need for the securities in the State's portfolio.

The Office continues to increase minority business participation in the investment of State funds. Twenty-four MBE broker/dealers are on the Office's approved list for fiscal year 2015, and they have handled investments of \$254 million out of \$690 million so far this fiscal

year. This compares with fiscal year 2014, when the Office had twenty-four approved MBE broker/dealers who handled \$150 million out of \$761 million in investments by the end of April.

The Maryland Local Government Investment Pool (MLGIP) AAA rating was reaffirmed by Standard and Poor's on March 30, 2015. The Pool balance at April 30, 2015 was \$3,641,489,090 compared with \$3,603,166,747 for the same date in 2014. This is an increase of over \$38 million dollars due to participants' higher available cash balances and lack of trusted alternative investments. The MLGIP is paying 0.06% as of April 30, 2015 compared to 0.06% last year. The 302 participants continue to use the Pool due to the lack of safe short-term investment alternatives for Investment Pool members at a comparable yield. The MLGIP is in total compliance with the 2010 changes in Money Market rules and regulations and preparing to comply with the proposed changes for October 2016. The MLGIP Advisory Board is monitoring all changes proposed by the SEC and GASB for Institutional Money Market Funds. The State Treasurer's Office has been very active lobbying the SEC and now GASB about proposed changes to the Funds and the way in which the changes might adversely impact local investment pools managed by states across the country.

The Office continues to invest according to the officially adopted State Treasurer's Investment Policy, which sets out investment goals, priorities and constraints. The overriding goal is to assure sufficient liquidity to maintain uninterrupted funding of State government and legislated payments. As revenues have become less predictable and more volatile, the strategy has been adjusted to ensure liquidity. The State Treasurer's Office continues to review and compare our cash management and investment policies and practices with those of peer AAA-rated States to ensure best practices are followed and implemented.

## DEBT MANAGEMENT DIVISION

### Ratings

On February 19th, in conjunction with the sale of Maryland's General Obligation Bonds State and Local Facilities Loan of 2015, Series A and B, Moody's Investors Service, Standard & Poor's (S&P) and Fitch Ratings all affirmed their AAA ratings for Maryland's General Obligation debt. Maryland is one of only ten states to hold the coveted AAA rating, the highest possible rating, from all three major rating agencies. S&P has rated the bonds AAA since 1961. Moody's has assigned the bonds a rating of Aaa since 1973, and Fitch Ratings has rated the bonds AAA since 1993. The other nine states that hold AAA ratings from all three rating agencies are Alaska, Delaware, Georgia, Iowa, Missouri, North Carolina, Texas, Utah and Virginia.

#### *Meetings with Rating Agencies*

The Treasurer's Office has provided the rating agencies with regular updates on the financial condition of the State. The next conference call with the rating agencies is expected prior to the July sale of the 2015 Second Series General Obligation Bonds.

#### *Ratings Reports*

Generally there is consensus among the rating agencies in evaluating the State's credit strengths and weaknesses. All three major rating agencies cite Maryland's debt policies, fiscal management and economy as credit positives and the State's debt burden and pension funding as concerns.

#### *Financial Management*

All three rating agencies point to the State's history of strong, sound financial management as a credit strength. Moody's cites a "history of strong financial management" and "adequate reserve levels despite recent draws" as two of the three highlighted "strengths" of Maryland's credit profile. In assessing Maryland's management practices, S&P assigned a rating of "strong" to this factor, noting: "Long history of proactive financial and budget management, including implementation of frequent and timely budget adjustments to align revenues and expenditures." Fitch Ratings further said: "Financial operations are conservative, and the state maintains a well-funded rainy day fund. The state took repeated action during the course of the recession to address projected budget gaps, including raising tax revenues, cutting spending, and using rainy day and other balances."

#### *Debt Policies and Debt Burden*

In the case of all three rating agencies, the State's debt affordability guidelines and rapid amortization of debt are considered credit strengths and help offset concerns the rating agencies have regarding the State's debt burden. Fitch describes the State's debt management as "strong and centralized" and specifically highlights the debt affordability policies and the constitutional

requirement to amortize debt within 15 years. Moody's states the constitutional limit "help[s] restrain growth in the outstanding balance." The Capital Debt Affordability Committee is referred to as having a positive role in debt management by both Moody's and S&P with S&P stating "the clearly defined debt affordability process" has a positive stabilizing effect on the state's debt profile.

### *Economy*

In assigning its 'AAA' long-term rating and stable outlook, S&P said: "The rating reflects what we view as the state's: Broad and diverse economy, and; Strong wealth and income levels." S&P further states: "The stable outlook on Maryland reflects our view of the state's proactive midyear adjustments to align the budget with slower-than-anticipated revenue growth." Fitch simply says "the state has a diverse, wealthy economy, benefiting from its proximity to the nation's capital". Fitch states Maryland's "diverse and wealthy service-oriented economy remains a source of credit strength", citing a lower than national unemployment and high personal income as strengths of the Maryland economy.

Each rating agency cites ties to the federal government as both having benefits and risks to Maryland's economy. Moody's noted "the impact of federal sequestration may be tapering off, reducing this source of drag on state economic and revenue growth." S&P noted "While federal fiscal policy remains a challenge to the state's budget and long-term financial plan, we believe that Maryland continues to monitor developments and has options to mitigate this risk based on its well-developed budget policies and financial reserves." In assessing the state's economy, Fitch indicated "[t]he state's economy has long benefited from proximity to the nation's capital, although the prospect of federal budget austerity poses a degree of uncertainty for the state given its large federal agency presence and associated private contracting."

### *Pension and other liabilities*

Pension reforms enacted during the 2011 Legislative Session, the teacher pension sharing enacted during the 2012 Legislative Session, and the phase-out of the corridor funding method that was enacted during the 2013 Legislative Session are noted by each of the three rating agencies. Fitch Ratings noted "Despite pensions being a comparative credit weakness, the state has taken multiple steps to reduce their burden and improve sustainability over time." Moody's indicated "The financial condition of Maryland's retirement system represents a credit challenge for the state" but goes on to recognize that "[t]he state has taken a number of measures to reduce its pension burden." While noting the reforms, including those enacted in 2013, "investment returns in recent years have been greater than actuarially assumed,... potentially providing an additional opening for the legislature to again reduce the supplemental contributions to the system." S&P indicated "[t]he state's below- average pension funded ratios and annual contributions that do not meet the full ARC also continue to represent downside risk to the rating."

The current rating reports are available on the Treasurer's website at [www.treasurer.state.md.us](http://www.treasurer.state.md.us).

## **Closed Financings - General Obligation Bonds**

Since our last report, the State has conducted one sale of General Obligation bonds. The 2015 First Series was sold on March 4, 2015 and totaled \$883,360,000. The proceeds were used to finance new projects and refund existing bonds. The sale closed on March 17, 2015 and had two series:

Series A: \$518.0 million in Tax-Exempt Bonds sold in a competitive sale primarily to institutions

Series B: \$365.4 million of Tax-Exempt Refunding Bonds

The Series A bonds provided \$518.0 million, at a TIC (True Interest Cost) of 2.65%, to finance investments in capital projects critical to our State. The Series B refunding bonds saved taxpayers \$21.8 million in debt service costs. In addition, the State received a premium of \$74,682,961 to offset FY2016 debt service costs and provide \$48.4 million to fund capital projects on a pay go basis.

### **Closed Financing – Qualified Zone Academy Bonds**

Qualified Zone Academy Bonds (QZAB) totaling \$4.6 million were issued on December 18, 2014. The bonds earn federal tax credits at the rate of 4.38% per annum for Branch Banking & Trust Company until maturity on December 15, 2029.

### **Closed Financing – Leases**

The Capital Lease-Financing Program allows State agencies to acquire equipment and pay for those items over a three, five, or ten year time frame. Between December 1, 2014 and May 31, 2015, \$1,878,900 in capital equipment was leased by State agencies through the State Treasurer's Office. A total of \$28.1 million remains of the \$35 million authorized by the LPC through June 30, 2016.

The Treasurer's Office also finances Energy Performance Leases in cooperation with the Department of General Services, providing funding for energy conservation improvements at State facilities. The program finances significant up-front investments in conservation projects; the lease is paid using the savings in operating costs. No energy leases were financed since our last report.

### **Status of the Annuity Bond Fund**

Debt service on General Obligation Bonds is paid from the Annuity Bond Fund and the primary source of revenue for this fund is real property tax receipts. Over the years the debt service has also been supported on occasion by appropriations from the General Fund, as well. The Commission on State Debt met and released its annual report on April 15, 2015. In fiscal year 2016, \$252.4 million is appropriated from the General Fund to support debt service. On April 29, 2015, the Board of Public Works set the State property tax rate for FY 2016 at the same rates that have been in effect for FY 2015. Assuming current property tax rates are maintained



and other assumptions remain as currently estimated, a continued General Fund subsidy is projected for fiscal years 2017 - 2020. The complete report is available on the Treasurer's website at: <http://www.treasurer.state.md.us/debtmanagement/csd-reports.aspx>

## **INSURANCE DIVISION**

The Insurance Division is responsible for administering the State's Insurance Program which includes both commercial insurance coverage and self-insurance. Commercial insurance policies are procured to cover catastrophic property and liability losses, and other obligations derived from State contracts, statutes and regulations. Among the several exposures covered by commercial policies are State maintained toll bridges, tunnels and roads, the Baltimore Washington International Thurgood Marshall Airport, the Port of Baltimore, Maryland Transit Administration liability, assorted professional liability exposures, and student athlete accident insurance. The State self-insures a significant portion of its exposures and maintains the State Insurance Trust Fund to pay claims and the costs associated with handling those claims. Self-insurance coverage includes State-owned real and personal property, vehicles, and liability claims covered under the Maryland Tort Claims Act.

The Insurance Division contains three Units: Underwriting; Loss Prevention; and Claims, which includes Tort Litigation. The Division's goal is to provide statewide risk management through loss protection (Underwriting), loss control (Loss Prevention), and loss restoration (Claims and Tort Litigation).

### **Underwriting Unit**

The Insurance Division procures broker services for the purchase of commercial insurance to protect the State Insurance Trust Fund from catastrophic loss, to meet statutory or regulatory requirements, and for compliance with agency contractual agreements. Underwriting highlights for the past six months include the following:

- The Underwriting unit buys marine liability insurance to cover State-owned watercraft. The broker approached the incumbent carrier and three others for the January 1, 2015, renewal. The number of vessels is up from last year's 1,126 to 1,131. Our renewal reflected a 3.36% rate reduction, and even with the increased number of vessels, our premium went down \$302.
- The Maryland Port Administration's auto liability insurance coverage, effective January 1, 2015, was marketed to the incumbent carrier, Selective, and three other carriers, but only the incumbent offered a quote. There are limited insurance companies willing to write auto insurance policies with no collateral business. The number of vehicles has not changed from the expiring policy. The incumbent came in with a 3.7% rate increase which generated a premium increase of \$1,931.
- The Maryland Port Administration's liability coverage was renewed on January 31, 2015. The broker shopped the coverage to the incumbent carrier and two others. The Port's revenue is estimated to go up 2.63% in 2015. The successful offeror, Starr, submitted the most attractive quote with a flat premium on the primary policy and a 17% decrease in the excess layer; they reduced the deductible from \$25,000 to zero and included broader terrorism coverage.

The Underwriting Unit frequently addresses agencies' questions about commercial insurance and self-insurance coverage. Examples include:

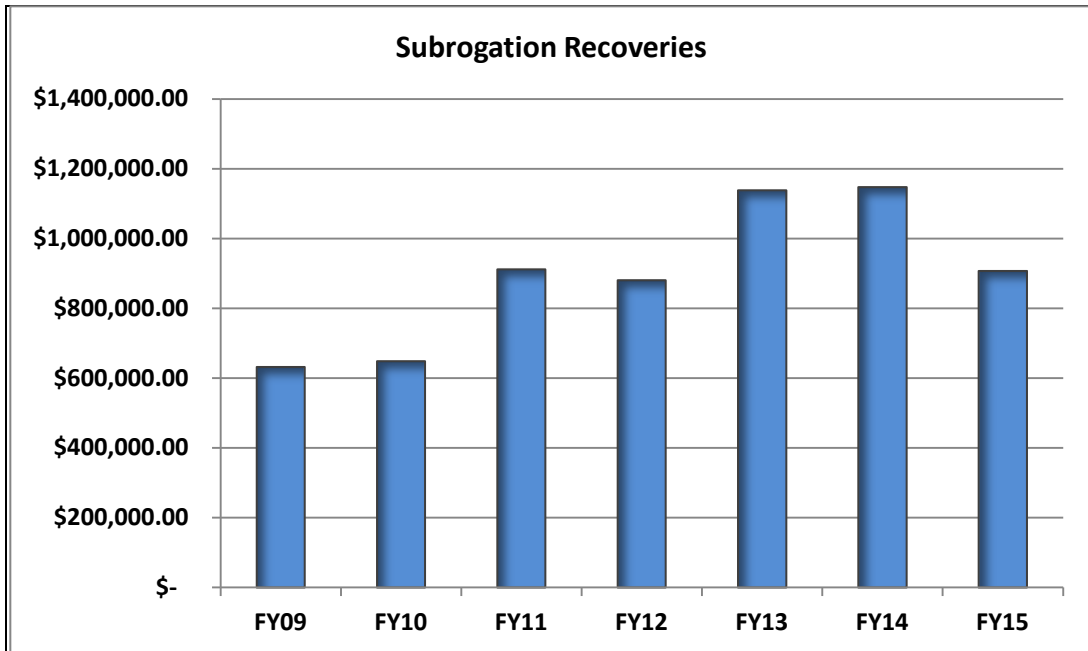
- Maryland Aviation Administration (MAA) requested our assistance on four contracts and RFPs regarding insurance requirements.
- MAA also had questions related to insurance for a community outreach project they are working on with the Baltimore City Department of Parks and Recreation.
- Department of Budget and Management asked for our input on insurance requirements on two RFPs.
- Maryland Energy Administration asked for assistance on minimum insurance requirements for an RFP for "Offshore Wind Services."
- Our broker hosted a webinar on March 31, 2015 for all 10 Maryland Colleges and Universities participating in the athletic participant's insurance that provides coverage for athletic injuries. The webinar addressed health care reform and its impact on their insurance coverage, and also addressed two ways the schools can lower the amount of claims which will affect their future insurance premiums.

## **Claims**

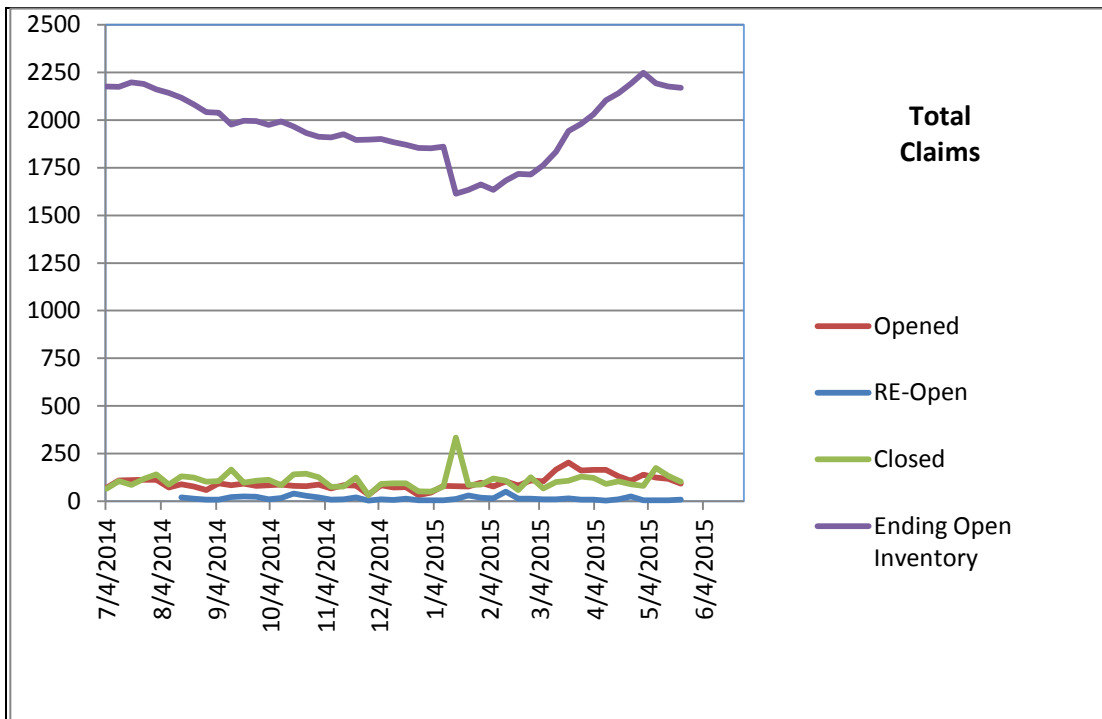
The Insurance Division's Claims Unit investigates and resolves liability claims filed under the Maryland Tort Claims Act, MD State Government Code Ann. §12-101 *et seq.* The Unit also handles claims for damage to State-owned property arising from sudden and accidental perils such as collision and comprehensive losses to autos, and a number of other perils such as fire, hail, lightning, and wind which may cause damage to State structures, equipment, and contents.

In addition to adjusting claims filed under the Maryland Tort Claims Act, the Unit is also charged with recovering the cost of damage to State automobiles and property caused by others. This subrogation recovery process helps to offset State Insurance Trust Fund liabilities and positively affects the Fund's solvency. Since 2007, the Claims Unit has focused on increasing subrogation recoveries by designating specific claims personnel to pursue these debts.

The year-to-date subrogation recoveries total for fiscal year 2015 is \$906,805. The total recovery for fiscal year 2014 was \$1,147,263; which surpassed both fiscal year 2013's recovery total of \$1,138,168 by 0.8% and fiscal year 2012's recovery total of \$880,929 by over 30.2%. FY 2015 subrogation recoveries are on track to meet or exceed FY 2014 recoveries.



In addition to subrogation activity, the open and closed claims are tracked to gauge activity and inventory. From November 1, 2014 through May 1, 2015, 2630 claims were opened, and 2567 claims were closed; which reflects a 1.02:1 open-to-close ratio.

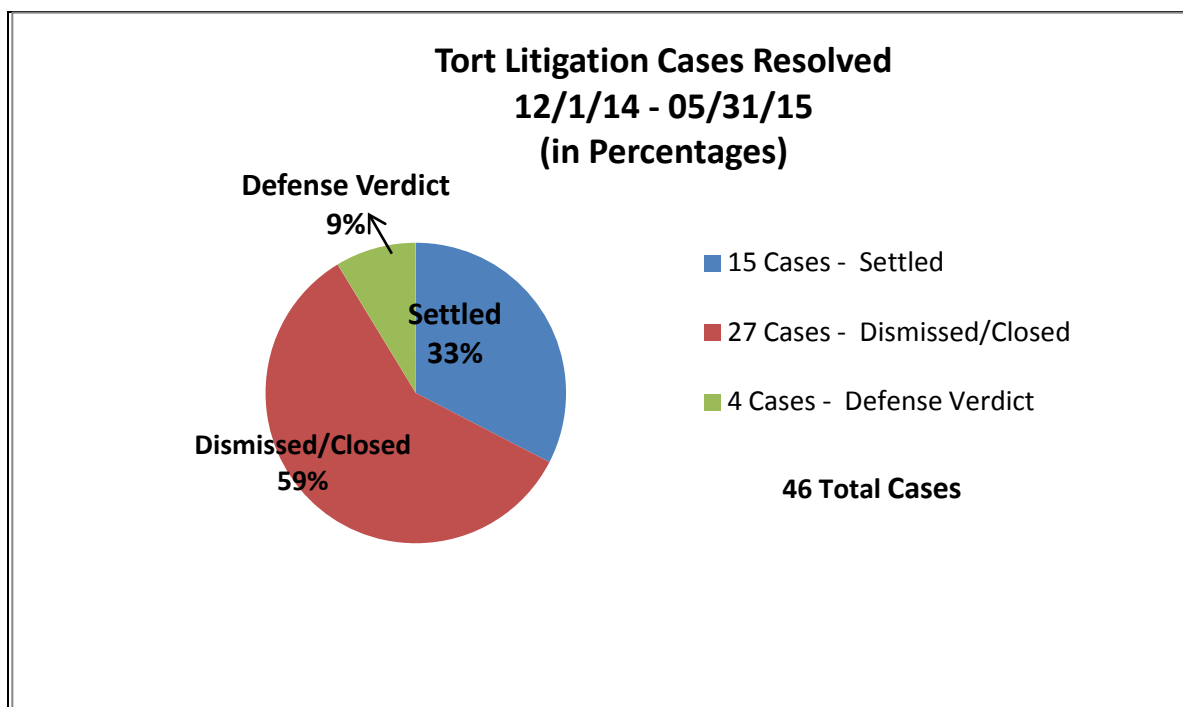


## Tort Litigation Management

The Litigation Manager works closely with the Office of the Attorney General to proactively resolve cases in litigation. The Litigation Manager investigates, evaluates and extends settlement authority to the Assistant Attorneys General on behalf of the Treasurer. In cases valued over \$100,000, the Litigation Manager briefs the Insurance Review Committee which includes the Chief Deputy Treasurer, the Supervising Tort Attorney, and other stakeholders.

The Litigation Manager also attends settlement conferences and other court mandated activities, along with providing updates on the status of certain litigation claims of interest. The Litigation Manager provides feedback to adjusters during the discovery process and upon resolution to help improve the adjusters' investigation and develops strategies on similar claims that may arise.

The Tort Unit handles a rolling docket of approximately 110 - 120 litigation claims. The Litigation Manager actively monitors trial verdicts and appeals and assesses the potential impact on the State Insurance Trust Fund. The Litigation Manager also analyzes the data in order to track the litigation outcomes. The disposition of the cases between December 1, 2014 and May 31, 2015 is noted in the following table:



## Loss Prevention

The aim of loss prevention is to help State agencies develop specific action plans and safety practices to mitigate or eliminate the most frequent or severe sources of preventable losses.

Monthly loss reports are distributed to the top agencies and universities with the highest claims frequency. Meetings are also arranged with representatives from the agencies and universities to discuss their loss prevention programs, mitigation, and claims handling. Specific topics include preventative maintenance, pre-loss activities related to weather events, freeze-up prevention, facility self-audit inspections, contractor management, fire protection impairment programs, and claims impact. Between December 2014 and May 2015, State agencies and universities visited include Baltimore City Community College, Saint Mary's College of Maryland, Morgan State University, MD Military-Camp Fretterd, University of Baltimore, Department of Public Safety and Correctional Services and State Highway Administration.

Similar discussions and visits were arranged with other locations in advance of the property surveys conducted by the State's excess property carrier. These included a follow-up visit with Morgan State University and visits with Towson University, Frostburg State University, Bowie State University, Coppin State University, and the Hippodrome. Agencies also received a Loss Prevention CD of resource documents and guidance materials aimed at preventing or minimizing loss to State-owned property.

In January, February and March 2015, the carrier for Boiler and Machinery and Loss Prevention coordinated two day sessions for boiler training which was held for over 100 State employees whose responsibilities include maintenance of facilities and electrical/mechanical systems. The training sessions were hosted at Salisbury State University, University of Maryland Fire and Rescue Institute, and Towson State University.

In April 2015 agencies and universities participated in a live webcast and discussion on elements of a flood emergency plan, and precautions and preparations to take before, during, and after a major windstorm event. Throughout the year, Loss Prevention provides weather alerts (flood, hurricane, tornado and tropical storms), loss prevention checklists and recommendations to facility directors, maintenance personnel, safety officers, risk managers and insurance coordinators.

***The Treasurer appreciates the opportunity to provide this Report to the Legislative Policy Committee on a regular schedule. A copy of this Report is also available on the State Treasurer's website: [www.treasurer.state.md.us](http://www.treasurer.state.md.us). If the Committee or its members would care to pursue further these or other STO developments, or any other aspects of the Treasurer's activities, please call the Treasurer at (410) 260-7160 or Chief Deputy Treasurer Bernadette T. Benik at (410) 260-7390.***