

Howard County

M A R Y L A N D

**SPENDING AFFORDABILITY
ADVISORY COMMITTEE
REPORT**



Fiscal Year 2016

Spending Affordability Advisory Committee

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**Howard County Maryland
Spending Affordability
Advisory Committee
Report for Fiscal Year 2016**

March 2015

Purpose

County Executive Allan Kittleman renewed the Spending Advisory Committee in December 2014. His charge to the committee was to:

1. Review in detail the status and projections of revenues and expenditures for the county, not only for fiscal year 2016, but also for fiscal years 2017 through 2020.
2. Evaluate future county revenue levels and consider the impact of economic indicators such as changes in personal income, assessable base growth, and other data which the committee considers applicable.
3. Evaluate expenditure levels with consideration of the long-term obligations facing the county, and the best way to pay for them.

The committee shall present to the County Executive a report including:

- a. Projections of revenue for the upcoming fiscal year
- b. A recommended level of new county debt authorization
- c. The anticipated effect of the committee's budget recommendations on future budgets
- d. Other findings and/or recommendations that the committee deems appropriate

The Committee met seven times in January and February receiving presentations from economists, county agencies, and local educational institutions that addressed the County's economic outlook, revenue outlook, debt affordability, economic development, long-term planning, and critical operating and CIP needs. The Committee reviewed the significant fiscal issues that the County faces today and in the foreseeable future, brainstormed on potential options that could potentially help address such challenges, and summarized our findings and suggestions in this report. We would like to thank all Committee members for taking this task very seriously and diligently participating in the discussions and offering great ideas and thoughtful input. We also want to thank all the presenters who shared valuable information and insight with the Committee.

The report can be separated to two parts. The first part summarizes all major findings and recommendations of the Committee. The second part provides detailed background information on economic outlook, revenue outlook, debt indicators and the County's multi-year projections model.

I. SUMMARY OF FINDINGS AND RECOMMENDATIONS

The Committee was tasked with making recommendations on revenue projections, the debt ceiling, and long-term fiscal conditions, and providing other observations and recommendations, as appropriate. These are listed below.

1. Projections of Revenue for the Upcoming Fiscal Year

FY 2016 projected revenue is \$999,076,790, an increase of 1.5% (\$15,200,341) over the approved FY2015 budget (excluding use of fund balance). Unless additional revenues are realized or created, the Committee believes that spending must stay within that amount. The County is required by law to adopt a balanced budget and should spend within its means. The Committee believes that it is imperative that the County deliberately consider a range of revenue and expenditure options in order to position itself for the new norm of moderate revenue growth. The County also needs to monitor revenues closely, and make necessary expenditure adjustments swiftly.

This slowdown in revenue growth is partially attributable to one-time factors such as the impact on income tax reconciliation figures of the significant drop in capital gains between 2012 and 2013 because consumers realized capital gains in advance in anticipation of a "fiscal cliff", but also is attributable to a slowdown in personal income. Personal income in the County grew by only 1.5% in 2013. And, while property taxes continue to show signs of recovery, the overall General Fund revenues are anticipated to realize only moderate growth in the near future. Reductions in the State aid based on the Governor's proposed budget and the unknowns surrounding Federal government spending levels that impact Federal grants and/or employment of County residents working directly or indirectly for Federal agencies pose additional constraints on revenues.

2. A Recommended Level of New County Debt Authorization

Authorized new General Obligation bonds in FY 2016 should be limited to \$90 million. In addition, the County should keep a close eye on actual debt issuance and maintain future debt services below 10% of the total of General Fund and Fire tax revenues. The Committee recommends including fire taxes, which support CIP bond financing, in this calculation to align this measure with that applied by most other counties. The County is rapidly approaching its 10% policy ceiling for this debt indicator and risks exceeding it in the near future, based on existing and anticipated new bonds, unless the County keeps its average annual new bond authorization at or lower than \$90 million over the next six years. The Committee believes limiting new bond authorization to \$90 million is a reasonable and necessary approach partly because the County already has \$485 million in bonds previously authorized but unsold yet that will continue to add to its

existing debt obligations in coming years. Moreover, the actual cost of the debt services for bonds authorized for FY 2016 will likely increase due to an anticipated rise in interest rates and given the average lag of one to three years between bond authorization and bond issuance. The County should also continue to take advantage of refinancing opportunities, as practicable.

While it is understandable that the County issued bonds at higher than historical levels in recent years in an attempt to take advantage of low interest rates and to address rising needs in CIP projects, with the interest rate environment changing and revenue growth slowing down, it is important to make adjustments now so that the level of new debt taken on is affordable. This effort is necessary not just to meet industry standards and limit debt burden and liability, but also to provide resources to support other operating priorities of the County. The committee also encourages the County to develop long-term debt affordability models beyond five years, since most General Obligation (GO) bonds have 20-year terms with long-term liabilities and implications on future operating budget expense obligations.

3. The Anticipated Effect of The Committee’s Budget Recommendations on Future Budgets

A multi-year revenue and expenditure model developed by the Budget Office indicates that **County General Fund revenues will likely show a growth of 3.6% per year on average over the four years beyond FY 2016.** The County must budget to spend within its means during this period. The Committee suggests that the County develop a multi-year fiscal plan that strategically balances service needs and resources to build a sound fiscal structure that supports our priorities.

It is important that the government and community leaders understand and adapt to the “new norm” with regard to growth in Howard County. We are still a vibrant and attractive County to new businesses and residents, but the land available for development (both in quantity and configuration) as well as the decreases in Federal spending and State funding will impact our near term growth. The development of growth corridors and re-development of Downtown Columbia will contribute to our long term economic vitality, but the County will need to adjust to a different period of growth, given our present constrained land inventory. As a result, the Committee urges the County to continue to explore a range of options to improve operational efficiencies and fund needed services in the long run.

4. Other Findings and/or Recommendations that the Committee Deems Appropriate

While the County continues to enjoy such strengths as a highly-educated workforce, net gains in income difference between those migrating in and those moving out, access to Fort Meade, etc., it also has certain limiting factors that impact its short-term and long-term development:

- ◆ Undiversified revenue structure (which limits fund raising capacity and increases volatility)
- ◆ Limits of large parcel greenfield land or space for development (which limits the County’s future revenue streams)
- ◆ Preponderance of Federal government reliant employment (which contributed to a slowdown in income growth in 2013)

With a slowdown in revenue growth but continuous high demands in expenditures, it is clear that in FY 2016 the County will face a significant fiscal challenge. According to the County Budget Office, mandated and committed funding needs alone, including Maintenance of Effort (MOE) for the Board of Education, cost increases based on existing collective bargaining unit agreements, benefit increases, and debt services, already exceed projected revenue growth significantly. Moreover, the Committee is concerned about the County’s ability to fund and support its development and services in the long run, in the face of a moderate rather than a strong revenue growth anticipated in the next several years coupled with land development

concerns.

The committee considered a variety of options that could help the County address such challenges in FY 2016 and beyond, and identified the options recommended for consideration shown below. These options are arranged in three categories – revenue options, expenditure control, and other / innovative approaches.

Revenue Options

- ◆ **Ambulance Fee:** The Committee suggests that the County explore the option of implementing an ambulance fee for use of EMT and Transportation Service to area hospitals. Other counties, including Montgomery County and Prince George’s County, collect such fees. This cost is reimbursable from most insurance carriers and a safety net can be implemented for those who do not have insurance or cannot afford the service. This revenue could help support the increasing operating expenses and potential CIP projects in the Fire Department. It is also suspected that without an ambulance fee, the County has been subsidizing surrounding jurisdictions that charge such a fee currently in term of regional insurance premiums.
- ◆ **Special Event Charges / County Cost Reimbursement:** The Committee strongly suggests that deployment (usually at overtime rates) of County Police (and other agencies) to support “for profit” events be reviewed with consideration to charge a fee to cover the additional cost of providing those services. As those fees will likely be included in a minor increase in the ticket price, the direct impact on those businesses will be minimal. The County should consider a fee schedule with a tiered system (e.g., free for non-profits headquartered in Howard, lower fees for non-profits outside of the County, and higher fees for private businesses). In addition, we recommend such fees be reviewed periodically for needed adjustments to align with the actual service costs.
- ◆ **Transfer Tax**
 - The Committee recommends consideration of an increase in the Transfer Tax by 50 basis points (BP) primarily in support of existing and new funding for education capital projects. This rate increase would make Howard County’s Transfer Tax rate comparable with most of the other metropolitan contiguous counties in Maryland and would generate an estimated \$13 million in revenue on an annual basis, which could leverage \$160~\$175 million in additional construction accumulatively through bond funding (based on 4%~5% interest rates).
 - The Committee also suggest that the County measure the present allocation of revenue on the existing 1% transfer tax every five years against existing needs to determine if it can be more appropriately re-allocated (with the support of the State Delegation through local legislation in the General Assembly) to best match the County’s existing capital investment needs. If the County decides to increase Transfer Tax to 1.50% to support school capital project expenditures, the allocation of new revenues from the additional 50 basis points should also be subjected to the same reviews every five years to assure that revenues and needs are appropriately matched.
 - In addition, the Committee recommends that the Offices of Finance and Budget review individual programs or sub-funds supported by the transfer tax fund on an annual basis and engage with the County Executive and County Council in determining if one-time transfers are achievable. For the purpose of illustration, a multi-year debt model produced by the County’s Finance Department for the Agricultural Preservation portion of the transfer tax fund

is included in the Appendix of this report. According to that model, (1) the agricultural preservation program or sub-fund will likely have outstanding fund balances in the next several years even after assuming \$18.5 million new land purchase needs in the next several years (which may or may not materialize), and (2) starting from FY 2023, its fund balance will likely grow significantly to approximately \$170 million by FY 2044. Based on these assumptions, opportunities may exist for one-time transfers without hurting the program's designated purpose and/or restructuring of transfer tax rates and reallocation of designated revenues in the future.

- ◆ **Storm Water Remediation Fee:** The Committee recommends that the County not remove the Storm Water Remediation Fee prior to establishment of an alternative fee structure. Otherwise, those mandated costs would further stress the General Fund budget by approximately \$10 million. Where it correlates with the priorities established by the Office of Sustainability, the County needs to ensure that the revenues are used for capital projects that would otherwise be bond funded. Another thought might be to use the fees as a revenue source for bonds issued specifically for storm drainage capital projects using the fees to leverage the debt.
- ◆ **Property Tax:** Property tax is the number one revenue source of the County and contributes nearly half of our total General Fund revenue. An increase of 1 cent of County real property tax rate equates to \$4.5 million of revenue annually. While the impact of any increase in the property tax must be considered carefully the Committee recommends that it remain on the table given the magnitude of potential new revenue capacity generated by raising this tax by one cent or two.

The Committee also suggests that the County look into other revenue options, including those applied by other counties in Maryland but not in Howard County (e.g., Telecommunications Tax, Energy Tax, etc.). However, in exploring any of the listed revenue options, it is important that the County compare the overall tax burden of its residents and businesses with those in other counties to make sure that the County maintain its competitive advantage in term of taxation. The Committee also wants to make it clear that it is our role to offer revenue and expenditure options for the County to explore, rather than to direct the County on its own policy decisions.

Expenditure Control Options

- ◆ **Maintenance of Effort (MOE) Contribution:** The school system's MOE increase (including the required teacher pension contribution) is \$10.9 million in FY 2016. While the County was able to fund in excess of the MOE amount in certain years, it has no obligation to fund over that amount. In fact, during FY 2009~FY 2013, the County only funded the MOE level due to its own fiscal constraints.
- ◆ **Other Post Employment Benefit (OPEB) Contribution beyond PAYGO:** The County Executive may opt to place a temporary hold on incremental OPEB funding in FY 2016 given the County's fiscal constraints. However, the County should resume using current revenues to fund OPEB incremental amount in FY 2017. While it is important that the County develop and execute a long-term plan to gradually increase funding to eventually fully fund OPEB, the amount and timing has to be examined and adjusted in consideration of other priorities.
- ◆ **Collective Bargaining Agreements:** The Committee recommends that the County Executive re-open negotiations with the Police and Fire collective bargaining units to explore an option of delaying the authorized 4% pay increase for FY 2016. This could greatly help address the FY 2016 budget challenge, while still funding the agreed upon total pay increases.

- ◆ **Pension Reforms Exploration:** The County should consider hiring an actuary to study the potential savings from introducing a defined contribution (DC) pension plan for new employees such as a 401k model with a small County match. Different governments, including the Federal government, have started to introduce or consider such options as pension cost has become one of the key cost drivers for most governments. Most private companies already use a similar retirement funding mechanism, which is portable and moves with the employee. As younger generations appear to be less inclined to stay in one job for one's whole life, introducing a portable pension plan could be appealing to new recruits while generating savings to the government compared to the current defined benefit (DB) plans, especially in long run with the mix of DB and DC employees change over time.
- ◆ **Use of Fund Balance:** The County Executive may want to consider implementing more restrictive policies on using prior year fund balances. For example, the Committee recommends utilizing no more than 50% of prior year unassigned fund balances in the upcoming fiscal year with the rest spread out over future years. This approach can avoid potential steep swings in the budget and also helps minimize the volatility in PAYGO funding for CIP projects. Similarly, the County can consider a policy of restricting PAYGO funding to capital projects only to provide a consistent support to cash-funded CIP projects (e.g., road resurfacing has historically been "PAYGO" funded).
- ◆ **Privatization:** The County should study the potential savings from privatizing fleet operations and contracting out other functions where feasible.

Other / Innovative Approaches

- ◆ **Fund/Agency Restructuring:** The County may want to consider changing the Department of Health into an operating agency. While a large percentage of that department's revenues are from the County General Fund, it is budgeted as a special revenue fund because of the nature of its relationship within the State health system and carries a separate fund balance as a result of relatively high rate of employee turnover that is subject to State authorization. Presently the monies remain in that fund versus other county agencies.
- ◆ **Partnership / Commercial Base Development:** The Committee recommends that the County, in consultation with the Economic Development Authority, aggressively review all vehicles to attract new businesses and employees in the Technology and Commercial businesses, which typically employ predominantly high wage employees. For example, the County can study and implement best practices for maximizing the function of Revenue Authorities based on positive contributions to the General Fund and measurable economic development results. As the County is focused on maintaining and improving quality of life in Howard County, seeking opportunities to jointly leverage resources to attract businesses to development corridors should be explored. This should include consideration of pooling resources to increase Economic Development Authority's capacity to attract commercial growth. Continued emphasis and increased support for entrepreneurship, innovation and small business programs will also help diversify the employment base. In addition, creative approaches to incentivize redevelopment will accelerate alternatives for a decreasing supply of greenfield options.
- ◆ **Buildable land use inventory:** A quantitative analysis of industrially zoned, vacant, buildable (total parcel size minus environmental and physical constraints) land should be performed to better assess the actual amount of possible new development. This analysis compared to historical patterns and rates would give a more accurate projection of development and provide a framework for new zoning needs or redevelopment requirements.

- ◆ **IT Investment for Efficiency & Productivity:** The Committee strongly recommends that the County aggressively pursue the integration of the SAP technology platform across County operations for enhanced efficiencies that should be achieved by exemplary execution. This may require an investment in personnel or contract talent to drive the required best in class performance. The Committee further suggests that specific objectives and metrics should be established to clearly measure progress.
- ◆ **Wynne Case Liability:** Within the budget process, it may be prudent for the County to set aside funding for a possible unfavorable ruling in the Wynne case by the Supreme Court this summer, as some other Counties have done.
- ◆ **Long-Term Facility Evaluation:** Consider the development of a comprehensive evaluation of the County's facilities (possibly including County roads) and the near-term and long-term needs and uses of these facilities. The evaluation should consider the County's uses and need for the facility, current condition, and the cost to rehabilitate if needed, and to maintain/sustain in an optimal condition.

II. DETAILS / BACKGROUND

1. Economic Outlook

The Howard County Budget Office retained Richard Clinch, PhD, Research Economist at the Battelle Memorial Institute's Technology Partnership Practice to prepare a county personal income projection through Fiscal Year 2018 and a report on overall national, state and regional economic trends and their expected impact on the County's economy and government finances. Dr. Clinch reported the following key findings to the County's Spending Affordability Committee:

National Economy

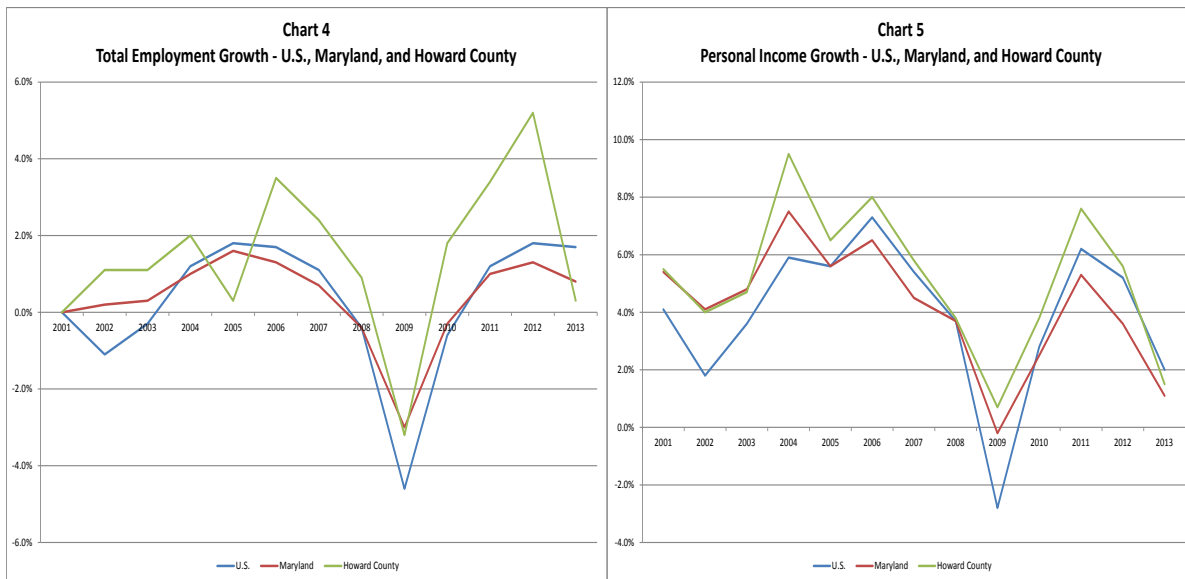
- ◆ The U.S. economic recovery from the "Great Recession" continued to strengthen in 2014. After experiencing a decline in the first quarter, real Gross Domestic Product (GDP) grew at an annual rate of 4.6% in the second quarter and 5% in the third. The nation added over 2.5 million jobs and the national unemployment rate fell from 6.7% in December 2013 to 5.6% in December of 2014.
- ◆ According to Moody's Economy.com (Moody's), U.S. GDP is projected to grow by 2.2% in 2014, 3.5% in 2015 and by 3.4% in 2016 in real terms. The Maryland Bureau of Revenue Estimates (BRE) projects slower GDP growth of 2.2%, 2.6% and 2.8% respectively.
- ◆ According to Moody's forecast, U.S. employment is projected to grow by 1.8% in 2014, by 2.4% in 2015 and by 2.6% in 2016, while the Maryland BRE is projecting slower U.S. employment growth of 1.8%, 1.9 and 1.5% respectively.
- ◆ While the magnitude of the two sources of forecast differs, both Moody's Economy.com and the Maryland BRE anticipate a continuous gradual improvement of the national economy.

State Economy

- ◆ While Maryland's reliance on federal spending cushioned it relative to other states during the past two recessions, in today's context of reductions in federal spending, this dependence on federal spending has suppressed Maryland's economic recovery relative to the rest of the nation. While economic conditions are improving in Maryland, Maryland has lagged the nation and many states in GDP, income and employment growth over the past three years. **Maryland's slower than national recovery is expected to continue into the future.**
- ◆ The recovery of Maryland's economy is expected to continue in the coming year but at a moderate pace. The Maryland BRE is predicting a continued slow recovery, while Moody's Economy.com is predicting a stronger growth. However, **both sources predict that Maryland's economic growth will continue to lag behind the national average.**
- ◆ Each organization has made the following forecasts:
 - The Maryland BRE has reduced its estimates for employment and personal income growth from last year. The BRE forecasts Maryland employment growth of 0.7% in 2014, 1.1% in 2015 to 1.3% in 2016. The BRE forecasts Maryland personal income growth of 3.3% in 2014, 3.8% in 2015 and to 4.1% in 2016.
 - Moody's Economy.com predicts that Maryland employment will increase by 1.0% in 2014, by 2.2% in 2015 and by 2.5% in 2016, with State personal income growth of 2.9%, 5.7% and 6.4% respectively over the same period.

Howard County Economy

- Until recently, Howard County has outperformed the nation and the State in terms of economic, employment, and population growth over the past decade. While overall employment fell with the recession, the County employment base had fully recovered by 2011 and the County had actually added jobs in the high wage professional services, education and health care sectors since 2007. Howard County led the State in private sector job creation in this period of time.
- However, this picture changed in 2013. As shown in Chart 4 below, in 2013, Howard County lagged both the nation and State of Maryland in employment growth for the first time since 2005. The County's professional and technical services employment numbers actually fell in 2013 for the first time in a decade. The County's personal income growth also lagged the nation for the first time in the last fourteen years as shown in Chart 5. County personal income growth in 2013 slowed down significantly to only 1.5%, compared to 5.6% in 2012. It is clear that the federal spending driven slowdown in Maryland is impacting the Howard County economy.



- Federal employment and spending, especially BRAC and cyber related activities at Fort Meade, has been a significant driver of the County economy. There is considerable uncertainty about future trends in federal spending at the national, State and local level. While there is a general consensus that the worst of the cuts appear to be over and federal spending will be less of a drag on the national and local economy, the future of spending at Fort Meade is uncertain, with some predicting continued strong growth and others a slower growth rate. Dr. Clinch noted that in this period of economic uncertainty, “the County needs to be cautious in its projections for future economic activity.”
- Dr. Clinch predicted that County personal income will recover gradually with a projected growth of 3.9% in 2014, 5.6% in 2015, 5.8% in 2016, 6.3% in 2017 and 4.5% in 2018. This translates to a predicted growth of 2.7% in FY 2014, 4.8% in FY 2015, 5.7% in FY 2016, 6.1% in FY 2017 and 5.4% in FY 2018. However, near term projections have been lowered from last year's report. He also produced an alternative scenario with more conservative assumptions, projecting County personal income growth at 4.1% in FY 2014, 4.7% in FY 2015, 5.0% in FY 2016, 6.3% in FY 2017, and 4.5% in FY 2018.

2. Revenue Outlook

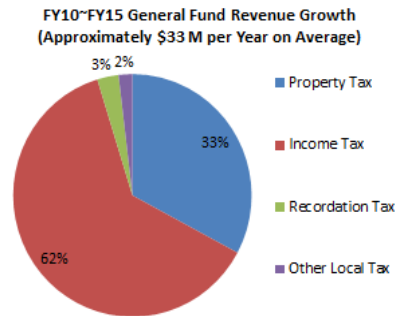
Howard County’s General Fund revenues rely primarily on property taxes and income taxes. In the FY 2015 budget, 90% of the General Fund revenues come from these two taxes. In addition, 95% of the General Fund revenue growth during the past five years was attributable to these two sources. Total General Fund revenues are projected to experience a weak growth of 1.5% between the FY 2015 and FY 2016 budgets, primarily due to a predicted revenue shortfall in income taxes in FY 2015.

Property Taxes and Income Taxes Represent 90% of General Fund Revenues



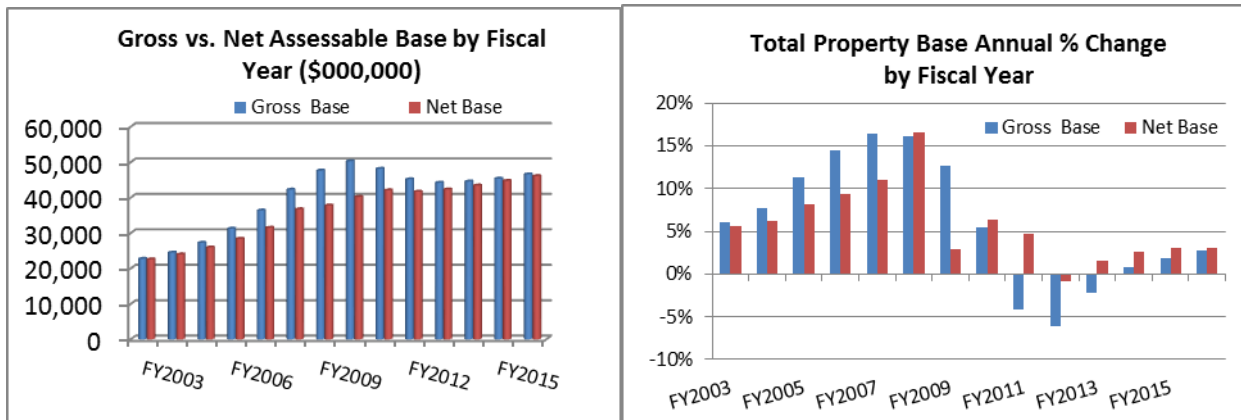
FY 2015 General Fund (not including one-time funds)

Property Taxes and Income Taxes Drive 95% of the Revenue Growth in the Past Five Years



Property Taxes are projected to continue the growth momentum of 4.0% in FY 2016 (over the FY 2015 budgeted level). County real property reassessment growth in 2015 for group 3 is 10.5% (prior to implementation of the three-year phase-in), the highest in the County over the past seven years. However, this growth rate is lower than the State average of 10.8% for the first time in four years; before that Howard County’s reassessment growth exceeded the statewide average three years in a row. Moreover, County commercial base reassessment growth of 13.4% in FY 2015 lags behind the state average of 18.6%.

The County’s net real property tax growth continues to benefit from diminishing assessments subject to the homestead tax credit. Unrealized revenues attributable to the homestead tax credit are expected to decrease from approximately \$11.4 million in FY 2014 to \$6.3 million in FY 2015 and \$4.9 million in FY 2016. And, as in past years, new construction will likely contribute to minor growth to total real property taxes each year. Personal property taxes also are projected to maintain a minor growth each year with the gradual improvement of the economy.



Income Taxes are projected to stay relatively flat between FY 2015 budget and FY 2016, based on the anticipated revenue shortfall in FY 2015 and limited recovery in FY 2016. In FY 2015, County income tax

is projected to basically stay unchanged from the FY 2014 actual level, or \$16.6 million lower than the original FY 2015 budget. This significant downward revenue adjustment is attributable to a huge drop in FY 2015 year-to-date income tax distributions in relation to prior year tax reconciliation. This revenue shortfall is partly attributable to a weakening in personal income growth, which was a mere 1.5% in tax year 2013 largely due to the impact of reductions in Federal spending related employment, and partly attributable to a one-time double-digit decrease in capital gains from an artificially high level in tax year 2012 resulting from consumer behavior changes in anticipation of a “fiscal cliff” and higher taxations.

In FY 2016, income taxes are projected to show some recovery with a predicted 3.9% growth from the estimated FY 2015 level. Still, that represents a budget-to-budget negative growth of -0.3% due to the revenue shortfall in FY 2015. The projected income tax growth is based on a potential improvement in personal income, which is expected to grow by 3.9% in 2014 and 5.6% in 2015 according to Dr. Clinch. These projections also factor in a potential revenue loss of \$2.5 million from the Wynne case, which, if the State and local governments lose the lawsuit, could result in an estimated \$2.5 million on-going annual loss and one-time loss of as high as \$20 million since the payback is retroactive by nature. The results of the Supreme Court decisions on the Wynne case won't be available until early summer.

Other revenues are projected to either stay flat or experience minor growth. Recordation taxes are expected to maintain a growth rate of 4.4%~4.5% in FY 2015 and FY 2016. The County's median home sales price experienced a moderate growth of 2% in calendar year 2014 and home sales volume stayed largely the same as a year ago. State aid to Howard County in FY 2016 is expected to suffer a reduction from the current application of funding formulas, but, in general, still demonstrates flat to minor growth over the FY 2015 level. According to the Governor's proposed budget, Howard County will lose \$7.9 million in State aid in FY 2016 compared to that available under current law. Most of the reductions impact education (\$6.6 million) and other funds; State aid to the County's General Fund is reduced by \$119,412.

3. Debt Indicators

In order to determine Howard County's relative debt position, the Committee in past years has evaluated Howard County's debt based on measures used and published by Moody's Investor Service and International City/County Management Association publications. Four measures have been used to evaluate the County's debt burden and debt affordability:

- ◆ Debt measured as a percent of the county's assessable base. The current County charter limit is set at 12 percent of assessed value. Because the State of has moved from the 40 percent cash value assessment of real property to a full cash value assessment, County debt should not exceed 4.8 percent of the full value assessment in order to remain consistent with the Charter limitation.
- ◆ Debt measured against the population on a per capita basis. Per capita debt exceeding \$1,200 (unadjusted for inflation over the past 10 years) may be considered excessive by rating agencies.

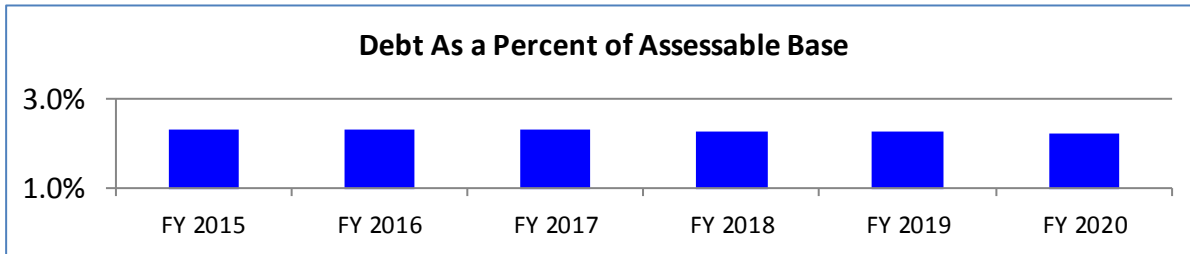
Per capita debt measured as a percent of the jurisdiction's per capita personal income. This measure should not exceed 10 percent in the view of many analysts.

- ◆ Debt Service as a percent of current revenues. This is the most important debt indicator among the four listed. Ten percent or below is considered an appropriate level, with 15 percent and above regarded a danger point.

The latest values of these four debt indicators are listed below with projected values for future years including critical indicators. (Note: The previous year's measures are shown in brackets []).

Measure #1: Debt as a Percent of the Assessable Base

As of June 30, 2014[2013], Howard County had an assessable base of **\$45,552,141,271** [\$44,201,087,307] and a General Obligation (GO) Debt of **\$989,035,000**[\$943,831,000]. This means that the ratio of debt to base was **2.17%** [2.13%] of assessed value versus the 4.8% limit. Preliminary projections indicate that this measure will remain low in coming years.



Measure #2: Debt measured against the population on a per-capita basis.

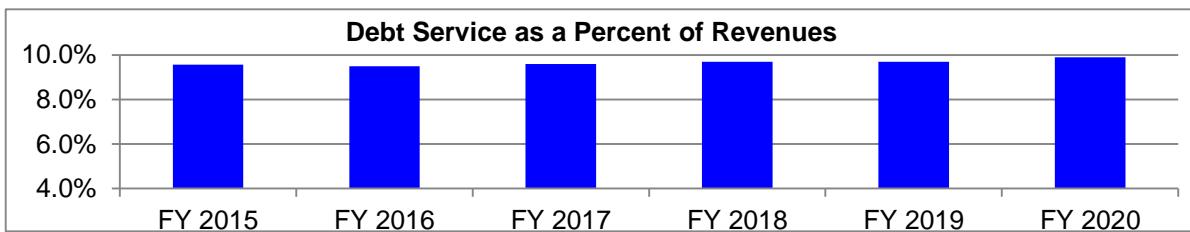
As of June 30, 2014[13], Howard County had a population of **302,311** [297,732] and a General Obligation Debt of **\$989,035,000**[\$943,831,000] generating a per-capita debt of **\$3,271** [\$3,170].

Measure #3: Per-capita debt measured as a percent of per-capita income.

For 2014[13], Howard County residents had an estimated per-capita personal income of **\$74,151** [\$75,336] and a per-capita debt of \$3,271 [\$3,170] equaling a per-capita debt of **4.4%** [4.2%] of per-capita income.

Measure #4: Debt Service as a percent of current revenues.

In FY 2014 [13], the County received **\$1,028,684,001** [\$992,189,221] in revenues from the General Fund and Fire and Rescue Fund and paid debt service of **\$97,553,138** [\$90,611,471]. Thus, debt service equaled **9.48%** [9.13%] of current revenues. This debt indicator is the most important measure of the four, indicating not only debt affordability but also the ability of the General Fund to support other strategic priorities (after dedicating resources to debt obligations). It is also a measure of concern because assuming a three-year lag between bond authorization and debt service payments based on practice, new bond authorization of \$90 million per year in FY 2016 and beyond, and current revenue projection of 3.6% growth per year (except FY 2016), debt service payments as a percentage of revenues will likely increase continuously and gradually approach the 10% cap in the next five years. The projected growth of debt burden is partially attributable to the significant increase of bond authorization (from \$95 million per year to \$118~\$120 million per year in FY 2014 and FY 2015), which has a lagged impact, and anticipated interest rate increases in coming years.

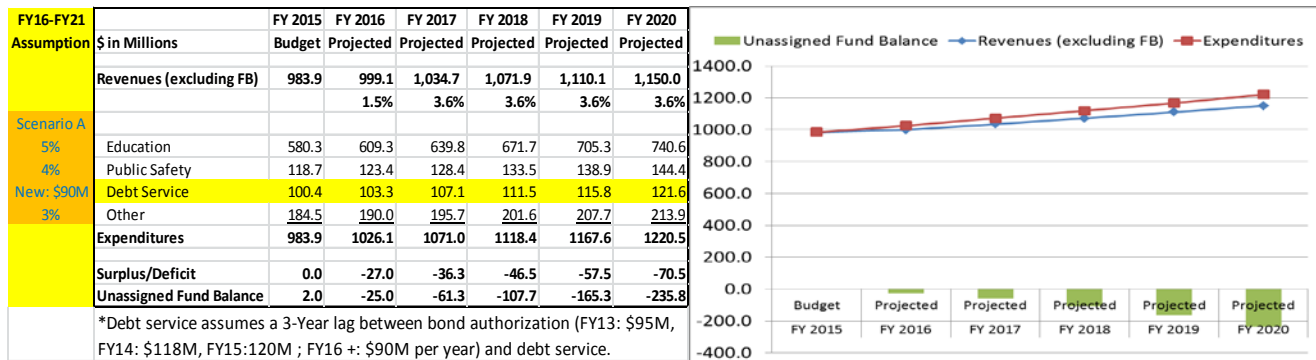


4. Multi-Year Projections

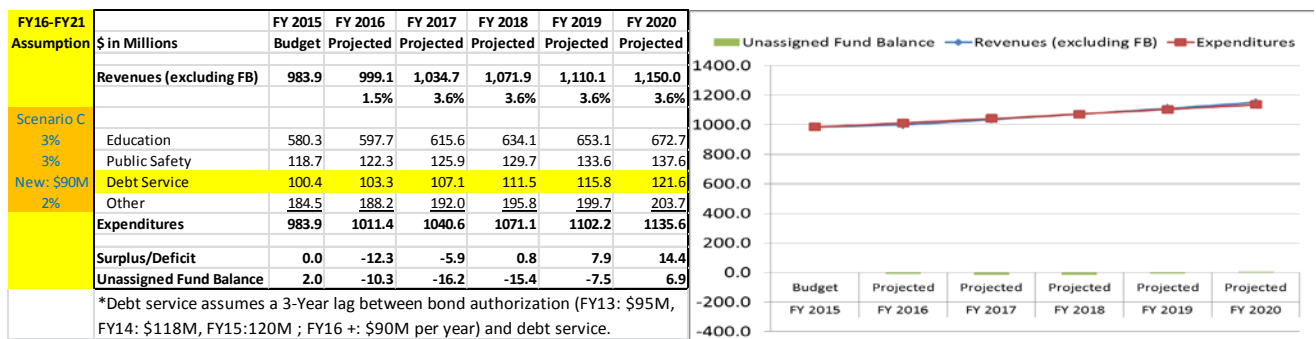
The County’s budget office developed multi-year projections based on historical trends and anticipated drivers of revenue growth and expenditure costs. Preliminary projections show that General Fund revenue growth during FY 2016 will be a weak 1.5% over the FY 2015 budgeted level, but will resume a moderate growth of 3.6% per year during the FY 2017~FY 2020 period. Such a level of growth is regarded solid but lower than what the County has been enjoying in some years in the past.

The Committee is concerned that such a moderate level of revenue growth may not meet the expenditure demands driven by education needs, potential growth in compensation and fringe benefits for existing employees, and other cost increases related to maintaining existing services. For illustration purposes, two scenarios are listed.

Scenario A assumes 5% growth for Education funding (including County contributions to BOE, Community College and Library), a 4% increase for Public Safety agencies, a 3% increase for all other agencies, and debt service payments calculated based on existing bond authorization of \$118~120 million per year in FY 2014 and FY 2015 and \$90 million new bond authorization per year in FY 2016 and beyond with a three-year lag between bond authorization and debt service payments (with 4%~5% interest rates). As shown below, projected expenditures would exceed projected revenues each year in the next six years with accumulative unassigned fund balance turning negative in FY 2016 (-\$25 million) and expanding to a shocking -\$235.8 million by FY 2020. It is clear that such a growth pattern is not affordable.



An alternative scenario was run, assuming 3% growth for Education and Public Safety, 2% growth for all other agencies and debt service payments assumptions unchanged. This time the financial situation improves, but as shown below, even with such a moderate growth rate, the County may not be able to afford the increase in costs over the next two to three years. FY 2016 and FY 2017 will likely experience an annual deficit with accumulative unassigned fund balance staying negative four years in a row (-\$16.2~-\$7.5 million). In other words, based on current revenue projections, the County has to manage its expenditures to limit growth in FY 2016 and FY 2017, before it can expect an improved growth forecast in later years.



The Committee urges the County to explore various options to boost revenues, manage expenditure growth and/or take innovative approaches to improve efficiency and productivity. Some of the options are discussed in detail in the first section of this report.

As in all models, the multi-year projection scenarios listed are based on a set of assumptions that could change when new information becomes available or the impact of changes in policy are considered. Nevertheless, this model provides a useful tool in identifying the affordable level of growth and understanding the implications of different scenarios.

Details of the multi-year revenue projections and one of the many possible expenditure scenarios that match the projected revenue growth are shown in Appendix II of this report.

Appendix I. Agricultural Land Preservation Program (Fund 2020) Cash Flow Model

Howard County Maryland										
Agricultural Land Preservation Program (Fund 2020)										
Cash Flow Analysis										
As of January 15, 2015										
	Revenues		Expenses							
	Beginning		Existing Debt Service		Projected					
Fiscal	Fund	Total		New	TOTAL DEBT	Other Exp.	Total	Ending		
Year	Balance	Revenues	Net	Debt Service	SERVICE	(Adm. etc.)	Expenses	Balance		
2015	16,785,157	6,881,963	7,890,482	41,343	7,931,826	2,273,301	10,205,127	13,461,993		
2016	13,461,993	7,061,155	8,000,382	578,818	8,579,200	1,435,848	10,015,048	10,508,100		
2017	10,508,100	7,262,345	7,826,373	787,433	8,613,806	1,575,173	10,188,980	7,581,465		
2018	7,581,465	7,469,861	7,395,882	1,064,363	8,460,244	1,615,679	10,075,923	4,975,403		
2019	4,975,403	7,684,623	7,147,723	1,352,234	8,499,956	1,657,399	10,157,355	2,502,671		
2020	2,502,671	7,906,357	6,784,879	1,635,415	8,420,294	1,475,371	9,895,665	513,362		
2021	513,362	8,136,136	5,453,788	1,643,890	7,097,678	1,519,632	8,617,310	32,188		
2022	32,188	8,376,729	4,424,291	1,617,196	6,041,488	1,565,221	7,606,709	802,208		
2023	802,208	8,627,704	4,153,703	1,590,503	5,744,206	1,612,178	7,356,383	2,073,528		
2024	2,073,528	8,887,403	4,103,828	1,563,810	5,667,638	1,660,543	7,328,181	3,632,751		
2025	3,632,751	9,155,517	3,246,470	1,537,116	4,783,586	1,710,359	6,493,946	6,294,322		
2026	6,294,322	9,434,314	3,171,540	1,510,423	4,681,963	1,761,670	6,443,633	9,285,003		
2027	9,285,003	9,722,098	2,888,115	1,483,729	4,371,844	1,814,520	6,186,364	12,820,738		
2028	12,820,738	10,019,654	2,834,658	1,457,036	4,291,694	1,868,956	6,160,650	16,679,742		
2029	16,679,742	10,326,680	2,262,187	1,430,343	3,692,530	1,925,025	5,617,554	21,388,868		
2030	21,388,868	10,644,752	1,976,675	1,363,939	3,340,614	1,982,775	5,323,390	26,710,230		
2031	26,710,230	10,973,544	1,925,796	1,338,117	3,263,913	2,042,259	5,306,171	32,377,603		
2032	32,377,603	11,312,666	385,589	1,312,295	1,697,884	2,103,526	3,801,410	39,888,859		
2033	39,888,859	11,666,145	223,810	1,286,472	1,510,283	2,166,632	3,676,915	47,878,089		
2034	47,878,089	12,030,861		1,260,650	1,260,650	2,231,631	3,492,281	56,416,669		
2035	56,416,669	12,407,293		933,195	933,195	2,298,580	3,231,775	65,592,187		
2036	65,592,187	12,795,969		796,470	796,470	2,367,537	3,164,008	75,224,148		
2037	75,224,148	13,196,758		662,351	662,351	2,438,563	3,100,914	85,319,992		
2038	85,319,992	13,610,009		436,878	436,878	2,511,720	2,948,598	95,981,403		
2039	95,981,403	14,036,314		216,095	216,095	2,587,072	2,803,167	107,214,550		
2040	107,214,550	14,476,037				2,664,684	2,664,684	119,025,903		
2041	119,025,903	14,929,556				2,744,625	2,744,625	131,210,834		
2042	131,210,834	15,396,728				2,826,963	2,826,963	143,780,599		
2043	143,780,599	15,877,963				2,911,772	2,911,772	156,746,790		
2044	156,746,790	16,373,684				2,999,126	2,999,126	170,121,348		
Total			108,786,606		137,686,720		233,172,323			
*Actual	Beginning fund	#Includes encumbrances								
Includes \$18.5 million in new funding, 5%down, 20 amort, current market rates										

Appendix II. Howard County Revenue/Expenditure Growth Projection Model

The County's Budget Office develops multi-year projections for its General Fund. The following model shows updated FY 2015 and FY 2016 revenue projections as of February 2015. It also includes preliminary revenue projections for five years beyond FY 2016. On the expenditure side, there are multiple potential expenditure scenarios that could fit the revenue projections. What is shown in the table below, for illustration purpose, is just one of the many expenditure options that are affordable based on projected revenue level.

General Fund Multi-Year Projections (\$ in thousands)

	Actual	Budget	Estimated	Variance	Projected	Projected	Projected	Projected	Projected
	FY14	FY15	FY15	FY15	FY16*	FY17	FY18	FY19	FY20
Property Taxes	459,016	472,586	477,488	4,902	491,707	508,916	525,710	542,533	558,809
Income Taxes	392,661	408,780	392,212	(16,568)	407,699	424,822	443,939	463,916	486,184
Other Local Taxes	27,172	30,860	28,381	(2,480)	29,941	30,658	31,395	32,153	32,931
State Shared Taxes	1,247	1,547	1,547	0	1,532	1,563	1,594	1,626	1,658
Charges for Svcs./Other	28,011	27,366	26,271	(1,094)	27,162	27,641	28,131	28,633	29,148
Investments/Transfers	40,502	42,738	42,191	(547)	41,036	41,074	41,137	41,202	41,269
Prior Year Funds	14,734	43,674	43,674	0	-	-	0	0	0
Total Revenues	963,343	1,027,550	1,011,763	(15,787)	999,077	1,034,675	1,071,907	1,110,063	1,149,999
% Change (w/o Fund Balance)	3.8%	3.7%	2.1%		1.5%	3.6%	3.6%	3.6%	3.6%
Education	544,294	580,282	579,766	(516)	590,302	609,618	629,028	648,549	668,002
Public Safety	109,363	118,716	116,087	(2,629)	120,497	124,112	128,207	132,054	136,015
Public Facilities	69,497	62,040	61,322	(718)	62,970	64,860	67,000	69,010	71,080
Community Services	36,772	58,073	55,916	(2,157)	58,945	60,713	62,716	64,598	66,536
General Government	36,277	25,878	22,028	(3,850)	26,267	25,763	25,104	25,911	26,810
Legislative & Judicial	22,138	24,400	24,371	(29)	24,766	25,509	26,351	27,142	27,956
Debt Service	97,553	100,392	100,392	0	103,330	107,100	111,500	115,800	121,600
PAYGO/Other/Contingency	47,450	52,769	46,880	(5,888)	2,000	2,000	2,000	2,000	2,000
OPEB	-	5,000	5,000	0	10,000	15,000	20,000	25,000	30,000
Total Expenditures	963,343	1,027,550	1,011,763	(15,787)	999,077	1,034,674	1,071,907	1,110,063	1,149,999

* FY 2016 projected growth from FY 2015 Est. = 3.2%; FY 2016 Projected Growth from FY 2015 Budget = 1.5%

Note: expenditure projections are shown for illustration purpose and do not represent long-term fiscal plans.