Y01A
State Reserve Fund

Operating Budget Data

($ in Thousands)

	FY 14 Actual	FY 15 Working	FY 16 Allowance	FY 15-16 Change	% Change Prior Year
General Fund	$55,256	$19,714	$200,000	$180,286	914.5%
Contingent & Back of Bill Reductions	0	-4,928	-50,000	-45,072	
Adjusted General Fund	**$55,256**	**$14,786**	**$150,000**	**$135,215**	**914.5%**
Adjusted Grand Total	**$55,256**	**$14,786**	**$150,000**	**$135,215**	**914.5%**

Note: The fiscal 2015 working appropriation reflects deficiencies and the Board of Public Works reductions to the extent that they can be identified by program. The fiscal 2016 allowance reflects back of the bill and contingent reductions to the extent that they can be identified by program.

- The fiscal 2016 appropriation into the reserve fund totals $150 million.

- If the Revenue Stabilization Account (Rainy Day Fund) balance is less than 7.5% of general fund revenues, the Administration is required to appropriate at least $50 million into the fund. The appropriation includes $50 million for the Rainy Day Fund. The Administration's plan is to transfer $34 million from the Rainy Day Fund, leaving a fund balance that is equal to 5% of general fund revenues.

- Beginning in fiscal 2016, the Governor is required to reimburse Program Open Space for $90 million of fiscal 2006 transfer tax revenues that were transferred to the general fund. The allowance includes the required initial repayment of $50 million. The Budget Reconciliation and Financing Act (BRFA) of 2015 proposes to repeal this requirement and keep these funds into the general fund instead.

- In fiscal 2015, the Administration's BRFA proposes to transfer $100 million from the Local Income Tax Reserve Account into the general fund. The fiscal 2016 allowance appropriates $100 million into the Dedicated Purpose Account to reimburse the Local Income Tax Reserve Account.

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

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Analysis in Brief

Major Trends

Rainy Day Fund Balance Remains at 5% of Revenues: If the fund balance is below 7.5%, the Governor is required to appropriate at least $50 million into the fund. To maintain a balance that is equal to 5.0% of general fund revenues, at least $16 million in appropriations is required. The Administration's budget plan proposes to transfer $34 million out of the Rainy Day Fund, leaving $814 million in the fund and a 5% balance at the end of fiscal 2016.

Issues

Local Income Tax Reserve Account Transfers Repayment: In fiscal 2011, $550 million was transferred from the Local Income Tax Reserve Account to general fund to support the operating budget. There is no plan to reimburse $350 million that was transferred. **The Secretary should brief the committees on plans to reduce the unfunded liability in the Local Income Tax Reserve Account.**

Rainy Day Fund Use and Replenishment Options: Since fiscal 2008, the Rainy Day Fund balance has hovered around 5% of general fund revenues. Unlike other AAA-rated states, Maryland has not used the fund balance to manage short-term cash needs. Instead, the State has transferred other fund balances into the general fund. This is an inefficient use of the fund. **The Department of Legislative Services recommends that the State reconsider its policies that limit the use of the Rainy Day Fund and instead adopt policies and practices that encourage the use and replenishment of the fund.**

Recommended Actions

		Funds
1.	Strike budget bill language making $50 million to repay transfer tax revenue contingent on the Budget Reconciliation and Financing Act.	
2.	Add language requiring the transfer of $100 million to the Local Income Tax Reserve Account on July 1, 2015.	
3.	Strike language appropriating $50 million for transfer tax repayment.	
4.	Delete transfer tax repayment appropriation.	$ 50,000,000

5. Adopt narrative recommending use of the Revenue Stabilization Account (Rainy Day Fund) to provide short-term liquidity when revenues underattain.

Total Reductions	**$ 50,000,000**

Operating Budget Analysis

Program Description

The State Reserve Fund provides a means to designate monies for future use. It comprises four individual accounts:

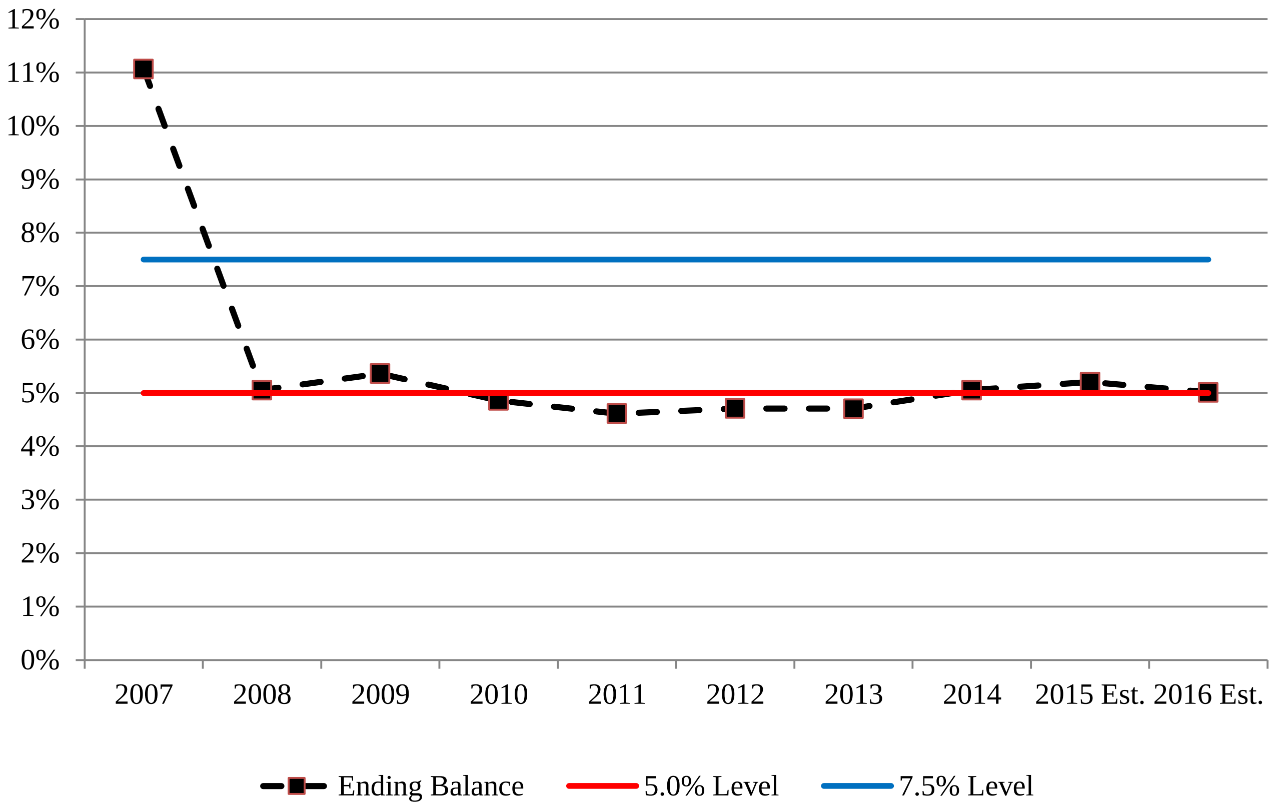
- Revenue Stabilization Account (Rainy Day Fund);
- Dedicated Purpose Account (DPA);
- Catastrophic Event Account; and
- Economic Development Opportunities Account (Sunny Day Fund).

The purpose and status of three of these accounts is discussed in more detail in this analysis. Discussion of the Sunny Day Fund can be found in the analysis of the Department of Business and Economic Development.

1. Rainy Day Fund Balance Remains Near 5% of Revenues

Section 7-311 of the State Finance and Procurement Article establishes a target reserve balance of 7.5% of estimated general fund revenues. The Governor is authorized to expend balances down to 5.0% in the annual budget bill, which has been the case over the past eight fiscal years, as the State grappled with structural deficits. **Exhibit 1** provides the actual and estimated closing balances in the Rainy Day Fund since fiscal 2007. The fund reached a peak of 11.0% in fiscal 2007, which was drawn down to 5.0% to aid in balancing the fiscal 2008 budget. Since then, annual appropriations to the fund have been used to help balance annual budgets following the 2008 recession.

Exhibit 1
Rainy Day Fund End-of-year Balances
Fiscal 2007-2016 Est.



Source: Department of Budget and Management, January 2015

Fiscal 2015 Actions

Cost Containment

On January 7, 2015, the Governor proposed that $4.9 million be transferred from the Rainy Day Fund to the general fund. The Board of Public Works (BPW) approved the transfer. The Governor may transfer any fund balance in excess of 5.0% of general fund revenues without legislation. In December 2014, the Board of Revenue Estimates reduced fiscal 2015 general fund revenues projections. This resulted in $4.9 million in Rainy Day Fund balances in excess of 5.0%, so BPW reduced the appropriation to the fund.

Proposed Budget

Exhibit 2 shows that the fiscal 2016 allowance totals $150 million, an increase of $135 million over the fiscal 2015 working appropriation. This includes $50 million for the Rainy Day Fund and another $100 million for the Dedicated Purpose Account.

Exhibit 2
Proposed Budget
State Reserve Fund
($ in Thousands)

How Much It Grows:	**General Fund**	**Total**
2015 Working Appropriation	$14,786	$14,786
2016 Allowance	150,000	150,000
Amount Change	$135,215	$135,215
Percent Change	914.5%	914.5%

Where It Goes:	
Dedicated Purpose Account	
Unassigned fiscal 2014 general fund surplus to reimburse Program Open Space	$50,000
Budget Reconciliation and Financing Act of 2015 proposal to repeal the requirement to reimburse Program Open Space	-50,000
Repay $100 million transfer in fiscal 2015 from Local Income Tax Reserve to the general fund	100,000
Rainy Day Fund	
Unassigned fiscal 2014 general fund surplus	44,063
Remainder required to appropriate at least $50 million into Rainy Day Fund	5,937
Delete fiscal 2015 appropriation net of Board of Public Works reduction	-14,785
Total	**$135,215**

Note: Numbers may not sum to total due to rounding. The fiscal 2015 working appropriation reflects deficiencies and the Board of Public Works reductions to the extent that they can be identified by program. The fiscal 2016 allowance reflects back of the bill and contingent reductions to the extent that they can be identified by program.

Dedicated Purpose Account

The DPA includes $100 million to reimburse the Local Income Tax Reserve Account. State law requires that the Administration also include $50 million to repay a portion of a $90 million transfer from Program Open Space (POS) made in fiscal 2006. This appropriation also includes language that proposed to delete the funds.

Program Open Space

The Administration is required to appropriate $50 million into the DPA in fiscal 2016 to repay previous fund transfers. In fiscal 2006, $90 million in transfer tax revenues were transferred to the general fund, instead of being appropriated in POS. Section 13-209 of the Tax-Property Article requires that transfers after fiscal 2005 must be reimbursed beginning in fiscal 2016.[1] The required appropriation is an amount equivalent to the unassigned general fund surplus that exceeds $10 million, limited to $50 million per year. The Comptroller's Office advises that the fiscal 2014 unassigned surplus is $104 million, thus requiring a $50 million appropriation.

In the Budget Reconciliation and Financing Act (BRFA) of 2015, the Administration is proposing to repeal this requirement. The transfer tax revenues to which this section applies were transferred to the general fund a decade ago, in fiscal 2006. When payment was last due, the statute was changed to defer repayment. Instead of deferring repayment again, the Administration proposes to eliminate the requirement. **The Department of Legislative Services (DLS) concurs with repealing the requirement.**

Local Income Tax Reserve Account

The State maintains a Local Income Tax Reserve Account. According to generally accepted accounting principles (GAAP), the State is supposed to maintain a sufficient fund balance to pay future refunds in case the income tax is no longer collected. Recently, the State has transferred funds from this account to balance the State budget. The Administration is proposing to transfer funds again. The Administration's plan assumes that $100 million from this account is transferred to the general fund in fiscal 2015. To reimburse the account, $100 million is appropriated into the DPA in fiscal 2016.

Rainy Day Fund

If there is an unassigned surplus at the end of fiscal 2014, the Administration is required to appropriate an amount equal to any remaining surplus exceeding $60.0 million ($10.0 million is retained by the general fund and $50.0 million is appropriated into the DPA for POS into the Rainy Day Fund. Insofar as the fiscal 2014 unassigned surplus is $104.1 million, the Administration has appropriated the remaining $44.1 million into the Rainy Day Fund.

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[1] There have been other transfers of transfer tax revenues since fiscal 2006. However, it is not necessary to reimburse Program Open Space (POS) for these transfers because subsequent Budget Reconciliation and Financing Acts exempted the transfers from repayment. Capital budget bill authorized general obligation bonds to offset reductions to POS' special fund appropriations.

Additionally, the Administration is required to appropriate at least $50.0 million into the Rainy Day Fund if the balance is below 7.5%. Since the balance is hovering near 5.0%, an additional $5.9 million is required to be appropriated into the Rainy Day Fund.

Exhibit 3 provides an overview of State Reserve Fund activity between fiscal 2015 and 2016. Detail for each account may be found in **Appendix 3** (Rainy Day Fund), **Appendix 4** (DPA), and **Appendix 5** (Catastrophic Event Account).

Exhibit 3
State Reserve Fund Activity
Fiscal 2015-2016
($ in Millions)

	Rainy Day Fund	Dedicated Purpose Account	Catastrophic Event Account
Estimated Balances 6/30/14	**$763.6**	**$0.0**	**$0.2**
Fiscal 2015 Appropriations	19.7	0.0	0.0
Board of Public Works Reduction	-4.9	0.0	0.0
Transfer to General Fund	0.0	0.0	0.0
Estimated Interest	7.7	0.0	0.0
Estimated Balances 6/30/15	**$786.1**	**$0.0**	**$0.2**
Fiscal 2016 Appropriations	50.0	100.0	0.0
Transfer to General Fund	-34.0	0.0	0.0
Transfer to Local Income Tax			
Reserve Account	0.0	-100.0	0.0
Interest	12.0	0.0	0.0
Estimated Balances 6/30/16	**$814.1**	**$0.0**	**$0.2**
Percent of Revenues in Reserve	**5.0%**		

Source: Department of Budget and Management, January 2015

Issues

1. Local Income Tax Reserve Account Transfers Repayment

As discussed in the Proposed Budget section of this analysis, the State maintains a Local Income Tax Reserve Account. The State collects income taxes for local jurisdictions and makes payments to the counties and Baltimore City from this account. According to GAAP, the State is supposed to maintain a sufficient fund balance to pay future refunds, in case the income tax is no longer collected. If the account is insufficiently capitalized at the end of a fiscal year, the State is required to report the underfunding as an unfunded liability in the *Comprehensive Annual Financial Report* (CAFR). If the State has a plan in place to reimburse the account, the State does not need to show an unfunded liability in the CAFR. This is a concern because the State has transferred funds from this account to support general fund spending.

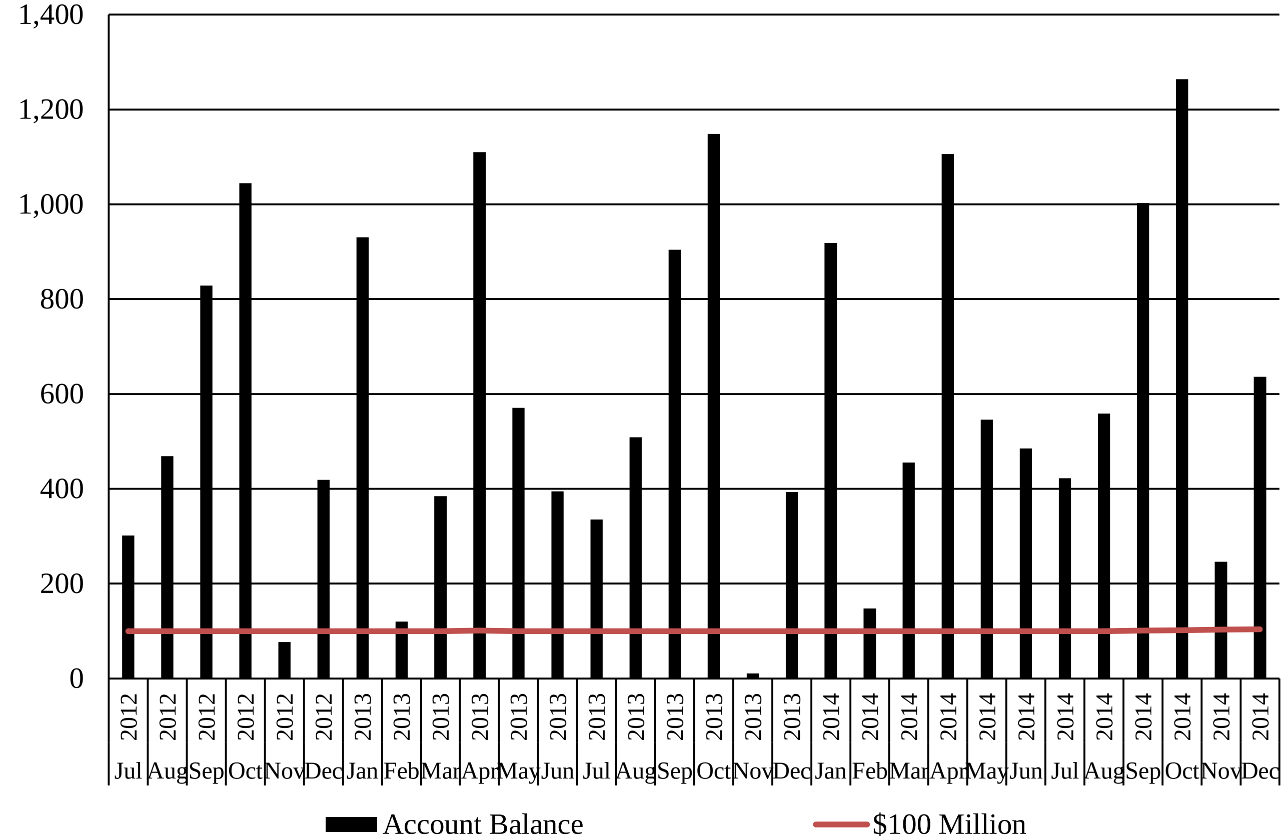
Local Income Tax Reserve Account Monthly Balances Fluctuate

The State collects income taxes for local jurisdictions and makes payments to the counties and Baltimore City from this account. The funds are distributed to the counties quarterly. The counties get their distributions in the second month after the quarter ends. For example, the fourth calendar year quarter (second fiscal year quarter) ends in December, and the distribution is made in February.

The payments that are made to the local jurisdictions fluctuate substantially from month to month. The largest payments are in February and November. February distributions are large because the fourth calendar year quarter tends to receive the most revenue, and November payments tend to be large because many taxpayers defer completing income taxes until October, resulting in large refunds in November. Payments can increase by over $1 billion from one month to the next. Consequently, account balances can fluctuate substantially.

Exhibit 4 shows that since August 2012, the fund balance dipped below $100 million in two months; November 2012 ended with a $77 million fund balance, and November 2013 ended with an $11 million fund balance. It is possible that transferring $100 million out of the account permanently could deplete the account to the point that there are insufficient funds for subsequent February or November payments.

Exhibit 4
Local Income Tax Reserve Account Balances
July 2012 to December 2014
($ in Millions)



Source: State Comptroller's Office

Transfers from Local Income Tax Reserve Account

To fund the State budget, funds have been transferred out of this account in fiscal 2009 and 2011. In fiscal 2009, $366.8 million was transferred to the general fund to support operating budget spending. In fiscal 2011, $550.0 million was transferred from the Local Reserve Account to help balance the State budget. This included:

- $350.0 million to the Education Trust Fund. Chapter 484 (the BRFA of 2010) required that this amount be repaid in $50.0 million increments from fiscal 2014 through 2020; and

- $200.0 million for Medicaid. Chapter 484 required this amount to be repaid from fiscal 2021 through 2026 at $33.3 million per year.

Chapter 1 of the first special session of 2012 (BRFA) repealed the requirement that local governments reimburse the $366.8 million taken in fiscal 2009. Chapter 425 (the BRFA of 2013) removed the requirement that the State reimburse the $350.0 million taken in fiscal 2011. The State now reports these unfunded liabilities in the CAFR, but does not have a plan in place to reimburse the account.[2]

Credit rating agencies are aware of this liability and have commented about it in their ratings reports. For example, before the most recent bond sale in July 2014, Moody's noted that the State has "thin available balances," which it attributes to "the state's transfer of local income tax reserves for budget balancing purposes in fiscal 2009 and 2011."

It is curious that the State attempts to manage its cash flows by transferring funds out of the Local Income Tax Reserve Account, which was created to transfer funds to the local governments and to hold funds to maintain proper GAAP balances, rather than use the Rainy Day Fund, which was created to manage short-term cash shortfalls.

As long as there is not a plan to replenish the funds that were transferred in fiscal 2011, the State will continue to have this unfunded liability. In past recessions, funds have been transferred to the general fund and then reimbursed when the recession ends. The concern is that the account has not yet been reimbursed and there is no plan to fully reimburse the account. This creates a GAAP balance that the State is disclosing in the annual CAFR and also will limit the State flexibility during the next recession. **The Secretary should brief the committees on plans, if any, to reduce the unfunded liability in the Local Income Tax Reserve Account beyond the $100 million repayment proposed in the budget.**

2. Rainy Day Fund Use and Replenishment Options

Since 1986, the State has had a Rainy Day Fund. The purpose of the fund is to retain revenues that can be transferred to the general fund to provide short-term liquidity when revenues underperform. Originally, the fund was required to maintain a balance of 2.0% of estimated general fund revenues. This was increased to 5.0% at the 1993 session, then 7.5% at the 2006 session. State law requires the Governor to appropriate funds into the account if the balance is below 7.5%. Specifically, repayment to the fund requires annual appropriations of $100 million if the balance falls below 3.0% and $50 million if the balance is below 7.5%. An amount equal to unappropriated general funds above $10 million at closeout are also required to be appropriated into the fund. Maryland has no requirement for a minimum general fund balance. In the budget bill, the Administration can withdraw funds above 5.0% from the Rainy Day Fund and transfer them to the general fund in the annual budget bill.

[2] Page 73 of the fiscal 2014 *Comprehensive Annual Financial Report* shows $550 million payable to the Local Income Tax Reserve Account. The note on the following page clarifies that there is a plan to reimburse $200 from fiscal 2021 to 2026. The note also mentions that the State has not specified when the remaining funds will be reimbursed.

However, if the Rainy Day Fund balance falls below 5% of general fund revenues, the Administration must submit separate legislation (such as a BRFA) to transfer funds to the general fund.

Compared to Other States, Maryland Is Not Fully Taking Advantage of Its Rainy Day Fund

Rainy Day Funds were transferred to the general fund during the first recession after the fund was created. In response to the 1991 recession, the fund was depleted. The general fund received $127 million in fiscal 1991 and $15 million in fiscal 1992. After the recession, funds were appropriated and funds as a share of general fund revenues increased so that they exceeded 5% by fiscal 1996.

Since fiscal 1996, the end-of-year Rainy Day Fund balance has been at least 5% of general fund revenues each year. The fund balance increased over time, and by fiscal 2001, the end-of-year fund balance was 9% of revenues. To manage cash flows during a recession, funds were transferred and by fiscal 2004 the balance had been reduced to 5% of revenues. Similarly, the fund balance reached 11% of revenues in fiscal 2007 before the Great Recession began. In fiscal 2008, funds were transferred to the general fund, which reduced the balance to 5% of revenues. Since fiscal 2008, the Rainy Day Fund balance has hovered near 5% of general fund revenues.

Because the State did not reduce the balance below 5%, the State did not take full advantage of the Rainy Day Fund during the Great Recession. Maryland went into the recession with a balance that was equal to 11% of revenues in fiscal 2007. This balance was quickly spent down to 5%. After reaching the 5% threshold, the State no longer used the Rainy Day Fund.

This approach is different than those taken by other AAA-rated states. When the Great Recession began, there were seven states with AAA ratings from all three major rating agencies (Fitch, Moody's, and Standard and Poor's). In addition to Maryland, the states were Delaware, Georgia, Missouri, North Carolina, Utah, and Virginia. All these states have Rainy Day Funds.

Exhibit 5 shows that three of the states, Georgia, North Carolina, and Virginia, aggressively used their balances to mitigate the short-term effects of the Great Recession. Rating agencies have said that this approach is appropriate and that using the balance from the Rainy Day Fund has not resulted in a loss of AAA ratings for states that have transferred fund balances. **Appendix 6** reviews Rainy Day Fund policies and recent actions of other AAA-rated states.

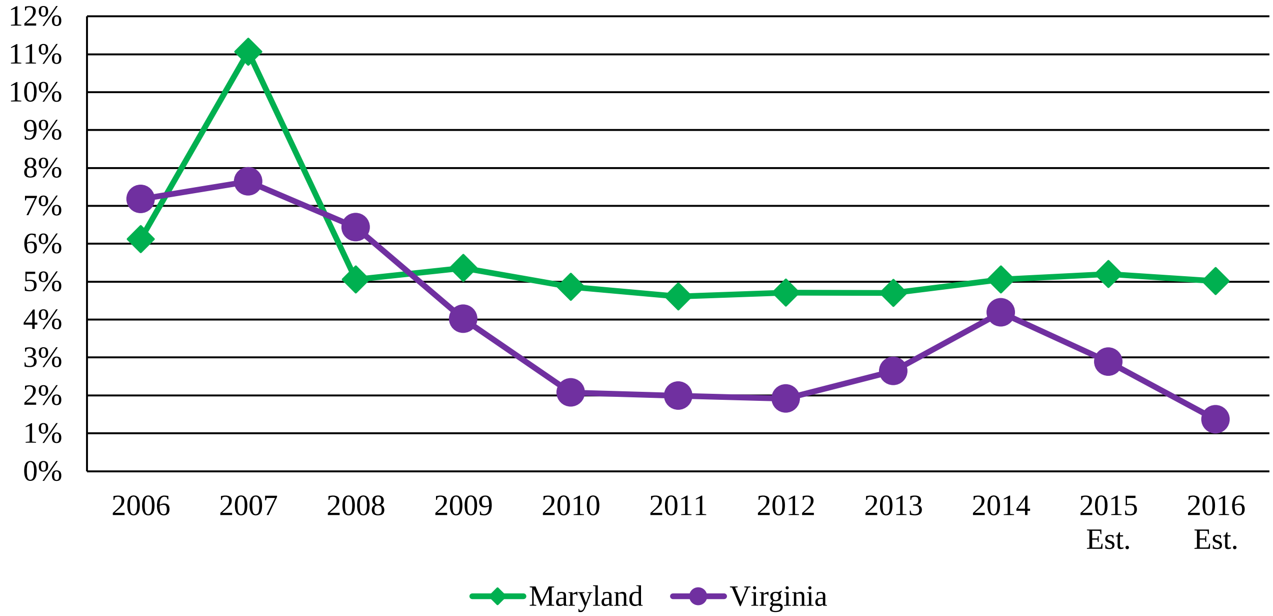
Exhibit 5
AAA-rated States' Rainy Day Fund Responses to Great Recession

State	Pre-recession Balance	Response to Recession	Assessment
Delaware	5.0% of revenues in fiscal 2007 and 2008	Maintained 5.0% of revenues in fiscal 2009 and 2010	No Rainy Day Fund actions taken
Georgia	9.0% of revenues in fiscal 2007	Withdrew funds and reduced balance to 1.0% of revenues by fiscal 2009	Aggressively used funds to manage recession cash flows
Missouri	7.5% of general fund revenue	Small withdrawals but maintained balance near Statutory limit	No substantial Rainy Day Fund actions taken
North Carolina	4.0% of revenues in fiscal 2008	Withdrew funds and reduced balance to 1.0% of revenues by fiscal 2009	Aggressively used fund to manage recession cash flows
Utah	8.0% of revenues in fiscal 2008	Withdrew funds and reduced balance to 5.0% of revenues in fiscal 2009 and 2010	Moderate use of fund to manage recession cash flows
Virginia	8.0% of revenues in fiscal 2007	Withdrew funds and reduced balance to 2.0% of revenues by fiscal 2010	Aggressively used funds to manage recession cash flows

Source: State Budget Offices and State Legislative Fiscal Offices

Even more recently, the State has not fully taken advantage of the fund. Since fiscal 2006, Virginia's approach has been to withdraw Rainy Day Funds during times of fiscal stress and replenish the fund as the economy improves. **Exhibit 6** shows that Virginia's fund balances have fluctuated from approximately 8% of revenues in fiscal 2007 to 2% by fiscal 2010 and were replenished to reach 4% again in fiscal 2014. By contrast, Maryland's fund balance has hovered near 5% since fiscal 2008, after an initial withdrawal.

Exhibit 6
End-of-year Rainy Day Fund Balances as a Percent of General Tax Revenues
Fiscal 2006-2016 Est.



Note: Excludes transportation-related tax revenues.

Source: Maryland Department of Budget and Management; Virginia Department of Budget and Planning

The federal budget crisis in 2011 and subsequent sequestration has slowed federal spending. The economies of Maryland and Virginia have underperformed as a result. Virginia proposes to respond to this by using the Rainy Day Fund. In the amendments to the budget proposed in December 2014, the Governor of Virginia proposed to withdraw approximately $450 million from the Rainy Day Fund in fiscal 2015 and 2016 to offset underattaining revenues. Maryland's approach has not provided any short-term transfers to manage revenue shortfalls.

By maintaining a Rainy Day Fund balance that is 5% of general fund revenues, the State maintains an $800 million account that does not provide any liquidity when funds are needed. This is an inefficient use of such a substantial amount of money.

Instead of Using the Rainy Day Fund, Other Fund Balances Are Transferred to the General Fund

Instead of using the Rainy Day Fund to manage cash flow, the State has transferred revenues from other funds. Approaches taken include transferring funds from GAAP accounts, transferring funds from special funds, and ending general fund appropriations for some programs. As mentioned in the previous issue, funds have been transferred from GAAP accounts (Local Income Tax Reserve Account, for example). Housing programs no longer receive operating budget support; instead general obligation bonds are authorized. As discussed in more detail in the Public Debt analysis, taxable bonds are issued for housing programs at a greater cost than the tax-exempt bonds generally used for the State's capital program. Special funds dedicated for capital programs, like POS, are transferred to the general fund, and the spending is moved into the capital program. Doing this crowds out other capital projects (such as education and State facilities) and also adds to the already significant pressure to continuously increase capital spending.

This has prompted the legislature to adopt legislation that restricts the transfer of special funds into the general fund. Examples include creating a lockbox around the Transportation Trust Fund (TTF) and requiring the repayment of transfer tax revenues diverted from POS. Chapter 422 of 2013 proposed a constitutional amendment, which was approved by voters in 2014. The amendment prohibits the transfer or diversion of funds from the TTF to the general fund or a special fund unless the transfer or diversion is approved through legislation passed by a three-fifths majority of specified full standing committees in each of the two houses of the General Assembly and then enacted into law. The bill creates exceptions to the prohibition on TTF transfers but only for defense or relief purposes and if the State is invaded or a major catastrophe occurs and the Governor proclaims a state of emergency and declares that TTF funds are necessary for the immediate preservation of public health or safety. Similarly, Section 13-209 of the Tax-Property Article requires that any transfer tax funds diverted from POS should be reimbursed. In recent years, the State has complied with this by exempting POS transfers from repayment.

Like other AAA-rated States, Maryland Should Use Its Rainy Day Fund to Manage Revenue Shortfalls

Based on recent Rainy Day Fund activity in other AAA-rated states, having the fund's balance fall below 5% does not, by itself, endanger the AAA rating. Instead of transferring balances from other funds, the Rainy Day Fund, which was created to manage short-term revenue shortfalls, should be used.

The State should also increase the Rainy Day Fund balance to the target that the law has set, which is 7.5% of general fund revenues. Other AAA states have set targets that are greater than 5.0%, for example:

- Georgia and Virginia have 15.0% targets;

- Iowa has a 10.0% target, including 7.5% for their Cash Reserve Fund and 2.5% for their Economic Emergency Fund. There is an automatic replenishment mechanism and the funds are currently at 10.0%;

- Missouri has set a 7.5% target for its Budget Reserve Fund, which is automatically replenished and is at the target;

- North Carolina has an 8.0% target; and

- Utah's target is 8.0% for the General Fund Budget Reserve Account and 9.0% for the Education Fund Budget Reserve Account. The funds are automatically replenished.

Like other AAA states, Maryland should increase its fund balance over 5.0% of general fund revenues. This provides more flexibility when revenues underattain. It also reduces the pressure to transfer special fund balances into the general fund when revenues underattain. One obstacle to increasing the fund balance to 7.5% is the ease at which funds may be withdrawn if the balance is between 5.0% and 7.5%. Separate legislation is required if the fund balance is below 5.0%, but the budget bill is sufficient if balances are above 5.0%. **Instead of requiring separate legislation to withdraw Rainy Day Funds if the fund balance falls below 5.0%, DLS recommends that a statutory change increasing the level at which separate legislation to withdraw funds from the Rainy Day Fund be increased to 7.5% be enacted.**

To encourage the use of the Rainy Day Fund, instead of the transfer of special funds balances from other funds or accounts, the following committee narrative is recommended:

Use of Rainy Day Funds: The budget committees are concerned with the continued reliance on fund transfers from accounting reserves and dedicated fund balances for support of the budget. Other states, even AAA-rated states, put much more reliance on their revenue stabilization funds to address acute revenue shortfalls and have done so without altering their credit ratings. In Maryland, the practice of continually discounting funds and balances has prompted legislation creating barriers to future transfers and requiring funds lost to be replenished with the effect of burdening future budgets. The budget committee thereafter suggests that budgeting practices be altered to include use of the Revenue Stabilization Account as a resource of first resort to address budget gaps.

Recommended Actions

1. Strike the following language from the general fund appropriation:

   ~~, provided that this appropriation shall be reduced by $50,000,000 contingent upon the enactment repealing the required repayment of transfer tax revenue.~~

   Explanation: The Administration is required to appropriate $50 million into the DPA in fiscal 2016 to repay previous fund transfers. This language clarifies that the funds are contingent upon failure to enact of legislation removing the funds. Since the language is not required the General Assembly, the language is removed.

2. Add the following language to the general fund appropriation:

   ,provided that $100,000,000 of this appropriation shall be transferred to the Local Income Tax Reserve Account on July 1, 2015

   Explanation: The budget includes $100 million to be transferred to the Local Income Tax Reserve Account. The funds are transferred to reimburse the $100 million that was transferred from the account to the general fund in fiscal 2014. One purpose of the Local Income Tax Reserve Account is to transfer income tax receipts that the State collects on behalf of local jurisdictions to those jurisdictions. Since fund balances have fallen below $100 million after especially large transfers to local governments, it is unclear the fund has sufficient revenues to support local income tax payments without this $100 million. To ensure that funds in this account are sufficient to fully support local income tax payments, the administration included $100 million in the Dedicated Purpose Account to be transferred to the Local Income Tax Reserve Account. This language requires that these funds are transferred to the account on the first day, so that the account has sufficient reserves throughout the fiscal year.

3. Strike the following language from the general fund appropriation:

   ~~Transfer Tax Reimbursement………50,000,000~~

   Explanation: This is a technical amendment clarifying that the transfer tax appropriation is deleted.

		Amount Reduction	
4.	Delete transfer tax repayment appropriation. The Administration is required to appropriate $50 million into the DPA in fiscal 2016 to repay previous fund transfers. In fiscal 2006, $90 million in transfer tax revenues were transferred to the general fund, instead of being appropriated in POS. Section 13-209 of the Tax-Property Article requires that transfers after fiscal 2005 must be reimbursed beginning in fiscal 2016. The required appropriation is an amount equivalent to the unassigned general fund surplus that exceeds $10 million, limited to $50 million per year. The Comptroller's Office advises that the fiscal 2014 unassigned surplus is $104 million, thus requiring a $50 million appropriation. The transfer tax revenues to which this section applies were transferred to the general fund a decade ago, in fiscal 2006. When payment was last due, the statute was changed to defer repayment. Instead of deferring repayment again, the Administration proposes to eliminate the requirement.	$ 50,000,000	GF

5. Adopt the following narrative:

Use of Rainy Day Funds: The budget committees are concerned with the continued reliance on fund transfers from accounting reserves and dedicated fund balances for support of the budget. Other states, even AAA-rated states, put much more reliance on their revenue stabilization funds to address acute revenue shortfalls and have done so without altering their credit ratings. In Maryland, the practice of continually discounting funds and balances has prompted legislation creating barriers to future transfers and requiring funds lost to be replenished with the effect of burdening future budgets. The budget committee thereafter suggests that budgeting practices be altered to include use of the Revenue Stabilization Account as a resource of first resort to address budget gaps.

Total General Fund Reductions	**$ 50,000,000**

Appendix 1

Current and Prior Year Budgets

Current and Prior Year Budgets
State Reserve Fund
($ in Thousands)

	General Fund	Special Fund	Federal Fund	Reimb. Fund	Total
Fiscal 2014					
Legislative Appropriation	$55,256	$0	$0	$0	$55,256
Deficiency Appropriation	0	0	0	0	0
Budget Amendments	0	0	0	0	0
Reversions and Cancellations	0	0	0	0	0
Actual Expenditures	**$55,256**	**$0**	**$0**	**$0**	**$55,256**
Fiscal 2015					
Legislative Appropriation	$19,714	$0	$0	$0	$19,714
Cost Containment	0	0	0	0	0
Budget Amendments	0	0	0	0	0
Working Appropriation	**$19,714**	**$0**	**$0**	**$0**	**$19,714**

Note: Numbers may not sum to total due to rounding. The fiscal 2015 working appropriation does not include January 2015 Board of Public Works reductions and deficiencies.

Fiscal Summary
State Reserve Fund

Program/Unit	FY 14 Actual	FY 15 Wrk Approp	FY 16 Allowance	Change	FY 15 - FY 16 % Change
01 Revenue Stabilization Account	$ 55,256,263	$ 19,713,999	$ 50,000,000	$ 30,286,001	153.6%
02 Dedicated Purpose Account	0	0	150,000,000	150,000,000	0%
Total Expenditures	**$ 55,256,263**	**$ 19,713,999**	**$ 200,000,000**	**$ 180,286,001**	**914.5%**
General Fund	$ 55,256,263	$ 19,713,999	$ 200,000,000	$ 180,286,001	914.5%
Total Appropriations	**$ 55,256,263**	**$ 19,713,999**	**$ 200,000,000**	**$ 180,286,001**	**914.5%**

Note: The fiscal 2015 working appropriation does not include January 2015 Board of Public Works reductions and deficiencies. The fiscal 2016 allowance does not reflect contingent or across-the-board reductions.

Appendix 3

Revenue Stabilization Account (Rainy Day Fund)
Section 7-311 State Finance and Procurement Article

Account Characteristics

- ***Purpose:*** The account was established in 1986 to retain State revenues to meet future short-term funding needs and to reduce the need for future tax increases by moderating revenue growth.

- ***Appropriations:*** The account consists of direct appropriations in the budget bill and interest earned from all reserve fund accounts.

- ***Required Appropriations If Account Balance Is Less Than 7.5% of General Fund Revenues:*** Current law requires that if the fund balance is between 3.0% and 7.5% of projected general fund revenues, annual appropriations of at least $50.0 million must be made until the account balance reaches 7.5% of estimated general fund revenues. If the account balance is below 3.0%, State law requires an appropriation of at least $100.0 million.

- ***Sweeper Provision:*** State law requires that the Administration appropriate an amount equal to any unassigned general fund balance at closeout in excess of $10.0 million into the Rainy Day Fund. This appropriation is made to the budget two years after the unassigned general fund surplus is realized. For example, fiscal 2008 closed with an unassigned surplus totaling $185.7 million, thus the Administration's fiscal 2010 allowance included a $175.7 million appropriation to the Rainy Day Fund. This appropriation to the Rainy Day Fund is referred to as the "sweeper."

- ***Transfer Tax Repayment:*** Section 13-209(g) of the Tax-Property Article requires that any Transfer Tax revenues transferred to the general fund after fiscal 2005 be repaid starting in fiscal 2012. The law stipulates that the first $10.0 million of unassigned general fund surplus shall be credited to the general fund, followed by a maximum of $50.0 million annually to the Transfer Tax special fund. Amounts above $60.0 million are credited to the Rainy Day Fund. The only transfer to which this applies was made in fiscal 2006, for $90.0 million. No part of the $90.0 million has yet to be paid, as mandate relief in budget reconciliation legislation led to no appropriation in fiscal 2012, and funds were cut from the fiscal 2013 allowance to ensure a sufficient general fund balance. The fiscal 2014 Budget Reconciliation and Financing Act delayed the earliest repayment until fiscal 2016.

Mechanisms for Transferring and Spending Funds

To transfer funds from the Rainy Day Fund requires specific authorization by an Act of the General Assembly or specific authorization in the budget bill if the transfer results in a Rainy Day Fund balance that is at least 5% of projected general fund revenue. To transfer an amount that would reduce the Rainy

Day Fund balance below 5% requires the transfer to be authorized in an Act of the General Assembly other than the budget bill.

Rainy Day Fund Activity

The following table illustrates fiscal 2012 through 2016 activity in the Rainy Day Fund. In fiscal 2012, mandate relief included in budget reconciliation legislation exempted the closeout sweeper provision to avoid conflicting with the requirements of the federal American Recovery and Reinvestment Act of 2009. Appropriations totaling $27.8 million in fiscal 2013 and $55.3 million in fiscal 2014 were made to ensure a minimum 5.0% fund balance. The Budget Reconciliation and Financing Act of 2012 authorized the transfer of $5.0 million to fully fund Teacher Retirement Supplemental grants. In fiscal 2015, the Board of Public Works (BPW) withdrew $4.9 million of the appropriation to the fund. This amount is withdrawn because the Administration anticipates that this is the amount above the 5.0% fund balance target. Since the fund balance is below 7.5% of revenues, the fiscal 2016 budget includes the minimum $50.0 million appropriation. The Administration also proposes to transfer $34.0 million into the general fund and maintain a fund balance of 5.0% at the end of fiscal 2016.

Revenue Stabilization Account Status
Fiscal 2012-2016 Est.
($ in Millions)

	2012	2013	2014	2015 Est.	2016 Est.
Beginning Balance	$624.4	$671.5	$700.4	$763.6	$785.7
Appropriation	0.0	27.8	55.3	19.7	50.0
Transfer to General Fund	0.0	0.0	0.0	0.0	-34.0
Board of Public Works Reduction	0.0	0.0	0.0	-4.9	0.0
Transfer from Transportation Trust Fund	40.0	0.0	0.0	0.0	0.0
Fund Projects and Programs	0.0	-5.0	0.0	0.0	0.0
Interest Earnings	7.1	6.1	7.9	7.3	12.5
Ending Balance	**$671.5**	**$700.4**	**$763.6**	**$785.7**	**$814.2**

Note: Numbers may not sum due to rounding.

Source: Department of Budget and Management, January 2015

Governor's Out-year Forecast

In the out years, the Administration's Rainy Day Fund forecast projects that the fund balance will remain at 5.0% through fiscal 2020. Since the fund balance is projected to be less than 7.5% of general fund revenues, a minimum $50.0 million appropriation is assumed from fiscal 2016 to 2019. The forecast also assumes that funds above 5.0% are transferred back to the general fund. The forecast period ends with an estimated balance of $939.0 million at the end of fiscal 2020.

Appendix 4

Dedicated Purpose Account
Section 7-310 State Finance and Procurement Article

Account Characteristics

- ***Purpose:*** The account was established in 1986 to retain appropriations for major, multi-year expenditures where the magnitude and timing of cash needs are uncertain and to meet expenditure requirements that may be affected by changes in federal law or fiscal policies, or other contingencies.

- ***Appropriations:*** The account consists of direct appropriations in the budget bill committed to a specific purpose. Interest earnings generated by the account are credited to the Rainy Day Fund.

- ***Other:*** The unspent balance of an appropriation reverts to the Rainy Day Fund four years after the end of the fiscal year for which the appropriation was made.

Mechanisms for Transferring and Spending Funds

To transfer funds from the Dedicated Purpose Account (DPA):

- funds may be reflected in the State budget subject to appropriation;

- after submission to the budget committees and review and approval by the Legislative Policy Committee (LPC) funds may be transferred by budget amendment to the appropriate Executive Branch agency; or

- the Governor may declare appropriations to the DPA surplus and may transfer funds by budget amendment to the Rainy Day Fund following review by the budget committees and LPC.

Dedicated Purpose Account Activity

The following table illustrates the activity in the DPA from fiscal 2012 through 2016. The account ends the period with no fund balance. As discussed in the analysis, the Budget Reconciliation and Financing Act (BRFA) of 2015 proposes to repeal the requirement that Program Open Space (POS) be reimbursed for $90 million of transfer tax revenues that supported the general fund instead of POS in fiscal 2006. The Administration is required to appropriate $50 million for POS in fiscal 2016, but the BRFA proposes to delete this requirement, so the Administration's plan does not include this repayment. The Administration's fiscal 2015 spending plan transfers $100 million from the Comptroller's Local

Income Tax Reserve Account to the general fund to balance the fiscal 2015 budget. The funds are replenished with a $100 million appropriation in fiscal 2016.

Dedicated Purpose Account Status
Fiscal 2012-2016
($ in Millions)

	2012	2013	2014	2014 Est.	2016 Est.
Beginning Balance	**$0.0**	**$0.0**	**$10.0**	**$0.0**	**$0.0**
Appropriation	**$15.0**	**$10.0**	**$0.0**	**$0.0**	**$150.0**
Local Income Tax Reserve Repayment					100.0
Transfers	**-$15.0**	**$0.0**	**-$10.0**	**$0.0**	**-$150.0**
Local Reserve Account Repayment					-100.0
Prince George's County Hospital	-15.0				
Federal Sequestration			-10.0		
Ending Balance	**$0.0**	**$10.0**	**$0.0**	**$0.0**	**$0.0**

Source: Department of Budget and Management, January 2015

Governor's Out-year Forecast

The Administration does not have any plans to appropriate any funds into the DPA through fiscal 2020.

Appendix 5

Catastrophic Event Account
Section 7-324 State Finance and Procurement Article

Account Characteristics

- ***Purpose:*** The account was established in 1990 to enable the State to respond quickly to a natural disaster or catastrophe that could not be addressed within existing State appropriations.

- ***Appropriations:*** The account consists of direct appropriations in the budget bill. Interest earnings generated by the account are credited to the Rainy Day Fund.

Mechanisms for Transferring and Spending Funds

Prior to transferring funds by budget amendment to the appropriate Executive Branch agency, the Administration must notify the Legislative Policy Committee of the proposed amendment and allow the committee 45 days to review and approve the proposed amendment.

Catastrophic Event Purpose Account Activity

The following table shows that the account's balance was $1.0 million at the start of fiscal 2012. In fiscal 2013, $432,313 was transferred to provide relief for victims of Hurricane Sandy and the derecho storm. In fiscal 2014, $394,750 was provided to support the Military Department's deployment during severe snow storms in February 2014. The account is expected to close fiscal 2016 with a $172,937 balance.

Catastrophic Event Account
Fiscal 2012-2016
($ in Thousands)

	2012	2013	2014	2015	2016
Beginning Balance	$1,000	$1,000	$568	$173	$173
Appropriation	0	0	0	0	0
Snow Storms	0	0	-395	0	0
Hurricane Sandy and Derecho Storm Relief	0	-432	0	0	0
Ending Balance	$1,000	$568	$173	$173	$173

Source: Department of Budget and Management, January 2015

Appendix 6

Rainy Day Fund Practices and Activity of AAA-rated States

Ten states have AAA ratings from all three major bond rating agencies: Alaska, Delaware, Georgia, Iowa, Maryland, Missouri, North Carolina, Texas, Utah, and Virginia. All AAA-rated states have a Rainy Day Fund. The exhibit compares reserve fund policies. Most states' Rainy Day Fund balances were substantially reduced from fiscal 2007 to 2010. This was due to revenue reductions attributable to the Great Recession. Two states with substantial energy revenues (Alaska and Texas) did not substantially reduce Rainy Day Fund balances. Delaware was able to get through the period without using its Rainy Day Fund.

Recent State Rainy Day Fund Actions

AAA-rated states had built up their Rainy Day Fund balances before the 2008 recession began. In response to the downturn, a number of states have withdrawn funds from their reserves. Examples of states' actions include:

- **Alaska:** The Statutory Budget Reserve and the Constitutional Budget Reserve had a combined balance of $14.1 billion, which is more than 200.0% of the fiscal 2014 budget. Because of higher oil-related revenues, Alaska did not need to use reserve fund balances following the 2008 recession.

- **Delaware:** The Budget Reserve Account ended fiscal 2013 with a balance totaling $186.4 million, which is 5.0% of general fund revenues. Delaware has never used the balance of its reserve account since its inception.

- **Georgia:** The Revenue Shortfall Reserve's balance peaked at $1.5 billion in fiscal 2007. Funds were transferred out of the account to help balance the budget after the recession, with the balance declining to $103.7 million at the end of fiscal 2009 (equal to 1.0% of revenues). The fund has been partially replenished, with a balance of $862.8 million at the end of fiscal 2014. This represents about 5.0% of prior year revenue.

- **Iowa:** From fiscal 2009 to 2011, the balances in the reserve funds fell below the statutory maximums due to the recession that caused state tax revenues to decline. During this period, the reserves were used to offset state general fund appropriation reductions for numerous programs (primarily Medicaid). The reserves ended fiscal 2011 with a combined balance of $440.0 million, which was $102.0 million below the $543.0 million target. At the end of fiscal 2014, the combined balances in the reserve funds reached $651.7 million, which meets the statutory maximum of 10.0% of revenues. The administration's budget plans to maintain the fund balances at 10.0% of revenues.

- **Missouri:** The Budget Reserve Fund balance has been used to help balance budgets in recent years. It decreased from $557.0 million at the end of fiscal 2008 to approximately

$556.3 million at the end of fiscal 2014. This is about 7.0% of net general fund revenue collections.

- **North Carolina:** The projected balance for the end of fiscal 2008 was $787.0 million, which was approximately 4.0% of the prior year's general fund appropriation. The state used some of these funds in fiscal 2009; the account balance declined to $150.0 million by the end of fiscal 2009. Appropriations to the reserve account increased the fund balance to $651.4 million by the end of fiscal 2014, bringing the balance to over 3.2% of the prior year's appropriation.

- **Texas:** Unlike most states, Texas' Economic Stabilization Fund increased its ending balances from fiscal 2007 ($1.3 billion) to 2010 ($7.7 billion). Funds increased because of high levels of oil and natural gas production transfers and limited use of the fund. In fiscal 2011, $3.2 billion was transferred to reduce the projected budget shortfall. Another $1.9 billion was transferred in a supplemental appropriation to support wildfire and water development board projects. At the end of fiscal 2014, the fund balance was $6.7 billion, which is 13.7% of the Texas General Revenue Fund fiscal 2014 revenues.

- **Utah:** The general fund Budget Reserve Account and Education Fund Budget Reserve Account balances peaked at $429.0 million at the end of fiscal 2008. Funds were withdrawn, and the balances were actually at $210.0 million at the end of fiscal 2010. At the end of fiscal 2014, the fund balances increased to $431.7 million. Fund balances are 8.0% of general and education fund appropriations.[3] The administration does not propose to withdraw additional funds.

- **Virginia:** The Revenue Stabilization Fund's balance peaked at the end of fiscal 2007 at $1.2 billion. Funds were withdrawn to help balance post-recession budgets, leaving the fund with a balance of $295.2 million at the end of fiscal 2010. At the end of fiscal 2014, the fund balance was $687.5 million, which is almost 4.2% of revenues. The Administration proposes to transfer funds to the general fund in fiscal 2015 and 2016, leaving a $238.8 million balance (1.4% of revenues) by the end of fiscal 2016.

[3] In Utah, substantial revenues, such as individual and corporate income taxes, are deposited into the education fund instead of the general fund. Since these revenues are general fund revenues for other states, the Rainy Day Fund balance comparison to general funds includes education funds.

AAA-rated States' Rainy Day Funds

State	Fund Name	Determination of Fund Size	Procedure for Expenditures
Maryland	Revenue Stabilization Account	Statutory 7.5% of general fund revenues.	Authorization in legislation or budget bill for balances above 5.0%. Separate legislation to spend balance below 5.0%.
Alaska	Statutory Budget Reserve (SBR), Constitutional Budget Reserve (CBR) Fund, and the Alaska Housing Capital Corporation Fund (AHCC)	Appropriations are made to the funds and there is no limit on fund balance.	The SBR and the AHCC can be used for any purpose upon a simple majority vote of the legislature. If the amount appropriated is less than the prior fiscal year the CBR can be accessed up to the prior year's appropriation, upon a three-fourths vote of the legislature.
Delaware	Budget Reserve Account	Excess unencumbered funds, no greater than 5.0% of gross general fund revenues set by joint resolution for the next fiscal year.	Three-fifths vote of the legislature for unanticipated deficit or revenue reduction resulting from legislative action.
Georgia	Revenue Shortfall Reserve	Capped at 15.0% of the prior year's net revenue.	The Governor can spend balances over 4.0%, but not below 4.0% unless there is a revenue shortfall at the end of a fiscal year. A mid-year allocation is made for education if revenues exceed estimates by 1.0% or more at closeout.
Iowa	Cash Reserve Fund (CRF) and Economic Emergency Fund (EEF)	The CRF is capped at 7.5% of estimated revenues, and the EEF is capped at 2.5% of revenues. The EEF can support a prior year deficit up to $50 million if certain conditions are met.	Appropriations by the General Assembly with funds replenished each year.

State	Fund Name	Determination of Fund Size	Procedure for Expenditures
Missouri	Budget Reserve Fund	Capped at 7.5% of net general revenue. If the balance is less than 7.5%, general revenues appropriated into fund.	Up to one-half of the fund balance may be transferred upon a request from the Governor after he has either declared an emergency or reduced expenditures below their appropriations due to a cash shortfall, and a two-thirds super majority vote by the legislature.
North Carolina	Savings Reserve Account	July 2007 established a goal that the balance equal at least 8.0% of the prior years' general fund operating budget.	Appropriations by the General Assembly.
Texas	Economic Stabilization Fund	The fund receives an amount equal to 75.0% of oil and natural gas production revenues in any fiscal year that exceeds fiscal 1987 collections and one-half of any unencumbered General Revenue Fund (GRF) balance at surplus at the end of each biennium. The fund balance cannot exceed 10.0% of certain GRF revenues.	Funds may be appropriated to close a deficit caused by a revenue decline if approved by three-fifths of the legislature. For other purposes, two-thirds of the legislature must approve an appropriation.
Utah	General Fund Budget Reserve Account and Education Fund Budget Reserve Account	25.0% of end-of-year general fund surplus is deposited into the Budget Reserve Fund, and 25.0% of any education fund revenue surplus is deposited in the Education Reserve Fund. An additional 25.0% of any surplus is deposited when funds have been used until balances are replenished to prior levels. Automatic year-end deposits are capped at 8.0% of general fund appropriations and 9.0% of education fund appropriations for that year. The legislature can appropriate above those levels.	Expenditures are limited to retroactive tax refunds, legal settlements, and operating deficits, upon legislative approval.

State	Fund Name	Determination of Fund Size	Procedure for Expenditures
Virginia	Revenue Stabilization Fund	Capped at 15.0% of average annual tax revenues on income and retail sales tax receipts for the three years immediately preceding that fiscal year.	Legislative appropriation of the lesser of the deficit or one-half of the fund's balance if income and sales tax revenue falls more than 2.0% below projections in the enacted budget.

Source: State Legislative Fiscal Offices