

**U10B00**  
**Maryland Environmental Service**

***Operating Budget Data***

(\$ in Thousands)

	<u>Fiscal 2014</u>	<u>Fiscal 2015</u>	<u>Fiscal 2016</u>	<u>Change Fiscal 2015-16</u>
Total Assets	\$92,776	\$104,742	\$81,836	-\$22,906
Total Liabilities	72,209	82,725	58,011	24,714
<b>Total Net Assets</b>	<b>\$20,567</b>	<b>\$22,017</b>	<b>\$23,825</b>	<b>\$1,808</b>
Total Revenue	\$110,317	\$141,173	\$159,505	\$18,332
Total Expenditures	108,956	139,335	157,447	18,112
<b>Operating Income</b>	<b>\$1,361</b>	<b>\$1,838</b>	<b>\$2,058</b>	<b>\$220</b>

- Between fiscal 2015 and 2016, net operating income of the Maryland Environmental Service (MES) increased by \$220,000 for all operations excluding the Midshore Regional Landfill Private Purpose Trust Fund. According to MES's audited financial statements, the principal reason for the increase in operating income was an increase in indirect cost recovery as a result of the growth in labor revenue in the solid waste business type activity.
- Revenues and expenditures increased between fiscal 2015 and 2016, primarily due to new local government projects: Harford County Solid Waste, Baltimore County Solid Waste – Eastern Acceptance, and the Prince George's County Materials Recycling Facility.
- In fiscal 2017, MES paid the State \$2,039,861 in unearned revenue from operating reimbursable projects that came in under budget. This is reflected as a \$2,000,000 adjustment to revenues in fiscal 2017 in Appendix A of the Governor's Budget Highlights.
- MES considers its undesignated unrestricted net assets to be its fund balance. Undesignated unrestricted net assets decreased from \$2.7 million in fiscal 2015 to \$2.1 million in fiscal 2016. This is down from \$5.3 million in undesignated unrestricted net assets in fiscal 2014. MES notes that it entered into a contract for the \$3.2 million purchase of an adjacent property in fiscal 2015 in order to alleviate parking constraints. However, there was an underlying increase of \$0.6 million in undesignated unrestricted net assets in fiscal 2015; thus, there was a net decrease of only \$2.5 million between fiscal 2014 and 2015.

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

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- An informal goal reflected by MES in the past is to reduce the overhead rate charged to State agencies and other clients as a result of increasing MES's client base, thus spreading overhead over more clients. In fact, overhead rates have declined as follows: fiscal 2015 – 45.29%, fiscal 2016 – 44.75%, fiscal 2017 – 44.54%, and fiscal 2018 – 43.60%. MES notes that as its labor index – the amount of work contracted – rises, and costs remain unchanged or decrease, the overhead rate will decrease.

***Personnel Data***

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	<b><u>FY 16 Actual</u></b>	<b><u>FY 17 Working</u></b>	<b><u>FY 18 Allowance</u></b>	<b><u>FY 17-18 Change</u></b>
Regular Positions	816.00	816.00	854.00	38.00
Contractual FTEs	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>	<u>0.00</u>
<b>Total Personnel</b>	<b>816.00</b>	<b>816.00</b>	<b>854.00</b>	<b>38.00</b>

***Vacancy Data: Regular Positions***

Turnover and Necessary Vacancies, Excluding New Positions	0.00	0.00%
Positions and Percentage Vacant as of 12/31/16	n/a	n/a

- Regular positions increase by 38 in the fiscal 2018 allowance. This reflects new positions based on anticipated needs.

## *Analysis in Brief*

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### **Major Trends**

***Used Antifreeze and Oil Recycling Continues to Decline:*** There has been a recent decline in the amount of antifreeze recycled and a longer term trend in the decline in the amount of used oil recycled between fiscal 2004 and 2015. MES notes that the decrease in the amounts of used oil collected since fiscal 2013 is due to local governments withdrawing from the Maryland Used Motor Oil Recycling Program, the use of longer lasting synthetic oils, commercial establishments offering recycling services, auto service centers specializing in oil changes, and routine vehicle maintenance that are convenient and reasonably priced. **The Department of Legislative Services (DLS) recommends that MES comment on which two local government sites are reopening and why they are reopening.**

***Worker Safety Meets Goal:*** MES has met its worker safety goal each year since fiscal 2012. MES notes that this is because of the following: (1) accidents that have occurred have not resulted in serious injury so employees that did have accidents were able to return to work on modified duty, resulting in decreased accident leave usage; (2) MES continues to grow in staff numbers, which increases the total hours worked and decreases the percent of accident leave as a percent of total hours worked; and (3) the MES Safety Program continues to train staff in best practices, which helps prevent accidents. **DLS recommends that MES comment on whether accidents are concentrated in any particular business type activity or client base.**

***Client Satisfaction Rate Goal Met:*** MES has met the goal of achieving a client satisfaction result of 75% or more in each of the years in which it has administered a client satisfaction survey since fiscal 2012. MES notes that it uses feedback from customer service reports to direct operating groups to respond to concerns noted within 48 hours. In addition, MES senior staff, such as the executive director and/or the division chief visit all field offices at least once per year in order to interact and improve communication with field staff.

### **Issues**

***Project Advances and Reimbursable Project Relationship Audit Findings:*** MES's April 2016 audit contained the finding that it did not maintain documentation to support the need for the full amount of funding advances received for certain State projects and that a 1979 Board of Public Works (BPW) policy may no longer be the appropriate mechanism for establishing the contractual relationships with State agencies. MES notes that it will continue to use project advances and that it delivered a formal request to its assistant Attorneys General's office on April 13, 2016, in regard to BPW policy but has not heard back. **DLS recommends that MES comment on the amount and timing of cash advances for all of its projects and on what a sufficient framework for supporting reimbursable arrangements with State agencies would reflect, including the possibility of policy, regulatory, and statutory changes.**

## **Recommended Actions**

1. Nonbudgeted.

## **Updates**

***Project Reserve Funds Status:*** MES has the authority to create project reserve funds under § 3-103(h) of the Natural Resources Article. The General Assembly created specific project reserve funds with caps under Chapter 397 of 2011, the Budget Reconciliation and Financing Act. The December 2016 fund balances are generally within the caps.

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***Operating Budget Analysis***

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**Program Description**

The Maryland Environmental Service (MES) was created as a unit within the Department of Natural Resources (DNR) in 1970 to provide water supply, wastewater treatment, and waste management services to State agencies, local governments, and private entities. During the 1993 session, the General Assembly adopted legislation that created MES as an instrumentality of the State and a public corporation independent of DNR. The organization's primary goals are to improve the environment, work more safely, and provide excellent customer service and satisfaction. MES provides technical services including engineering, design, financing, construction, and operation of water supply and wastewater treatment facilities. MES also provides similar services in the area of hazardous and solid waste facility management, including sanitary landfills, incinerators, and resource recovery facilities. Additional services offered include sludge and dredged materials management, recycling and marketing of end products, regulatory monitoring, and renewable energy needs servicing.

As of January 2017, MES operates and maintains 974 projects. An individual facility may have multiple projects going on at any given time. Some of the 974 projects are at 263 State-owned facilities, such as the Poplar Island Environmental Restoration Project; the Hart-Miller Island Dredged Material Containment Facility; Cox Creek Dredged Material Containment Facility; recyclable material processing facilities in Baltimore, Montgomery, and Prince George's counties; two municipal solid waste transfer facilities in Baltimore County; yard waste composting facilities in Montgomery and Prince George's counties; the Midshore I and II regional landfills; and the Hawkins Point Hazardous Waste Landfill (now in post-closure monitoring phase).

MES operates on a fee-for-service (FFS) basis. Operating funds are generated from six sources: State agency contracts, local government contracts, federal government contracts, private contracts, MES enterprises, and grants. In addition, MES receives State general obligation bond appropriations for capital improvements at State-owned facilities and may issue revenue bonds to finance local government projects. Revenues from State agency contracts derive from the operation and maintenance of State-owned water and wastewater treatment plants and from specific projects and services such as environmental cleanup or recycling program management. Revenues from local governments, the federal government, and the private sector derive from the operation and maintenance of water and wastewater treatment facilities and solid waste management services. MES enterprise revenues are generated by efforts such as yard waste composting, waste oil recovery, and geographic information system services.

Four goals guide MES's activities:

- improving the environment;
- improving infrastructure to convey and treat water and wastewater in the State;

- working more safely; and
- providing excellent customer service and satisfaction.

MES's mission and vision statements follow.

- **Mission Statement:** To provide operational and technical services to protect and enhance the environment for the people of Maryland.
- **Vision Statement:** An innovative and leading edge solver of environmental problems, a responsible and successful manager of environmental operations, and a great place to work.

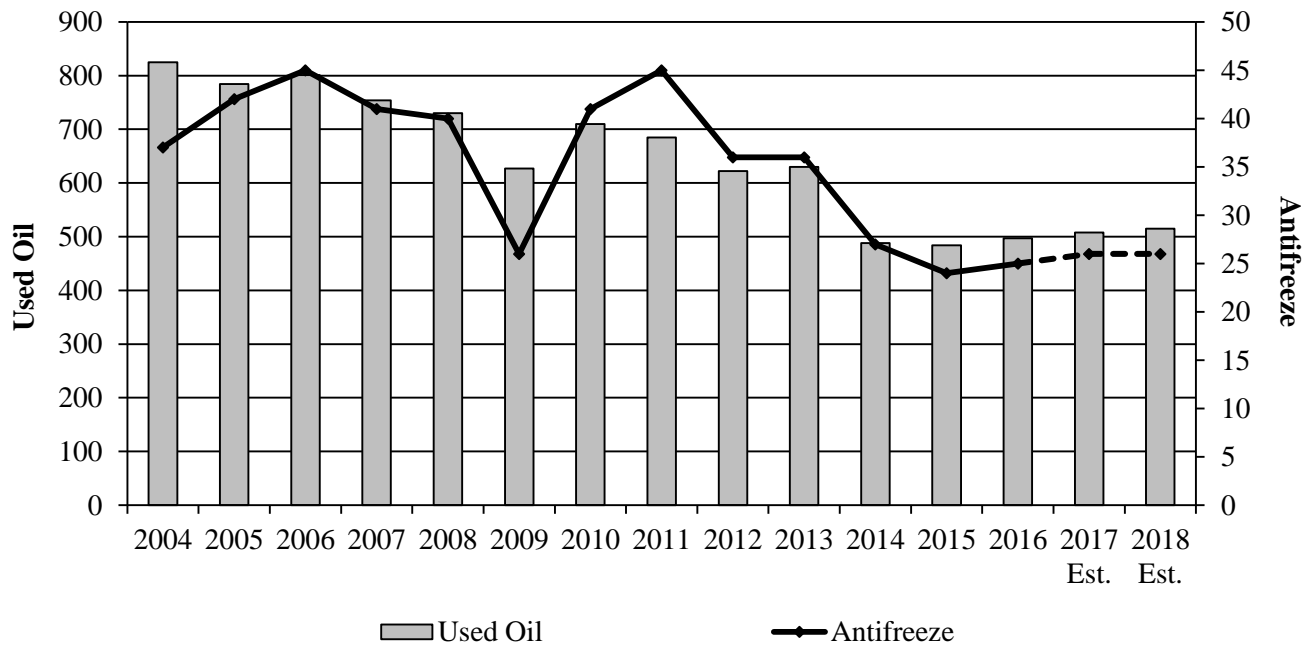
## **Performance Analysis: Managing for Results**

The MES performance measures reflected in this analysis cover three of MES's four goals: to improve the environment through MES's activities, to work more safely, and to provide excellent customer service and satisfaction.

### **1. Used Antifreeze and Oil Recycling Continues to Decline**

Two of the outputs under MES's goal of improving the environment are gallons of used antifreeze recycled and gallons of used oil recycled as part of the Maryland Used Motor Oil Recycling Program, which MES administers through an Intergovernmental Agency Agreement with the Maryland Department of the Environment. There has been a recent decline in the amount of antifreeze recycled and a longer term decline in the amount of used oil recycled between fiscal 2004 and 2015, as shown in **Exhibit 1**. MES notes that the decrease in the amounts of used oil collected since fiscal 2013 is due to local governments withdrawing from the Maryland Used Motor Oil Recycling Program, the use of longer lasting synthetic oils, commercial establishments offering recycling services, auto service centers specializing in oil changes, and routine vehicle maintenance that are convenient and reasonably priced. Looking forward, the slight increase anticipated in fiscal 2017 and 2018 for used oil recycled is the result of new sites added at private marinas and a reopening of two local government sites with new and larger capacity tanks. **The Department of Legislative Services (DLS) recommends that MES comment on which two local government sites are reopening and why they are reopening.**

**Exhibit 1**  
**Gallons of Used Oil and Antifreeze Recycled**  
**Fiscal 2004-2018 Est.**  
**(Thousands of Gallons)**

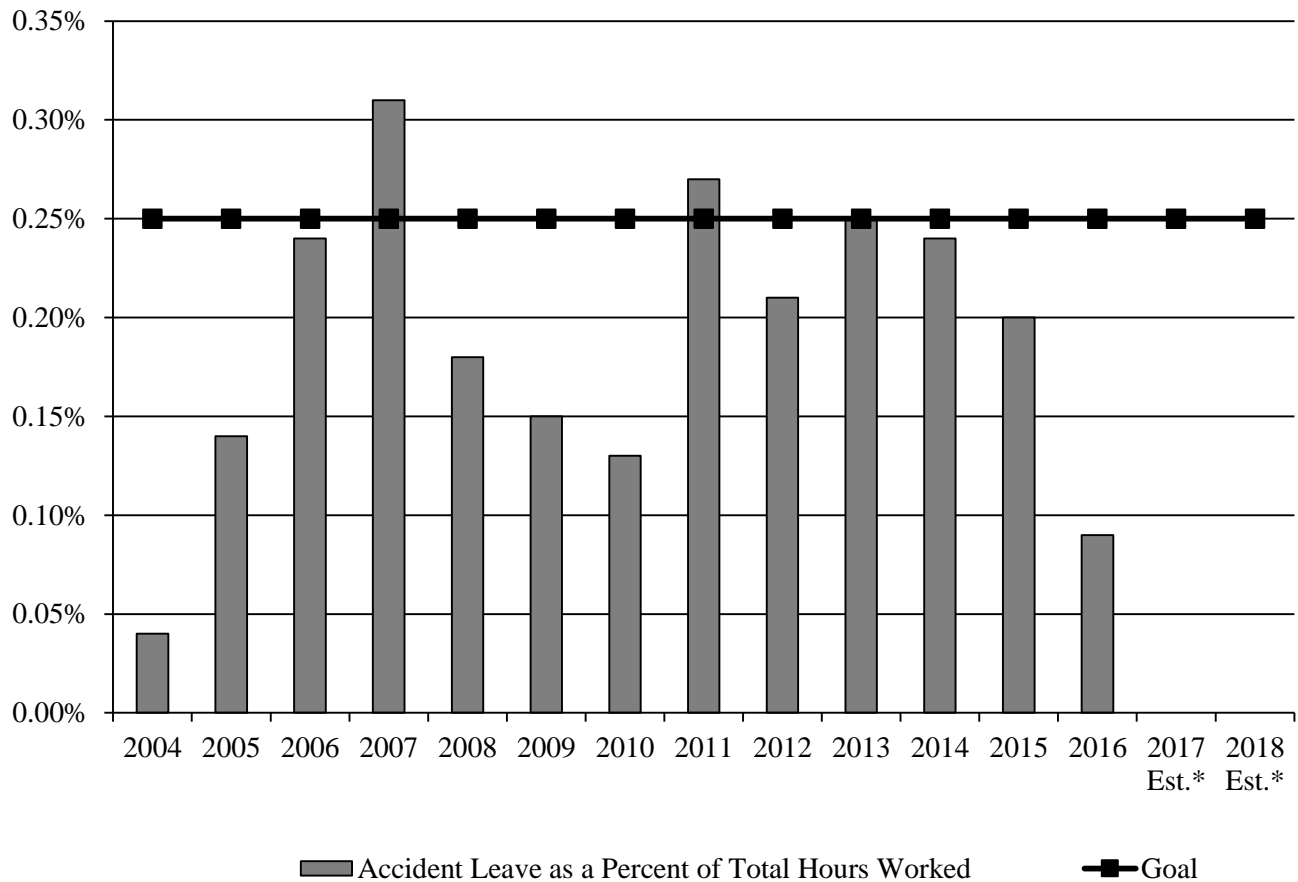


Source: Governor's Budget Books, Fiscal 2007-2016; Department of Budget and Management

## 2. Worker Safety Meets Goal

Another MES goal is to work more safely. One outcome related to this goal relates to accident leave as a percent of total hours worked, which is derived by dividing the total number of accident leave hours by the total billable hours for MES. MES's goal for this measure is to have accident leave be less than 0.25% of total hours worked, or less than one accident for every 400 hours worked. By this standard, MES met its goal in fiscal 2013 through 2016, as shown in **Exhibit 2**. In fact, MES was well under the 0.25% of total hours worked goal in fiscal 2016. MES notes that this is because of the following: (1) accidents that have occurred have not resulted in serious injury, so employees that did have accidents were able to return to work on modified duty, resulting in decreased accident leave usage; (2) MES continues to grow in staff numbers, which increases the total hours worked and decreases the percent of accident leave as a percent of total hours worked; and (3) the MES Safety Program continues to train staff in best practices, which helps prevent accidents. **DLS recommends that MES comment on whether accidents are concentrated in any particular business type activity or client base.**

**Exhibit 2**  
**Accident Leave as a Percent of Total Hours Worked**  
**Fiscal 2004-2018 Est.**



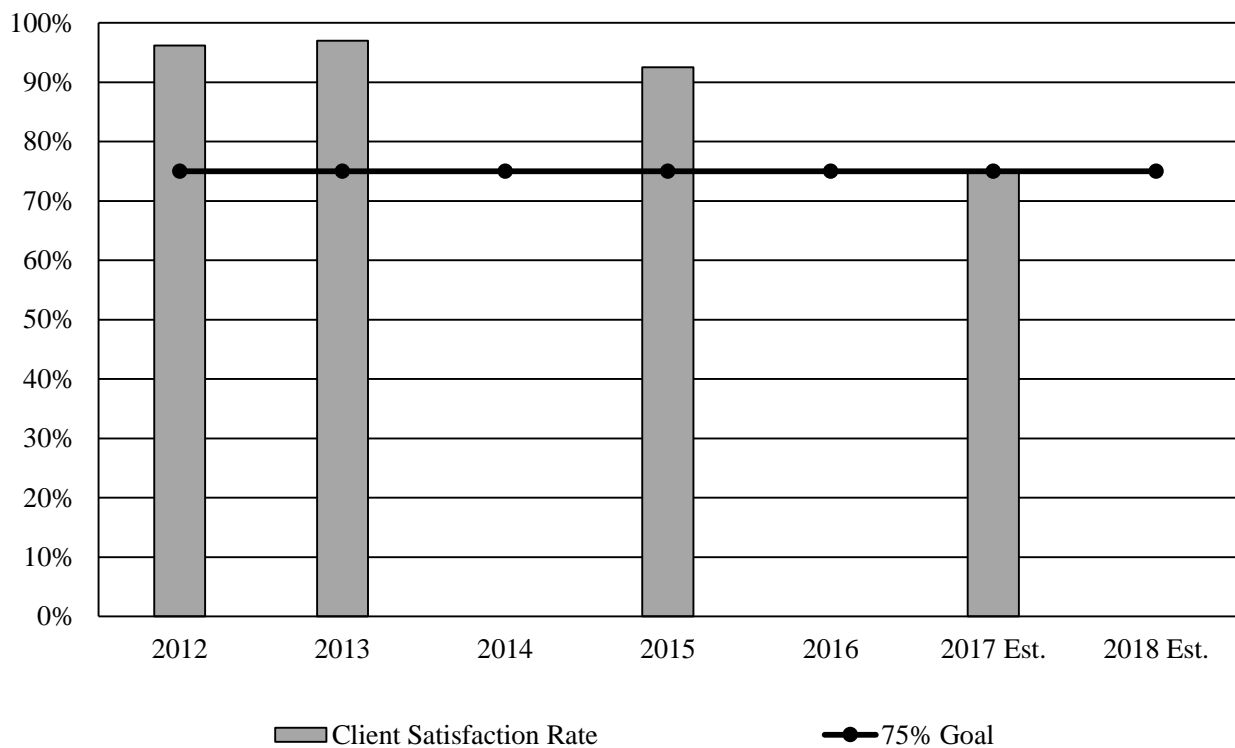
\*Fiscal 2017 and 2018 estimates for accident leave as a percent of hours worked are for less than 0.25%.

Source: Governor's Budget Books, Fiscal 2007-2016; Department of Budget and Management

### 3. Client Satisfaction Rate Goal Met

Under MES's fourth goal – provide excellent customer service and satisfaction – MES has the objective to achieve a client satisfaction result of 75% or more. As shown in **Exhibit 3**, MES has met this goal in each of the years in which it has administered a client satisfaction survey since fiscal 2012. MES notes that it uses feedback from customer service reports to direct operating groups to respond to concerns noted within 48 hours. In addition, MES senior staff, such as the executive director and/or the division chief, visit all field offices at least once per year in order to interact and improve communication with field staff. MES also conducts at least one education outreach program annually. During the last quarter of every other fiscal year, it distributes a client satisfaction survey for each client to complete; responses are averaged to calculate an overall client satisfaction rate.

**Exhibit 3**  
**Client Satisfaction Rate**  
**Fiscal 2012-2018 Est.**

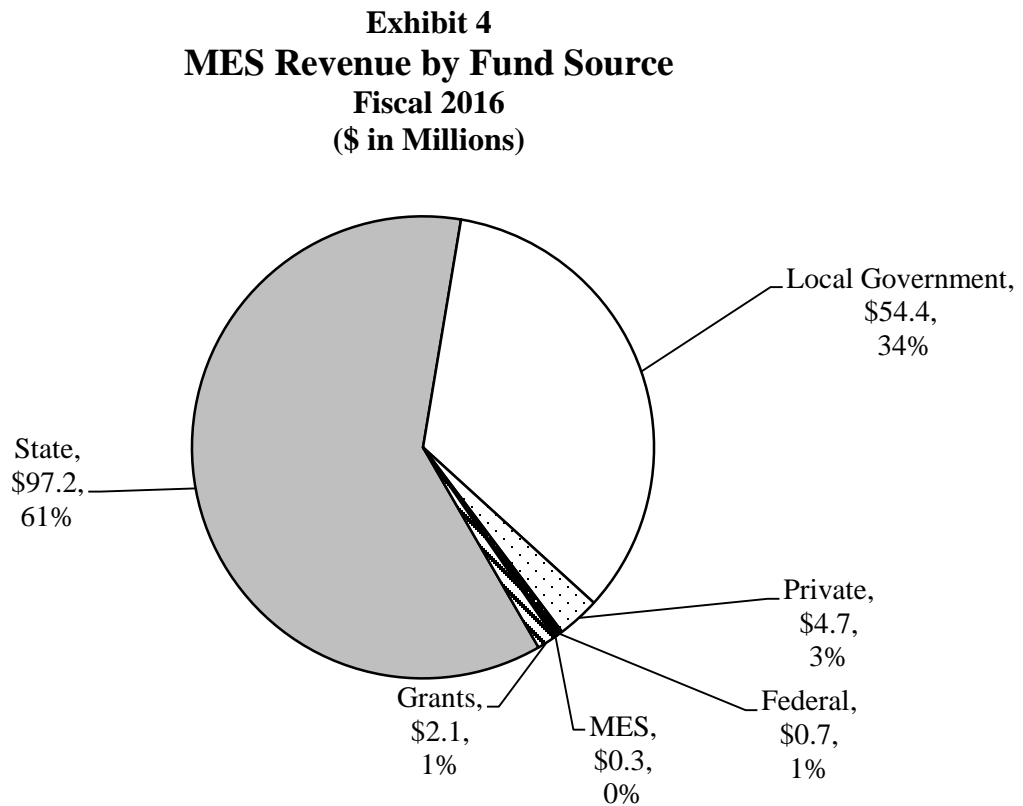


Note: The Maryland Environmental Service conducts a client satisfaction survey every other year.

Source: Governor's Budget Books, fiscal 2007-2016; Department of Budget and Management

## MES's Fiscal 2016 Financial Position

MES breaks down its revenue by fund sources and type of business activity. **Exhibit 4** provides an overview of fiscal 2016 revenue by fund source and shows that approximately 95% of MES's revenue comes from State and local government. In terms of its relationship with the State, MES has two arrangements: (1) reimbursable projects are related to Executive Order 01.01.1971.11 and the Board of Public Works (BPW) directive that MES operate wastewater and drinking water plants for State agencies; and (2) contractual projects for which MES has a contract with a State agency to do the work.



MES: Maryland Environmental Service

Source: Maryland Environmental Service

MES reimbursable project spending may be viewed as (1) engineering and maintenance spending; and (2) operations and maintenance spending. MES indicates that it was under budget for fiscal 2016 by \$2,474,890 in terms of State reimbursable projects. Of this amount, \$112,594 is special funds that were returned to DNR, leaving \$2,362,296 in general fund unearned revenue. The calculation for general fund unearned revenue, the \$2,362,296 that MES was under budget for

fiscal 2016, is reflected in **Exhibit 5**. Exhibit 5 also reflects the \$2,039,861 general fund amount – a subset of the \$2,362,296 unearned revenue – that was returned to the State after accounting for allocations to two of MES’s three project reserve funds, which are discussed as an Update in this analysis. MES notes that the reverted money reflects predominately funds that were budgeted for heating oil at a much higher level than they were budgeted in prior years.

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**Exhibit 5**  
**General Fund Unearned Revenue Amount**  
**Fiscal 2016**

	<b><u>Legislative</u></b> <b><u>Approp.</u></b>	<b><u>Actual</u></b>	<b><u>Difference</u></b>
<b>Spending</b>			
Engineering and Maintenance	\$3,138,454	\$3,337,153	-\$198,699
Operations and Maintenance	22,230,309	19,886,863	2,343,446
<b>Total</b>	<b>\$25,368,763</b>	<b>\$23,224,016</b>	<b>\$2,144,747</b>
Adjustments			\$330,143
<b>Unearned Revenue</b>			<b>\$2,474,890</b>
DNR Special Funds Returned			-\$112,594
<b>General Fund Unearned Amount</b>			<b>\$2,362,296</b>
State Reimbursable Project Contingency Fund Allocation			-\$22,436
ECI Steam Turbine Contingency Fund Allocation			-300,000
Miscellaneous Adjustment			1
<b>General Fund Amount Returned to the State</b>			<b>\$2,039,861</b>

DNR: Department of Natural Resources

ECI: Eastern Correctional Institution

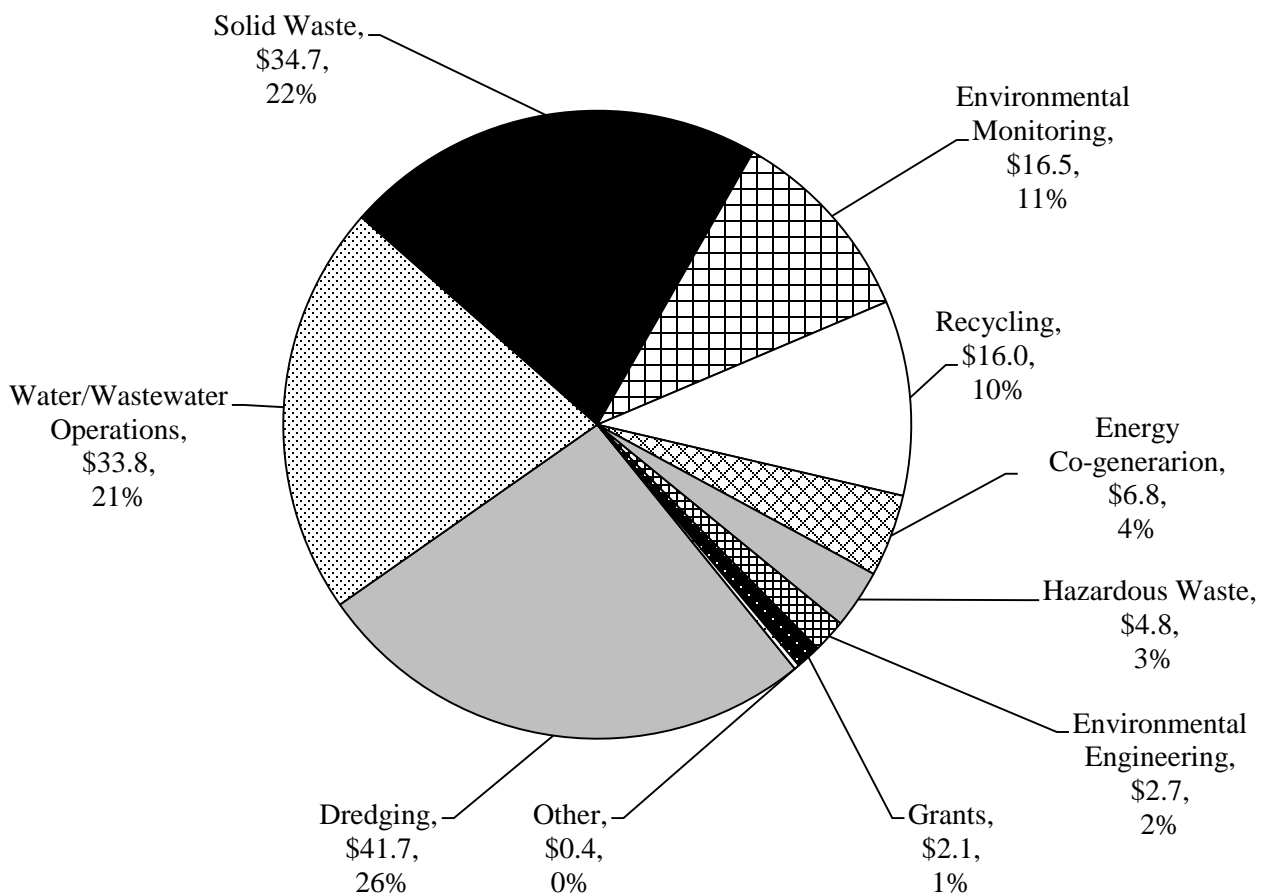
Note: The fiscal 2016 spending is reflected as \$23,224,016 for unearned revenue purposes in the exhibit, whereas elsewhere in this analysis, the fiscal 2016 actual spending is reflected as \$23,147,475. This is because the fiscal 2016 unearned revenue spending and the fiscal 2016 actual spending are accounting for costs in slightly different ways. The \$23,224,016 unearned revenue spending in the exhibit includes \$198,699 for engineering and maintenance billings that did not occur but need to be accounted for as part of unearned revenue, and \$87,845 charged for Minority Business Outreach and Maryland Correctional Institution labor, which are offset partially by a reduction of \$210,000 to reflect lower Maryland Correctional Institution – Hagerstown power plant fuel oil costs.

Source: Maryland Environmental Service; Department of Legislative Services

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**Exhibit 6** provides an overview of fiscal 2016 revenue by business activity type and shows that the largest three categories are dredging, solid waste, and water/wastewater operations. These three business activity types account for 69% of MES's revenue. In recent years, MES has entered the market for energy efficiency and renewable energy.

**Exhibit 6**  
**MES Revenue by Business Activity Type**  
**Fiscal 2016**  
(\$ in Thousands)



MES: Maryland Environmental Service

Source: Maryland Environmental Service

## Financial Changes

MES's operating income increased by \$220,000 between fiscal 2015 and 2016. MES's revenues increased by \$18.3 million between fiscal 2015 and 2016 as shown by the revenue by business type activity in **Exhibit 7**. This reflects the following:

- **Solid Waste Management:** An increase of \$18.4 million due to four new projects that came online during fiscal 2016 – Harford County Solid Waste and Baltimore County Solid Waste – Eastern Acceptance and Prince George's County Materials Recycling Facility – and the operation of the Maryland Correctional Institution – Hagerstown power plant which, along with all other energy generation projects, is included in solid waste management;
- **Water/Wastewater Operations:** An increase of \$9.6 million due to construction project revenue changes including upgrades to the Freedom District plant and other smaller plants throughout the State; and
- **Environmental Dredging and Restoration:** A decrease of \$11.7 million due to the completion of the Masonville Dredged Material Containment Facility construction project.

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**Exhibit 7**  
**Revenues by Business Type Activity**  
**Fiscal 2012-2016**  
**(\$ in Thousands)**

<b><u>Business Type Activity</u></b>	<b><u>2012</u></b>	<b><u>2013</u></b>	<b><u>2014</u></b>	<b><u>2015</u></b>	<b><u>2016</u></b>	<b><u>Change 2014-15</u></b>	<b><u>Change 2015-16</u></b>
Environmental Dredging and Restoration	\$23,924	\$20,816	\$31,222	\$53,325	\$41,666	\$22,103	-\$11,659
Solid Waste Management	11,363	12,118	15,831	16,289	34,738	458	18,449
Water/Wastewater Operations	21,920	21,839	22,753	24,196	33,809	1,443	9,613
Environmental Monitoring	15,015	11,888	12,879	14,596	16,499	1,717	1,903
Recycling	16,817	12,139	12,599	14,295	16,001	1,696	1,706
Energy Co-generation	6,666	6,162	6,264	7,891	6,769	1,627	-1,122
Hazardous Waste Treatment	5,846	4,881	5,175	5,500	4,819	325	-681
Environmental Engineering	2,303	2,244	2,048	1,908	2,735	-140	827
Grants	1,666	1,215	1,050	2,663	2,061	1,613	-602
Other	384	621	496	510	408	14	-102
<b>Total Revenues</b>	<b>\$105,904</b>	<b>\$93,923</b>	<b>\$110,317</b>	<b>\$141,173</b>	<b>\$159,505</b>	<b>\$30,856</b>	<b>\$18,332</b>

Source: Maryland Environmental Service

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As shown in the **Exhibit 8** expenses by object display, MES's overall operating expenses decrease by \$7,297,000 between fiscal 2016 and 2017 but are anticipated to increase by \$1,605,000 between fiscal 2017 and 2018 for salaries, wages, and fringe benefits. The two major changes between fiscal 2016 and 2017 are a decrease of \$9,736,000 for contractual services and \$8,454,000 for land and structures. MES notes that fiscal 2016 funding reflects work for three major construction projects – Freedom Enhanced Nutrient Removal Upgrade, Seagirt Dundalk Access Dredging, and Baltimore County Solid Waste – Eastern Acceptance facility construction – which incur large pass through expenses. Therefore, the difference between fiscal 2017 and 2018 is largely due to the status of current and anticipated construction projects.

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**Exhibit 8**  
**Operating Expenses**  
**Fiscal 2016-2018**  
**(\$ in Thousands)**

<u>Operating Expense</u>	<u>Expenditures</u> <u>2016</u>	<u>Legislative</u> <u>Appropriation</u> <u>2017</u>	<u>Allowance</u> <u>2018</u>	<u>Change</u> <u>2016-2017</u>	<u>Change</u> <u>2017-2018</u>
Salaries, Wages, and Fringe Benefits	\$50,090,000	\$50,395,000	\$52,000,000	\$305,000	\$1,605,000
Technical and Special Fees	10,006,000	12,500,000	12,500,000	2,494,000	0
Communication	620,000	500,000	500,000	-120,000	0
Travel	296,000	255,000	255,000	-41,000	0
Fuel and Utilities	6,501,000	9,000,000	9,000,000	2,499,000	0
Motor Vehicle Operation and Maintenance	3,952,000	5,000,000	5,000,000	1,048,000	0
Contractual Services	39,736,000	30,000,000	30,000,000	-9,736,000	0
Supplies and Materials	8,886,000	10,000,000	10,000,000	1,114,000	0
Equipment – Replacement	2,323,000	3,500,000	3,500,000	1,177,000	0
Fixed Charges	1,583,000	4,000,000	4,000,000	2,417,000	0
Land and Structures	33,454,000	25,000,000	25,000,000	-8,454,000	0
<b>Total Operating Expenses</b>	<b>\$157,447,000</b>	<b>\$150,150,000</b>	<b>\$151,755,000</b>	<b>-\$7,297,000</b>	<b>\$1,605,000</b>

Source: Maryland Environmental Service

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## **Types of MES Operations**

MES's business type activities can generally be viewed as FFS and revenue generating activities. Revenue generating activities can be further divided into products and services. Before the sale of the scrap tire recycling facility in January 2008, MES sold recycled crumb rubber products. Now, MES produces two products – Leafgro and Leafgro Gold. Leafgro – composted yard waste such as grass clippings and leaves – and Leafgro Gold – composted food residual and yard waste – are produced under the contract that MES has to operate composting facilities for Montgomery and Prince George's counties; thus, the two counties receive the revenues from sales. However, MES continues to perform three revenue generating services: yard waste grinding, waste oil collection, and geographic information system services.

**Exhibit 9** reflects MES's revenue generating services. As can be seen, expenses exceeded revenues for two of MES's three revenue generating activities in fiscal 2016 – used oil collection and geographical information system (GIS) services. In addition, expenses have exceeded revenues for GIS services for three of the last four years, and in fiscal 2016, expenses increased faster than revenues for yard waste grinding. MES notes that the operating loss for used oil collection in fiscal 2016 reflects the decrease in demand in the market for used oil, as well as the decrease in price. The operating loss for GIS services in fiscal 2016 reflects an update to the billing process that dropped six billing days. Prior to fiscal 2016, GIS services did not include an additional GIS service center that was added in fiscal 2013, which accounts for a portion of the operating losses in fiscal 2013 and 2015 and the relatively modest operating surplus in fiscal 2014. MES notes that it works diligently to find new and innovative ways to improve, renew, and develop services each year and that the prognosis for revenue generating services is good.

**Exhibit 9**  
**Revenue Generating Services**  
**Fiscal 2013-2016**  
**(\$ in Thousands)**

	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>Difference</u> <u>2015-2016</u>
<b>Used Oil Collection</b>					
Revenue	\$721	\$753	\$585	\$218	-\$367
Expense	-368	-338	-301	-242	59
<b>Total</b>	<b>\$353</b>	<b>\$415</b>	<b>\$284</b>	<b>-\$24</b>	<b>-\$308</b>
<b>GIS Services</b>					
Revenue	\$2,878	\$3,447	\$4,549	\$4,546	-\$3
Expense	-3,137	-3,404	-4,600	-4,753	-\$153
<b>Total</b>	<b>-\$259</b>	<b>\$43</b>	<b>-\$51</b>	<b>-\$207</b>	<b>-\$156</b>
<b>Yard Waste Grinding (Tubgrinding)</b>					
Revenue	\$510	\$347	\$516	\$570	\$54
Expense	-378	-282	-345	-498	-153
<b>Total</b>	<b>\$132</b>	<b>\$65</b>	<b>\$171</b>	<b>\$72</b>	<b>-\$99</b>

GIS: geographical information system

Source: Maryland Environmental Service

## Proposed Budget

The proposed budget discussion focuses on the State reimbursable projects portion of MES's budget. As shown in **Exhibit 10**, MES's reimbursable project charges to State agencies decrease from \$25,957,718 in fiscal 2017 to \$24,810,713 in fiscal 2018, a net reduction of \$1,147,005, or 4.4%. The major change between fiscal 2017 and 2018 is the reflection of a lower budgeted amount for fuel oil. The fiscal 2017 budget was submitted before the lower fuel oil costs were realized, which inflated the fiscal 2017 budget. There is also an increase of \$1,062,850 for salaries, wages, and fringe benefits.

**Exhibit 11** shows specific project changes between fiscal 2017 and 2018. Selected changes are as follows:

- **Department of Public Safety and Correctional Services (DPSCS) – Eastern Correctional Institution Co-Generation Facility:** An increase of \$272,297 is due to a 3% salary increase.

**Exhibit 10**  
**Reimbursable Projects Funding Schedule**  
**Fiscal 2016-2018**

<b><u>Operating Expense</u></b>	<b><u>Expenditures</u></b> <b><u>2016</u></b>	<b><u>Legislative</u></b> <b><u>Appropriation</u></b> <b><u>2017</u></b>	<b><u>Allowance</u></b> <b><u>2018</u></b>	<b><u>Change</u></b> <b><u>2016-17</u></b>	<b><u>Change</u></b> <b><u>2017-18</u></b>
Salaries, Wages, and Fringe Benefits	\$12,971,173	\$13,523,024	\$14,585,874	\$551,851	\$1,062,850
Technical and Special Fees	646,417	558,752	492,625	-87,665	-66,127
Contractual Services	1,973,361	1,577,413	1,437,625	-395,948	-139,788
Equipment Operations and Maintenance	344,010	502,226	429,881	158,216	-72,345
Fixed Charges	481	0	0	-481	0
Communication	96,564	101,356	109,047	4,792	7,691
Travel	16,718	12,963	12,658	-3,755	-305
Fuel and Utilities	4,774,595	7,819,051	5,664,066	3,044,456	-2,154,985
Supplies and Materials	2,349,307	1,862,933	2,078,937	-486,374	216,004
Non-operating Revenue Expense	-25,151	0	0	25,151	0
<b>Total Operating Expenses</b>	<b>\$23,147,475</b>	<b>\$25,957,718</b>	<b>\$24,810,713</b>	<b>\$2,810,243</b>	<b>-\$1,147,005</b>

Note: The Maryland Environmental Service indicates that it has consolidated the following operating expense categories: engineering and maintenance is included in salaries, wages, and fringe benefits; motor vehicle operations and maintenance is included in equipment operations and maintenance; and replacement equipment and additional equipment are no longer separately considered.

Source: Maryland Environmental Service

**Exhibit 11**  
**Reimbursable Projects**  
**Fiscal 2018 Allowance Data**

<b><u>Facilities</u></b>	<b><u>Expenditures</u></b> <b><u>2016</u></b>	<b><u>Allocation</u></b> <b><u>2017</u></b>	<b><u>Allowance</u></b> <b><u>2018</u></b>	<b><u>Change</u></b> <b><u>2016-17</u></b>	<b><u>Change</u></b> <b><u>2017-18</u></b>	<b><u>Percent</u></b> <b><u>Change</u></b> <b><u>2016-17</u></b>	<b><u>Percent</u></b> <b><u>Change</u></b> <b><u>2017-18</u></b>
DPSCS – Eastern Correctional Institution Co-Generation Facility	\$6,966,079	\$6,886,868	\$7,159,165	-\$79,211	\$272,297	-1.1%	4.0%
DPSCS – Eastern Correctional Institution	1,995,846	2,086,905	2,295,769	91,059	208,864	4.6%	10.0%
DNR – Public Lands	2,582,371	2,756,584	2,931,285	174,213	174,701	6.7%	6.3%
DPSCS – Dorsey Run Correctional Facility	1,678,668	1,906,112	2,037,930	227,444	131,818	13.5%	6.9%
DJS – Boys’ Village of Maryland and RICA Cheltenham	432,720	421,479	484,462	-11,241	62,983	-2.6%	14.9%
DHMH – Crownsville Hospital Center	448,327	471,202	531,024	22,875	59,822	5.1%	12.7%
Maryland Veterans’ Home Commission	594,678	411,156	461,567	-183,522	50,411	-30.9%	12.3%
DPSCS – Western Correctional Institution	213,128	136,921	161,690	-76,207	24,769	-35.8%	18.1%
DJS – Juvenile Services Administration Youth Centers	352,082	411,018	435,310	58,936	24,292	16.7%	5.9%
DHMH – Springfield Hospital Center	656,625	452,010	473,128	-204,615	21,118	-31.2%	4.7%
DJS – Victor Cullen Center	303,249	295,242	315,639	-8,007	20,397	-2.6%	6.9%
Military Department	202,579	233,435	253,192	30,856	19,757	15.2%	8.5%
DNR – Fisheries Service	55,953	54,907	69,691	-1,046	14,784	-1.9%	26.9%
St. Mary’s College of Maryland	65,021	72,295	76,710	7,274	4,415	11.2%	6.1%
University of Maryland Center for Environmental Studies – Horn Point	85,708	69,757	71,362	-15,951	1,605	-18.6%	2.3%

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<u>Facilities</u>	<u>Expenditures 2016</u>	<u>Allocation 2017</u>	<u>Allowance 2018</u>	<u>Change 2016-17</u>	<u>Change 2017-18</u>	<u>Percent Change 2016-17</u>	<u>Percent Change 2017-18</u>
DPSCS – Maryland Correctional Institution – Jessup	624,497	653,913	655,066	29,416	1,153	4.7%	0.2%
DPSCS – Patuxent Institution	531,979	557,037	558,018	25,058	981	4.7%	0.2%
DHMH – Rosewood Hospital	3,754	8,124	8,897	4,370	773	116.4%	9.5%
DPSCS – Maryland Correctional Institute of Women – Jessup	254,425	266,409	266,878	11,984	469	4.7%	0.2%
DHMH – Clifton T. Perkins Hospital Center	208,166	217,971	218,355	9,805	384	4.7%	0.2%
Maryland Aviation Administration	25,982	28,115	25,523	2,133	-2,592	8.2%	-9.2%
DPSCS – Maryland Correctional Institution – Hagerstown	1,719,770	1,803,450	1,772,790	83,680	-30,660	4.9%	-1.7%
DPSCS – Maryland Correctional Institution – Hagerstown: Power Generation	3,145,868	5,756,808	3,547,262	2,610,940	-2,209,546	83.0%	-38.4%
<b>Total</b>	<b>\$23,147,475</b>	<b>\$25,957,718</b>	<b>\$24,810,713</b>	<b>\$2,810,243</b>	<b>-\$1,147,005</b>	<b>12.1%</b>	<b>-4.4%</b>

DHMH: Department of Health and Mental Hygiene  
 DJS: Department of Juvenile Services  
 DNR: Department of Natural Resources  
 DPSCS: Department of Public Safety and Correctional Services  
 RICA: Regional Institute for Children and Adolescents

Note: The fiscal 2016 actual spending is reflected as \$23,147,475 in the exhibit, whereas elsewhere in the analysis, the fiscal 2016 unearned revenue is reflected as \$23,224,016. This is because the fiscal 2016 actual spending and the fiscal 2016 unearned revenue spending are accounting for costs in slightly different ways. The \$23,224,016 unearned revenue spending elsewhere in this analysis includes \$198,699 for engineering and maintenance billings that did not occur but need to be accounted for as part of unearned revenue, and \$87,845 charged for Minority Business Outreach and Maryland Correctional Institution labor, which are offset partially by a reduction of \$210,000 to reflect lower Maryland Correctional Institution – Hagerstown power plant fuel oil costs.

Source: Governor’s Budget Books, Fiscal 2018

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- ***DPSCS – Eastern Correctional Institution:*** An increase of \$208,864 is due to the startup costs and chemicals required for the new drinking water plant and to a salary increase for the wastewater treatment plant.
- ***DNR – Public Lands:*** An increase of \$174,701 is due to a 3% salary increase and the fact that maintenance staff are budgeted directly to individual facilities.
- ***DPSCS – Dorsey Run Correctional Facility:*** An increase of \$131,818 is due to a 3% salary increase and the fact that maintenance staff are budgeted directly to individual facilities.
- ***DPSCS – Maryland Correctional Institution – Hagerstown: Power Generation:*** A decrease of \$2,209,546 reflects that fuel oil was budgeted at \$4.355 million in fiscal 2017, after the fiscal 2016 actual of \$1.9 million was realized, and so fiscal 2018 costs reflect \$2.1 million for fuel oil (this also explains the \$2,610,940 increase between fiscal 2016 and 2017).

## Issues

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### 1. Project Advances and Reimbursable Project Relationship Audit Findings

MES's April 2016 audit contained two findings concerning its State projects as shown in Exhibit 12. DLS recommends that MES comment on the amount and timing of cash advances for all of its projects, and on what a sufficient framework for supporting reimbursable arrangements with State agencies would reflect, including the possibility of policy, regulatory, and statutory changes.

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#### Exhibit 12 MES Audit Findings April 2016

<u>Finding</u>	<u>Recommendation</u>	<u>Status</u>
The Maryland Environmental Service (MES) did not maintain documentation to support the need for the full amount of funding advances received for certain State projects.	Prepare and retain documentation supporting the need for advance amounts and duration; and periodically evaluate advances received and return to State agencies funds in excess of the needs established in the contracts, including the appropriate portion of the advances for the aforementioned seven projects.	MES notes that large scale construction and technical engineering projects require large amounts of cash on hand but that as a fee for service organization, MES cash on hand is not enough to fund client capital projects and agency needs. As a result, contracts are negotiated for 90-day funding of cash advances, to ensure the timely payments to vendors. MES notes that improved communication and documentation has facilitated the completion of projects.
(Policy Issue) A 1979 Board of Public Works (BPW) policy, which addresses the services provided by MES to State agencies for reimbursable projects, may no longer be the appropriate mechanism for establishing the contractual relationships between those parties.	Consult with legal counsel and obtain formal advice regarding the appropriateness of the existing BPW policy statement or whether the contractual arrangements between MES and State agencies should be handled in a different manner, such as through regulation; and reassess existing contractual requirements with State agencies and ensure they are sufficient.	MES notes it delivered a formal request to its assistant Attorneys General's office on April 13, 2016, in regard to BPW policy. MES notes that the assistant Attorneys General's office is preparing advice.

Source: Office of Legislative Audits; Maryland Environmental Service

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## ***Recommended Actions***

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1. Nonbudgeted.

## *Updates*

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### 1. Project Reserve Funds Status

MES has the authority to create project reserve funds under § 3-103(h) of the Natural Resources Article. The General Assembly created specific project reserve funds with caps under Chapter 397 of 2011, the Budget Reconciliation and Financing Act. **Exhibit 13** reflects the recent project reserve fund history.

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#### Exhibit 13 Project Reserve Fund Status December 2016

<u>Project Reserve Fund Activity</u>	<u>Amount</u>	<u>Cap</u>	<u>Difference</u>
<b>State Reimbursable Project Contingency Fund</b>			
Beginning Balance (June 30, 2016)	\$977,564		
Approved Retainage	22,436		
Interest Earned	616		
<b>Current Balance</b>	<b>\$1,000,616</b>	<b>\$1,000,000</b>	<b>\$616</b>
<b>ECI Steam Turbine Contingency Fund</b>			
Beginning Balance (June 30, 2016)	\$1,007,001		
Approved Retainage	300,000		
Interest Earned	659		
<b>Current Balance</b>	<b>\$1,307,660</b>	<b>\$1,500,000</b>	<b>-\$192,340</b>
<b>DNR Project Contingency Fund</b>			
Beginning Balance (June 30, 2016)	\$3,383		
Approved Additions	0		
Funds Used	0		
Interest Earned	2		
<b>Current Balance</b>	<b>\$3,385</b>	<b>\$500,000</b>	<b>-\$496,615</b>

DNR: Department of Natural Resources

ECI: Eastern Correctional Institution

Source: Maryland Environmental Service; Department of Legislative Services

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**Appendix 1**  
**Audit Findings**

Audit Period for Last Audit:	December 9, 2011 – March 23, 2015
Issue Date:	April 2016
Number of Findings:	5
Number of Repeat Findings:	0
% of Repeat Findings:	0%
Rating: (if applicable)	n/a

**Finding 1:** Maryland Environmental Service (MES) did not maintain documentation to support the need for the full amount of funding advances received for certain State projects.

**Finding 2 (Policy Issue):** A 1979 Board of Public Works policy, which addresses the services provided by MES to State agencies for reimbursable projects, may no longer be the appropriate mechanism for establishing the contractual relationships between those parties.

**Finding 3:** Internal controls over collections were not adequate and cash receipts and account receivable duties were not adequately separated.

**Finding 4:** Human resources and payroll system user capabilities were not adequately restricted. In addition, independent documented reviews of personnel and payroll transactions were not performed.

**Finding 5:** MES had not established adequate controls to ensure the propriety of access capabilities assigned to users of its automated financial management system.

\*Bold denotes item repeated in full or part from preceding audit report.

**Appendix 2**  
**Object/Fund Difference Report**  
**Maryland Environmental Service**

<u>Object/Fund</u>	<u>FY 16 Actual</u>	<u>FY 17 Working Appropriation</u>	<u>FY 18 Allowance</u>	<u>FY 17 - FY 18 Amount Change</u>	<u>Percent Change</u>
<b>Positions</b>					
01 Regular	816.00	816.00	854.00	38.00	4.7%
<b>Total Positions</b>	<b>816.00</b>	<b>816.00</b>	<b>854.00</b>	<b>38.00</b>	<b>4.7%</b>
<b>Objects</b>					
01 Salaries and Wages	\$ 50,090,000	\$ 50,395,000	\$ 52,000,000	\$ 1,605,000	3.2%
02 Technical and Spec. Fees	10,006,000	12,500,000	12,500,000	0	0%
03 Communication	620,000	500,000	500,000	0	0%
04 Travel	296,000	255,000	255,000	0	0%
06 Fuel and Utilities	6,501,000	9,000,000	9,000,000	0	0%
07 Motor Vehicles	3,952,000	5,000,000	5,000,000	0	0%
08 Contractual Services	39,736,000	30,000,000	30,000,000	0	0%
09 Supplies and Materials	8,886,000	10,000,000	10,000,000	0	0%
10 Equipment – Replacement	2,323,000	3,500,000	3,500,000	0	0%
13 Fixed Charges	1,583,000	4,000,000	4,000,000	0	0%
14 Land and Structures	33,454,000	25,000,000	25,000,000	0	0%
<b>Total Objects</b>	<b>\$ 157,447,000</b>	<b>\$ 150,150,000</b>	<b>\$ 151,755,000</b>	<b>\$ 1,605,000</b>	<b>1.1%</b>
<b>Funds</b>					
07 Nonbudgeted Fund	\$ 157,447,000	\$ 150,150,000	\$ 151,755,000	\$ 1,605,000	1.1%
<b>Total Funds</b>	<b>\$ 157,447,000</b>	<b>\$ 150,150,000</b>	<b>\$ 151,755,000</b>	<b>\$ 1,605,000</b>	<b>1.1%</b>

Note: Does not include targeted reversions, deficiencies, and contingent reductions.

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