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Department of Labor, Licensing, and Regulation

Operating Budget Data

(\$ in Thousands)

	<u>FY 07</u>	<u>FY 08</u>	<u>FY 09</u>	<u>FY 08-09</u>	<u>% Change</u>
	<u>Actual</u>	<u>Working</u>	<u>Allowance</u>	<u>Change</u>	<u>Prior Year</u>
General Fund	\$15,727	\$15,737	\$16,383	\$646	4.1%
Special Fund	35,420	40,656	28,583	-12,073	-29.7%
Federal Fund	115,945	106,748	118,990	12,241	11.5%
Reimbursable Fund	<u>6,579</u>	<u>8,051</u>	<u>8,068</u>	<u>16</u>	<u>0.2%</u>
Total Funds	\$173,672	\$171,192	\$172,023	\$831	0.5%

- The allowance provides a fiscal 2008 general fund deficiency of \$173,132 for the reclassification of financial examiner positions within the Division of Financial Regulation. The allowance also provides a \$5.5 million federal fund deficiency for grants associated with adult training services under the Workforce Investment Act program and employment market analysis related to the Base Realignment and Closure process.
- The fiscal 2009 allowance increases by \$830,908, or 0.5%, from the fiscal 2008 working appropriation. However, this change is distorted due to changes in health insurance budgeting. Absent health insurance costs, the budget actually declines by approximately \$6.4 million, or 4.0%.
- Special funds decline by over \$12 million, largely due to the one-time use of Reed Act funds in fiscal 2008 for unemployment insurance administration. Federal funds rebound from fiscal 2008; however, health insurance costs overstate this increase. Absent health insurance, federal funds increase by about 6.5% from the fiscal 2008 working appropriation.

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

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Personnel Data

	<u>FY 07 Actual</u>	<u>FY 08 Working</u>	<u>FY 09 Allowance</u>	<u>FY 08-09 Change</u>
Regular Positions	1,474.55	1,472.75	1,460.65	-12.10
Contractual FTEs	<u>177.22</u>	<u>187.02</u>	<u>162.35</u>	<u>-24.67</u>
Total Personnel	1,651.77	1,659.77	1,623.00	-36.77

Vacancy Data: Regular Positions

Turnover, Excluding New Positions	55.50	3.80%
Positions Vacant as of 12/31/07	96.63	6.56%

- Regular positions total 1,460.65 in the fiscal 2009 allowance, a net decrease of 12.1 positions from the fiscal 2008 working appropriation. There were 16.1 positions eliminated from a variety of units, most from the Workforce Development and Unemployment Insurance divisions.
- The fiscal 2009 allowance also includes four new positions: two wage and hour investigators within the Employment Standards Services Unit and two wage and hour investigators within the Prevailing Wage Unit.
- Contractual full-time equivalent positions fell by 24.7. Again, most of this decline is recorded in the Workforce Development and Unemployment Insurance divisions.

Analysis in Brief

Major Trends

Consumer Complaints Fall as Enforcement Rises: Increased enforcement efforts by the Division of Financial Regulation correlate to a recent decline in consumer complaints against banking institutions, mortgage brokers, debt collection agencies, and other financial services providers.

After Loss of Funding, Employment Standards Services Unit Performance Fails to Rebound: The Employment Standards Services Unit within the Division of Labor and Industry was not funded in the fiscal 2006 appropriation. Despite legislatively mandated funding beginning in fiscal 2007, the unit's performance has not rebounded to pre-2006 levels.

Complaint Resolution Standards Fall within Occupational and Professional Licensing: Reversing a decade long trend of exceeding goals, the Division of Occupational and Professional Licensing fails to reach complaint resolution standards in fiscal 2007. Further, the division does not expect to return to form until fiscal 2009.

Issues

Department Responds to the Increase in Foreclosures in Maryland: Maryland, like the rest of the country, is experiencing a significant downturn in the housing market accompanied by an alarming increase in the number of foreclosures. In the wake of this crisis, the Administration created the Homeownership Preservation Task Force in 2007, naming the Secretary of the department as co-chair. In response to the current housing situation and based on recommendations of the task force, the department's Division of Financial Regulation is increasing its efforts in regulating the mortgage industry. **The department should brief the budget committees on how it is responding to the mortgage crisis and the extent to which it is implementing the recommendations of the Governor's Homeownership Preservation Task Force.**

Funding Imbalance within the Division of Unemployment Insurance: Fluctuations in federal funding for the administration of the unemployment insurance program pose concerns for long-term budgeting of the division and may be contributing to a slight decline in performance standards. **The department should brief the budget committees on its plans for stabilizing the funding stream for unemployment insurance administration. In the absence of such a plan, the department should discuss how it will handle continued year-to-year fluctuations in its budget.**

Safety Inspection Vacancies Persist: Salary constraints exacerbate a persistent turnover problem with boiler inspectors within the Division of Labor and Industry's Safety Inspection program. **The Department of Legislative Services recommends the adoption of committee narrative requesting the department to apply to the Department of Budget and Management (DBM) for the upward reclassification of boiler inspector positions with the Division of Labor and**

Industry. As part of this effort, DBM should include a special focus on boiler inspectors in the next statewide annual salary review to ensure competitiveness with the private sector.

Recommended Actions

	<u>Funds</u>	<u>Positions</u>
1. Delete a long-term vacant position.	\$ 44,066	1.0
2. Delete two new positions within the Employment Standards Services Unit.	79,776	2.0
3. Reduce travel and equipment funds associated with two new positions.	10,000	
4. Adopt committee narrative requesting the department to review the salary structure of safety inspection positions within the Division of Labor and Industry.		
Total Reductions	\$ 133,842	3.0

Updates

Healthy Balance in the Unemployment Insurance Trust Fund: Committee narrative in 2007 requested the department to report on the inputs and outputs that comprise the balance of the unemployment trust fund.

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Department of Labor, Licensing, and Regulation

Operating Budget Analysis

Program Description

The Department of Labor, Licensing, and Regulation (DLLR) includes many of the State's agencies and boards responsible for licensing and regulating various businesses, professions, and trades. The department also administers a variety of federally funded employment service programs. In addition to the Office of the Secretary, the department has six operating divisions:

- **Division of Labor and Industry** is responsible for safety inspections of boilers, elevators, amusement rides, and railroads. It also enforces certain protective labor laws and administers the Maryland Occupational Safety and Health Act.
- **Division of Workforce Development** operates workforce development programs including job services, Workforce Investment Act, and labor market information programs.
- **Division of Unemployment Insurance** operates the federally funded unemployment insurance programs.
- **Division of Occupational and Professional Licensing** licenses, regulates, and monitors 21 different professions and trades through boards and commissions. All but 7 boards are supported by the general fund.
- **Division of Racing** regulates thoroughbred and harness racing at tracks across the State. Responsibilities include assigning racing days, regulating wagering on races, collecting the wagering tax, licensing all racetrack employees, and operating a testing laboratory. The division also pays the salaries and stipends of all racetrack employees who are appointed by the State Racing Commission.
- **Division of Financial Regulation** regulates commercial banks, trust companies, credit unions, mortgage lenders and originators, collection agencies, and consumer loan companies.

Each division has its own set of goals and objectives based on its mission, but the department's general goals are to:

- provide a worker safety net, protect workers' rights, and foster work force development;
- improve workplace safety and worker health;
- prevent injuries and save lives of people using railroads, boilers, escalators, pressure vessels, and amusement rides;

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- assure the basic competence and regulation compliance of occupational and professional licensees;
- maintain the integrity of the horse racing industry; and
- protect consumers of financial services.

Performance Analysis: Managing for Results

Consumer Complaints Fall as Enforcement Rises

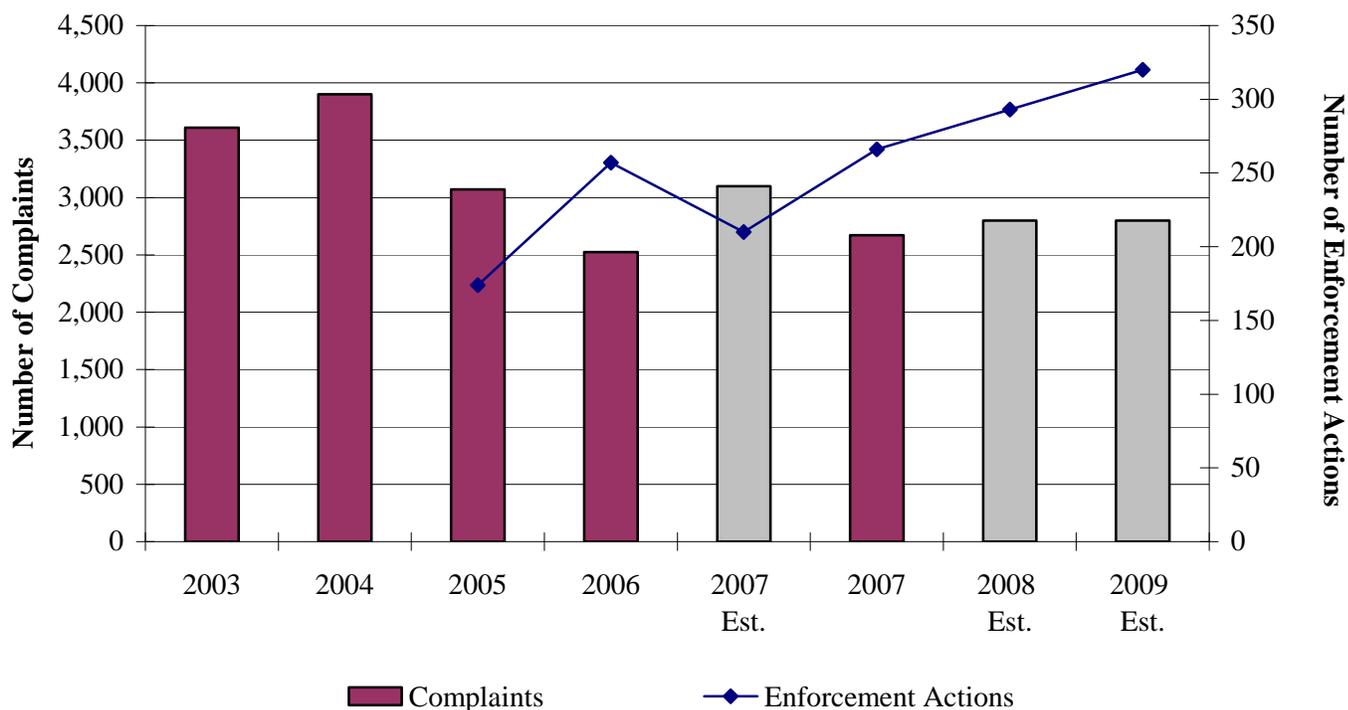
The Division of Financial Regulation strives to protect financial services customers, ensure appropriate licensing, and maintain soundness in the State's financial services industry. It accomplishes this, in part, by addressing consumer complaints and by taking enforcement or disciplinary actions.

The division created its enforcement unit in fiscal 2000. The unit investigates fraud complaints and reviews unlicensed activity. Further, it suspends or revokes licenses and when necessary, prepares cases for criminal prosecution. In fiscal 2005, the division began measuring the performance of this unit. Enforcement actions have increased each year since 2005 and are expected to continue to increase at a 10% per annum rate. As a preventative measure, the division also conducts compliance examinations. The compliance staff, which has doubled over the last several years, can detect potential problems and allows licensees to correct any issues.

Increased enforcement and compliance efforts appear to influence the number of consumer complaints against financial institutions. As shown in **Exhibit 1**, such complaints have fallen significantly since 2004 despite the increase in the number of licensed entities under regulation by the division. From 2004 to 2006, complaints fell by 35%. Complaints rebounded slightly in fiscal 2007, but the level remained far below what was originally estimated. The rebound was likely due to licensure of approximately 10,000 mortgage originators following the enactment of Chapter 590 of 2005. However, the division's sustained enforcement effort is expected to keep complaints well below the recent high in fiscal 2004.

Given the current climate in the housing and mortgage industry, the department should be prepared to discuss the impact of its enforcement efforts on consumer confidence in the State's financial services sector. Additionally, given the large increase in the number of licensed entities, the department should consider a new performance measure. The new measure should report the number of complaints per regulated entity to ensure proper year-to-year comparisons despite growth in licensees.

**Exhibit 1
Financial Regulation
Enforcement of Financial Institutions
Fiscal 2003-2009**



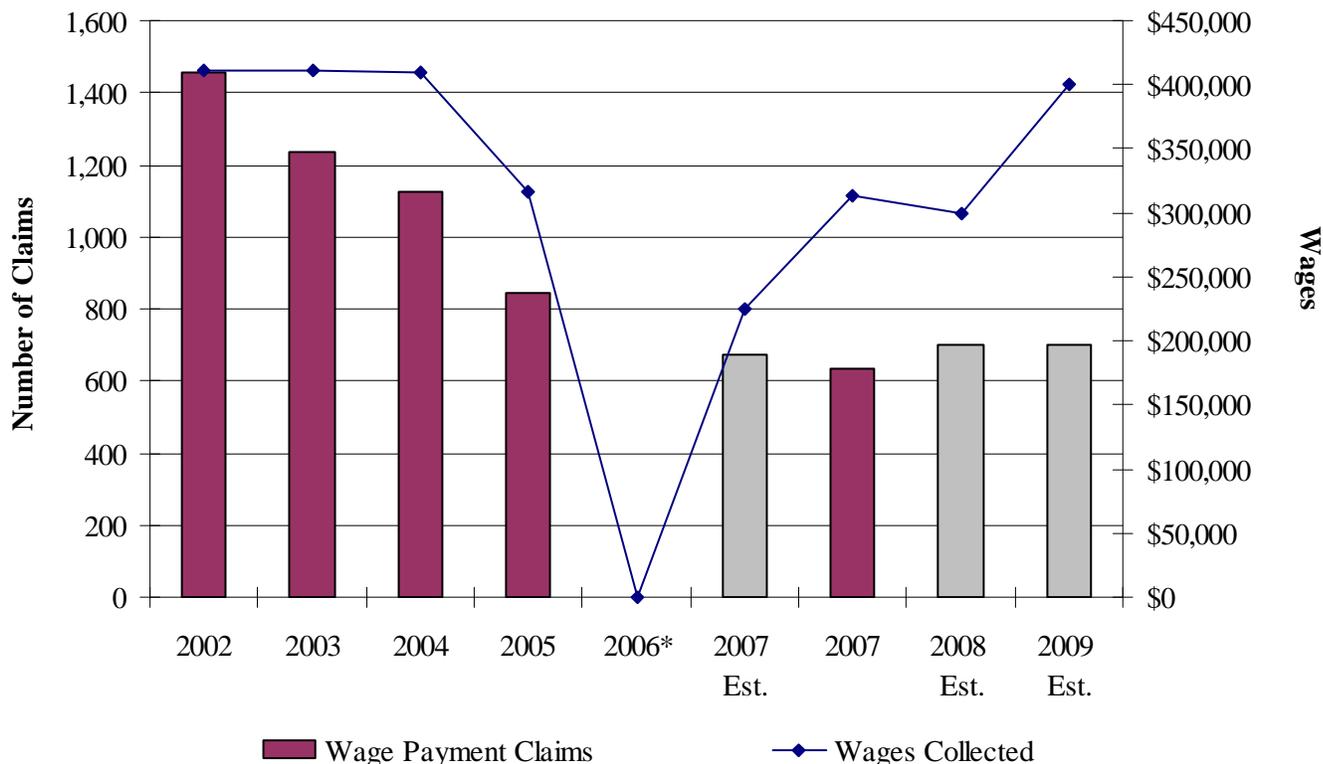
Source: Department of Labor, Licensing, and Regulation

After Loss of Funding, Employment Standards Services Unit Performance Fails to Rebound

The department’s Employment Standards Services Unit is responsible for the enforcement of the State’s Wage Payment and Collection Law. Under the direction of the Commissioner of Labor and Industry, the unit is required to administer and enforce provisions of the law concerning the employment of minors, wages and hours, wage and payment collection, and equal pay for equal work.

The fiscal 2006 budget as proposed did not include funding for this unit; however, legislation passed during the 2005 session mandating an appropriation of at least \$315,000 for the Employment Standards Service Unit beginning in fiscal 2007, and for each subsequent fiscal year. This funding has been in place since fiscal 2007; however, the performance of the unit has not returned to pre-2006 levels as shown in **Exhibit 2**.

**Exhibit 2
Employment Standards
Wage Claim Activity
Fiscal 2002-2009**



*Program not funded.

Source: Department of Labor, Licensing, and Regulation

The unit reached a disposition on 634 wage claims in fiscal 2007, less than half of its work load five years prior. The department has acknowledged that there will be a start-up period that results in lower performance levels. However, the number of wage claims processed was even less than the department expected in fiscal 2007. Additionally, departmental estimates show significantly less activity expected in fiscal 2009 than was experienced prior to fiscal 2006.

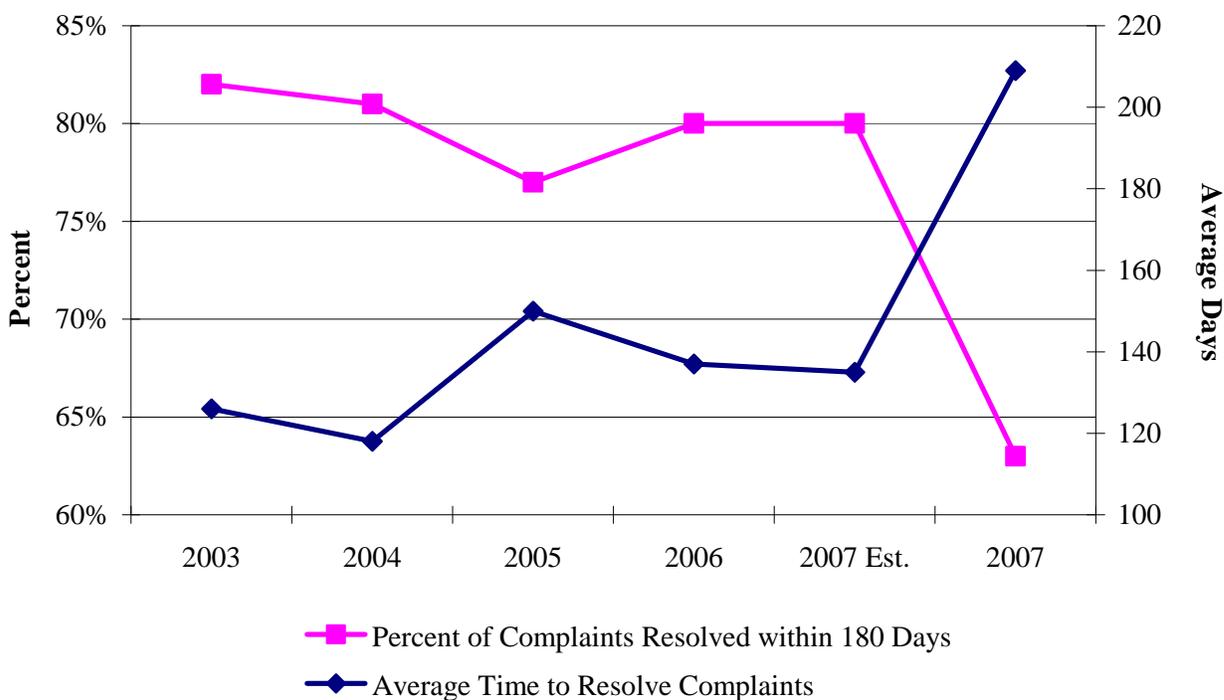
It should be noted that in January 2008, the department provided employment standards data that conflicts with the data presented in this analysis and in the Governor’s budget books. However, the general productivity trends are comparable. Even using the different numbers, productivity has not returned to pre-2006 levels.

The department should discuss the performance of the Employment Standards Services Unit and steps it will take to improve outputs.

Complaint Resolution Standards Fall within Occupational and Professional Licensing

Similar to the Division of Financial Regulation, the Division of Occupational and Professional Licensing handles calls and complaints from consumers against those licensed by the department or against individuals or companies that should be licensed by the department. For the first time this decade, the division failed to meet its goal of closing at least 70.0% of its complaints within 180 days of receipt. As shown in **Exhibit 3**, the division resolved only 63.4% of complaints within its desired time frame. The exhibit also shows how the average number of days to resolve complaints has increased, reaching an average of almost 209 days in fiscal 2007, 52.0% longer than the prior year. This is far below the level of estimated performance for 2007.

Exhibit 3
Occupational and Professional Licensing
Complaint Resolution
Fiscal 2003-2007



Source: Department of Labor, Licensing, and Regulation

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The vast majority of complaints, approximately 75%, are related to activities regulated under the Home Improvement Commission. The number of home improvement complaints has increased by 16% over the last five years. Further, vacancies within the commission have compounded the issue.

The department should discuss how it will reverse the trend of diminished efficiency within the Division of Occupational and Professional Licensing, especially within the Home Improvement Commission.

Fiscal 2008 Actions

Proposed Deficiency

A fiscal 2008 deficiency appropriation of \$173,132 is included in the fiscal 2008 allowance under the Division of Financial Regulation. The general funds will be used to increase salaries of 20 financial examiners within the division. After a salary study, the department determined that previous salary schedules for bank examiners were not comparable to the federal government or the private sector. Furthermore, the department advises that the current crisis in the subprime mortgage market exacerbates the need for experienced State examiners.

An additional fiscal 2008 deficiency of \$5.5 million is included in the allowance to provide federal funds under the Workforce Investment Act and to address workforce development issues associated with the expected influx of jobs related to the Base Realignment and Closure (BRAC) process.

Impact of Cost Containment

The Administration's fiscal 2008 cost containment effort resulted in the reduction of \$1,133,983 in total funds for the department. Reflecting the department's funding sources, over half of this reduction is derived from federal funds. However, an effort was made to reduce general funds in a greater proportion to the general funds in the total appropriation. The department eliminated 6.4 full-time equivalent (FTE) positions, 5.0 of which were in the Division of Administration and 3.0 positions were filled at the time of the reduction. Much of the remaining reductions fell under contractual services and replacement equipment. The cost containment actions do not appear to have adversely impacted the performance of the department.

Governor's Proposed Budget

As shown in **Exhibit 4**, the fiscal 2009 allowance increases by \$830,908, or 0.5% from the fiscal 2008 working appropriation. However, this change is distorted due to the manner in which health insurance is budgeted. Absent health insurance costs, the budget actually declines by approximately \$6.4 million, or 4.0%.

Exhibit 4
Governor’s Proposed Budget
Department of Labor, Licensing, and Regulation
(\$ in Thousands)

How Much It Grows:	<u>General</u> <u>Fund</u>	<u>Special</u> <u>Fund</u>	<u>Federal</u> <u>Fund</u>	<u>Reimb.</u> <u>Fund</u>	<u>Total</u>
2008 Working Appropriation	\$15,737	\$40,656	\$106,748	\$8,051	\$171,192
2009 Governor’s Allowance	<u>16,383</u>	<u>28,583</u>	<u>118,990</u>	<u>8,068</u>	<u>172,023</u>
Amount Change	\$646	-\$12,073	\$12,241	\$16	\$831
Percent Change	4.1%	-29.7%	11.5%	0.2%	0.5%

Where It Goes:

Personnel Expenses

New positions.....	\$189
Abolished/transferred positions	-927
Increments and other compensation.....	1,096
Employee and retiree health insurance	2,437
Health insurance – long-term Other Post Employment Benefits liability.....	4,890
Workers’ compensation premium assessment	-257
Turnover adjustments.....	233
Other fringe benefit adjustments.....	-360

Other Changes

Office of the Secretary and Administration

Reduction of 6 contractual full-time equivalents (FTE)	-61
Decline in communications, travel, and other administrative expenses	-517

Division of Financial Regulation

Increase in out-of-state travel to enhance licensee examinations	46
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Division of Labor and Industry

Decrease in travel.....	-87
Decline in fees for Internet-based inspection data system.....	-106
Decrease in equipment purchases	-62

Division of Racing

Reduction of 1 contractual FTE.....	-42
Decline in impact aid due to decline in expected racing days	-280
Decline in laboratory expenses	-314

Division of Occupational and Professional Licensing

Increase of 3 contractual FTEs.....	234
Initial funding of the Elevator Safety Review Board.....	96

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Where It Goes:

E-licensing enhancement	260
Division of Workforce Development	
Decline of 5.5 contractual FTEs	-121
Increase in federal grants – Base Realignment and Closure and Workforce Investment Act	3,640
Decline in rent paid to the Department of General Services.....	-56
Division of Unemployment Insurance	
Decline in one-time funds for the implementation of the Maryland Imaging Data Access System and an automated voice response system.....	-4,501
Decline in 3.7 contractual FTEs.....	-584
Decline in federal funds for the Information Technology Support Center	-264
Increase in postage based on new federal regulations	735
Decline in travel, telephone, and other administrative expenses	-497
Loss of federal funds for personnel-related expenses	-3,759
Decline in one-time building repairs.....	-256
Other Changes	26
Total	\$831

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

Impact of Cost Containment

Cost containment efforts drive much of the underlying decline the fiscal 2009 allowance. Savings of approximately \$927,000 is realized by the elimination of 15.1 positions which are abolished in January 2008 as part of the statewide abolition of 500 positions. Additionally, the department focused much of the cost containment effort on its contractual staff. Close to 25.0 contractual FTEs were eliminated, mostly in the administrative and workforce development functions. Across the department, contractual staff costs fell by about \$528,000.

Personnel

The allowance includes funds for four new wage and hour investigators across two programs to investigate minimum wage and living wage complaints. The positions are assigned to the Employment Standards Services Unit and the Prevailing Wage Unit. Chapter 2 of 2006 increased the State’s minimum wage, and Chapter 284 of 2007 increased the living wage for employees working under State contracts. The allowance includes \$189,000 in additional general funds for these positions.

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As mentioned above, a number of vacant positions were eliminated due to cost containment and other efficiency efforts: 5.5 administrative positions, 1.0 technical support specialist, 1.0 boiler inspector, 1.0 assistant chemist, 4.0 job service specialists, and 3.6 unemployment insurance specialists. Savings equate to approximately \$927,000 in general, special, and federal funds.

Division of Racing

The division provides impact funds to those jurisdictions that contain or are located near thoroughbred racetracks. The number of estimated racing days in fiscal 2009 has declined from fiscal 2008. Accordingly, the amount of budgeted impact aid for local jurisdictions is lower. Impact aid falls from \$1,485,600 to \$1,205,600 in special funds. The decline will affect the following jurisdictions: Anne Arundel and Howard counties, Baltimore City, and Laurel.

Expenses related to the analytical laboratory fall in the fiscal 2009 allowance by about \$314,000 in special funds due to the fact that the laboratory no longer performs out-of-state testing.

Division of Occupational and Professional Licensing

Chapter 703 of 2001 established the Elevator Safety Review Board and required elevator contractors and mechanics to be licensed by the board before conducting business in Maryland. At the time of enactment, DLLR estimated that there were 1,250 elevator mechanics and 150 elevator contractors in the State. A board was appointed in 2001, and several meetings were held to discuss regulations and to process grandfathered applications. Through fiscal 2008, due to lack of funding, the department had not processed any applications, issued any licenses, or collected any related fees. However, funding is included in the fiscal 2009 allowance to regulate this industry. General funds of \$98,543 are provided for one full-time position and related expenses.

Special funds increase by \$260,000 to enhance the e-licensing program for the special funded boards, including the Board of Public Accountancy, the Real Estate Commission, and the design boards. This will allow new applicants for licenses to apply on-line, freeing staff from many data entry duties.

Division of Workforce Development

The department has been awarded, as a region with Virginia and Washington, DC, \$10 million in National Emergency Grant funds focusing on BRAC-related workforce development needs. Maryland's share is \$4 million. A portion of these funds is included in the 2008 deficiency allowance. The funds will in part be awarded to local jurisdictions in order to fund BRAC project coordinator positions. The department also plans to upgrade one-stop career centers in the areas of the State most directly impacted by BRAC. Additionally, a temporary one-stop center is planned for Fort Monmouth, NJ, the area from which Maryland will receive the most new residents.

Division of Unemployment Insurance

Total funding for the Division of Unemployment Insurance falls by about \$4.2 million in fiscal 2009. The most significant change in the allowance is the reduction of funds associated with the Maryland Imaging Data Access System (MIDAS). When it is fully operational, this system will be the core means of collecting wage data and employer tax data for the administration of the unemployment insurance program. Approximately \$2.3 million was appropriated for the system, which is expected to be operational this year. No further funds are provided.

Federal funds and special funds for this program have fluctuated in recent years. A more thorough discussion of this funding and its implications for the program can be found under the Issues section of this analysis.

Issues

1. Department Responds to the Increase in Foreclosures in Maryland

Due to good real estate market conditions over the last five years, the traditional mortgage market has evolved from mortgages primarily originated and provided by local banks and financial institutions to mortgages originated through mortgage brokers for nonbank lenders. Through nontraditional mortgages, lenders began to ease borrowing restrictions to allow lower credit borrowers to qualify for mortgages, greatly expanding the subprime market. Subprime loans, which are higher-cost loans, provide opportunities for a wide range of higher-risk borrowers. Further, lenders made loans to customers based on less stringent or no income and asset verification requirements.

During calendar 2006, the real estate market changed as sales of housing and home prices declined and interest rates increased. Terms of many of the nontraditional loans included adjustable rates. As the low interest rate period ended, many borrowers found that they were unable to make the payments due during the high interest rate period. Further, borrowers realized that they were unable to refinance due to prepayment penalties or to sell their property due to a decrease in their property's value. Investors of rental property found that they were unable to get the rent needed to pay their mortgages and were unable to sell due to the depressed resale market. Accordingly, many borrowers were subject to foreclosure.

Homeownership Preservation Task Force

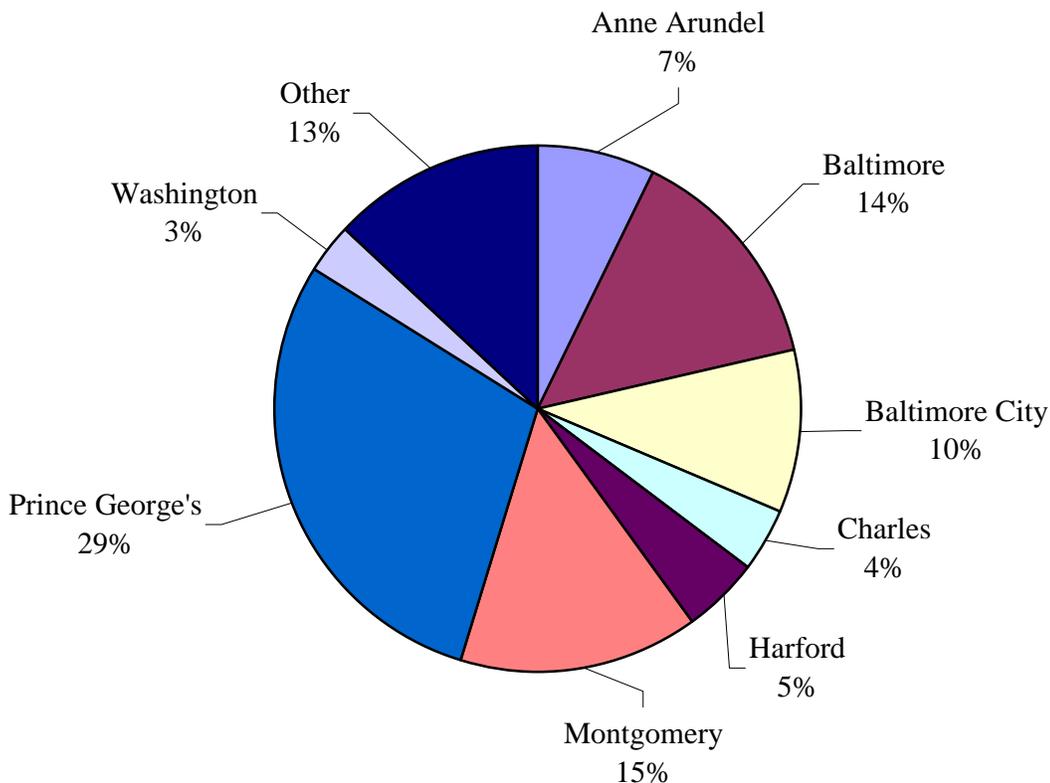
In June 2007, the Governor created the Homeownership Preservation Task Force in response to rising mortgage defaults and foreclosures in the State. The task force is co-chaired by the Secretaries of DLLR and the Department of Housing and Community Development. It is comprised of representatives of nonprofit organizations; foundations; housing advocates and counselors; representatives from the federal, State, and local governments; government sponsored enterprises (Fannie Mae and Freddie Mac); mortgage lenders; mortgage insurance companies; mortgage services companies; and industry associations (Maryland Bankers Association, Maryland Mortgage Bankers Association, and Maryland Association of Realtors). The task force was charged with:

- analyzing data to plan for current and future needs of Maryland families regarding homeownership;
- developing a wide-ranging list of financial resources and programs available to homeowners to minimize the number of foreclosures;
- recommending ongoing outreach, counseling, and educational programs and activities that focus on foreclosure prevention and direct support to homeowners; and

- reviewing the current laws and regulations in Maryland and recommending appropriate foreclosure protocols, including legislative actions.

The task force issued its report in November 2007. According to the task force report, Maryland experienced a 344% increase in foreclosure events from the second quarter of 2006 to the second quarter of 2007. Prince George’s, Montgomery, and Baltimore counties had the highest number of foreclosure events, while Harford and Washington counties had the greatest increase in foreclosure events. **Exhibit 5** shows each jurisdiction’s share of foreclosure events.

Exhibit 5
Foreclosure Events*
By Jurisdiction – Second Quarter 2007



*Includes notices of default, notices of foreclosure sale, or a foreclosure sale.

Source: Homeownership Preservation Task Force Report, November 2007

State Response

The department encourages and preserves homeownership through its role as the regulatory agency of the mortgage industry. It licenses and regulates mortgage brokers, lenders, and most recently, originators, and it investigates and pursues instances of fraud.

In response to the current crisis, the department's Division of Financial Regulation is increasing its efforts in regulating the mortgage industry. As discussed in this analysis, the division reclassified many of its positions, increasing salaries in an effort to compete with the private sector and to retain more qualified examiners. Also, the division began licensing mortgage originators in fiscal 2007. This is meant to regulate the increasing number of employees who work for licensed mortgage lenders and who originate mortgage loans.

Despite these efforts, a recent legislative audit has revealed some shortcomings in the division's regulatory processes. For example, the division is required to perform periodic examinations of mortgage lenders to ensure compliance with licensure regulations. The audit revealed that in 2007, 13 of 20 lenders were overdue for examination. Also, the division did not appear to verify that lenders who did not renew their licenses were no longer conducting business in the State. Complete audit findings may be found in **Appendix 2** of this analysis.

Next Steps

The Homeownership Preservation Task Force issued recommendations that would further strengthen the department's ability to regulate the mortgage industry and ideally would prevent a worsening of the foreclosure crisis. The recommendations that specifically relate to the department and improving regulatory oversight are aimed at providing accountability for all players in the mortgage industry. For example, the task force recommends tracking the transactions of mortgage lenders and originators by requiring them to put their license number on any recorded security instrument they originate. Currently, if a loan is sold after the loan is settled, it is difficult to determine if a specific originator has an inappropriately high number of loans ending in foreclosure. A tracking system would allow the Commissioner of Financial Regulation to target investigations to originators that have a significant number of originated loans that ended in foreclosure or default.

Another recommendation is to establish a bifurcated licensing structure for brokers and lenders which would help to track questionable practices. Currently, a licensed mortgage lender may be a mortgage broker, mortgage lender, or mortgage service, making it impossible to determine with whom a borrower is dealing. With a separate licensing structure, brokers and lenders could be required to include their license number on all loan documents. Mortgage lenders could be required to report the number of foreclosures by broker. The department could use the foreclosures data to audit and investigate the brokers and lenders with the most foreclosures.

The division's regulatory responsibilities serve a unique and crucial role in protecting homeownership in the State. The current state of the housing and mortgage industries will put further pressure on the department to expand its regulatory responsibilities.

The department should brief the budget committees on how it is responding to the mortgage crisis and the extent to which it is implementing the recommendations of the Governor’s Homeownership Preservation Task Force.

2. Funding Imbalance within the Division of Unemployment Insurance

The funding of the administration of the State’s unemployment insurance (UI) program is almost exclusively provided by the federal government through the Federal Unemployment Tax Act (FUTA). A portion of the federal proceeds are returned to the State to administer the UI program. Such funds are based on workload indicators of the UI division such as initial claims filed, appeals, and decisions rendered. Fiscal restraints at the federal level are also a contributing factor. In the past several years, the comparative positive economic condition of Maryland has led to a decline in federal funds for UI administration costs.

In 2002, the federal government passed legislation designed as a stimulus package in the aftermath of increased unemployment after September 11, 2001. The legislation included a distribution of \$8.0 billion known as the Reed Act distribution. Funds were to be used to pay unemployment benefits or to enhance UI benefits. Allowable uses also included administration of UI and employment services programs. Maryland received approximately \$142.9 million of the Reed Act allotment. The allotment was placed in the State’s Unemployment Insurance Trust Fund where it staved off an employer surcharge trigger. It also enabled the department to use other funds to increase unemployment benefits in fiscal 2003.

Included in the fiscal 2008 appropriation as special funds was Reed Act funding to offset losses of federal funding. The \$12.5 million in a 2007 deficiency and the \$11.2 million in 2008 Reed Act funding replaced lost federal funds to fund the cost of administering the UI program and to a lesser extent, some costs associated with employment services. About \$119.3 million of the original Reed Act distribution remained in the trust fund. No further Reed Act funds are included in the fiscal 2009 allowance.

The division reports that in calendar 2007, UI claims increased by 6%. In the last 10 weeks of the year, claims increased by 14% from the same period in 2006. As such, the allowance includes an expected increase in federal funds. However, the increase does not make up for the previous loss of federal funds or the current absence of Reed Act special funds.

Changes to federal regulations lead to further fluctuations in the budget. A new regulation requires postage to be paid by the State with federal funds, where previously, postage was paid directly by the federal government. This appears as an increase in federal funds; however, this cannot be viewed as an enhancement or as a real rebound in federal funding levels.

Performance Standards

The loss of federal funding over the last several years appears to coincide with a slight but persistent decline in the performance standards of the division. The division measures the number of

days it takes to complete initial unemployment insurance tax liability determinations. Since fiscal 2004, performance has declined over 2% annually. Also, the division measures customer satisfaction. This has declined 1% annually since fiscal 2004. The department expects both measures to fall again in fiscal 2008.

Funding Stabilization

The use of Reed Act funds in fiscal 2008 helped to stabilize the division's funding. To the extent necessary, such funds are still available to supplant any federal funding shortfalls. However, this can only be a temporary solution.

A long-term option is for the State to participate in a pilot program allowing it to directly collect the unemployment insurance tax paid by Maryland employers. In calendar 2005, Maryland employers paid \$135 million in taxes, of which, \$68 million was returned to the State for UI and other workforce programs. Departmental estimates show that participating in the pilot program would allow the State to retain an additional \$35 million in taxes paid by Maryland employers. Under the pending pilot program, the State, not the federal government, would administer the tax. This would require both State and federal enabling legislation.

The department should brief the committee on its plans for stabilizing the funding stream for unemployment insurance administration. In the absence of such a plan, the department should discuss how it will handle continued year-to-year fluctuations in its budget.

3. Safety Inspection Vacancies Persist

The Division of Labor and Industry's Boiler and Pressure Vessel Safety Inspection Unit has statutory responsibility for inspecting uninsured boilers and pressure vessels as well as boilers that are overdue for inspection by the insurance industry. The unit also investigates any boiler and pressure vessel accidents. The inspections further the division's goal to limit serious injuries from boiler and pressure vessels to no more than four in any given year. While this goal has consistently been met, the number of annual inspections has fluctuated greatly. In fiscal 2007, inspections fell to a recent low of 6,022, well below the estimate of 10,400.

Historically, there has been a concern about whether the unit has enough staff to complete all scheduled inspections as well as eliminate a past-due backlog. There are an estimated 55,000 boilers and pressure vessels in the State. The unit is responsible for inspecting approximately 20% of the units; about one-third of which are past due for inspection. In fiscal 2008, the unit added 4 new boiler inspector positions in an effort to ameliorate the backlog problem. However, of the 15 total inspector positions, 7 are unfilled. Many have remained unfilled for over a year.

The inspector turnover rate contributes to the backlog problem for the unit. The unit inspectors are regularly recruited by higher paying insurance firms, and consequently, the inspector turnover rate has been high. The State bears the costs of training new inspectors, only to be unable to

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compete with a competitive pay scale. This results in the unit having a relatively inexperienced staff and numerous vacancies.

The Department of Legislative Services recommends the adoption of committee narrative requesting the department to apply to the Department of Budget and Management (DBM) for the upward reclassification of boiler inspector positions with the Division of Labor and Industry. As part of this effort, DBM should include a special focus on boiler inspectors in the next statewide annual salary review to ensure competitiveness with the private sector.

Recommended Actions

	<u>Amount Reduction</u>		<u>Position Reduction</u>
1. Delete a long-term vacant position (031001) within the Office of Budget and Fiscal Services which has been vacant for over 18 months.	\$ 4,407	GF	1.0
	6,610	SF	
	33,049	FF	
2. Delete two new positions within the Employment Standards Services Unit. Any new positions within this unit should be delayed until such time that performance standards return to the level achieved prior to a temporary lapse in funding.	79,776	GF	2.0
3. Reduce the increase in in-state travel and computer equipment associated with new positions under the Employment Standards Services Unit.	10,000	GF	
4. Adopt the following narrative:			

Safety Inspector Salary Reclassification: The persistent vacancies that exist within the Division of Labor and Industry and the backlog of inspections caused by those vacancies compromise the safety of Marylanders. The committees request that the Department of Labor, Licensing, and Regulation review the salary structure of safety inspection positions within the division, specifically boiler inspection positions. The department should appeal to the Department of Budget and Management (DBM) for reclassification of inspection positions to aid in retention. To facilitate the reclassification, the committees further request that DBM place special focus on inspection positions during the next statewide annual salary review.

Total Reductions	\$ 133,842		3.0
Total General Fund Reductions	\$ 94,183		
Total Special Fund Reductions	\$ 6,610		
Total Federal Fund Reductions	\$ 33,049		

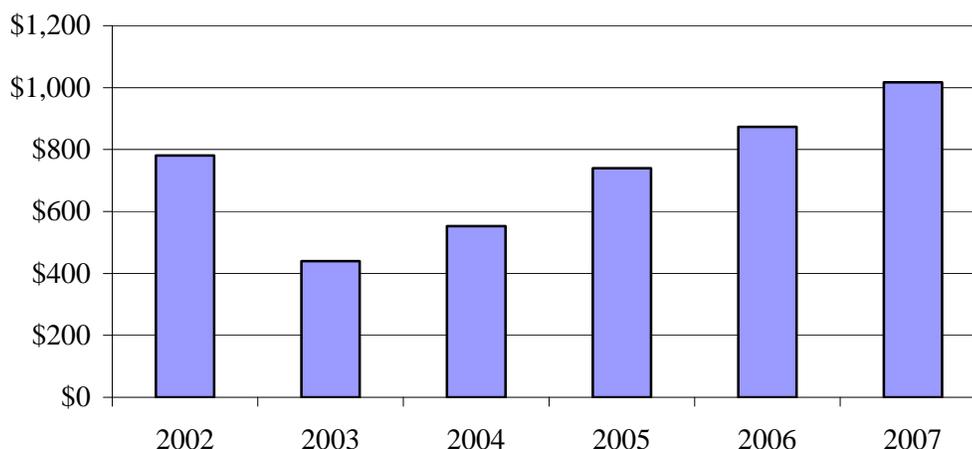
Updates

1. Healthy Balance in the Unemployment Insurance Trust Fund

Committee narrative adopted in the 2007 *Joint Chairmen's Report* expressed the budget committees' request for additional oversight of the Unemployment Insurance Trust Fund. The narrative asked for the department to provide details on the aggregate inflows, outflows, and balances in the Unemployment Insurance Trust Fund on at least a quarterly basis. Recent changes to the UI charging and taxation system and the use of the Reed Act funds for administration prompted the need for additional oversight.

The department has provided the Department of Legislative Services with access to several years' worth of monthly data on the activities in the trust fund. This will allow the General Assembly and its staff to analyze the health of the trust fund. To date, the healthy balance in the trust fund allows the State to remain in the lowest tax rate bracket for employers. **Exhibit 6** shows year-end balance in the trust fund for calendar 2002 through 2007.

Exhibit 6
Unemployment Insurance Trust Fund
Year-end Balance
Calendar 2002-2007
(\$ in Millions)



Source: Department of Labor, Licensing, and Regulation

According to the department, the State will remain in the lowest tax rate bracket in 2009 based on the expectation of a \$70 million cushion in the trust fund.

Current and Prior Year Budgets

Current and Prior Year Budgets Department of Labor, Licensing, and Regulation (\$ in Thousands)

	<u>General Fund</u>	<u>Special Fund</u>	<u>Federal Fund</u>	<u>Reimb. Fund</u>	<u>Total</u>
Fiscal 2007					
Legislative Appropriation	\$16,036	\$25,738	\$136,203	\$6,780	\$184,757
Deficiency Appropriation	0	12,965	0	0	12,965
Budget Amendments	-32	204	0	0	172
Reversions and Cancellations	-277	-3,487	-20,258	-201	-24,223
Actual Expenditures	\$15,727	\$35,420	\$115,945	\$6,579	\$173,671
Fiscal 2008					
Legislative Appropriation	\$15,917	\$37,565	\$107,409	\$6,717	\$167,608
Cost Containment	-378	-96	-661	-251	-1,386
Budget Amendments	198	3,186	0	1,585	4,969
Working Appropriation	\$15,737	\$40,655	\$106,748	\$8,051	\$171,191

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

Fiscal 2007

In total, actual fiscal 2007 expenditures for the department were over \$11 million less than what was originally appropriated. This was due in large part to significant cancellations of special and federal funds.

The original general fund appropriation was reduced by approximately \$32,000. This net reduction resulted from several budget amendments that both increased (salary enhancements and cost-of-living adjustments (COLAs)) and decreased (cost containment) the appropriation.

The decline in the department's expenditures was also mitigated by several deficiency appropriations. A fiscal 2007 deficiency appropriation provided \$495,000 in special funds from license and examination fees to cover the costs of four contractual employees and related equipment required to process mortgage originator applications due to Chapter 590 of 2005.

An additional fiscal 2007 deficiency appropriation of \$12,469,830 was included in the fiscal 2008 allowance under the Office of the Secretary. The special funds were taken from the 2002 Reed Act Distribution to the State's Unemployment Insurance Trust Fund. The funds were used to offset losses due to a significant reduction in federal UI income. Budget amendments further increased special funds by about \$204,000 due to salary enhancements and COLAs.

Conversely, approximately \$2.3 million in special funds was cancelled due to a delay in the implementation of a new MIDAS. Also, the department overestimated federal funds for workforce development and unemployment insurance programs in fiscal 2007. As it became clear that federal funds were not available, the department replaced the funds with special Reed Act funds through the deficiency appropriation and subsequently cancelled over \$20.0 million in budgeted federal funds.

The fiscal 2007 budget included \$2,478,200 in mandated funds for various grants paid from the horse racing special fund. All these funds were expended in fiscal 2007. Also, the fiscal 2007 allowance included \$700,000 in mandated general funds for the Employment Standards Services Unit and the Prevailing Wage Unit. However, the General Assembly cut funds by \$156,869 and requested the department to staff these units with existing vacant positions. By the end of the year, the department expended \$656,441 to staff the two units. Approximately \$15,000 was reverted to the general fund.

Fiscal 2008

Cost containment efforts in fiscal 2008 reduced the original appropriation by about \$1.4 million in total funds, largely in federal funds.

To date, budget amendments have increased general funds in fiscal 2008 by \$198,037 due to the COLA.

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Special funds also increased by \$468,421 due to the COLA. Special funds cancelled in fiscal 2007 were re-appropriated by budget amendment in fiscal 2008. These funds are for the implementation of the new MIDAS. A final special fund amendment increased the original appropriation by \$426,373. Funds are to increase staff within the enforcement unit of the Mortgage Originator program. The unit investigates cases as part of the department's initiative against mortgage fraud. The positions were transferred from other programs in the department, and the general funds associated with these positions were relinquished for the fiscal 2009 cost containment effort.

Reimbursable funds increased by \$1,584,611 from the original appropriation. In an effort to identify the real costs associated with the administrative support of the professional boards, the department reallocated certain expenses across the boards, which will in turn, reimburse the general administration office.

Audit Findings

Audit Period for Last Audit:	April 20, 2004 – May 6, 2007
Issue Date:	December 2007
Number of Findings:	5
Number of Repeat Findings:	2
% of Repeat Findings:	40%
Rating: (if applicable)	n/a

These findings pertain to the Division of Financial Regulation only.

Finding 1: Controls over cash receipts were not adequate.

Finding 2: Examinations of mortgage lenders were not being performed within the time frame required by State law.

Finding 3: License issuances were not reviewed and approved by supervisory personnel to ensure they were issued only to qualified applicants.

Finding 4: The office had not established adequate procedures to ensure that businesses that did not renew their licenses had discontinued conducting business in Maryland.

Finding 5: Documentation supporting payroll expenditures charged to the Mortgage Lender-Origination Fund was not maintained.

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

**Object/Fund Difference Report
Department of Labor, Licensing, and Regulation**

<u>Object/Fund</u>	<u>FY07 Actual</u>	<u>FY08 Working Appropriation</u>	<u>FY09 Allowance</u>	<u>FY08-FY09 Amount Change</u>	<u>Percent Change</u>
Positions					
01 Regular	1,474.55	1,472.75	1,460.65	-12.10	-0.8%
02 Contractual	177.22	187.02	162.35	-24.67	-13.2%
Total Positions	1651.77	1659.77	1623.00	-36.77	-2.2%
Objects					
01 Salaries and Wages	\$ 91,584,957	\$ 96,836,607	\$ 100,378,916	\$ 3,542,309	3.7%
02 Technical and Spec. Fees	6,313,774	5,634,276	5,105,591	-528,685	-9.4%
03 Communication	4,451,941	3,353,663	3,846,443	492,780	14.7%
04 Travel	1,294,560	1,472,750	1,211,439	-261,311	-17.7%
06 Fuel and Utilities	898,732	966,213	1,001,636	35,423	3.7%
07 Motor Vehicles	488,674	450,626	436,741	-13,885	-3.1%
08 Contractual Services	14,516,315	19,985,459	15,355,784	-4,629,675	-23.2%
09 Supplies and Materials	1,737,306	1,768,085	1,343,896	-424,189	-24.0%
10 Equipment – Replacement	484,641	659,303	432,049	-227,254	-34.5%
11 Equipment – Additional	282,163	249,782	395,966	146,184	58.5%
12 Grants, Subsidies, and Contributions	48,778,763	36,389,747	39,485,836	3,096,089	8.5%
13 Fixed Charges	2,839,994	3,168,884	3,028,212	-140,672	-4.4%
14 Land and Structures	0	256,206	0	-256,206	-100.0%
Total Objects	\$ 173,671,820	\$ 171,191,601	\$ 172,022,509	\$ 830,908	0.5%
Funds					
01 General Fund	\$ 15,727,075	\$ 15,736,929	\$ 16,382,837	\$ 645,908	4.1%
03 Special Fund	35,420,050	40,655,513	28,582,611	-12,072,902	-29.7%
05 Federal Fund	115,945,234	106,748,068	118,989,548	12,241,480	11.5%
09 Reimbursable Fund	6,579,461	8,051,091	8,067,513	16,422	0.2%
Total Funds	\$ 173,671,820	\$ 171,191,601	\$ 172,022,509	\$ 830,908	0.5%

Note: The fiscal 2008 appropriation does not include deficiencies.

**Fiscal Summary
Department of Labor, Licensing, and Regulation**

<u>Program/Unit</u>	<u>FY07 Actual</u>	<u>FY08 Wrk Approp</u>	<u>FY09 Allowance</u>	<u>Change</u>	<u>FY08-FY09 % Change</u>
0A Department of Labor, Licensing, and Regulation	\$ 10,810,946	\$ 10,364,837	\$ 10,502,502	\$ 137,665	1.3%
0B Division of Administration	17,456,900	17,471,598	17,900,364	428,766	2.5%
0C Division of Financial Regulation	7,481,114	7,536,272	8,431,116	894,844	11.9%
0D Division of Labor And Industry	13,273,296	14,585,661	15,342,156	756,495	5.2%
0E Division of Racing	6,558,973	6,807,255	5,834,638	-972,617	-14.3%
0F Division of Occupational and Professional Licensing	8,301,976	9,789,226	10,411,533	622,307	6.4%
0G Division of Employment and Training	49,954,780	46,551,690	49,687,395	3,135,705	6.7%
0H Division of Unemployment Insurance	59,833,835	58,085,062	53,912,805	-4,172,257	-7.2%
Total Expenditures	\$ 173,671,820	\$ 171,191,601	\$ 172,022,509	\$ 830,908	0.5%
General Fund	\$ 15,727,075	\$ 15,736,929	\$ 16,382,837	\$ 645,908	4.1%
Special Fund	35,420,050	40,655,513	28,582,611	-12,072,902	-29.7%
Federal Fund	115,945,234	106,748,068	118,989,548	12,241,480	11.5%
Total Appropriations	\$ 167,092,359	\$ 163,140,510	\$ 163,954,996	\$ 814,486	0.5%
Reimbursable Fund	\$ 6,579,461	\$ 8,051,091	\$ 8,067,513	\$ 16,422	0.2%
Total Funds	\$ 173,671,820	\$ 171,191,601	\$ 172,022,509	\$ 830,908	0.5%

Note: The fiscal 2008 appropriation does not include deficiencies.