Financial Statement Data

Maryland Economic Development Corporation Financial Statement
Fiscal 2006-2008
($ in Thousands)

	Fiscal 2006	Fiscal 2007	Fiscal 2008	Change FY 07-08
Total Assets	$1,893,537	$1,904,661	$2,100,757	$196,096
Total Liabilities	1,967,245	1,999,324	2,211,460	212,136
Net Assets (Deficit)	**-$73,709**	**-$94,663**	**-$110,703**	**-$16,040**
Total Operating Revenue	$112,273	$129,270	$133,898	$4,628
Total Operating Expenses	97,931	111,960	114,696	2,736
Operating Income Subtotal	**$14,342**	**$17,310**	**$19,202**	**$1,892**
Nonoperating Revenues and Expenses	-$35,758	-$38,264	-$35,243	$3,021
Net Income (Deficit)	**-$21,416**	**-$20,954**	**-$16,041**	**$4,913**
Depreciation and Amortization	$25,887	$28,354	$26,555	-$1,799

Change in Net Assets (Deficit) and Income (Deficit) by Source
Fiscal 2006-2008
($ in Thousands)

	Fiscal 2006	Fiscal 2007	Fiscal 2008	Change FY 06-07
Operating Facilities Net Assets	-$88,106	-$108,939	-$127,260	-$18,321
Other Operations Net Assets	14,397	14,277	16,556	2,279
Net Assets (Deficit)	**-$73,709**	**-$94,663**	**-$110,704**	**-$20,954**
Operating Facilities Net Income	-$20,190	-$20,833	-$18,321	-$643
Other Operations Net Income	1,227	-121	2,280	-1,348
Net Income (Deficit)	**-$21,416**	**-$20,954**	**-$16,041**	**-$1,991**

Note: Other operations are comprised of property and equipment rental and consultant and management fees. Certain figures from fiscal 2005 and 2006 are reclassified from those reported in the fiscal 2005 and 2006 financial statements.

Source: Maryland Economic Development Corporation financial statements

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

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- The Maryland Economic Development Corporation's (MEDCO) net income deficit totaled -$16.0 million for fiscal 2008, an increase of about $4.9 million. Operating income for fiscal 2008 was positive at $19.2 million, which is a key indicator of economic health. Noncash expenses such as depreciation and nonoperating items such as interest expense cause the income and assets deficits, and these deficits are not uncommon for real estate projects.

- Each year that the net income deficit persists, the corporation's equity position declines. The net assets deficit grew to -$110.7 million in fiscal 2008. The corporation reports that the growing net assets deficit is not a significant concern as long as operating revenues ($133.9 million) exceed cash operating expenses ($114.7 million).

- The corporation's net asset deficit is attributable to the accumulated losses of its operating facilities. In fact, the corporation's other operations showed positive income of $2.3 million. In fiscal 2008, operating facilities showed a net deficit of -$18.3 million.

Analysis in Brief

Overall Financial Position

Operating Revenues Exceed Operating Expenses: The corporation's net asset deficit has grown to -$110.7 million. However, in a key indicator of financial health, operating income was positive at $19.2 million in fiscal 2008.

MEDCO's Assets Exclusive of Operating Facilities Are Relatively Stable: Exclusive of operating facilities, MEDCO had $16.6 million in net assets in fiscal 2008, close to the 10-year average of $17.4 million. In fiscal 2008, MEDCO provided funding for 11 new projects.

Growth in Number of Operating Projects Has Increased Debt and Assets; Growth Rate Lower Since 2004: Debt and assets more than doubled in fiscal 2000 and averaged 30% growth each year from 2001 to 2003. However, growth rates have been lower since fiscal 2004. Average growth rates for the fiscal 2000-2008 time frame are about 16%.

Operating Facilities Financial Position

Net Assets Continue to Decrease: Operating facilities' net assets decreased by $18.3 million in fiscal 2008. However, this decrease is slightly less than the decreases experienced in fiscal 2007 and 2006.

Operating Income Improved in 2008; Four Projects Posted a Loss: Operating facilities' income increased to $12.8 million in fiscal 2008. However, four projects showed a loss, and two non-university projects were defined as problem projects in the corporation's financial statement. **The Department of Legislative Services (DLS) recommends that MEDCO comment on the**

outlook for Rocky Gap, especially in light of the current economic crisis and the rejection of the proposal for video lottery terminals by the State Lottery Commission.

Operating Income Grew to $7.2 Million Among University Housing Projects in Fiscal 2008: Operating income for university housing projects grew by $0.7 million in fiscal 2008. However, three projects are considered problem projects within the corporation's financial statements. **DLS recommends that MEDCO comment on the university projects, especially those identified as problem projects. Further, MEDCO should comment on what, if any, impact the current economic climate has on university projects.**

Recommended Actions

1. Nonbudgeted.

Operating Budget Analysis

Program Description

The Maryland Economic Development Corporation (MEDCO) is a nonbudgeted entity that allows the State to own or develop property for economic development purposes. MEDCO was created in 1984 with the mission to help expand, modernize, and retain existing Maryland business and to attract new business to the State.

MEDCO purchases or develops property that is leased to others under favorable terms. MEDCO also makes direct loans to companies throughout the State to maintain or develop facilities, and it often serves as the conduit for loans administered by the Department of Business and Economic Development (DBED). MEDCO issues bonds to raise funds for its loans. The bond debt consists primarily of revenue bonds and notes payable to government agencies such as DBED. The debt represents non-recourse obligations because MEDCO is not liable to bondholders and lenders in the event of a project or borrower default. Each project must have self-supporting revenues, and no projects are cross-collateralized. As a result, MEDCO debt is not debt of the State, and there is no implied State guaranty or State obligation to protect bondholders from losses.

MEDCO has been involved in 213 projects through fiscal 2008. Of these, MEDCO currently owns and operates 13 as operating facilities, meaning the agency is involved in management decisions and has a hand in ensuring successful daily operations. For all other projects, MEDCO serves as an arms-length financing entity.

The corporation is governed by statute under the Economic Development Article, Sections 10-101 though 10-132. A 12-member board of directors manages the corporation’s affairs and appoints the executive director. The Secretaries of DBED and the Maryland Department of Transportation serve as ex-officio voting members. MEDCO’s activities complement the marketing and financing programs of DBED. There are currently 9 full-time and 2 part-time professional staff members.

Chapter 338 of 2001 was enacted as emergency legislation to amend MEDCO’s corporate powers to conform to current practices. In addition, MEDCO’s statutory authority was amended to be more consistent with the Maryland Economic Development Revenue Bond Act and economic development revenue bond enabling legislation that is in effect in other states competing for opportunities. MEDCO’s legislative purpose now is to (1) relieve the conditions of unemployment; (2) encourage increased business activity and commerce and a balanced economy; (3) assist in the retention and attraction of new business activity; (4) promote economic development; and (5) generally promote the present and prospective health, happiness, safety, right of employment, and general welfare of State residents.

MEDCO's Overall Financial Position

Operating Revenues Exceed Operating Expenses

MEDCO reports that a primary indicator of financial health is operating income, which was positive at $19.2 million in fiscal 2008, as shown on page 1 of this analysis. Operating revenues did not cover all non-operating expenses; therefore, the agency had a net income deficit of -$16.0 million in fiscal 2008. This was less of an income deficit when compared to the losses experienced in fiscal 2006 and 2007. Operating revenues ($133.9 million) exceeded cash operating expenses ($114.7 million).

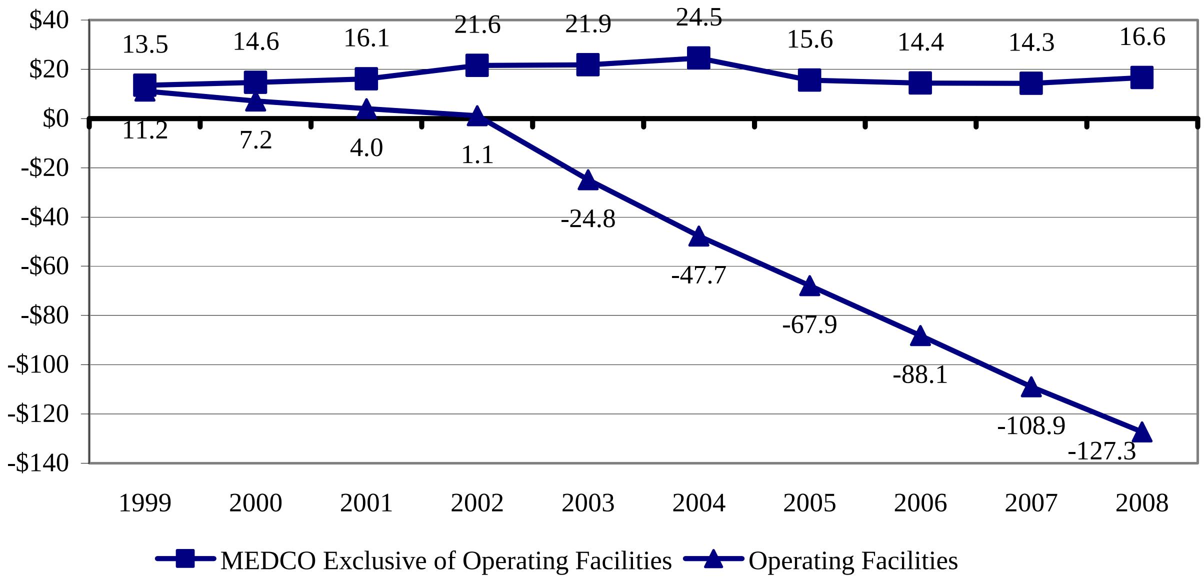
Each year that the net income deficit persists, the corporation's equity position declines. The net assets deficit grew to -$110.7 million in fiscal 2008, as shown on page 1. The corporation reports that the growing net assets deficit is not a significant concern as long as operating revenues exceed cash operating expenses. MEDCO reports that net losses and assets deficits are not uncommon for real estate companies. With these companies, the market value of the assets generally exceeds the book value, and MEDCO says that real estate investors look at market value or, more specifically, cash flow coverage rather than book value.

MEDCO's Assets Exclusive of Operating Facilities Are Relatively Stable

Exhibit 1 shows the value of MEDCO's net assets with operating facilities extracted. MEDCO, exclusive of operating facilities, had $16.6 million in net assets in fiscal 2008. The balance has averaged $17.4 million for the last 10 years. These funds represent the accumulation of excess fees over operating expenses that MEDCO attains as it conducts financing transactions each year. In fiscal 2008, MEDCO provided financing for 11 new projects: 5 nonprofit entities, 3 manufacturers, 1 nursing home, 1 solid waste disposal project, and 1 energy generation/pollution control project.

MEDCO has 13 operating facilities in its portfolio. The net assets deficit for these facilities grew to -$127.3 million in fiscal 2008, as shown in Exhibit 1. The operating net assets deficit began to grow dramatically in fiscal 2003. It was at this time that MEDCO greatly expanded its operating facility portfolio, including the Chesapeake Bay Conference Center and several university housing projects. The net assets deficit is a direct result of adding new operating real estate facilities. MEDCO's operating projects often have net income deficits (as explained above), and with the addition of each operating project, a net income deficit is added to the accounts, which in turn adds to the overall net assets deficit.

Exhibit 1
MEDCO Net Assets
Fiscal 1999-2008
($ in Millions)



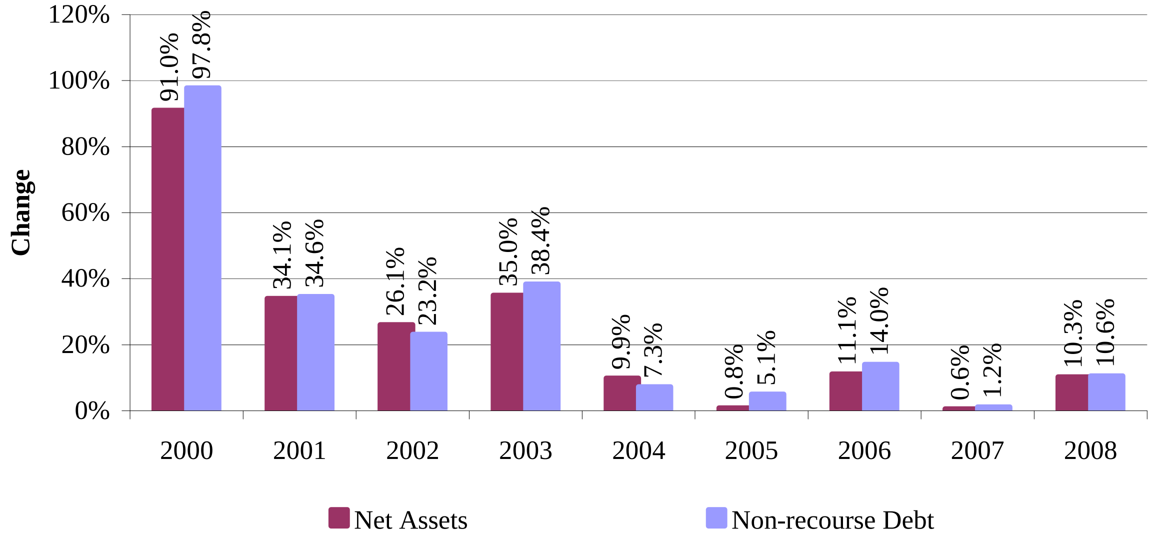
MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Growth in Number of Operating Projects Has Increased Debt and Assets; Growth Rate Lower Since 2004

As a result of the growth in operating projects, MEDCO's debt and assets have increased significantly. **Exhibit 2** shows that debt and assets nearly doubled in fiscal 2000, and averaged 30% growth each year from 2001 to 2003. Growth rates have been lower since fiscal 2004, and average growth rates for the fiscal 2000 to 2008 time frame are about 16%. MEDCO reports that management decided to moderate the growth in operating projects in order to allow more time to advise on facilities that the agency operates and to improve internal controls.

Exhibit 2
Changes in MEDCO Assets and Debt
Fiscal 2000-2008



	2000	2001	2002	2003	2004	2005	2006	2007	2008
Total Assets ($ in Millions)	$674	$904	$1,139	$1,538	$1,690	$1,704	$1,893	$1,905	$2,101
Non-recourse Debt ($ in Millions)	$635	$855	$1,053	$1,457	$1,563	$1,642	$1,872	$1,894	$2,095
Projects (Cumulative)	108	124	143	160	172	182	191	202	213

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Considering all projects, including operating and nonoperating, the agency has financed about 10 to 20 new projects each year since fiscal 2000. Cumulative projects totaled 108 in fiscal 2000 and totaled 213 in 2008.

Operating Facilities Financial Position

Net Assets Continue to Decrease

Exhibit 3 shows the increases and decreases in MEDCO's net assets by project. Operating facilities' net assets decreased by $18.3 million in fiscal 2008. This decrease is slightly less than the decreases experienced in fiscal 2006 and 2007.

Exhibit 3
MEDCO Increase (Decrease) in Net Assets by Project
Fiscal 2006-2008

	2006	2007	2008	Total Net Assets (Deficit) at End of 2008
University Student Housing				
Morgan State University	-$1,700,979	-$1,351,195	-$921,987	-$6,349,796
Bowie State University	-1,515,874	-1,196,674	-936,236	-3,718,376
Frostburg State University	-278,592	-768,382	-228,772	-2,577,447
Salisbury University	-512,855	-354,820	-883,443	-1,836,110
University of Maryland, Baltimore	-2,061,997	-1,509,667	-1,389,348	-6,443,207
University of Maryland Baltimore County	-1,375,103	-509,418	-414,219	-3,057,420
University of Maryland, College Park Housing	-1,864,020	-2,107,921	-2,480,171	-7,187,638
University Village at Sheppard Pratt	-992,184	-873,596	-855,062	-6,827,554
Subtotal	**-$10,301,604**	**-$8,671,673**	**-$8,109,238**	**-$37,997,548**
Other Facilities				
Chesapeake Bay Conference Center (Hyatt Cambridge)	-$10,060,537	-$7,676,832	-$6,316,113	-$62,795,412
Chesapeake Hills Golf Course	-632,314	-723,647	-499,501	-2,487,128
Compass Pointe Golf Course	3,422,385	0	0	0
Maryland Technology Development Center	173,544	-222,990	32,007	5,662,992
Rockville Innovation Center	0	-185,430	1,296,306	1,110,876
Rocky Gap Golf Resort	-3,973,208	-4,569,074	-5,751,843	-37,189,540
University of Maryland, College Park Energy	1,182,138	1,216,166	1,027,558	6,435,467
Subtotal	**-$9,887,992**	**-$12,161,807**	**-$10,211,586**	**-$90,559,051**
Subtotal Operating Facilities	**-$20,189,596**	**-$20,833,480**	**-$18,320,824**	**-$127,260,293**
MEDCO Exclusive of Operating Facilities	**-$1,250,917**	**-$110,442**	**$2,290,302**	**$15,046,997**
Elimination (Accounting Adjustment)	**$24,020**	**-$10,405**	**-$10,405**	**-$770,464**
Grand Total	**-$21,416,493**	**-$20,954,327**	**-$16,040,927**	**-$114,280,066**

MEDCO: Maryland Economic Development Corporation

Note: MEDCO sold Compass Pointe Golf Course to Anne Arundel County in fiscal 2006. Certain figures from fiscal 2006 are reclassified from those reported in the fiscal 2006 financial statements.

Source: Maryland Economic Development Corporation

Operating Income Improved in 2008; Four Projects Posted a Loss

Exhibit 4 shows MEDCO operating income and loss by project. The data indicates whether projects are bringing in enough revenues to cover annual operating expenses. Operating facilities' income increased to $12.8 million in fiscal 2008, as compared to $11.6 million in 2007.

Exhibit 4
MEDCO Operating Income (Loss) by Project
Fiscal 2006-2008

	2006	2007	2008	Total 2006-2008
University Student Housing				
Morgan State University	$389,817	$840,102	$1,198,783	$2,428,702
Bowie State University	-483,659	-111,979	119,757	-475,881
Frostburg State University	712,325	201,269	737,291	1,650,885
Salisbury University	171,174	284,829	-204,727	251,276
University of Maryland, Baltimore	-290,092	274,320	400,715	384,943
University of Maryland Baltimore County	975,747	748,156	940,530	2,664,433
University of Maryland, College Park Housing	1,372,386	3,355,477	2,973,627	7,701,490
University Village at Sheppard Pratt	895,595	941,441	1,050,366	2,887,402
Subtotal	**$3,743,293**	**$6,533,615**	**$7,216,342**	**$10,276,908**
Other Facilities				
Chesapeake Bay Conference Center (Hyatt Cambridge)	$2,487,784	$4,377,308	$6,115,887	$12,980,979
Chesapeake Hills Golf Course	-201,888	-350,845	-220,552	-773,285
Compass Pointe Golf Course	0	0	0	0
Maryland Technology Development Center	151,268	-263,091	-14,411	-126,234
Rockville Innovation Center	0	-168,862	-623,682	-792,544
Rocky Gap Golf Resort	-1,157,775	-1,788,826	-2,925,098	-5,871,699
University of Maryland, College Park Energy	3,531,249	3,308,890	3,283,532	10,123,671
Subtotal	**$4,810,638**	**$5,114,574**	**$5,615,676**	**$9,925,212**
Subtotal Operating Facilities	**$8,553,931**	**$11,648,189**	**$12,832,018**	**$20,202,120**
MEDCO Exclusive of Operating Facilities	**$5,764,017**	**$5,671,849**	**$6,380,905**	**$17,816,771**
Elimination (Accounting Adjustment)	**$24,020**	**-$10,405**	**-$10,405**	**$3,210**
Grand Total	**$14,341,968**	**$17,309,633**	**$19,202,518**	**$38,022,101**

MEDCO: Maryland Economic Development Corporation

Note: MEDCO sold Compass Pointe Golf Course to Anne Arundel County in fiscal 2006. Certain figures from fiscal 2006 are reclassified from those reported in the fiscal 2006 financial statements.

Source: Maryland Economic Development Corporation

According to the corporation's financial statement, there are five operating projects identified in fiscal 2008 as problem projects for failure to meet debt coverage ratios. Two of these projects are non-university projects. It should be restated that each of these and all other MEDCO projects needs to be considered on its own merits because no MEDCO projects are cross-collateralized and each project must support itself with its own revenues.

- **Rocky Gap Lodge and Golf Resort:** Rocky Gap consists of a 215-room hotel and conference center and an 18-hole Jack Nicklaus Signature golf course situated on about 260 acres within Rocky Gap State Park. The facility has incurred significant net operating losses, totaling $2.9 million in fiscal 2008 alone, as shown in Exhibit 4. In fact, the fiscal 2008 losses were 64% higher than in fiscal 2007. Occupancy at the hotel declined in 2008, causing a $417,000 decline in revenues.

  Rocky Gap had been generating enough cash to cover its operating expenses, but not enough to cover its debt payments to investors, much less noncash expenses such as depreciation. The investors had, for a time, agreed to forego the amounts owed to them in hopes that cash flow would improve. In an effort to improve the cash flow, MEDCO restructured the debt to get a lower interest rate and to allow operating costs to be paid before debt. In November 2008, an item came before, and was approved by the Board of Public Works (BPW) to extend the ground lease between the Department of Natural Resources (DNR) and MEDCO to 2065. This is the lease under which DNR leases to MEDCO 260 acres in Rocky Gap State Park. The original lease expired in 2031. The BPW item also would permit DNR to subordinate to senior debt any past due charges owed to DNR. Finally, the item designated an 18-acre parcel as the location for a facility to house video lottery terminals.

  The approval of this item set the stage to allow MEDCO to restructure the original debt issued for the facility, which it did on December 1, 2008. MEDCO retired the previously issued bonds and replace them with new debt bearing a lower interest rate.

  The corporation is taking other steps to increase efficiency at Rocky Gap. For example, to save operating expenses, the corporation closed the golf course at the facility for the current winter season.

- **Chesapeake Hills Golf Course:** The Chesapeake Hills Golf Course is in Calvert County just five miles north of Solomons Island. The project is experiencing continued losses, totaling -$220,552 in fiscal 2008 alone, as shown in Exhibit 4. However, this is a smaller loss than what was experienced in fiscal 2007. In fiscal 2009, the county has relieved MEDCO of the notes payable associated with the golf course and is taking over the operation of the facility.

The Department of Legislative Services (DLS) recommends that MEDCO comment on the outlook for Rocky Gap especially in light of the current economic crisis and the rejection of the proposal for video lottery terminals by the State Lottery Commission.

Operating Income Grew to $7.2 Million Among University Housing Projects in Fiscal 2008

Operating income for the university housing projects increased to $7.2 million in fiscal 2008, as compared to $6.5 million in 2007. These projects accounted for more than half of operating facility income in fiscal 2008. However, all the housing projects incurred decreases in net assets when nonoperating revenues and expenses were considered.

- **Bowie State University:** The Bowie State University (BSU) housing project had a $111,979 operating loss in fiscal 2007 and is considered a problem project within the corporation's financial statement. This was the only university housing project to experience an operating loss in fiscal 2007. It has since rebounded a bit in fiscal 2008, posting operating revenue of $119,757. MEDCO reports that BSU has had difficulty in collecting rent payments from students. The collection rate has improved but is still problematic. The corporation expects that the collection rate will continue to improve with establishment of a new process in the university's finance office. Currently, students who are residents in the housing facility and receive financial aid are asked to voluntarily sign a form that authorizes housing payments to be withdrawn directly from financial aid funds and then the student receives the remaining funds.

- **Morgan State University:** The Morgan State University housing project is also listed as a problem project under the financial statement standards. MEDCO reports similar problems in collecting rent payments from students. However, it shows positive signs in operating income for fiscal 2008. Operating income grew by 42.7% in fiscal 2008 over fiscal 2007.

- **University of Maryland, Baltimore:** The housing project at University of Maryland, Baltimore is the final project that is considered problematic in the financial statements. MEDCO reports that the project did not anticipate the differing needs of graduate level students in the housing design; therefore, demand is not as was expected. However, the operating income did improve in fiscal 2008.

MEDCO became involved in university housing projects in 1999 when the University System of Maryland approached the agency because the customary owner – the Collegiate Housing Foundation – came under investigation by the Internal Revenue Service. MEDCO studied the cash flow potential of the projects and found it to be solid.

MEDCO believes that university housing is a good fit for its financing, and it plans to continue to become involved in such projects. The corporation reports that the universities do not want to own and operate the facilities themselves, and yet, a university campus is not necessarily an ideal environment for a traditional private real estate entity.

MEDCO has explained that it is not unusual for its real estate projects to show deficits, and it cautions that in the case of university housing, deficits are essentially guaranteed. There is a provision in the bond issuances that specifies that excess cash goes back to the university as additional rent or a ground lease rather than into the projects' equity. MEDCO reports that university housing bond issuances usually are structured this way, and it is for this reason that housing bonds are at the low end of investment grade ratings.

DLS recommends that MEDCO comment on the university projects, especially those identified as problem projects. Further, MEDCO should comment on what, if any, impact the current economic climate has on university projects.

Other Operating Projects

- **Chesapeake Bay Conference Center (CBCC):** CBCC is a 400-room hotel and golf resort in Cambridge. The project experienced $6.1 million in operating income during fiscal 2008. This represents a 40% increase in income over fiscal 2007. Higher occupancy and a higher average room rate contributed to this increase.

- **Maryland Technology Development Center:** The Maryland Technology Development Center (MTDC) is a business incubator in Montgomery County. The facility experienced a $14,411 operating loss in fiscal 2008. This is in contrast to a much larger loss in fiscal 2007 of $263,091. MEDCO reports that fiscal 2007 was an aberration that occurred because the county did not provide an annual subsidy as it usually does and also charged the incubator for certain services. The county agreed to change the way it handled financing beginning in fiscal 2008 so that the incubator is not negatively affected.

- **Rockville Innovation Center:** The Rockville Innovation Center (RIC) is a new business incubator in Montgomery County that opened in June 2007. The facility is in the Rockville redevelopment area next to the library. MEDCO reports that the project had more private sector financing than MTDC, but it still receives an operating subsidy from the county, and MEDCO obtained a loan of $4.7 million to help construct the facility. In fiscal 2008, the project had an operating loss of $623,682 due to greater than expected unleased space.

Other Factors Affect 2008 Results

Several other factors influenced MEDCO's financial position for fiscal 2008. Capital assets increased due to the construction of a new student housing project, Towson West, and the final disbursements for completion of RIC. Other assets increased because of the issuance of two large conduit debt issuances for the Howard Hughes Medical Center and Constellation Energy.

Recommended Actions

1. Nonbudgeted.