Maryland Economic Development Corporation

Financial Statement Data

Maryland Economic Development Corporation Financial Statement
Fiscal 2009-2011
($ in Thousands)

	2009	2010	2011	Change 2010-2011
Total Assets	$763,762	$724,063	$679,110	-$44,953
Total Liabilities	894,834	887,572	872,539	-15,033
Net Assets (Deficit)	**-$131,072**	**-$163,509**	**-193,429**	**-$29,920**
Total Operating Revenue	$129,171	$125,461	$129,982	$4,521
Total Operating Expenses	112,101	113,320	118,457	5,137
Operating Income Subtotal	**$17,070**	**$12,141**	**$11,525**	**-$616**
Non-operating Revenues and Expenses	-37,439	-44,578	-41,444	3,134
Net Income (Deficit)	**-$20,369**	**-$32,437**	**-$29,920**	**$2,517**

Change in Net Assets (Deficit) and Income by Source
Fiscal 2009-2011
($ in Thousands)

	2009	2010	2011	Change 2010-2011
Operating Facilities Net Assets	-$148,774	-$176,378	-$206,274	-$29,896
Other Operations Net Assets	17,701	12,868	12,845	-23
Net Assets (Deficit)	**-$131,073**	**-$163,509**	**-$193,429**	**-$29,920**
Operating Facilities Net Income	-$20,732	-$27,604	-$29,897	-$2,293
Other Operations Net Income	363	-4,832	-23	4,809
Net Income (Deficit)	**-$20,369**	**-$32,437**	**-$29,920**	**$2,517**

Note: Other operations are comprised of property and equipment rental and consultant and management fees.

Source: Maryland Economic Development Corporation financial statements

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

For further information contact: Jody J. Sprinkle Phone: (410) 946-5530

- The Maryland Economic Development Corporation's (MEDCO) net income deficit totaled -$29.9 million for fiscal 2011, a decrease of about $2.5 million. Operating income for fiscal 2011 was positive at $11.5 million, which is a key indicator of economic health. Noncash expenses, such as depreciation, and non-operating 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 -$193.4 million in fiscal 2011.

- The corporation's net asset deficit is attributable to the accumulated losses of its operating facilities. The operating facilities' net income deficit grew by $2.3 million in fiscal 2011. The corporation also experienced a small net income deficit in its other operations.

Analysis in Brief

Overall Financial Position

Operating Revenues Exceed Operating Expenses: The corporation's net asset deficit has grown to -$193.4 million. Conversely, operating revenues continue to exceed operating expenses. However, operating income fell approximately $616,000 in fiscal 2011.

MEDCO's Assets Exclusive of Operating Facilities Are Relatively Stable: Exclusive of operating facilities, MEDCO had $12.8 million in net assets in fiscal 2011, less than the 10-year average of $17.3 million. In fiscal 2011, MEDCO provided funding for eight new projects.

Operating Facilities Financial Position

Net Assets Continue to Decrease: Operating facilities' net assets decreased by $29.9 million in fiscal 2011. This decrease is more than the decrease experienced in fiscal 2010.

Operating Income Increased in 2011; Three Projects Posted a Loss: Operating facilities' income increased slightly to $8.0 million in fiscal 2011. Three projects showed a loss, and one non-university project was defined as a "watch" project in the corporation's financial statement. **The Department of Legislative Services (DLS) recommends that MEDCO comment on the designation of the Chesapeake Bay Conference Center as a "watch" project.**

Operating Income Grew to $13.0 Million Among University Housing Projects in Fiscal 2011: Operating income for university housing projects grew to $13 million in fiscal 2011. However, one project is considered a "watch" project within the corporation's financial statements. **DLS recommends that MEDCO comment on the university projects and specifically on the designation of University of Maryland, Baltimore as a "watch" project.**

Rocky Gap Project Update: The Rocky Gap facility, as an operating project of the corporation, continues to post operating losses. However, there are developments toward the establishment of the resort as a video lottery terminal destination in the State. **DLS recommends that the corporation brief the budget committees on the steps taken to sustain the resort until the issuance of a video lottery terminal license.**

Other Projects: MEDCO has provided funds for projects that are outside its conventional financing, including the Maryland Center for Construction Education and the Baltimore Grand Prix. Also, legislation has been introduced (Senate Bill 435 of 2012) to alter the types of projects that the corporation may provide with bond financing. **DLS further recommends that the corporation comment on the use of its funds for projects outside its conventional financing role and the potential impact of Senate Bill 435.**

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 234 projects through fiscal 2011. Of these, MEDCO currently owns and operates 14 as operating facilities, meaning the corporation is involved in management decisions and has a hand in ensuring successful daily operations. For 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 oversees and approves actions pertaining to 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 10 full-time and 1 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 operates 14 facilities, and revenue from those facilities contributes to the corporation's bottom line. As shown on page 1 of this analysis, operating revenues did not cover all non-operating expenses; therefore, the corporation had a net income deficit of -$29.9 million in fiscal 2011. This is a smaller income deficit when compared to the losses experienced in fiscal 2010. However, operating revenues ($129.9 million) continue to exceed operating expenses ($118.5 million).

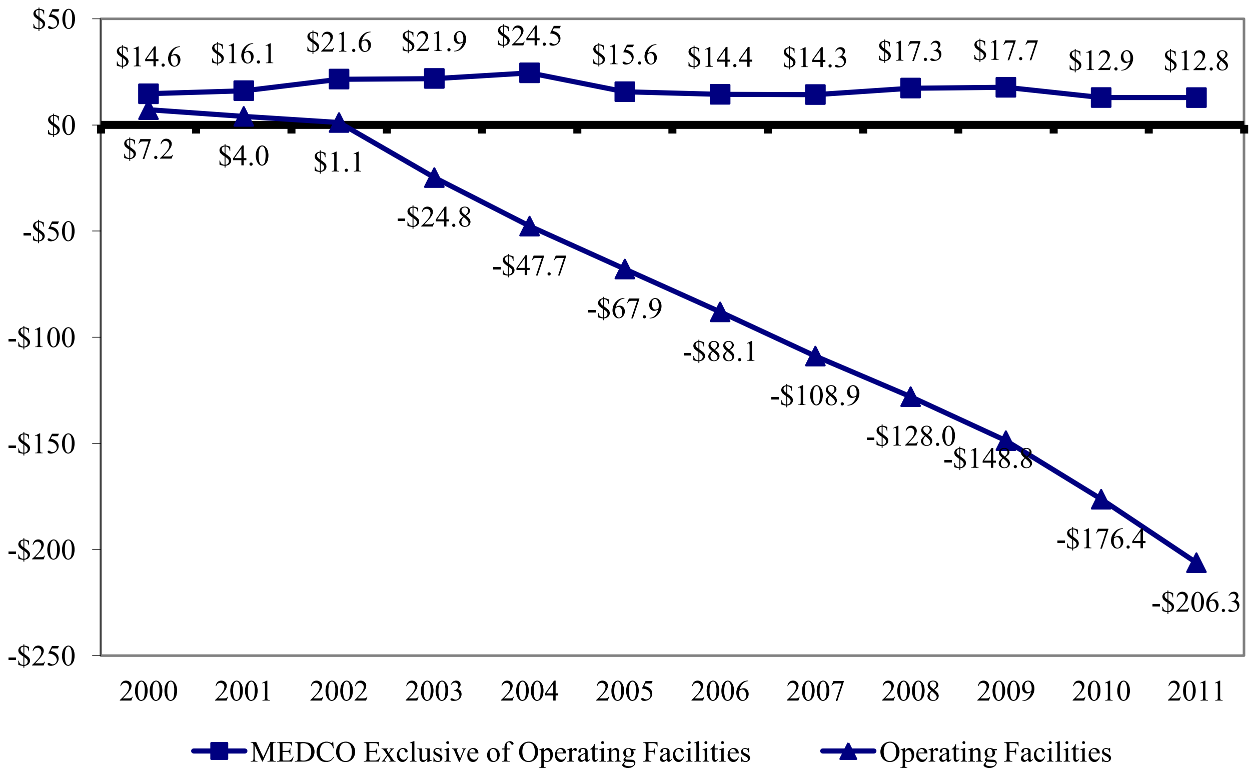
Each year that the net income deficit persists, the corporation's equity position declines. The net assets deficit grew to -$193.4 million in fiscal 2011, as shown on page 1. The corporation reports that the growing net assets deficit is not a significant concern as long as operating revenues exceed 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 $12.8 million in net assets in fiscal 2011. The balance has averaged $17.3 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 2011, MEDCO provided financing for eight new projects.

MEDCO has 14 operating facilities in its portfolio. The net assets deficit for these facilities grew to -$206.3 million in fiscal 2011, 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 2000-2011
($ in Millions)



MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Operating Facilities Financial Position

Net Assets Continue to Decrease

Exhibit 2 shows the increases and decreases in MEDCO's net assets by project. Operating facilities' net assets decreased by $29.9 million in fiscal 2011. This decrease is higher than the decrease experienced in fiscal 2010.

Exhibit 2
MEDCO Increase (Decrease) in Net Assets by Project
Fiscal 2009-2011

	2009	2010	2011	Total Net Assets (Deficit) at End of 2011
University Student Housing				
Morgan State University	-$103,032	$101,138	-$605,226	-$6,956,916
Bowie State University	-584,459	-933,396	-51,143	-5,287,374
Frostburg State University	-145,594	-221,928	40,818	-2,904,152
Salisbury University	-442,677	-253,562	-212,320	-2,744,669
Towson West	-573,459	-1,103,721	-853,684	-2,530,864
University of Maryland, Baltimore	-982,572	-1,131,682	-867,496	-9,424,957
University of Maryland Baltimore County	-216,102	144,486	286,207	-2,842,829
University of Maryland, College Park Housing	-1,789,945	-2,551,065	-3,125,429	-14,654,077
University Village at Sheppard Pratt	-770,269	-753,502	-666,804	-9,018,129
Subtotal	**-$5,608,109**	**-$6,703,232**	**-$6,055,077**	**-$56,363,967**
Other Facilities				
Chesapeake Bay Conference Center (Hyatt Cambridge)	-$10,779,761	-$14,383,265	-$14,526,159	-$102,484,597
Chesapeake Hills Golf Course	2,487,128	0	0	0
Shady Grove Innovation Center	-497,461	54,794	158,050	5,378,375
Rockville Innovation Center	-194,163	-416,970	-551,423	-51,680
Rocky Gap Golf Resort	-5,197,395	-5,667,383	-6,147,219	-54,201,537
University of Maryland, College Park Energy	-930,449	-502,753	-2,807,083	2,195,182
Subtotal	**-$15,112,101**	**-$20,915,577**	**-$23,873,834**	**-$148,612,834**
Subtotal Operating Facilities	**-$20,720,210**	**-$27,618,809**	**-$29,928,911**	**-$205,528,224**
MEDCO Exclusive of Operating Facilities	**$363,488**	**-$4,832,301**	**-$23,132**	**$12,868,486**
Elimination (Accounting Adjustment)	**-$12,208**	**$14,514**	**$32,432**	**-$746,131**
Grand Total	**-$20,368,930**	**-$32,436,596**	**-$29,919,611**	**-$192,886,878**

MEDCO: Maryland Economic Development Corporation

Note: MEDCO sold Chesapeake Hills Golf Course to Calvert County in fiscal 2008

Source: Maryland Economic Development Corporation

Operating Income Increased in 2011; Three Projects Posted a Loss

Exhibit 3 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 slightly to $8.0 million in fiscal 2011, compared to $7.5 million in 2010. Additionally, only three projects posted a loss in fiscal 2011, compared to four in the previous year, This is due to the fact that Shady Grove Innovation Center posted a gain instead of a loss in fiscal 2011. All of the university student housing projects posted gains in each year shown, as did the University of Maryland, College Park energy project.

Exhibit 3
MEDCO Operating Income (Loss) by Project
Fiscal 2009-2011

	2009	2010	2011	Total 2009-11
University Student Housing				
Morgan State University	$2,016,505	$2,303,309	$1,560,344	$5,880,158
Bowie State University	492,916	182,418	567,778	1,243,112
Frostburg State University	823,348	739,752	986,950	2,550,050
Salisbury University	270,948	485,229	512,435	1,268,612
Towson West	912,194	748,156	909,926	2,570,276
University of Maryland, Baltimore	885,115	759,907	998,838	2,643,860
University of Maryland Baltimore County	1,164,941	1,511,367	1,494,918	4,171,226
University of Maryland, College Park Housing	3,930,786	4,238,501	4,865,552	13,034,839
University Village at Sheppard Pratt	1,088,333	1,093,211	1,133,079	3,314,623
Subtotal	**$11,585,086**	**$12,061,850**	**$13,029,820**	**$36,676,756**
Other Facilities				
Chesapeake Bay Conference Center (Hyatt Cambridge)	-$390,074	-$3,699,379	-$3,577,916	-$7,667,369
Chesapeake Hills Golf Course	-20,637	0	0	-20,637
Shady Grove Innovation Center	-218,897	-51,777	102,744	-167,930
Rockville Innovation Center	-309,617	-489,791	-633,227	-1,432,635
Rocky Gap Golf Resort	-2,946,403	-3,811,819	-4,307,611	-11,065,833
University of Maryland, College Park Energy	3,501,757	3,534,151	3,348,641	10,384,549
Subtotal	**-$383,871**	**-$4,518,615**	**-$5,067,369**	**-$9,969,855**
Subtotal Operating Facilities	**$11,201,215**	**$7,543,235**	**$7,962,451**	**$26,706,901**
MEDCO Exclusive of Operating Facilities	**$5,881,138**	**$4,583,344**	**$3,529,674**	**$13,994,156**
Elimination (Accounting Adjustment)	**-$12,208**	**$14,514**	**$32,432**	**$34,738**
Grand Total	**$17,070,145**	**$12,141,093**	**$11,524,557**	**$40,735,795**

MEDCO: Maryland Economic Development Corporation

Note: MEDCO sold Chesapeake Hills Golf Course to Calvert County in fiscal 2008.

Source: Maryland Economic Development Corporation

According to the corporation's financial statement, there are two operating projects identified in fiscal 2011 as "watch" projects for failure to meet debt coverage ratios. This is an improvement over the prior year in which three projects were singled out as problematic. One of these projects is a non-university project. Each of these and all other MEDCO projects need to be considered on its own merits because no MEDCO projects are cross-collateralized, and each project must support itself with its own revenues.

- **Chesapeake Bay Conference Center:** The Chesapeake Bay Conference Center (CBCC) is located in Dorchester County. It houses a hotel, golf course, and conference facilities. Although it is experiencing an increase in revenue from its operations, the project is unable to meet its required debt coverage ratio. MEDCO secured a management consultant to suggest changes in pricing and expense reductions in order to bring the ratio into compliance.

The Department of Legislative Services (DLS) recommends that MEDCO comment on the designation of CBCC as a problem project.

Operating Income Grew to $13 Million Among University Housing Projects in Fiscal 2011

Operating income for the university housing projects increased to $13.0 million in fiscal 2011, compared to $12.1 million in 2010. However, all but two of the housing projects incurred decreases in net assets when non-operating revenues and expenses were considered. Further, one project was designated as a "watch" project.

- **University of Maryland, Baltimore:** The housing project at the 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 expected.

MEDCO became involved in university housing projects in 1999 when the University System of Maryland approached the corporation 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, in some instances, do not want to own and operate the facilities themselves; 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 and specifically on the designation of University of Maryland, Baltimore as a "watch" project.

Rocky Gap Project Update

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 $4.3 million in fiscal 2011 alone, as shown in Exhibit 3. Occupancy rates have fallen; in fact, occupancy has fallen by 50% in the last year.

Rocky Gap had generally been generating enough cash to cover its operating expenses (*i.e.*, costs of hotel management) but not enough to cover its debt payments and non-hotel expenses, 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. Despite these efforts, the project is not earning enough to pay debt.

Legislation adopted during the 2007 special session authorized the Rocky Gap (Allegany County) facility to become one of the State's five locations for video lottery terminals (VLT). A request for proposal (RFP) for a VLT facility at Rocky Gap was issued in 2008. After rejecting in February 2009, the single proposal received for Allegany County, the Video Lottery Facility Location Commission made several recommendations to the General Assembly related to the Allegany County location with the hope that the location could be made more attractive to potential applicants. In response, Chapter 624 was enacted in 2010, which altered several provisions regarding the Allegany County VLT facility location. Under Chapter 624, contingent upon the purchase of the Rocky Gap Lodge and Golf Resort by the licensee, 2.5% of VLT proceeds from the Allegany County facility, for the first five years of operations, that would otherwise be distributed to the Racetrack Facility Renewal Account would instead be distributed to the Allegany County facility licensee. Subsequent to the enactment of Chapter 624, the Location Commission issued a new RFP for the Allegany County location in July 2010, but no proposals were received by the November 2010 deadline.

In an effort to provide further incentives for potential applicants for the Allegany County location, Chapter 240 of 2011 made several changes related to the Allegany County location, including increasing the Allegany County licensee's share of the proceeds to 50% for the first 10 years of operations. The Location Commission issued another RFP for Allegany County in June 2011 and received three proposals on September 23, 2011, one of which was subsequently rejected for failing to meet various requirements contained in the RFP. A second proposal was also rejected in January 2012 for not satisfying the terms of the RFP. The third proposal is still pending.

DLS recommends that the corporation brief the budget committees on the steps taken to sustain the resort until the issuance of a VLT license.

Other Projects

The corporation has also provided funds for other projects that are atypical of its normal activities. For example, for the third year, the corporation is providing grant funds ($75,000) for the Maryland Center for Construction Education and Innovation which is housed at Towson University. The center is designed to partner with the private sector, universities, community colleges, and secondary schools to position construction as a career of choice, to promote the economic viability of construction in Maryland, and to serve as a resource for the industry, education, and government.

Additionally, the corporation has made a direct loan ($500,000) to the organizers of the Baltimore Grand Prix, an Indy Racing League event that took place in Baltimore last Labor Day weekend. A direct loan such as this has never before been made by the corporation. The loan was to cover working capital costs, and the terms include a provision that would allow the corporation an equity stake in the planned race. The race developer has since failed to pay vendors and certain taxes, and the prospect for subsequent races is uncertain. Similarly, the prospect of repayment to MEDCO is also uncertain.

Also, in fiscal 2011, MEDCO advanced $3.6 million, to the Maryland Jockey Club, to help close an operating deficit for the thoroughbred tracks. The Budget Reconciliation and Financing Act of 2011 included a provision to allow racetrack capital renewal funds to be used to repay the advance from MEDCO. This agreement allowed the racetracks to operate a 2011 racing schedule similar to the 2010 racing schedule with a 146-day racing season that includes the 136th running of the Preakness at Pimlico. This advance was repaid in full at the start of fiscal 2012.

Senate Bill 435 would alter the type of projects that MEDCO is authorized to finance. The bill qualifies that the prohibition against providing bond financing to an educational institution does not apply if (1) the property will be owned by the MEDCO or leased to MEDCO under a ground lease; and (2) the property will be leased by MEDCO back to the educational institution. The corporation contends that the change will provide a streamlined process for structuring, financing, and ownership opportunities for entities requesting assistance from MEDCO.

DLS further recommends that the corporation comment on the use of its funds for projects outside its conventional financing role and on the potential impact of Senate Bill 435.

Recommended Actions

1. Nonbudgeted.