2015 Session
Capital Budget Overview

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Summary of Issues

Future of State Center: This issue outlines the current uncertain status of the State Center redevelopment public-private partnership. The Department of Legislative Services (DLS) presents issues that should be addressed by the Department of General Services to aid the committees understanding of the implications for the State. There are various options that could be invoked by the State and the developer should the original Phase I development as outlined in the approved ground and occupancy leases executed between the State and the developer not be pursued by the current Administration.

Summary of Recommended Bond Actions

		Funds
1.	New Flight Training Facility	$2,100,000 GO
	Add authorization for flight training facility	
2.	Section 2 – Department of Labor, Licensing, and Regulation – 1100 North Eutaw Street Elevator	
	Approve the de-authorization of remaining funds not needed to complete the project.	
3.	Section 2 – Local Legislative Initiative – Carroll's Hundred Archeology Project	$100,000 GO
	Amend grant for the Carroll's Hundred Archaeology Project to change the grantee and extend the termination date and strike the de-authorization proposed by the Governor.	
	Total Additions	**$2,200,000**

Budget Overview

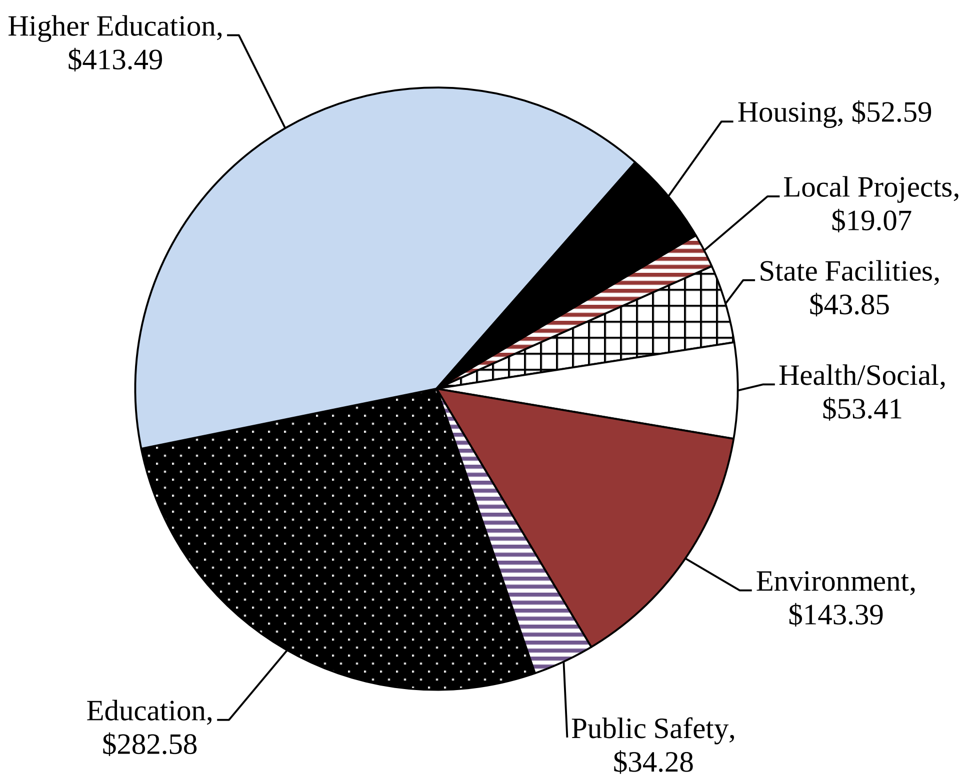
The Fiscal 2016 Nontransportation *Capital Improvement Program* Totals Approximately $1.44 Billion

In October, 2014, the Capital Debt Affordability Committee (CDAC) recommended that a maximum of $1,170.0 million in general obligation (GO) bonds may be authorized in the 2015 session. CDAC also recommended that an additional $300.0 million be added to the GO bond authorization over the next four years of the *Capital Improvement Program* (CIP) with a primary use of the funds to meet the State transportation Watershed Implementation Plan obligations and other projects accelerated by the General Assembly during the 2014 session. However, the Board of Revenue Estimates revenue write-down in December 2014 made the levels of debt proposed by CDAC no longer affordable. Projections suggested debt service payments will exceed the 8% debt service to revenue limit by fiscal 2018 were the CDAC recommendations adopted. To avoid this, the Spending Affordability Committee (SAC) recommended that the level of new GO bond authorizations for the 2015 session remain at the $1.095 billion level programmed in the 2014 CIP for the 2015 session. SAC further recommended that the 2015 session CIP not incorporate the $300.0 million increase over the remaining four years of the CIP. In addition, in recognition of the uncertain revenue outlook, the committee also recommended that the Treasurer and the Governor coordinate in the management of future issuances of State tax-supported debt so that debt limits are observed going forward. The Treasurer also weighed in on the impact of the revenue write-down on debt affordability and recommended that the level of new GO bond debt not exceed $1.045 billion in the 2015 session to remain within the debt affordability limits. The Governor's capital budget proposes a level of new GO bond authorizations of $994.6 million.

For fiscal 2016, the University System of Maryland (USM) intends to issue up to $34.5 million in academic debt, which is $2.5 million more than the amount issued in fiscal 2015. The increase will support additional USM projects and includes $5.0 million to support a long-term campuswide infrastructure improvement program at the University of Maryland, College Park, which began in fiscal 2013. This level of issuance will result in a debt service ratio within the 4.5% of current unrestricted funds and the mandatory transfers criterion recommended by the system's financial advisers. Morgan State University, St. Mary's College of Maryland, and Baltimore City Community College do not plan on issuing any academic revenue debt in fiscal 2016.

The capital program as introduced includes $994.6 million in new GO debt for State-owned facilities and grant and loan programs. An additional $9.0 million in GO bonds from prior years will be de-authorized, thus increasing the amount of GO debt included in the capital program to $1.004 billion (**Appendix 1**). The capital budget plan also includes the issuance of $4.6 million of Qualified Zone Academy Bonds (QZAB) and $34.5 million of Academic Revenue Bonds, bringing the total amount of debt funding to $1.043 billion. Of the $1.043 billion of GO debt, $66.2 million funds the replacement of prior year and proposed diversion of transfer tax revenues to the general fund; $327.0 million represents debt pre-authorized in the Maryland Consolidated Capital Bond Loan of 2014 excluding funds for transfer tax revenue replacement; and $260.7 million funds school construction projects, including QZAB and Aging Schools Program funded projects. **Exhibit 1** illustrates the GO bond distribution.

Exhibit 1
GO Bond, QZAB, and ARB Distribution
($ in Millions)



ARB: Academic Revenue Bond
GO: general obligation
QZAB: Qualified Zone Academy Bond

Source: Department of Budget and Management

Top bond funded programs/projects are shown in **Exhibit 2**

Exhibit 2
Top General Obligation/Revenue Bond Funded Programs and Projects
Fiscal 2016

Project Title	GO Bond	Revenue	Total Funds
BPW: Public School Construction Program	$250,000,000	$0	$250,000,000
UMB: Health Sciences Research Facility III	81,550,000	0	81,550,000
UMCP: Edward St. John Learning and Teaching Center	65,650,000	0	65,650,000
MHEC: Community College Facilities Grant Program	57,926,000	0	57,926,000
SU: New Academic Commons	40,680,000	12,500,000	53,180,000
BSU: New Natural Sciences Center	39,728,000	0	39,728,000
MSU: New Behavioral and Social Sciences Center	31,007,000	0	31,007,000
MISC: Prince George's Hospital System	30,000,000	0	30,000,000
DoIT: Public Safety Communication System	29,950,000	0	29,950,000
MDE: Biological Nutrient Removal Program	26,500,000	0	26,500,000
MDA: Maryland Agricultural Land Preservation Program	22,726,000	0	22,726,000
DPSCS: New Youth Detention Center	21,630,000	0	21,630,000
DNR: Rural Legacy Program	17,494,000	0	17,494,000
USMO: Capital Facilities Renewal Program	0	17,000,000	17,000,000
MSDE: State Library Resource Center	16,850,000	0	16,850,000
MES: Infrastructure Improvement Fund	16,471,000	0	16,471,000
DNR: Program Open Space – Stateside	14,500,000	0	14,500,000
DNR: Program Open Space – Local	14,500,000	0	14,500,000
DHCD: Homeownership Programs	11,800,000	0	11,800,000
SMCM: Anne Arundel Hall Reconstruction	10,482,000	0	10,482,000
UMCP: Campuswide Building System and Infrastructure Improvements	5,000,000	5,000,000	10,000,000
DHCD: Rental Housing Program	10,000,000	0	10,000,000
Subtotal Top Funded Programs and Projects	***$814,444,000***	***$34,500,000***	***$848,944,000***
Subtotal Other Funded Programs and Projects	***$193,726,000***	***$0***	***$193,726,000***
Total	**$1,008,170,000**	**$34,500,000**	**$1,042,670,000**
De-authorizations as Introduced	**-$8,973,134**	**$0**	**-$8,973,134**
Grand Total New Funding	$999,196,866	$34,500,000	$1,033,696,866

BPW: Board of Public Works
BSU: Bowie State University
DHCD: Department of Housing and Community Development
DNR: Department of Natural Resources
DoIT: Department of Information Technology
DPSCS: Department of Public Safety and Correctional Services
GO: general obligation
MDA: Maryland Department of Agriculture
MDE: Maryland Department of the Environment
MES: Maryland Environmental Services
MHEC: Maryland Higher Education Commission
MISC: Miscellaneous
MSDE: Maryland State Department of Education
MSU: Morgan State University
SMCM: St. Mary's College of Maryland
SU: Salisbury University
UMB: University of Maryland, Baltimore
UMCP: University of Maryland, College Park
USMO: University System of Maryland Office

Source: Department of Budget and Management

Issues

1. Future of State Center Uncertain

Background

State Center was conceived in 2005 as a transit-oriented mixed-use development to revamp 1.5 million square feet of existing State office space on the west side of Baltimore City. Located in close proximity to the State Center Metro in Baltimore City, State Center consists of a grouping of State-owned office buildings that house a number of State agencies. After several years of predevelopment efforts including the execution of a Master Development Agreement (MDA) in June 2009 and several years of significant involvement from the budget committees, in July 2010, the Board of Public Works (BPW) conditionally approved ground and occupancy leases for the project. The basic concept underpinning the development included the State ground leasing parcels in several phases to State Center LLC, with the State then having opportunities to rent office space back from the developer. In addition to opportunities to lease office space for the State, the development plan includes the construction of private commercial office space; retail space including a grocery store and a mix of low- and moderate-income rental and market rates for sale housing; and parking.

Efforts to start Phase I were blocked due to litigation filed by a group of downtown Baltimore City businesses principally on the grounds that the State's land transaction was a procurement and did not comply with competitive bidding requirements and procedures. A ruling handed down by the Baltimore City Circuit Court in January 2013 voided the development contract, citing the State's failure to competitively bid the development. However, in March 2014, the State Court of Appeals reversed the decision in the State's favor allowing the development to proceed.

Current Status

In December 2014, in the waning days of the prior Administration, the Department of General Services (DGS) and the Maryland Department of Transportation (MDOT) initiated the process to seek BPW approval of amendments to the MDA to allow for a reduction in the size of the parking structure. As previously approved by the BPW, Phase I development of State Center included the construction of a 980-space underground parking garage on lot G. The office leases that was conditionally approved alongside the garage called for the State to have 500 spaces for employees and 50 spaces on a 24/7 basis for fleet vehicles. The remaining parking spaces would support the anticipated private retail, commercial, and housing portion of the project. The cost of the parking garage was capped at $28.3 million to be financed with 20-year tax-exempt Maryland Economic Development Corporation (MEDCO) bonds. Based on the initial costs, the debt service would be roughly $2.5 million annually through the term of the bonds, which after additional costs for garage operations and offsetting parking revenue would result in an estimated annual loss of about $2.0 million to the Transportation Trust Fund (TTF). On November 1, 2014, DGS and MEDCO advised that increased cost estimates for constructing a sub-surface parking garage would require a reduction in scope down from the original 980 spaces to not less than 580 spaces. Although reduced in size, the garage would still provide the State with 500 spaces for employees and 50 spaces on a 24/7 basis for fleet vehicles, as originally approved. The construction of the parking garage represents the initial construction that would take place under Phase I State Center redevelopment.

The developer is also seeking to reduce the privately-owned mixed-use development within Phase 1 of the project. As proposed by the developer, a 150-unit apartment building would be replaced with 20 town homes, a grocery store would be deferred to a future phase and overall retail and speculative private office uses would be reduced from what was originally proposed for Phase 1. These changes would reduce the economic benefits presented to the BPW when the conditional approvals were granted. Furthermore, the reduction in private uses on Parcel G would reduce the parking revenues for the state-owned garage. Instead of generating $7.7 million in operating income over 20 years as projected in 2010, the modified development program would require a $3.0 million operating subsidy over 20 years, resulting in a negative net operating impact of $10.7 million to the State.

The agencies did not present the amendments to the BPW. The developer indicated it is reconsidering the size of the garage. In January 2015, MDOT and DGS asked for written confirmation of what the developer is now proposing for Phase 1, along with information to evaluate the changed economics of the project. In addition, the DGS project representative entered into a forebearance agreement with the developer in October 2014, in accordance with the force majeure provisions in the project agreements, extending the dates in the MDA and related agreements for a period of 57 months as a result of the delay occasioned by the lawsuit.

Issues

Changes in the State's fiscal condition since 2008 and the recent change in the Administration raise several policy issues. Issues include a lack of clarity concerning the status of the proposal as a capital or operating lease, which have persisted since 2009 and continue to remain unanswered; a lack of clarity concerning next steps under the MDA; and a lack of clear understanding of the implications of provisions in the MDA as they pertain to various State and developer options should the State decide not to move forward with leases of office space in the first phase of the project. Moreover, basis for periodic reporting and oversight by the budget committees is unclear.

Enforceability of the MDA and Clarity of State Options If State Center Office Leases Are Not Pursued

The State Center MDA executed in June 2009 provides the terms and conditions between the State and the developer that guide the phased development plan. The MDA, however, did not contemplate the lengthy judicial delay. **Representatives from DGS should be prepared to brief the committees on the legal standing and enforceability of the MDA. This should include (1) whether the MDA continues to define the terms and conditions of the development as contemplated at the time it was entered into; and (2) if amendments are necessary to better outline the timeframes for various State and developer rights and responsibilities as a result of the lengthy litigation delay.** The project appears to be in limbo as the developer has unresolved project issues and the new Administration grapples with the long-term consequences of potentially moving forward as planned versus other potential alternatives. To the extent that other alternatives may be in play, the MDA provides some guidance concerning State and developer rights and responsibilities if certain developer milestones are, or are not, met including State buy-out rights and development pursuant to an alternative ground lease. These provisions are, however, difficult to decipher and made more complicated by the fact that the timeframes established in the MDA in many instances are askew due to the lengthy litigation. **The Administration should articulate its vision for the State Center project. In particular, it is important to clarify if the MDA has any legal time limitation if the current Administration and the developer do not resolve the status of the State Center redevelopment during the Governor's current four-year term.**

Debt Affordability Implications

It is not known if the leases contemplated for Phase 1 of the project are capital or an operating leases. Based on the Administration's assumptions provided to the Treasurer in 2010, it was suggested that the project would be an operating lease, but this cannot be affirmed at this time. Accounting guidelines suggest that it is likely that the project is a capital lease**. DLS estimates that the additional lease cost of State Center would cause the State to exceed its debt limitation criteria that debt service not exceed 8% of State revenues. The proposed occupancy leases and whether they constitute capital leases should be determined in order to guide future decisions concerning the allocation of State tax supported debt amongst the competing demands.**

Project and Rent Costs and Net Effect on the General Fund

The Administration suggests that the essential elements that underpin the project, remain the same. However, the cost of construction materials and financing have changed since 2009. Phase 1 is also slated to open in July 2018, instead of 2014 as envisioned when BPW approval was granted. In October 2014, the Administration has reported that the "all-in" rent cost would approximate $35.85 per square foot for the Phase 1 20-year operating lease. Rent is expected to increase 15% every 5 years. The Administration assumes that additional rent expense will be offset by a reduction in the level of current general fund spending for utilities, security, maintenance, and other related expenses. In addition, Baltimore City has approved a payment in lieu of taxes to help defray the property taxes that the State would now be required to pay. A proposed Tax Increment Financing District would also be established in order to pay for $81.0 million of infrastructure upgrades (of which $15.0 million would apply to Phase 1). The State would also be responsible for moving expenses, estimated at $2.4 million for this phase only, as well as $5.8 million over 4 years for mothballing costs for existing State Center space pending renovation by the developer. It is also difficult to justify this additional expense until the State has resolved the ongoing general fund structural deficit. **The committees should request an update on the total project cost estimate and the Phase 1 cost estimate. It is unlikely that the State can afford an additional rent expense of at least $18.5 million, increasing by 15% every 5 years, for just Phase I of five project phases let alone future phases, until the structural deficit is resolved.**

Legislative Oversight

The requirements for legislative oversight and reporting are not clear for the State Center project. The project precedes Chapter 5 of 2013, which outlines processes for legislative review and oversight of Public Private Partnerships (P3s). While it is not clear if State Center would meet the definition of a P3, it is certainly of similar scale and complexity to a P3. **DLS recommends the committees consider legislation or provisions in the operating or capital budgets to restore some level of oversight to the redevelopment of State Center if the project MDA is determined to be in full force and effect without any time limitations.**

Future Options

At some point, and subject to the MDA to the extent is is legally enforceable, whether it be in the present form of the negotiated redevelopment or under some other redevelopment proposal, the State may wish to reevaluate its options as it relates to the State's continued occupancy of the building and facilities located at State Center.

- **Do Nothing:** The State could continue to occupy State Center under the current State ownership structure and defer any decision regarding the long-term solution to the problem. This would require continued annual funding to address the center's facility maintenance needs until such time that a more comprehensive renovation/infrastructure replacement plan could be completed. The amount of investment would depend upon the urgency of repairs and an annual assessment of what it would take to keep certain buildings operational. The drawback is that the State would continue to occupy space in facilities that are over 50 years old, are considered less than adequate, functionally inefficient, and in eventual need of substantial investment or future replacement.

- **State Funded Renovation/Replacement:** Another option is for the State to undertake its own infrastructure replacement plan for State Center as simple replacement of the existing office buildings. Alternatively, the State could purchase one or more office buildings to accommodate the State's office needs. This would require a substantial capital investment from the State and a reprioritization of the State's long-term capital infrastructure plans. The current five-year CIP does not contemplate a State-funded renovation/replacement plan for State Center. As discussed, additional general obligation debt would cause the State to breach its debt service limitations and requires higher property taxes or general fund supplements for debt service. Estimates from 2009 put the cost of renovations and some new construction in the ballpark of $215 million, but these assumptions and estimates would need to be re-evaluated and revised accordingly.

- **Sell State Center and Rent Office Space:** The State could choose to sell State Center and move the agencies currently occupying the site into leased office space. The State could take advantage of commercial office space vacancies in Baltimore and also potentially negotiate favorable lease terms due to the large amount of space that the State would pursue. Leasing space impacts the operating budget, but these costs could be partially offset by whatever the State collects in the sale of State Center and in the avoidance of any continuing deferred facility renewal and maintenance required to keep the facilities operational. Moreover, in this option, the cost of renovating and replacing the buildings is avoided. The downside is this creates a vast empty large tract of land in Baltimore City, pending any future development of the site.

- **Procure a New P3:** If the current MDA is no longer legally enforceable, the State could also re-bid an entirely new redevelopment plan under a P3 arrangement guided by Chapter 5 of 2013. In order to remain affordable though, the project would likely have to be scaled back to only include new State office space.

- **Stay the Course:** Allow the developer to complete the requirements to effectuate the ground and occupancy leases as they pertain to the Phase I development already approved by BPW. **To the extent that this option is chosen, DLS recommends that the parking structure be built to the original 980 spaces rather than the reduced 580-space scope recently put forth by DGS and MDOT. The reduced size will not accommodate the private-sector development that is essential to the overall development of the site. In order to build to the higher number of spaces and stay within the $28.3 million cost cap, consideration should be given to building the parking above ground rather than the much more expensive planned subterranean construction.**

Notable Projects/Programs Deferred or Reduced in Fiscal 2016

Exhibit 3 provides a summary of notable changes in the Governor's fiscal 2016 capital budget plan versus what was planned in the 2014 CIP and other changes made by the General Assembly in the 2014 session.

Exhibit 3
Notable GO Bond Project/Program Deferrals and Reductions
Fiscal 2016
($ in Millions)

Project/Program	Planned	Proposed	Purpose
Maryland School for the Deaf – Water Main Replacement Project	$3.2	$0.0	Design delay – programmed in fiscal 2017
State Library Resource Center	25.9	16.9	Multi-year funding plan extended one year through fiscal 2019
Department of Health and Mental Hygiene – Secure Evaluation and Therapeutic Treatment Center	7.9	0.0	Project size and scope under review – initial construction funds moved back one year to fiscal 2017
Community College Facilities Grant Program	80.0	57.9	Proposed amount based on project readiness and availability of local matching funds
Department of Juvenile Services – Baltimore Regional Treatment Facility	2.5	0.0	Acquisition funds moved to fiscal 2020 in CIP

Project/Program	Planned	Proposed	Purpose
Department of Juvenile Services – New Female Detention Facility	27.5	2.5	Design delays related to infrastructure and utilities studies – construction schedule moved back one year with initial construction funding now in fiscal 2017
Morgan State University – Student Services Building	2.5	0.0	Initial design funding moved to fiscal 2017
Department of Public Safety and Correctional Services – Simulated Training Environment Facility	3.2	0.0	Project no longer appears in CIP
Board of Public Works – Annapolis Post Office Renovation and Addition	4.6	0.0	Design delays – initial construction funding moved to fiscal 2017
Board of Public Works – Facilities Renewal	15.0	7.5	Reduced based on encumbrance activity and available funds
University of Maryland Medical System – New Ambulatory Care Center and Neonatal Intensive Care Unit	10.0	3.5	Although the CIP did not reflect any funding commitment in fiscal 2016, budget language expressed intent that $10.0 million annually be provided through fiscal 2018 – the project scope no longer includes the Ambulatory Care Center
University of Maryland College Park – New Bioengineering Building	42.2	1.0	The 2014 CIP did not program funding in fiscal 2016, but the project was accelerated by the General Assembly in the 2014 session with a pre-authorization of $42.2 million for construction in fiscal 2016 – the funding is programmed in fiscal 2017 where it was scheduled in the 2014 CIP
Towson University – New Science Facility	3.5	0.0	Addition design funds moved back one year to fiscal 2017 – project scope evaluation
University of Baltimore – Langsdale Library Renovation	11.6	0.0	The 2014 CIP programmed $4.2 million for fiscal 2016, but reductions taken in the project in fiscal 2015 were added in a pre-authorization for fiscal 2016 in the amount of $11.6 million – project construction moved back one year to fiscal 2017 due to slow place of private fundraising for the project
Coppin State University – Percy Julian	1.2	0.0	Not scheduled for funding in the 2014 CIP until fiscal 2017 – pre-authorization added initial design funding for fiscal 2016 – funding remains scheduled in fiscal 2017
University System of Maryland Office – Southern Maryland Regional Higher Education Center	5.7	0.0	Funding moved to fiscal 2019 to 2020 – program plan review required before funding is to be made available

Project/Program	Planned	Proposed	Purpose
Prince George's Regional Medical Center	40.0	30.0	The 2014 CIP scheduled $30.0 million for fiscal 2016, but language added to the fiscal 2015 authorization reflected the intent that $40.0 million be provided in fiscal 2016 to account for reductions taken to the project in fiscal 2015. The budget plan keeps the programmed CIP amount and adds $15.0 million in fiscal 2017

CIP: *Capital Improvement Program*
GO: general obligation

Source: Department of Budget and Management, 2015 *Capital Improvement Program*

GO Bond Recommended Actions

1. Add authorization for flight training facility

WA01A	New Flight Training Facility..	$ 2,100,000

Add the following language:

<u>WA01</u> <u>DEPARTMENT OF STATE POLICE</u>

<u>(A)</u> <u>New Flight Training Facility. Provide funds to acquire a flight training device and construct a new flight training facility at Martin State Airport</u> <u>2,100,000</u>

Allowance	**Change**	**Authorization**
0	2,100,000	2,100,000

Explanation: This action authorizes $2.1 million of general obligation bond funds to complete the funding for the flight training devise and new flight training facility for the Medevac helicopter fleet. Prior authorized funds are insufficient to fund the construction of the new facility.

2. Approve the de-authorization of remaining funds not needed to complete the project. .

ZF2700	Section 2 – Department of Labor, Licensing, and Regulation – 1100 North Eutaw Street Elevator..........	$ 0