

T00A99
Maryland Economic Development Corporation

Financial Statement Data

Maryland Economic Development Corporation Financial Statement
Fiscal 2015-2017
(\$ in Thousands)

| | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>Change 2016-2017</u> |
|-------------------------------------|-------------------|-------------------|-------------------|-----------------------------|
| Total Assets | \$625,928 | \$612,904 | \$545,733 | -\$67,172 |
| Total Liabilities | 854,245 | 854,141 | 770,826 | -83,315 |
| Net Assets (Deficit) | -\$228,317 | -\$241,237 | -\$225,094 | \$16,143 |
| Total Operating Revenue | \$132,352 | \$136,878 | \$137,302 | \$424 |
| Total Operating Expenses | 114,608 | 120,885 | 121,936 | 1,051 |
| Operating Income Subtotal | \$17,744 | \$15,993 | \$15,366 | -\$627 |
| Non-operating Revenues and Expenses | -\$25,171 | -\$28,913 | \$777 | \$29,690 |
| Net Income (Deficit) | -\$7,427 | -\$12,920 | \$16,143 | \$29,063 |

Change in Net Assets (Deficit) and Income by Source
Fiscal 2015-2017
(\$ in Thousands)

| | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>Change 2016-2017</u> |
|---------------------------------|-------------------|-------------------|-------------------|-----------------------------|
| Operating Facilities Net Assets | -\$227,050 | -\$240,294 | -\$254,000 | -\$13,706 |
| Other Operations Net Assets | -1,266 | -942 | 28,907 | 29,849 |
| Net Assets (Deficit) | -\$228,317 | -\$241,237 | -\$225,094 | \$16,143 |
| Operating Facilities Net Income | -\$7,107 | -\$13,244 | -\$13,706 | -\$462 |
| Other Operations Net Income | -320 | 324 | 29,849 | 29,525 |
| Net Income (Deficit) | -\$7,427 | -\$12,920 | \$16,143 | \$29,063 |

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: Jason A. Kramer

Phone: (410) 946-5530

T00A99 – Maryland Economic Development Corporation

- The Maryland Economic Development Corporation's (MEDCO) net income improved by \$29.1 million in fiscal 2017 to \$16.1 million. Noncash expenses, such as depreciation, and non-operating items, such as interest expense, cause the income and asset deficits, and these deficits are not uncommon for real estate projects.
- Operating income for fiscal 2017 was positive at \$15.4 million, which is a key indicator of economic health. The fiscal 2017 net operating income declined slightly from \$16 million in fiscal 2016.
- The corporation's net asset deficit improved to -\$225.1 million in fiscal 2017. This improvement was due primarily to realized gains from the sale of the Human Genome Sciences building in fiscal 2017.

Analysis in Brief

Overall Financial Position

Operating Revenues Continue to Exceed Operating Expenses: Although MEDCO continues to maintain a net asset deficit position, its operating revenues continue to exceed its operating expenses. Net operating income declined slightly in fiscal 2017.

MEDCO Net Assets in a Negative Position: The corporation's operating facilities have long posted negative assets due to accumulated annual losses. The sale of the Human Genome Sciences building in fiscal 2017 led to positive non-operating net assets for the first time in five years.

Operating Facilities Financial Position

Student Housing Projects Bolster Operating Project Net Assets: Large declines in net assets at operating projects such as the Chesapeake Bay Conference Center (CBCC) were offset by improvements at nearly all of MEDCO's university student housing projects.

Four Projects Post Losses: Operating facilities' income was \$12.9 million in fiscal 2017; a decrease of \$1.9 million, or 12.9%. However, four projects posted losses in fiscal 2017, including CBCC at \$5 million.

Recommended Actions

1. Nonbudgeted.

T00A99
Maryland Economic Development Corporation

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 businesses and to attract new businesses to the State. The stated legislative purpose of the corporation 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 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 Commerce (Commerce). 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 Commerce. The debt represents nonrecourse 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's 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 294 projects through fiscal 2017. 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 most other projects, MEDCO generally serves as an arms-length financing entity.

The corporation is governed by statute under Sections 10-101 through 10-132 of the Economic Development Article. A 12-member board of directors oversees and approves actions pertaining to the corporation's affairs and appoints the executive director. The Secretary of Commerce and the Secretary of Transportation serve as *ex-officio* voting members. MEDCO's activities complement the marketing and financing programs of Commerce. There are currently 9 regular and 1 part-time professional staff members.

Overall Financial Position

Operating Revenues Continue to Exceed Operating Expenses

MEDCO operates 14 facilities, and revenue from those facilities contributes to the corporation's bottom line. Operating revenues (\$137.3 million) continue to exceed operating expenses (\$121.9 million).

Each year, when the corporation experiences a net income deficit, the corporation's equity position declines. This has been the case for at least the last decade of operations. Noncash expenses, such as depreciation, and non-operating items, such as interest expense, cause the income and asset deficits.

The corporation reports that a growing net asset deficit is not a significant concern as long as operating revenues exceed cash operating expenses. MEDCO notes that net losses and net asset deficits are not uncommon for real estate companies. With these companies, the market value of the assets generally exceeds the book value, and MEDCO reports that real estate investors look at market value or, more specifically, cash flow coverage rather than book value. Accordingly, the MEDCO operating position (operating revenues exceeding expenses) continues to be positive.

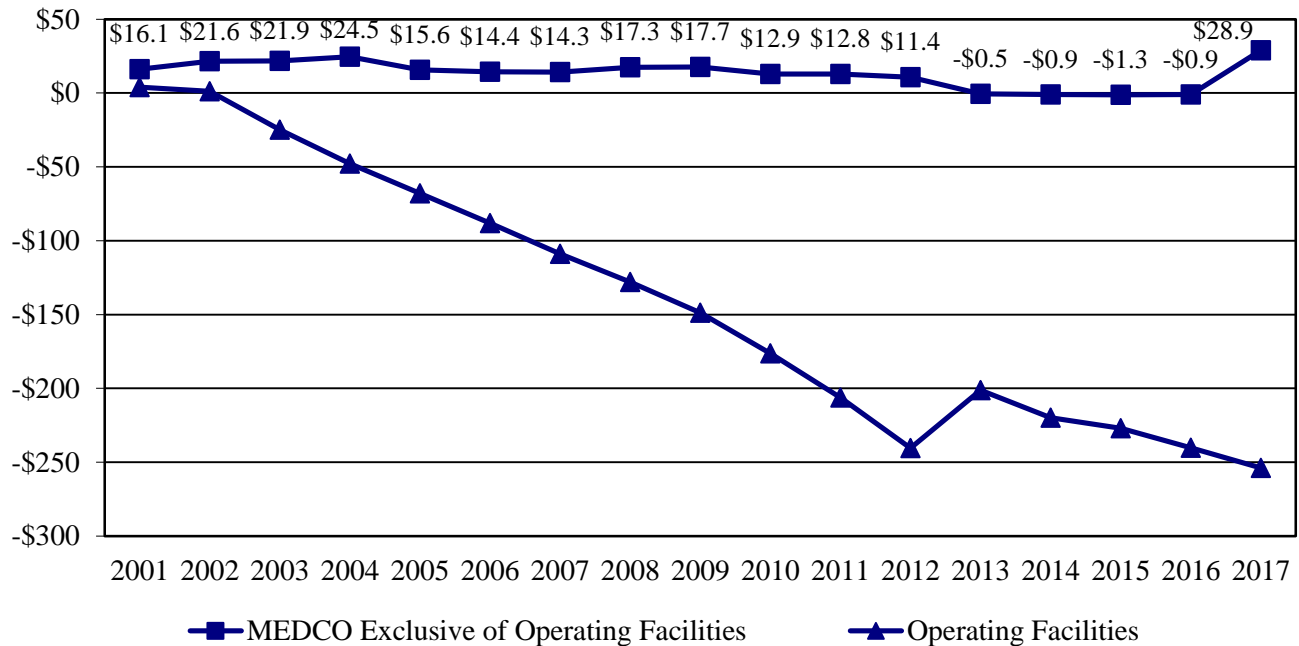
MEDCO Net Assets in a Negative Position

Historically, MEDCO has been involved in two types of projects: (1) operating projects – where MEDCO is involved in management decisions and has a hand in ensuring successful daily operations; and (2) conduit projects – where MEDCO generally serves only as an arms-length financing entity. **Exhibit 1** shows the value of MEDCO net assets with operating facilities extracted. This represents the cumulative effect of year-over-year income deficits.

The net asset 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 (CBCC) and several university housing projects. The net asset deficit is largely the result of adding new operating real estate projects. MEDCO operating projects often have net income deficits as explained above; with the addition of each project, a net income deficit is added to the accounts, which in turn adds to the overall net assets deficit. Conversely, the removal of an operating project (Rocky Gap in fiscal 2013) improves the net asset deficit position.

Also in fiscal 2013, MEDCO started to be more involved in other kinds of projects where MEDCO has property ownership (like operating projects) but no management duties (like conduit projects). The corporation sold the Human Genome Sciences building in fiscal 2017 that resulted in a noncash gain in net assets of \$28.3 million. The recognized gain is the result of the early debt retirement, offset by the depreciated book value of the property. The gain leads to the corporation holding \$28.9 million in non-operating net assets, breaking a four-year run in which the corporation's non-operating net assets were negative.

Exhibit 1
MEDCO Net Assets, Operating, and Non-operating
Fiscal 2001-2017
(\$ in Millions)



MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Operating Facilities Financial Position

Student Housing Projects Bolster Operating Project Net Assets

Exhibit 2 shows the increases and decreases in MEDCO net assets by project. Operating facilities net assets decreased by \$13.7 million in fiscal 2017. As discussed earlier, the decline is not uncommon. This is primarily due to a decline at CBCC, discussed further in the analysis. The Metro Centre project at Owings Mills also saw a decline in net assets of \$2.5 million in fiscal 2017. The corporation notes that the project, governed by a lease/sublease arrangement between the Maryland Transit Administration, MEDCO, and Baltimore County, is funded by a Tax Increment Financing (TIF) district, and that there is a lag from when expenses are incurred on the project to when the TIF revenues are received. The National Cybersecurity Center of Excellence and the

Rockville Innovation Center also saw declines in net assets. However, those declines were partially offset by increases at all but one of MEDCO's university student housing facilities. That sector of the corporation's portfolio saw a \$2.5 million increase in net assets.

Exhibit 2
MEDCO Increase/Decrease in Net Assets by Projects
Fiscal 2015-2017

| | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>Total Net Assets (Deficit) at End of 2017</u> |
|---|---------------------|----------------------|----------------------|--|
| University Student Housing | | | | |
| Morgan State University | \$419,282 | -\$346,323 | \$409,468 | -\$6,920,108 |
| Bowie State University | 451,217 | 931,508 | 223,773 | -4,346,466 |
| Frostburg State University | 130,461 | 148,827 | 190,585 | -3,991,815 |
| Salisbury University | 272,916 | 259,673 | 265,930 | -3,537,999 |
| Towson West | -114,755 | -143,017 | -35,618 | -5,018,529 |
| University of Maryland, Baltimore Campus | -596,563 | 227,440 | 216,568 | -11,255,086 |
| University of Maryland Baltimore County | 457,798 | -58,905 | 861,431 | -1,514,537 |
| University of Maryland, College Park Campus | -1,461,522 | -4,604,699 | 66,092 | -29,590,521 |
| University Village at Sheppard Pratt | 459,380 | 446,142 | 328,280 | -9,715,529 |
| Subtotal | \$18,214 | -\$3,139,354 | \$2,526,509 | -\$75,890,590 |
| Other Facilities | | | | |
| Chesapeake Bay Conference Center (Hyatt Cambridge) | -\$13,844,214 | -\$13,533,707 | -\$15,298,550 | -\$193,880,780 |
| National Cybersecurity Center of Excellence | 7,184,742 | 3,118,711 | -362,042 | 14,737,602 |
| Rockville Innovation Center | -598,027 | -233,440 | -116,698 | -1,525,173 |
| Metro Centre | -1,092,369 | -835,400 | -2,491,411 | -5,496,929 |
| University of Maryland, College Park Campus Energy | 1,196,106 | 1,696,290 | 1,990,176 | 8,959,219 |
| Subtotal | -\$7,153,762 | -\$9,787,546 | -\$16,278,525 | -\$177,206,061 |
| Subtotal Operating Facilities | -\$7,135,548 | -\$12,926,900 | -\$13,752,016 | -\$253,096,651 |
| MEDCO Exclusive of Operating Facilities | -\$319,838 | \$324,110 | \$29,848,913 | \$28,906,738 |
| Elimination (Accounting Adjustment) | \$28,364 | -\$317,070 | \$46,079 | -\$903,666 |
| Grand Total | -\$7,427,022 | -\$12,919,860 | \$16,142,976 | -\$225,093,579 |

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

Four Projects Post Losses

Exhibit 3 shows MEDCO operating income and loss by project. This data indicates where projects are bringing in enough revenues to cover annual operating expenses. Operating facilities' net income decreased to \$12.9 million in fiscal 2017 compared to \$14.9 million in fiscal 2016.

Exhibit 3 MEDCO Operating Income/Loss by Project Fiscal 2015-2017

| | <u>2015</u> | <u>2016</u> | <u>2017</u> |
|--|---------------------|---------------------|---------------------|
| University Student Housing | | | |
| Morgan State University | \$1,743,410 | \$964,441 | \$1,669,499 |
| Bowie State University | 1,721,021 | 1,664,302 | 920,817 |
| Frostburg State University | 766,322 | 768,240 | 794,079 |
| Salisbury University | 1,214,666 | 1,174,635 | 1,143,012 |
| Towson West | 2,140,757 | 2,047,789 | 2,458,869 |
| University of Maryland, Baltimore Campus | 1,456,664 | 1,395,877 | 1,489,558 |
| University of Maryland Baltimore County | 1,681,944 | 1,571,540 | 1,521,694 |
| University of Maryland, College Park Campus | 6,267,049 | 4,699,868 | 5,070,783 |
| University Village at Sheppard Pratt | 1,566,242 | 1,489,706 | 1,362,667 |
| Subtotal | \$18,558,075 | \$15,776,398 | \$16,430,978 |
| Other Facilities | | | |
| Chesapeake Bay Conference Center (Hyatt Cambridge) | -\$3,476,038 | -\$3,171,564 | -\$4,960,606 |
| National Cybersecurity Center of Excellence | -228,934 | -607,657 | -1,171,626 |
| Rockville Innovation Center | -466,367 | -604,127 | -684,569 |
| Metro Centre | -598,775 | 174,479 | -29,962 |
| University of Maryland, College Park Campus Energy | 2,945,018 | 3,305,700 | 3,363,598 |
| Subtotal | -\$1,825,096 | -\$903,169 | -\$3,483,165 |
| Subtotal Operating Facilities | \$16,732,979 | \$14,873,229 | \$12,947,813 |
| MEDCO Exclusive of Operating Facilities | \$983,029 | \$1,437,319 | \$2,372,569 |
| Elimination (Accounting Adjustment) | \$28,364 | -\$317,070 | \$46,079 |
| Grand Total | \$17,744,372 | \$15,993,478 | \$15,366,461 |

MEDCO: Maryland Economic Development Corporation

Source: Maryland Economic Development Corporation

T00A99 – Maryland Economic Development Corporation

According to the corporation's most recent financial statement, the CBCC operating project remains a "nonperforming" project. This designation was made after the June 2014 debt service payment was only partially made. Further, the project fails to meet the debt coverage ratio, as required in the trust indenture covering the bonds.

CBCC is located in Dorchester County and houses a hotel, golf course, and conference facilities. MEDCO had a forbearance agreement with bondholders through December 31, 2017, and is working on a continuation agreement. In recent years, the bond trustee has extended the agreement two or three months after the expiration of the prior period. The corporation expects that to continue.

CBCC scheduled a room improvement plan for the facility to be completed in April 2017. However, delays in furniture delivery kept 75 rooms from being completed by the end of June. The project was put on hold to allow for rooms to be sold during the busy summer travel season and was completed in December. Occupancy declined in fiscal 2017 to 52.6% from 57.3%, partially due to some rooms being unavailable during renovations. MEDCO notes that there is a new leadership team at the facility, including a new general manager, marketing director, food and beverage manager, and events manager. According to the corporation, bookings at CBCC are on pace to improve in fiscal 2018. CBCC is the only nonperforming project, and there are no projects with a "watch" designation.

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.

The Department of Legislative Services recommends that MEDCO comment generally on the status of its operating projects and specifically on the status of CBCC.

Recommended Actions

1. Nonbudgeted.