

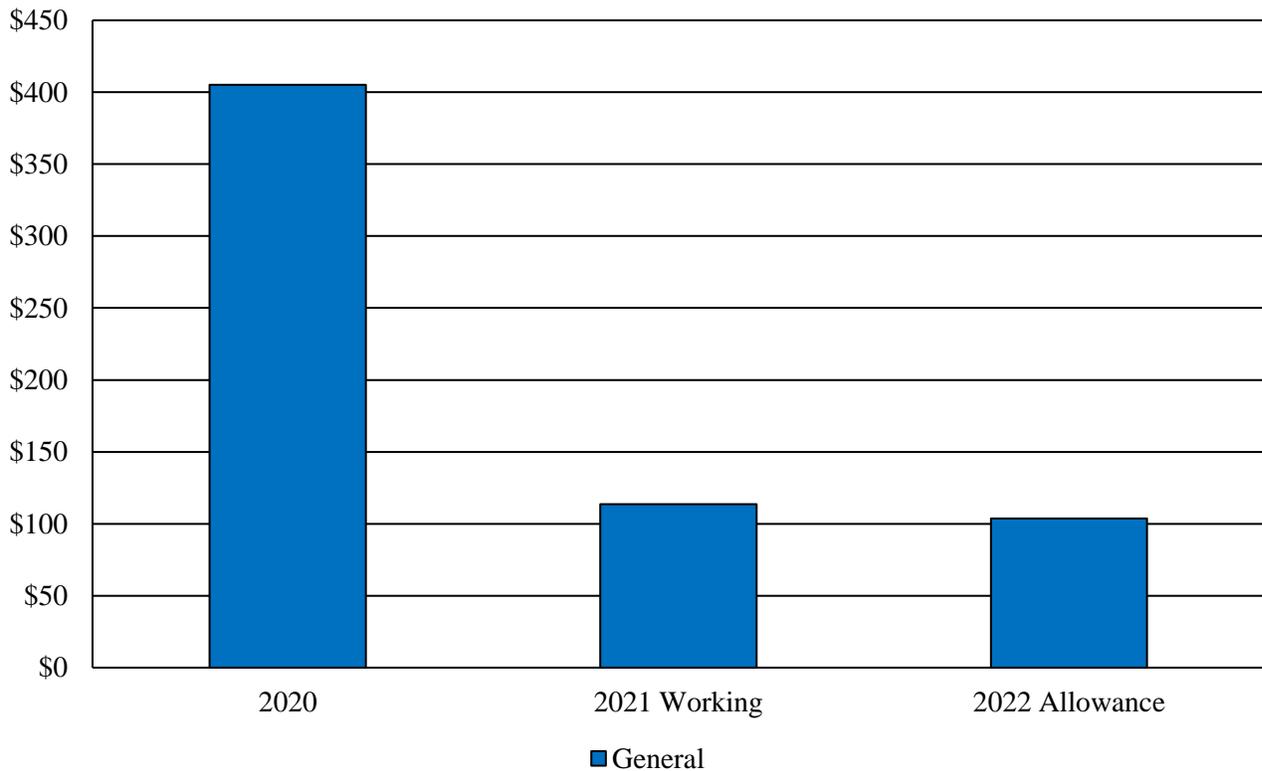
Y01A State Reserve Fund

Program Description

The State Reserve Fund provides a means to designate monies for future use. This analysis includes the Revenue Stabilization Account (Rainy Day Fund), the Dedicated Purpose Account (DPA), and the Catastrophic Event Account. Discussion of the Economic Development Opportunities Account can be found in the analysis of the Department of Commerce (Commerce).

Operating Budget Summary

Fiscal 2022 Budget Decreases \$9.7 Million, or 8.5%, to \$103.8 Million (\$ in Thousands)



Note: Adjustments to the fiscal 2022 allowance include \$515.9 million in contingent reductions.

- Reduced appropriations in fiscal 2021 and 2022 reflect the increased use of the Reserve Fund accounts to balance the General Fund.

For further information contact: Rebecca J. Ruff

Phone: (410) 946-5530

Overview of Agency Spending

Exhibit 1 provides detail on Reserve Fund activity for fiscal 2020 through the fiscal 2022 allowance, including \$515.9 million in contingent reductions.

Exhibit 1 State Reserve Fund Activity Fiscal 2020-2022 Allowance (\$ in Millions)

	<u>Rainy Day Fund</u>	<u>Dedicated Purpose Account</u>	<u>Catastrophic Event Account</u>
<i>Estimated Balances June 30, 2019</i>	\$876.5	\$0.0	\$2.5
Fiscal 2020 Appropriations	\$443.8	\$215.9	\$0.5
Transfer to General Fund	-158.0	0.0	0.0
May 2020 BPW Reductions	0.0	-97.0	0.0
Grant to WMATA	0.0	-75.0	0.0
DHCD Business Loan Repayment	0.0	0.0	0.9
Interest Earnings	14.9	0.0	0.0
<i>Estimated Balances June 30, 2020</i>	\$1,177.2	\$43.9	\$3.9
Fiscal 2021 Appropriations	\$7.0	\$145.0	\$0.0
Transfer to General Fund	-54.0	0.0	0.0
Governor's Economic Recovery Initiative	-250.0	0.0	0.0
July 2020 BPW Reductions	0.0	-38.0	0.0
Fiscal 2020 POS Transfer to General Fund	0.0	-43.9	0.0
Grant to WMATA	0.0	-97.0	0.0
Cybersecurity Assessments	0.0	-10.0	0.0
Interest Earnings	3.9	0.0	0.0
<i>Estimated Balances June 30, 2021</i>	\$884.2	\$0.0	\$3.9
Fiscal 2022 Appropriations	\$525.8	\$93.9	\$0.0
Draw Down Rainy Day Fund to 5%*	-422.0	0.0	0.0
Pension Sweeper*	0.0	-25.0	0.0
OPEB Liability Sweeper*	0.0	-25.0	0.0
Transfer to POS*	0.0	-43.9	0.0
Interest Earnings	3.0	0.0	0.0
<i>Estimated Balances June 30, 2022</i>	\$990.9	\$0.0	\$3.9
<i>Percent of Revenues in Reserve</i>	5.0%		

BPW: Board of Public Works

POS: Program Open Space

DHCD: Department of Housing and Community Development WMATA: Washington Metropolitan Area Transit Authority

OPEB: Other Post Employment Benefits

*Reduction contingent on action in the Budget Reconciliation and Financing Act of 2021.

Source: Department of Budget and Management; Department of Legislative Services

Fiscal 2020

Cost containment actions adopted at the May 20, 2020 Board of Public Works (BPW) meeting in response to the fiscal crisis created by the COVID-19 pandemic deleted \$62 million in funding restricted for legislative priorities and reduced funding for the State’s contribution to the Washington Metropolitan Area Transit Authority (WMATA) capital grant by \$35 million.

Fiscal 2021

In response to the COVID-19 pandemic, the Governor transferred \$250 million out of the Rainy Day Fund by budget amendment in October 2020 to provide economic relief to businesses in need of financial assistance. Funds were allocated to Commerce, the Maryland Department of Labor, the Department of Housing and Community Development, and the Maryland Technology Development Corporation. More on the specific allocation of these funds and impact to the Rainy Day Fund balance is discussed in the Key Observations section of this analysis.

Cost Containment

Cost containment actions adopted at the July 1, 2020 BPW meeting in response to the fiscal crisis created by the COVID-19 pandemic deleted \$10 million in funding for cybersecurity assessments and reduced funding for the State’s contribution to the WMATA capital grant by \$28 million.

Fiscal 2022 Proposed Budget

The fiscal 2022 allowance provides a total appropriation of \$619.7 million in general funds to the State Reserve Fund, before accounting for \$515.9 million in proposed reductions, contingent on provisions proposed in the Budget Reconciliation and Financing Act (BRFA) of 2021 (HB 589/SB 493).

The statutory sweeper provision for the Rainy Day Fund, which requires that the Administration appropriate an amount to the Rainy Day Fund equal to any unassigned general fund balance at closeout in excess of \$60 million (\$10 million reserved in the General Fund and \$50 million diverted to outstanding pension and other retired employee benefit liabilities), requires an appropriation of \$525.8 million. This is reduced by a \$422.0 million contingent reduction to reduce the fund balance to 5.0% of general fund revenues. Absent this reduction, the Rainy Day Fund balance would be projected to close fiscal 2022 with a fund balance of \$1.4 billion (7.1% of general fund revenues). With the reduction, the Rainy Day Fund is projected to close with a fund balance of \$991 million.

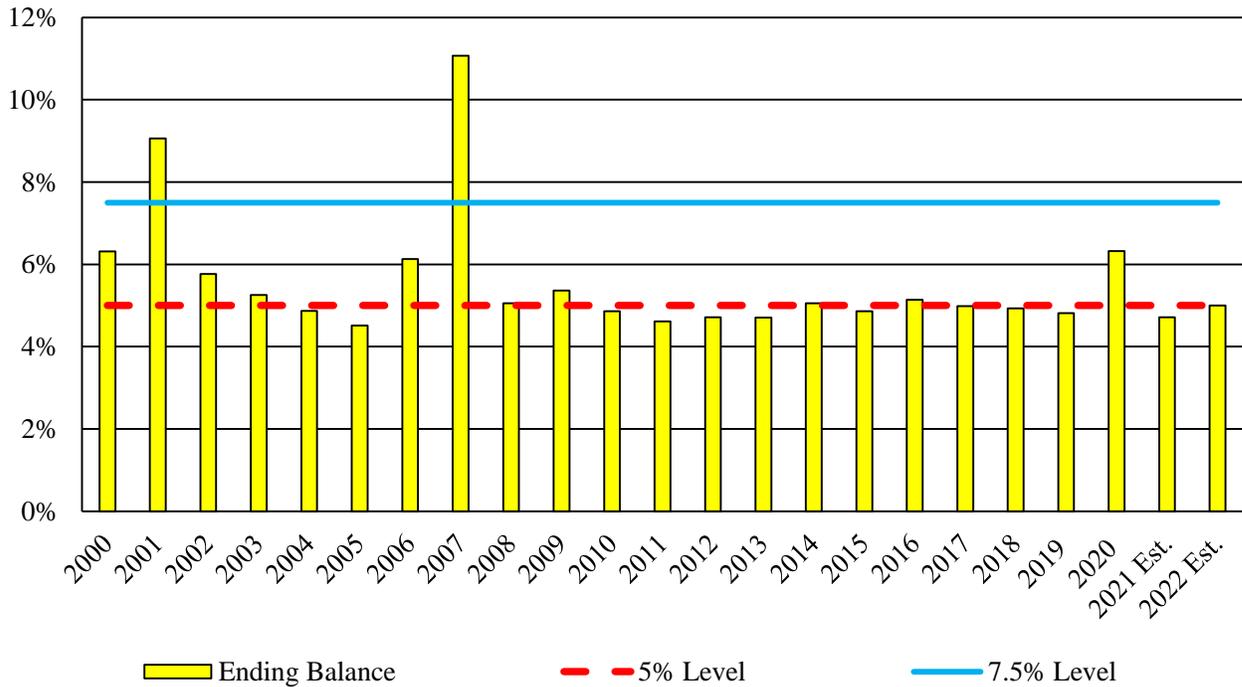
The fiscal 2022 allowance allocates \$93.9 million in general funds to the DPA to meet statutory mandates for reducing the previously mentioned unfunded pension and retired employee benefit liabilities (\$50 million) and funding repayment of previously borrowed transfer taxes otherwise used to fund Program Open Space (POS) (\$43.9 million). The BRFA proposes to delete funding for all three mandates in fiscal 2022. The transfer tax repayment is further modified to extend repayment until fiscal 2032. Additional discussion regarding the transfer tax and POS can be found in the analysis for the Department of Natural Resources.

Key Observations

1. Use of the Rainy Day Fund Has a History of Staving Off Fiscal Storms

Section 7-311 of the State Finance and Procurement Article establishes a target reserve balance of 7.5% of estimated general fund revenues. The Governor is authorized to expend balances down to 5.0% in the annual budget bill, which has been the case periodically over the past two decades as the State grappled with cash and structural deficits. **Exhibit 2** provides the actual and estimated closing balances in the Rainy Day Fund since fiscal 2000.

Exhibit 2
Rainy Day Fund End-of-year Balances
 Fiscal 2000-2022 Est.

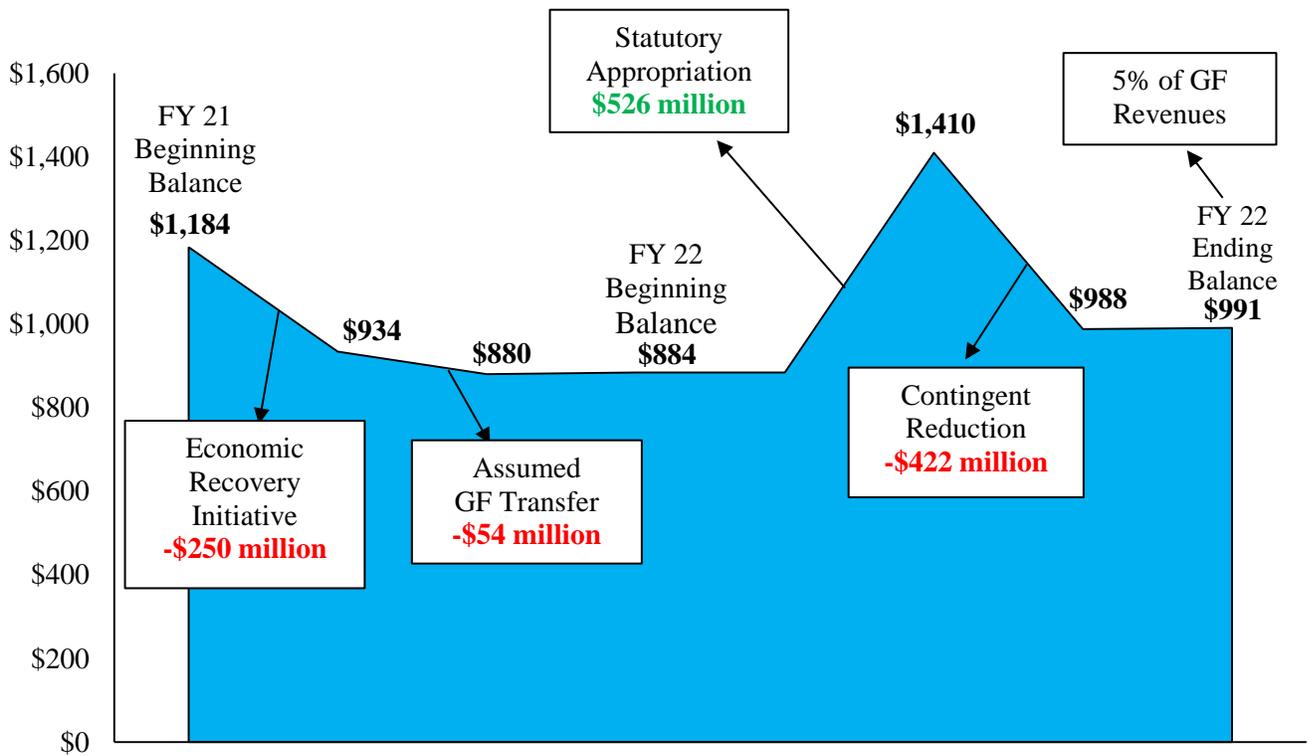


Source: Department of Legislative Services

The fund breached the 7.5% goal twice in the past two decades, reaching a peak of 11.0% in fiscal 2007 that was subsequently drawn down to 5.0% to aid in balancing the fiscal 2008 budget at the start of the Great Recession. The balance has breached the 5% targeted threshold 10 times in the past 25 years, including the projected closing balance for the current fiscal year. The diversion of \$284 million from the statutory appropriation, combined with the transfer of an additional \$54 million to create positive general fund balance in fiscal 2021, brought the projected Rainy Day Fund balance

down to an estimated 6% of general fund revenues at the close of the fiscal 2020 session. The use of an additional \$250 million in fund balance for the Administration’s Economic Recovery Initiative to provide business assistance in response to the COVID-19 pandemic reduced the balance to 4.7%. Emergency powers granted to the Governor with the declared state of emergency due to the pandemic allow the Governor to breach the 5% threshold without legislative input via a BRFA provision. **Exhibit 3** illustrates the recent activity occurring within the Rainy Day Fund since the beginning of fiscal 2021. **Exhibit 4** provides a summary of how the \$250 million in funds for the Economic Recovery Initiative were allocated. Additional information on the use of those funds is discussed in the respective agency analyses.

Exhibit 3
Fund Balance Activity Rainy Day Fund
Fiscal 2021-2022
(\$ in Millions)



GF: General Fund

Source: Department of Legislative Services

Exhibit 4
Maryland Strong: Economic Recovery Initiative

<u>Program</u>	<u>Agency</u>	<u>\$ in Millions</u>
Restaurant Relief	Commerce	\$80
COVID-19 Emergency Grant Program	Commerce	50
Support for Hotels/Hospitality Businesses	Commerce	50
Relief for Main Street Communities	DHCD	35
Layoff Aversion Program	MDL	20
Rural Businesses	TEDCO	5
MSBDFA	Commerce	5
Emergency Arts Grants	Commerce	3
Hometown Tourism Program	Commerce	2
Total		\$250

Commerce: Department of Commerce

DHCD: Department of Housing and Community Development

MDL: Maryland Department of Labor

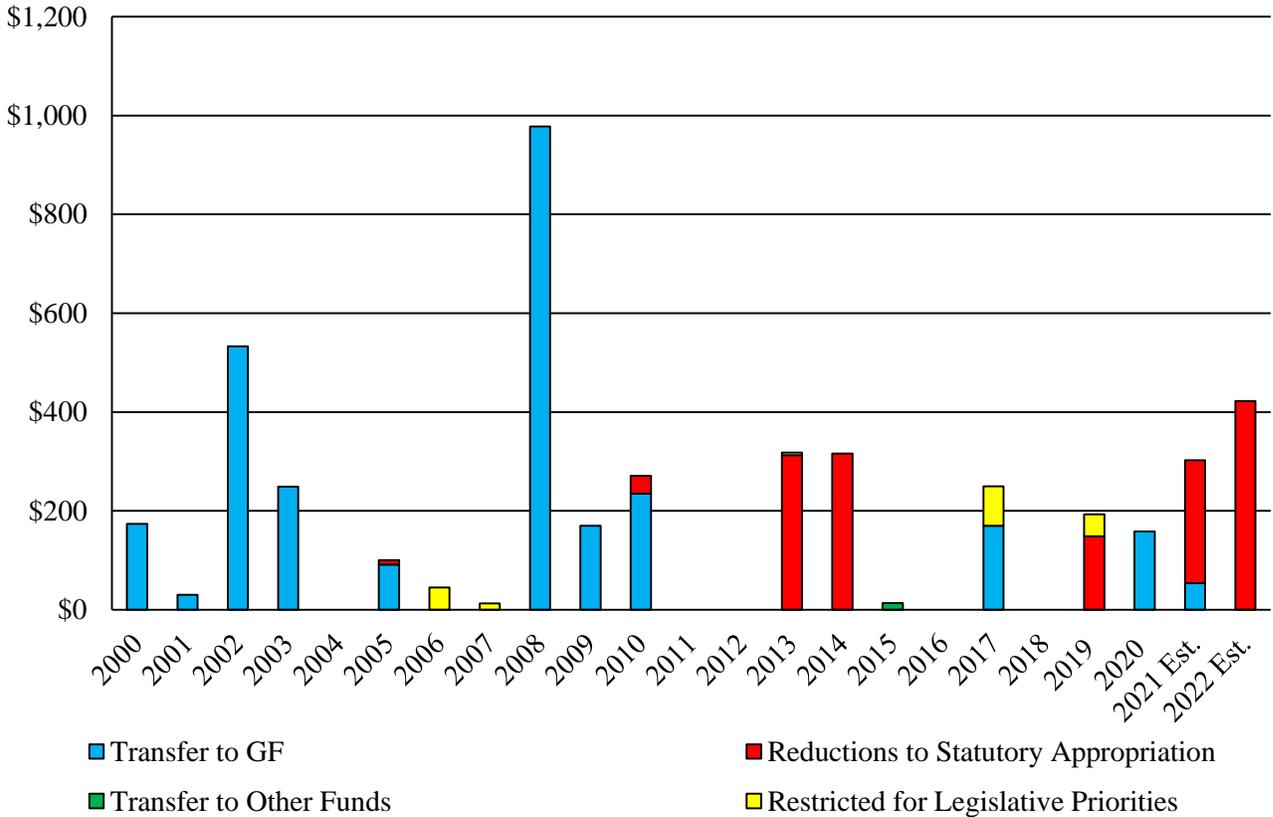
MSBDFA: Maryland Small Business Development Financing Authority

TEDCO: Maryland Technology Development Corporation

Source: Department of Budget and Management

The use of funds that would otherwise be held in what is essentially the State’s savings account is extremely common. Although the State has been very careful to avoid regularly dipping below the 5% goal, **Exhibit 5** shows that in all but 5 of the last 25 years, the State has accessed the Rainy Day Fund to avoid general fund deficits or fund priority programs and projects that would otherwise require general fund expenditures to complete. The cumulative total of funds diverted from the Rainy Day Fund balance since fiscal 2000 is approximately \$4.5 billion.

**Exhibit 5
Funds Diverted from the Rainy Day Fund
Fiscal 2000-2022 Est.
(\$ in Millions)**



GF: General Fund

Source: Department of Legislative Services

2. COVID-19 Pandemic Response and the Local Income Tax Reserve Fund

The BRFA of 2021 includes a provision to authorize certain State agencies, primarily the Maryland Department of Health, to temporarily charge expenditures related to the COVID-19 response that are eligible for reimbursement from the Federal Emergency Management Agency’s (FEMA) Public Assistance process to the Local Income Tax Reserve (LITR) Account. It further requires that the LITR be reimbursed once FEMA revenues are received, and if any charges are not fully reimbursed by FEMA Public Assistance, they will be reimbursed by the General Fund. The provision is effective

Y01A – State Reserve Fund

until the end of fiscal 2022 or until FEMA has made a final determination on all expenses charged against the LITR.

The State maintains the LITR for holding and disbursing income taxes collected by the State for local jurisdictions. According to generally accepted accounting principles, the State is supposed to maintain a sufficient fund balance to pay future refunds realized during the fiscal year in case the income tax is no longer collected. If the account is insufficiently capitalized at the end of a fiscal year, the State is required to report the underfunding as an unfunded liability in the *Comprehensive Annual Financial Report* (CAFR). If the State has a plan in place to reimburse the account, the State does not need to show an unfunded liability in the CAFR.

The State has transferred funds from this account to support general fund spending on four occasions since fiscal 2009. As of January 2020, the unfunded liability was \$738.6 million. Repayment plans are in place for two of the transfers and to continue to address the outstanding liability. **Appendix 2** provides a summary of repayment plans to the account. The cash balance as of December was \$1.5 billion due in part to the fact that distributions are not made to the local governments in December (or April). At the end of November, the cash balance was \$956 million.

FEMA's Public Assistance program requires the State to fund 100% of disaster relief costs and then request reimbursement for 75% of eligible expenses. The provision would allow the State to forward fund the 75% of costs expected to be reimbursed from the LITR, freeing up general fund resources to be used elsewhere. The State has an estimated \$550 million in fiscal 2020 expenses related to the COVID-19 pandemic response that are believed to be eligible for FEMA reimbursement. To date, \$341 million has been received, leaving approximately \$209 million in spending to potentially be charged against the LITR in order to close out fiscal 2020. The current estimated funding request for fiscal 2021 is \$200 million.

Despite the sizable fund balance, there is some concern that there will not be enough funds in the account to make the necessary monthly distributions, which average \$550 million per month over the next six months. The Comptroller has indicated that local distributions will be made on time and that if the account were for some reason short, it would come out of the general fund side of the income tax that month, even if that meant showing a negative general fund amount.

Operating Budget Recommended Actions

1. Adopt the following narrative:

Repayment of the Catastrophic Event Account and the Small, Minority, and Women-Owned Businesses Account: In September 2016, \$2.5 million was transferred from the Catastrophic Event Account, and \$2.3 million was transferred from the Small, Minority, and Women-Owned Businesses Account (SMWOBA) into the Department of Housing and Community Development (DHCD) Neighborhood BusinessWorks program to provide loans to businesses in Ellicott City. Another \$2.5 million was transferred from the Catastrophic Event Account in July 2018. As part of its review of the transfer of funds from the Catastrophic Event Account, the Legislative Policy Committee recommended that DHCD develop a process by which the funds or repaid loans are credited to the Catastrophic Event Account. DHCD and the Department of Budget and Management (DBM) should submit a report that provides data regarding the number and amount of loans provided, the outstanding balance of these loans, and the number and amount of any forgiven loans. This report should be submitted to the budget committees by January 15, 2022.

Information Request	Authors	Due Date
Report on Catastrophic Event Account and SMWOBA repayment	DHCD DBM	January 15, 2022

Appendix 1
2020 Joint Chairmen’s Report Responses from Agency

The 2020 *Joint Chairmen’s Report* (JCR) requested one report for the State Reserve Fund. Electronic copies of the full JCR responses can be found on the Department of Legislative Services Library website.

- ***Repayments to the Catastrophic Event Account and Small, Minority, and Women-Owned Businesses Account:*** In 2016 and again in 2018, Ellicott City was struck by natural/flooding disasters causing severe damage to the downtown area and its businesses. The State provided loan assistance in form of \$5.0 million from the Catastrophic Event Account and \$2.3 million from the Small, Minority, and Women-Owned Businesses (SMWOBA) account. In response to committee narrative in the 2020 JCR, the Department of Budget and Management and the Department of Housing and Community Development submitted an accounting of the funds that have been repaid to date. Of the \$5.0 million loaned from the Catastrophic Event Account, \$1.5 million went unused and was reverted to the fund, and \$1.3 million has been repaid through December 2020. Of the \$2.3 million from SMWOBA, \$719,000 went unused, and \$459,000 has been repaid. Due to the COVID-19 pandemic, all loans are in deferral status until September 2021.

Appendix 2
Local Income Tax Reserve Account
Repayments and Unfunded Liabilities
(\$ in Millions)

<u>Fiscal Year</u>	<u>Amount</u>	<u>Purpose</u>	<u>Repayment Status</u>
2009	\$366.8	Transfer to General Fund	Repayment cancelled (unfunded liability)
2010	350.0	Transfer to General Fund	Repayment cancelled (unfunded liability)
2016-2017	21.8	Overdistribution of funds to local governments	Repayment cancelled (unfunded liability)
2011	200.0	Transfer to General Fund	\$10 million annual revenue transfer for fiscal 2024 to 2043
2015	100.0	Transfer to General Fund	\$10.0 million annual revenue transfer for fiscal 2016 through 2025
2016	249.6	Required refunds from Wynne verdict	Beginning in May 2021, local jurisdictions are required to repay funds directly or Comptroller will reduce the quarterly distribution for a total of 80 quarterly payments

Note: Chapter 10 of 2018 extended the \$10.0 million revenue transfer reimbursement from 2015 indefinitely to reduce the total unfunded liability. Because there is a statutory payment plan for the 2010 and 2015 transfers and the Wynne refunds, they are not part of the unfunded liability, and the Comptroller recognizes a receivable to the account for each. The total unfunded liability is currently \$738.6 million.

**Appendix 3
Object/Fund Difference Report
State Reserve Fund**

<u>Object/Fund</u>	<u>FY 20 Actual</u>	<u>FY 21 Working Appropriation</u>	<u>FY 22 Allowance</u>	<u>FY 21 - FY 22 Amount Change</u>	<u>Percent Change</u>
Objects					
12 Grants, Subsidies, and Contributions	\$ 405,161,213	\$ 114,000,000	\$ 619,649,432	\$ 505,649,432	443.6%
Total Objects	\$ 405,161,213	\$ 114,000,000	\$ 619,649,432	\$ 505,649,432	443.6%
Funds					
01 General Fund	\$ 405,161,213	\$ 114,000,000	\$ 619,649,432	\$ 505,649,432	443.6%
Total Funds	\$ 405,161,213	\$ 114,000,000	\$ 619,649,432	\$ 505,649,432	443.6%

Note: The fiscal 2021 appropriation does not include deficiencies, targeted revenues, or across-the-board reductions. The fiscal 2022 allowance does not include contingent reductions or cost-of-living adjustments.