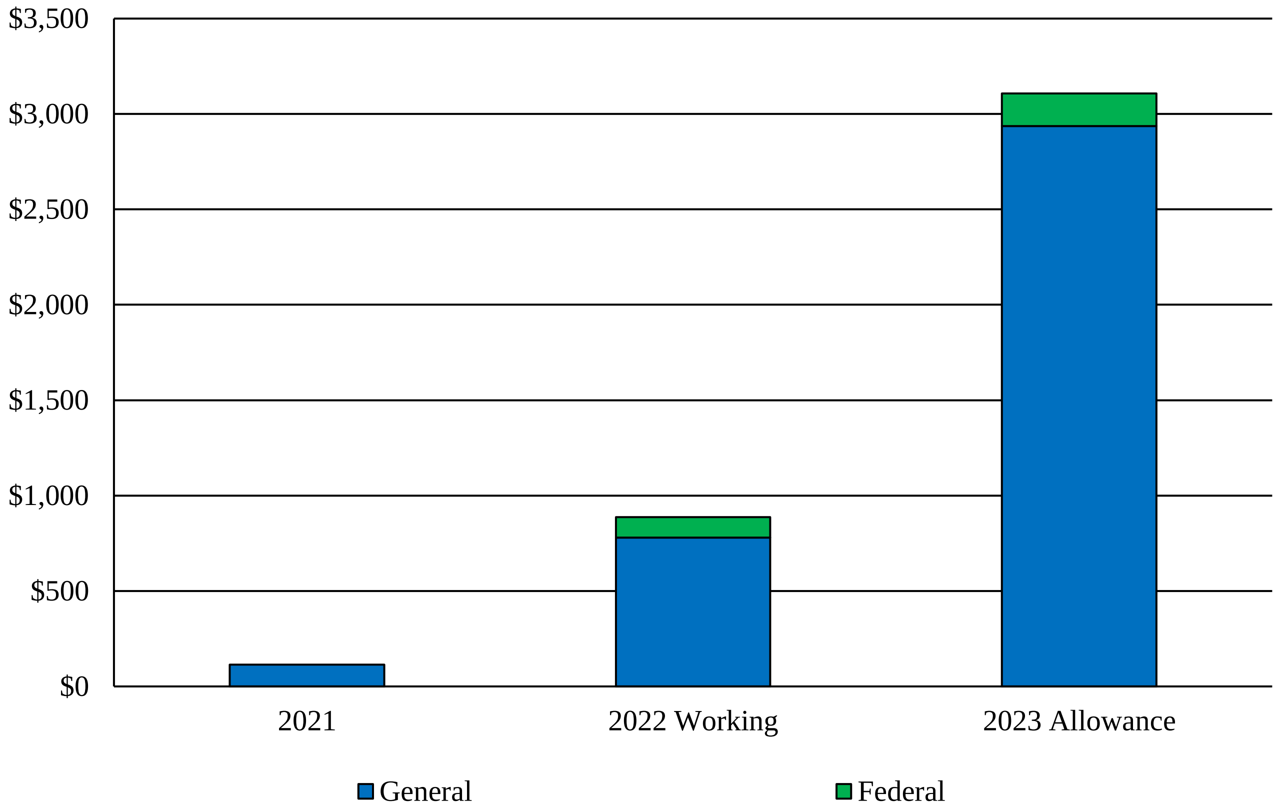
Y01A
State Reserve Fund

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. **Appendix 2** through **Appendix 4** provide detail on the characteristics and spending mechanisms for each account. Discussion of the Economic Development Opportunities Account can be found in the analysis of the Department of Commerce.

Operating Budget Summary

Fiscal 2023 Budget Increases $2.2 Billion, or 250%, to $3.1 Billion
($ in Millions)



- Better than anticipated revenues at fiscal 2021 closeout requires a statutory appropriation to the Rainy Day Fund of more than $2.4 billion in fiscal 2023.

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Fiscal 2022

Proposed Deficiency

Several deficiency appropriations combine to reduce fiscal 2022 funding in the Reserve Fund accounts by a total of $89.7 million. **Exhibit 1** provides detail on the individual items.

Exhibit 1
Fiscal 2022 Deficiency Appropriations

Budget Code	Account	Fund	Description	Amount
Y01A02.01	DPA	FF – ARPA	Realigns transitional supplemental instruction funding to MSDE in fiscal 2023.	-$46,000,000
Y01A02.01	DPA	FF – ARPA	Realigns public school HVAC funding to IAC in fiscal 2023.	-40,000,000
Y01A02.01	DPA	FF – ARPA	Realigns apprenticeship/employment training funding to MDL in fiscal 2023.	-37,500,000
Y01A02.01	DPA	FF – ARPA	Reduces funds for broadband infrastructure and deployment.	-71,223,815
Y01A02.01	DPA	FF – ARPA	Realigns IT improvement/teleworking funding to DoIT in fiscal 2023.	-5,000,000
Y01A02.01	DPA	GF	Cybersecurity assessments, mitigation efforts, and software tools for state agencies.	100,000,000
Y01A04.01	CEA	GF	Restore account in line with historic balances.	10,000,000
Total				**-$89,723,815**

ARPA: American Rescue Plan Act of 2021
CEA: Catastrophic Event Account
DoIT: Department of Information Technology
DPA: Dedicated Purpose Account
FF: federal funds
GF: general funds
IAC: Interagency Commission on School Construction
IT: information technology
MDL: Maryland Department of Labor
MSDE: Maryland State Department of Education

Source: Governor's Fiscal 2023 Budget Books

Nearly $200 million in federal American Rescue Plan Act (ARPA) funds are realigned from the DPA in fiscal 2022 to the respective agencies responsible for expending those funds in fiscal 2023. Offsetting those reductions is a $10 million general fund appropriation to restore the fund balance for the Catastrophic Event Account after it was depleted in response to Tropical Storm Ida and $100 million in general funds for cybersecurity assessments, mitigation efforts, and software tools.

There is no specific spending plan for the cybersecurity funds. The DPA currently has a $10 million balance in unspent cybersecurity funding appropriated in fiscal 2021. The use of those funds was delayed due to the COVID-19 pandemic. Funds budgeted in the DPA can be spent across several fiscal years. Although the Department of Information Technology (DoIT) is involved in the planning and coordinated use of these funds, it is likely that significant portions will be allocated directly to State agencies, as the need for these funds is prompted by a significant cyberattack on the Maryland Department of Health (MDH) that occurred in December 2021.

Overview of Agency Spending

Exhibit 2 provides detail on the Reserve Fund activity for fiscal 2021 through the 2023 allowance.

Exhibit 2
State Reserve Fund Activity
Fiscal 2021-2023 Allowance
($ in Millions)

	Rainy Day Fund	Dedicated Purpose Account[1]	Catastrophic Event Account
Estimated Balances June 30, 2020	***$1,177.2***	***$43.9***	***$3.8***
Fiscal 2021 Appropriations	$7.0	$145.0	$0.0
Governor's Economic Recovery Initiative	-556.0	0.0	0.0
July 2020 Board of Public Works Reductions[2]	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	2.9	0.0	0.0
Estimated Balances June 30, 2021	***$631.2***	***$0.0***	***$3.8***
Fiscal 2022 Appropriations	$525.8	$561.7	$10.0
Legislative Priorities Funded with ARPA	0.0	-317.8	0.0
OPEB Liability/Pension Sweepers	0.0	-50.0	0.0
State Center Relocation	0.0	-50.0	0.0
Transfer to POS	0.0	-43.9	0.0
Cybersecurity Assessments	0.0	-100.0	0.0
Tropical Storm Ida Recovery Assistance	0.0	0.0	-3.8
Interest Earnings	3.2	0.0	0.0
Estimated Balances June 30, 2022	***$1,160.2***	***$0.0***	***$10.0***
Fiscal 2023 Appropriations	$2,415.8	$692.0	$0.0
LGIF – Broadband	0.0	-171.2	0.0
Food Banks	0.0	-10.0	0.0
OPEB Liability/Pension Sweepers	0.0	-50.0	0.0
Facilities Renewal	0.0	-200.0	0.0
Transfer to POS	0.0	-30.5	0.0
New Veterans Home PAYGO	0.0	-63.3	0.0
Grant to WMATA	0.0	-167.0	0.0
Interest Earnings	11.8	0.0	0.0
Estimated Balances June 30, 2023	**$3,587.8**	**$0.0**	**$10.0**
Percent of Revenues in Reserve	***15.7%***		

ARPA: American Rescue Plan Act
LGIF: Local Government Infrastructure Fund
OPEB: Other Post Employment Benefits
PAYGO: pay-as-you-go
POS: Program Open Space
WMATA: Washington Metropolitan Area Transit Authority

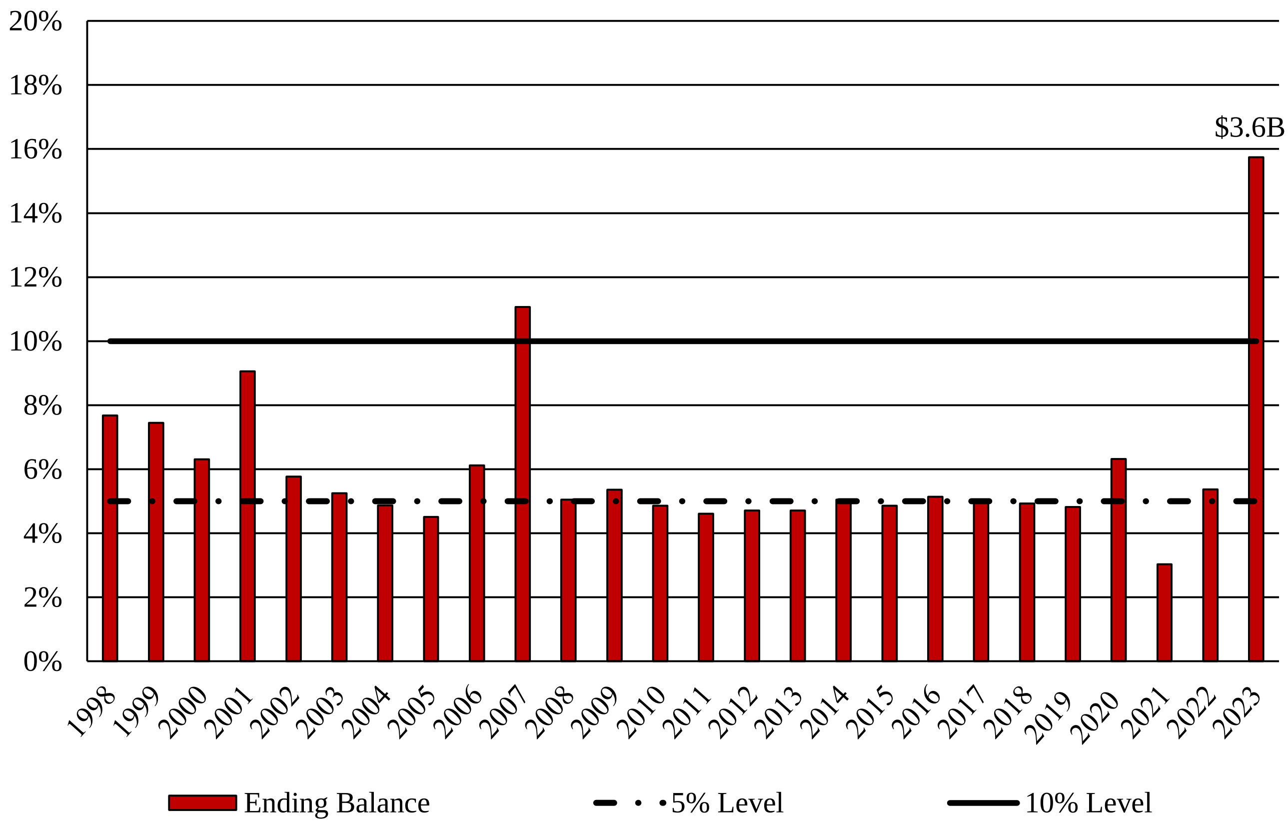
[1] It is customary for the Governor's Budget Books to reflect the assumption that all appropriations to the Dedicated Purpose Account are expended in the year appropriated. Statute allows for the expenditure of funds to occur over a period not to exceed five fiscal years.
[2] Cost containment actions adopted at the July 1, 2020 Board of Public Works meeting deleted $10 million in funding for cybersecurity assessment and reduced the State's contribution to the WMATA capital grant by $28 million.

Source: Governor's Budget Books; Department of Legislative Services

Rainy Day Fund

The statutory sweeper provision for the Rainy Day Fund 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). Fiscal 2021 revenues outperformed estimates by $1.7 billion at closeout, contributing to a statutorily required $2.4 billion appropriation to the Rainy Day Fund in fiscal 2023. As **Exhibit 3** shows, this results in an unprecedented $3.6 billion balance projected for the fund at the end of the allowance year, equating to 15.7% of general fund revenues. This is approximately $1.5 billion above the 9% balance recommended by the Spending Affordability Committee (SAC) in its 2021 interim report.

Exhibit 3
Rainy Day Fund Balance as a Percent of General Fund Revenues
Fiscal 1998-2023



Source: Department of Legislative Services

Dedicated Purpose Account

The DPA was established to retain appropriations for major, multi-year expenditures where the magnitude and timing of cash needs are uncertain and to meet expenditure requirements that may be affected by changes in federal law or fiscal policies or other contingencies. Activity in the DPA has increased considerably in fiscal 2022 and 2023, with appropriations exceeding $500 million in both years and including a significant amount of federal stimulus funds.

Annual Appropriations

The DPA includes several appropriations that appear annually. In the fiscal 2023 allowance, these appropriations total $247.5 million in general funds. This includes $25 million each to meet statutory mandates for reducing unfunded pension and retired employee benefit liabilities ($50 million total) and $30.5 million to fund repayment of previously borrowed transfer taxes otherwise used to fund Program Open Space. The allowance also includes $167 million to fund the entire mandated dedicated capital grant for the Washington Metropolitan Area Transit Authority required by Chapters 351 and 352 of 2018.

One-time Appropriations

Approximately $317.8 million in federal ARPA funding for legislative priorities was included in the DPA in fiscal 2022, along with $50 million in general funds to support the relocation of State agencies from the State Center property to other areas in Baltimore City. As previously discussed, fiscal 2022 deficiency appropriations provided in the proposed budget amend the DPA working appropriation by adding $100 million in general funds for cybersecurity initiatives and reducing federal stimulus funding by nearly $200 million to properly appropriate the funds in fiscal 2023. In addition, the Administration processed budget amendments during the fiscal year to reallocate $5 million to the Judiciary for fees incurred by offenders placed in home detention during the COVID-19 pandemic and $5 million to DoIT for teleworking improvements. As highlighted in **Exhibit 4**, over $258 million remains in the DPA in fiscal 2022.

Exhibit 4
Dedicated Purpose Account Funding Detail
Fiscal 2022
($ in Millions)

	Appropriation	Transfers Out	Remaining
Pension Sweeper	$25.0	-$25.0	$0.0
Other Post Employment Benefits Sweeper	25.0	-25.0	0.0
Program Open Space Repayment	43.9	-43.9	0.0
Cybersecurity	100.0		100.0
State Center Relocation	50.0		50.0
Subtotal General Funds	***$243.9***	***-$93.9***	***$150.0***
Municipal Broadband Access	$45.0		$45.0
Broadband Infrastructure Deployment	97.6	-$71.2	26.4
Rural Broadband and Digital Connectedness	23.7		23.7
Digital Inclusion Fund	2.0		2.0
Community-based Solutions for Gap Networks	5.0		5.0
USM Digital Divide	4.0		4.0
Fiscal 2023 Digital Navigator Program	2.0		2.0
Fiscal 2023 Public School HVAC	40.0	-40.0	0.0
Fiscal 2023 Transitional Supplemental Instruction	46.0	-46.0	0.0
IT Improvements and Teleworking	10.0	-10.0	0.0
Apprenticeship/Employment Training	37.5	-37.5	0.0
Home Detention Fees	5.0	-5.0	0.0
Subtotal Federal Stimulus Funds	***$317.8***	***-$209.7***	***$108.1***
Total	**$561.7**	**-$303.6**	**$258.1**

IT: information technology
USM: University System of Maryland

Source: Department of Legislative Services

Aside from the new funding provided in the cybersecurity deficiency appropriation, remaining fiscal 2022 appropriations primarily support future broadband expenditures (discussed in more detail in the Department of Housing and Community Development – S00A analysis) and the future need for moving expenses as State agencies begin relocating from State Center in early fiscal 2024. **Exhibit 5** outlines the relocation schedule per a Department of General Services *Joint Chairmen's Report* (JCR) response submitted in November 2021.

Exhibit 5
State Center Relocation Schedule

Agencies	RFP Schedule	Move Schedule
State Department of Assessments and Taxation	October 13, 2021	Fall 2023
Comptroller	November 2021	Fall 2023
Maryland Department of Health	November 2021	Fall 2023
Department of Budget and Management and MDOA	December 2021	Winter 2023
Maryland Department of Planning and Tax Court	January 2022	Winter 2024
MDL, DoIT, and MDOD – Telephone Relay	February 2022	Winter 2024

DoIT: Department of Information Technology
MDL: Maryland Department of Labor
MDOA: Maryland Department of Aging
MDOD: Maryland Department of Disabilities
RFP: request for proposals

Source: Department of General Services

The fiscal 2023 allowance appropriates $444.5 million to the DPA for expenses of a one-time, multi-year purpose, all but $10 million of which is capital pay-as-you-go (PAYGO) funds. There is $10 million allocated for one-time funding to continue supporting food banks through the pandemic. There is no allocation or timeline for expenditures as the food banks are still estimated to have federal resources available to prioritize before the State funds are awarded.

PAYGO funding provides $200 million for strategic investments in facility renewal and maintenance projects. **Exhibit 6** illustrates how the funding is allocated for State buildings, parks, and higher education.

Exhibit 6
Facility Renewal Funding
Fiscal 2023
($ in Millions)

	Allowance
State Agencies and Parks	
Department of General Services Facilities Renewal	$75
Department of Natural Resources Critical Maintenance	25
Subtotal: Statewide Facilities Renewal and Critical Maintenance	***$100***
Higher Education Facilities	
University System of Maryland Capital Facilities Renewal	$65
Community College Facilities Renewal	15
Morgan State University Deferred Maintenance and Site Improvements	10
St. Mary's College of Maryland Campus Infrastructure Improvements	5
Baltimore City Community College Deferred Maintenance	5
Subtotal: Higher Education	***$100***
Total Strategic Investments in Facility Renewal	**$200**

Source: Fiscal 2023 *Capital Improvement Program*; Governor's Budget Books

In addition, PAYGO funding in the DPA includes $171.2 million in federal funds from the Coronavirus Capital Projects Fund for Connect Maryland (formerly Broadband Infrastructure Grants) to support construction of new networks to unserved areas of 500 to 1,500 households. Approximately $63.3 million is provided to construct a new 128-bed skilled nursing facility for veterans in Sykesville, Maryland. This project is eligible for a federal grant to fund 65% of total expenditures; the funds in the DPA represent the State's general fund commitment for the project.

Key Observations

1. SAC Recommends Adopting Criteria for Future Rainy Day Fund Use

In response to the significant correction of the State's fiscal situation in fall 2021, SAC recommended utilizing a sizeable portion of available resources for one-time expenses, including capital PAYGO. The Administration's budget proposal responds with over $900 million in general fund PAYGO, $284 million of which is budgeted in the DPA. Governor Lawrence J. Hogan, Jr.'s plan also leaves an unprecedented amount of funding in the Rainy Day Fund for future use. In looking at the Administration's out-year general fund forecast and *Capital Improvement Program*, however, a portion of this future set-aside is not saved for a projected downturn but rather is used as an offset to the revenue reductions realized from implementing the proposed tax relief plan and to continue supporting an enhanced capital program.

The Administration's plan shows that approximately 75% of the over $400 million annually planned for PAYGO in fiscal 2025 through 2027 is supported by withdrawing $300 million each year from the Rainy Day Fund. Supporting this out-year commitment of funds is potentially troublesome in that it limits the amount of funds that could be diverted from the sizeable fiscal 2023 appropriation for other purposes. This plan commits $900 million of the $1.5 billion above the recommended SAC balance of 9% of general fund revenues. In addition, this would be setting a precedent of drawing down the fund balance of what is effectively the State's savings account to support capital projects as opposed to the more common practice of redirecting new appropriations into the fund for other priorities.

Although the historically high $3.6 billion fund balance achieved by committing the entire statutory appropriation to the fund may be larger than is necessary to protect the State against a moderate recession, this potential situation posed in the Governor's out-year plans is an example of why **the General Assembly may wish to establish general principles for when and for what purposes to withdraw funds from the Rainy Day Fund, along with the mechanisms for doing so**. This is consistent with the SAC recommendation made during the 2021 interim.

Recommended Guiding Principles

The Department of Legislative Services (DLS) recommends three guiding principles in establishing parameters for the Rainy Day Fund:

(1) maintain a balance that equates to 10% of general fund revenues when State revenues are stable or growing;

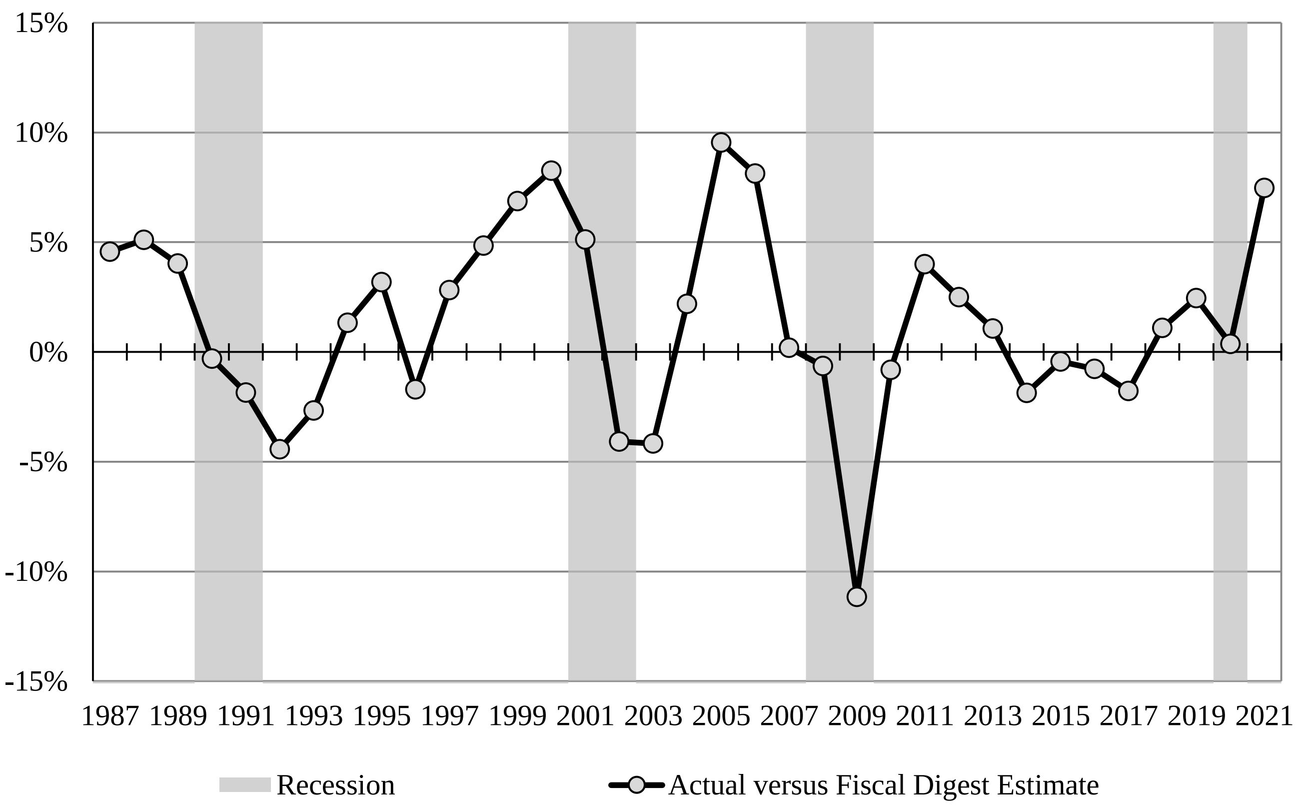
(2) use of reserves should be tied to a downward revision in the general fund revenue forecast; and

(3) funds should be withdrawn incrementally.

With the exception of a brief period at the end of fiscal 2021 when the Rainy Day Fund was tapped to support the RELIEF Act, Maryland has maintained a balance equivalent to at least 5% of general fund revenues in the Rainy Day Fund since the mid-1990s. During the Great Recession, State leaders elected not to draw the balance in the fund below 5% despite unprecedented revenue write-downs, instead opting to rely on dedicated funds and available balances from other various accounts. These funds have not necessarily been replenished in the subsequent years.

Having established the precedent of maintaining a 5% balance during more severe economic times has also deterred the use of the Rainy Day Fund during less severe downturns as well. Historically, however, revenues have been shown to fall by approximately 10% compared to the estimates in the first two years, as reflected in **Exhibit 7**.

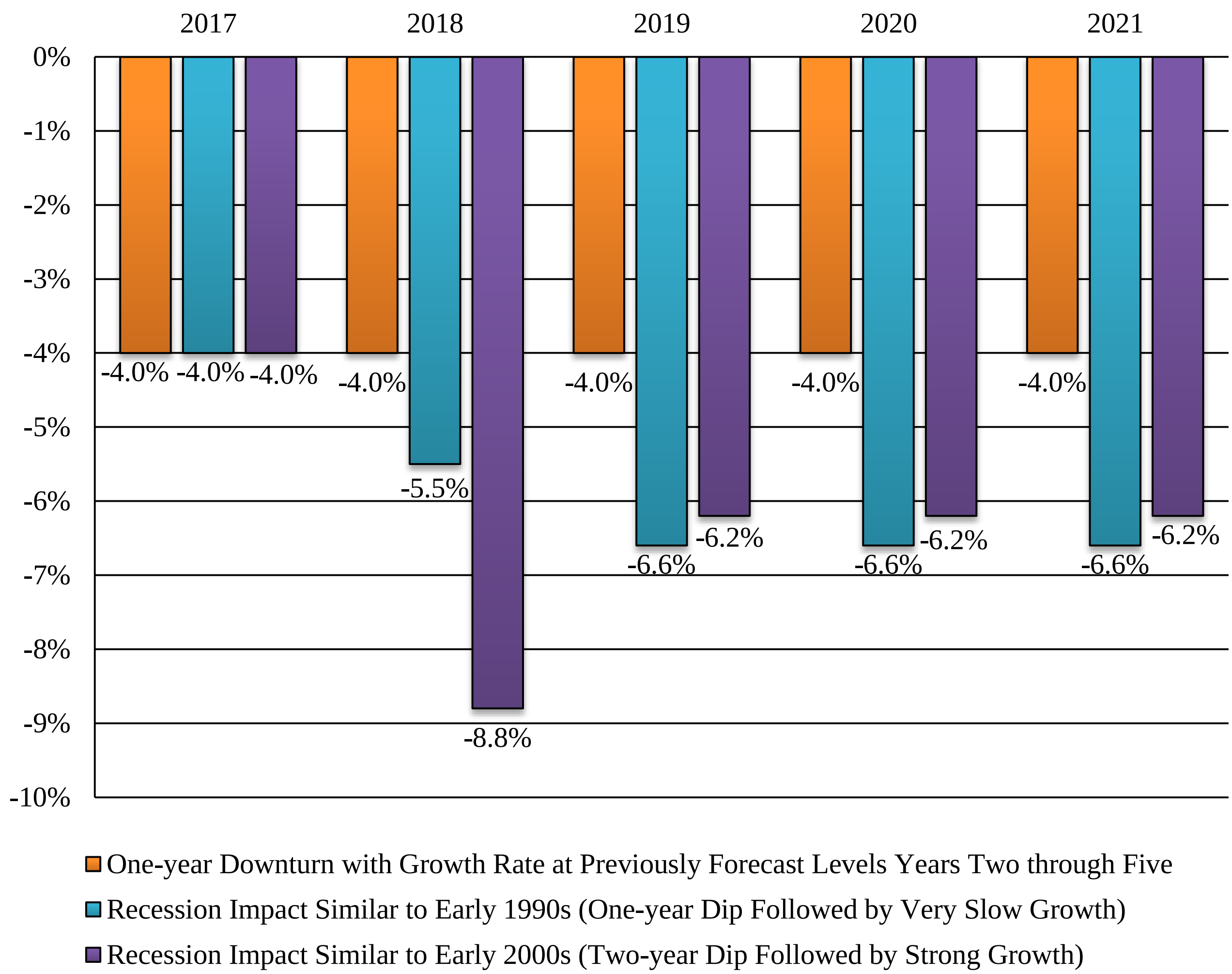
Exhibit 7
Total General Fund Revenues
Percent Difference Actual versus Estimate
Fiscal 1987-2021



Source: Comptroller of Maryland; Department of Legislative Services

Using the results of recession impact modeling conducted by DLS in 2016, when the legislature was crafting the State's revenue volatility structure, **Exhibit 8** illustrates that even a one-year dip in revenues results in revenues falling short of prerecession estimates for an extended time. To the extent the Great Recession were to have repeated itself, ongoing revenues would have been in excess of $1.1 billion less than estimates for each year reflected below.

Exhibit 8
Impact of Recession on Fiscal 2017 General Fund Revenue Forecast
Percent Ongoing Revenues Fall Below Baseline Forecast
Fiscal 2017-2021



Source: *Report on Revenue Volatility and Approaches to Reduce Risk to the State Budget*, 2016

Maintaining a balance of 10% of general fund revenues saved in the Rainy Day Fund would provide adequate funds to offset these lost revenues, and even if the State continued to be wary of going below the 5% benchmark, it would ease the initial strain and potentially delay the need to make difficult decisions. This, combined with the principle of incremental withdrawals, would afford the State the opportunity to better understand the magnitude of the recession and potentially mitigate the need for significant spending reductions over multiple years.

In establishing the State's revenue volatility structure, Chapters 4 and 550 of 2017 statutorily defined the goal of achieving a 10% balance in the Rainy Day Fund. To the extent that appropriations to the Fiscal Responsibility Fund materializes in the fiscal 2024 budget, having a 10% balance in the Rainy Day Fund would allow the entirety of those funds to be used as supplemental PAYGO appropriations for public school construction and other education-related capital projects. In addition, the State has an already established incremental approach to replenishing the Rainy Day Fund balance, requiring specific annual appropriation amounts at 3% and 7.5% until the 10% goal is met. This could easily be adapted in the inverse, using increasingly stringent criteria for accessing funds as the balance is drawn down.

Operating Budget Recommended Actions

1. Concur with Governor’s allowance.

Updates

- On January 4, 2022, Governor Lawrence J. Hogan. Jr. signed Budget Amendment 135-21 to charge $776,568,887 in COVID-19-related expenditures incurred by MDH against the Local Income Tax Reserve (LITR) Fund. The authorization to do this was provided in Chapter 150 of 2021, the Budget Reconciliation and Financing Act. The expenditures are eligible for reimbursement from the Federal Emergency Management Agency, although the timing of when the State will be reimbursed is not currently known. To date, the State has received approximately $537.1 million toward the more than $1 billion in eligible expenses, including $341.2 million in funding recognized in the fiscal 2022 budget. The remaining $195.9 million in reimbursements is approved and expected to replenish the LITR Fund immediately for a net withdrawal of $580.6 million. At the end of calendar 2021, the LITR Fund had a cash balance of over $2.5 billion.

  Current unfunded liabilities for the LITR Fund total $738.6 million. It is not currently anticipated that the $580.6 million will be reflected as an unfunded liability; however, the timing of the budget amendment means that the impact has yet to be reflected in the account detail. Therefore, this determination is not definitive.

Appendix 1
2021 *Joint Chairmen's Report* Responses from Agency

The 2021 JCR requested one report for the State Reserve Fund. Electronic copies of the full JCR responses can be found on the DLS Library website.

- ***Repayments to the Catastrophic Event Account and the Small, Minority, and Women-Owned Businesses Account (SMWOBA):*** 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 SMWOBA. At the January 5, 2022 meeting, the Board of Public Works approved an item forgiving the remaining loan balances from 39 loans totaling $1,991,876.

Appendix 2

Revenue Stabilization Account (Rainy Day Fund)

Section 7-311 State Finance and Procurement Article

Account Characteristics

- ***Purpose:*** The account was established in 1986 to retain State revenues to meet future short-term funding needs and to reduce the need for future tax increases by moderating revenue growth.

- ***Appropriations:*** The account consists of direct appropriations in the budget bill and interest earned from all reserve fund accounts.

- ***Required Appropriations If Account Balance Is Less Than 7.5% of General Fund Revenues:*** Current law requires that if the fund balance is between 3% and 7.5% of projected general fund revenues, annual appropriations of at least $50 million must be made until the account balance reaches 7.5% of estimated general fund revenues. If the account balance is below 3%, State law requires an appropriation of at least $100 million.

- ***Sweeper Provision:*** State law requires that the Administration appropriate an amount equal to any unassigned general fund balance at closeout in excess of $10 million into the Rainy Day Fund. This appropriation is made to the budget two years after the unassigned general fund surplus is realized. For example, fiscal 2008 closed with an unassigned surplus totaling $185.7 million, thus the Administration's fiscal 2010 allowance included a $175.7 million appropriation to the Rainy Day Fund. This appropriation to the Rainy Day Fund is referred to as the "sweeper."

  Per Chapter 557 of 2017, for fiscal 2021 and beyond, for surpluses above $10 million, the first $100 million is divided between the Rainy Day Fund, the Pension System, and the Postretirement Health Benefits Trust Fund so that the Rainy Day Fund receives 50%, the Pension System receives 25%, and the Postretirement Health Benefits Trust Fund receives 25% on a dollar-for-dollar basis. Amounts above $110 million are credited to the Rainy Day Fund.

Mechanisms for Transferring and Spending Funds

The Governor can transfer balance from the Rainy Day Fund above 5% of estimated general fund revenues in the budget bill. To transfer an amount that would reduce the Rainy Day Fund balance below 5% requires the transfer to be authorized in an Act of the General Assembly other than the budget bill.

Appendix 3
Dedicated Purpose Account
Section 7-310 State Finance and Procurement Article

Account Characteristics

- ***Purpose:*** The account was established in 1986 to retain appropriations for major, multi-year expenditures where the magnitude and timing of cash needs are uncertain and to meet expenditure requirements that may be affected by changes in federal law or fiscal policies or other contingencies.

- ***Appropriations:*** The account consists of direct appropriations in the budget bill committed to a specific purpose. Interest earnings generated by the account are credited to the Rainy Day Fund.

- ***Other:*** The unspent balance of an appropriation reverts to the Rainy Day Fund four years after the end of the fiscal year for which the appropriation was made.

Mechanisms for Transferring and Spending Funds

To transfer funds from the DPA:

- funds may be reflected in the State budget subject to appropriation;

- after submission to the budget committees and 45-day review and approval by the Legislative Policy Committee (LPC) funds may be transferred by budget amendment to the appropriate Executive Branch agency; or

- the Governor may declare appropriations to the DPA surplus and may transfer funds by budget amendment to the Rainy Day Fund following review by the budget committees and LPC.

Appendix 4
Catastrophic Event Account
Section 7-324 State Finance and Procurement Article

Account Characteristics

- ***Purpose:*** The account was established in 1990 to enable the State to respond quickly to a natural disaster or catastrophe that could not be addressed within existing State appropriations.

- ***Appropriations:*** The account consists of direct appropriations in the budget bill. Interest earnings generated by the account are credited to the Rainy Day Fund.

Mechanisms for Transferring and Spending Funds

Prior to transferring funds by budget amendment to the appropriate Executive Branch agency, the Administration must notify LPC of the proposed amendment and allow the committee to review and approve the proposed amendment. The committee has 15 days to review and comment.

Appendix 5
Object/Fund Difference Report
State Reserve Fund

Object/Fund	FY 21 Actual	FY 22 Working Appropriation	FY 23 Allowance	FY 22 - FY 23 Amount Change	Percent Change
Objects					
12 Grants, Subsidies, and Contributions	$ 114,000,000	$ 977,469,432	$ 3,107,780,846	$ 2,130,311,414	217.9%
Total Objects	**$ 114,000,000**	**$ 977,469,432**	**$ 3,107,780,846**	**$ 2,130,311,414**	**217.9%**
Funds					
01 General Fund	$ 114,000,000	$ 669,649,432	$ 2,936,557,031	$ 2,266,907,599	338.5%
05 Federal Fund	0	307,820,000	171,223,815	-136,596,185	-44.4%
Total Funds	**$ 114,000,000**	**$ 977,469,432**	**$ 3,107,780,846**	**$ 2,130,311,414**	**217.9%**

Note: The fiscal 2022 appropriation does not include deficiencies.