

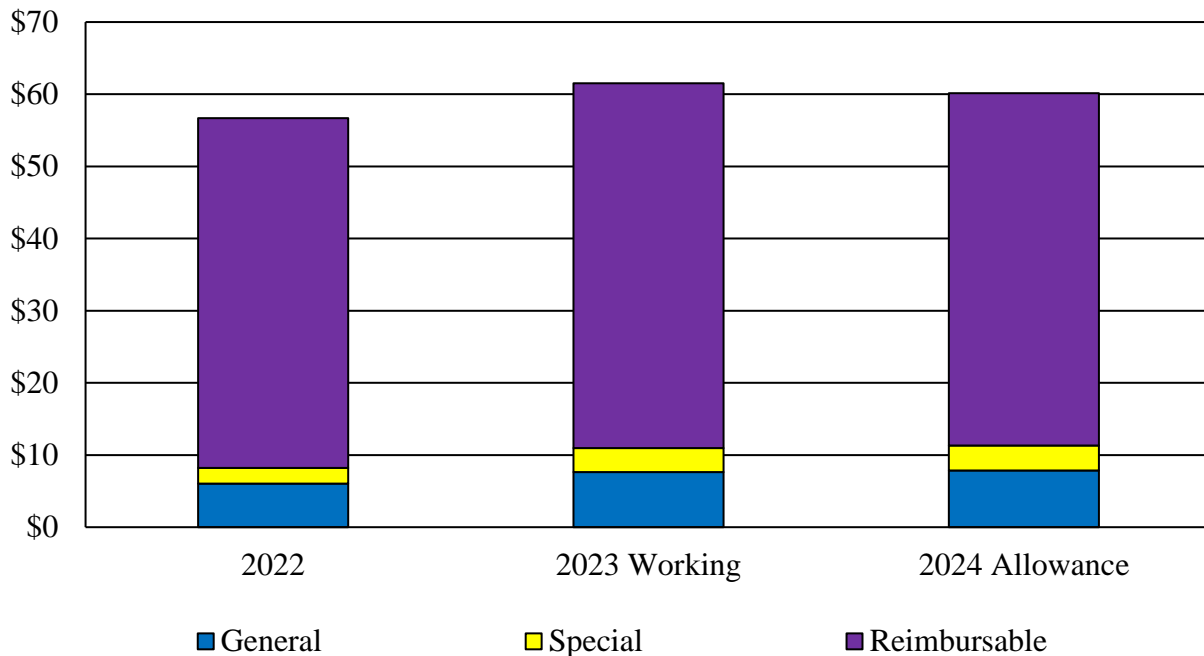
E20B State Treasurer

Program Description

The State Treasurer is responsible for the management and protection of State funds and property, which involves the receipt, disbursement, protection, and investment of State funds. The State Treasurer is a member of the Board of Public Works (BPW), State Retirement and Pension System Board of Trustees, Capital Debt Affordability Committee, and other committees. The State Treasurer's Office (STO) has a Treasury Management Division that provides banking and investment services to protect, receive, disburse, and invest the State's cash balances. The Insurance Division manages claims against the State in accordance with the Maryland Tort Claims Act (MTCA). The Debt Management Division manages bond sales and the master lease program and also directs State debt by advising policies to minimize borrowing costs and maintain the State's credit rating.

Operating Budget Summary

Fiscal 2024 Budget Decreases \$1.4 Million, or 2.3%, to \$60.1 Million (\$ in Millions)

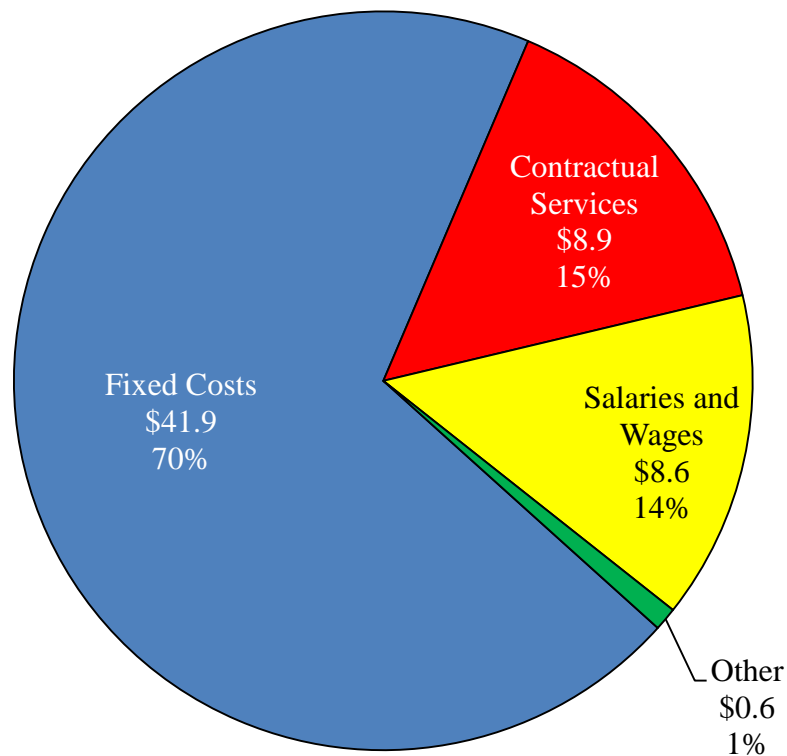


Note: The fiscal 2023 working appropriation includes deficiency appropriations including this agency's share of a deficiency appropriation budgeted in the Statewide Account within the Department of Budget and Management (DBM). Fiscal 2024 salary enhancements are budgeted in the Statewide Account within DBM.

Fiscal 2024 Overview of Agency Spending

Exhibit 1 illustrates the \$60.1 million fiscal 2024 allowance by object, of which 70% is fixed costs associated with the State’s self-insurance program.

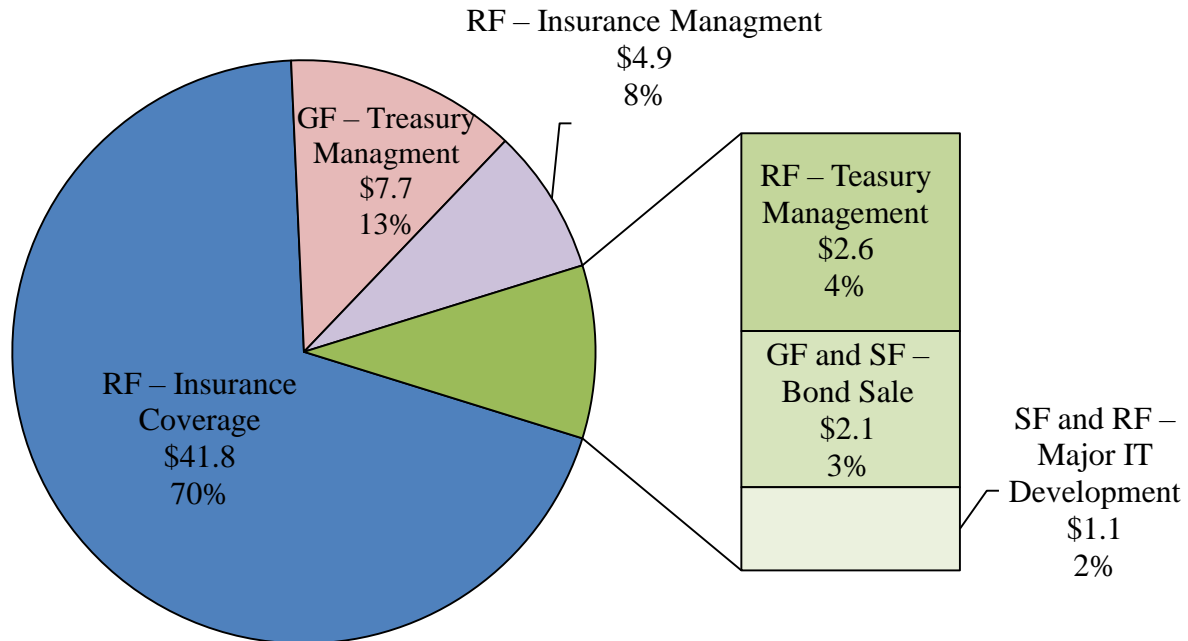
Exhibit 1
Overview of Agency Spending
Fiscal 2024 Allowance
(\$ in Millions)



Source: Governor’s Fiscal 2024 Budget Books

Exhibit 2 shows spending by revenue source, the largest of which is insurance premiums that provide reimbursable funds for Insurance Coverage and Management that is 78% of STO revenues. Another 4% of revenues is reimbursable funds for State agencies’ banking services. Special funds from bond sales support those sales, and special funds from investment fees support Treasury Management’s operations.

Exhibit 2
Overview of Agency Revenues
Fiscal 2024 Allowance
(\$ in Millions)



GF: general fund
 IT: information technology
 RF: reimbursable fund
 SF: special fund

Source: Governor's Fiscal 2024 Budget Books

Proposed Budget Change

Exhibit 3 provides details about changes in the budget, which declines \$1.4 million from fiscal 2023 to 2024. Lower spending is attributable to cash flow needs of the Financial Systems Modernization major information technology (IT) project, discussed in **Appendix 1**. General funds for this project are appropriated in the Department of Information Technology's budget and transferred to the STO budget as reimbursable funds by budget amendment. The fiscal 2023 working appropriation has a \$2.3 million budget amendment for this project. Similar budget amendments are anticipated in fiscal 2024, so actual spending is expected to increase.

Exhibit 3
Proposed Budget
State Treasurer
(\$ in Thousands)

How Much It Grows:	<u>General Fund</u>	<u>Special Fund</u>	<u>Reimb. Fund</u>	<u>Total</u>
Fiscal 2022 Actual	\$6,058	\$2,155	\$48,450	\$56,663
Fiscal 2023 Working Appropriation	7,632	3,326	50,568	61,526
Fiscal 2024 Allowance	<u>7,858</u>	<u>3,478</u>	<u>48,801</u>	<u>60,137</u>
Fiscal 2023-2024 Amount Change	\$226	\$152	-\$1,767	-\$1,389
Fiscal 2023-2024 Percent Change	3.0%	4.6%	-3.5%	-2.3%
Where It Goes:				<u>Change</u>
Personnel Expenses				
Employee and retiree health insurance.....				\$426
Increments and other compensation.....				168
Turnover adjustments.....				54
Annualization of 4.5% cost-of-living adjustment				47
Reclassifications.....				-319
Major Information Technology Project Development				
Financial Systems Modernization major information technology (IT) project.....				-2,989
Treasury and Insurance Management				
Contractors handling major IT project development				711
Licenses for new Financial Systems Modernization platform				215
Contractual staff for paralegal support, IT training, administrative support, and recruitment.....				192
Software developer support for new finance and operational modules of Financial Systems Modernization Project.....				150
Upgrade information technology equipment				135
Temporary support for operating legacy systems				125
Treasury management positions supported by State Insurance Trust Fund.....				116
Additional Bloomberg Terminal				48
Other.....				33
Temporary banking staffing to support depository banking conversion project ..				30
Treasury management system contract for offsite payment transaction support ..				-100
Changes in Treasury and Insurance Management contracts under \$50,000				-131

Where It Goes:	<u>Change</u>
Cash management database support contract.....	-\$300
Total	-\$1,389

Note: Numbers may not sum to total due to rounding. The fiscal 2023 working appropriation includes deficiency appropriations including this agency's share of a deficiency appropriation budgeted in the Statewide Account within the Department of Budget and Management (DBM). Fiscal 2024 salary enhancements are budgeted in the Statewide Account within DBM.

Personnel Data

	<u>FY 22 Actual</u>	<u>FY 23 Working</u>	<u>FY 24 Allowance</u>	<u>FY 23-24 Change</u>
Regular Positions	60.00	63.00	63.00	0.00
Contractual FTEs	<u>1.75</u>	<u>0.00</u>	<u>3.33</u>	<u>3.33</u>
Total Personnel	61.75	63.00	66.33	3.33

Vacancy Data: Regular

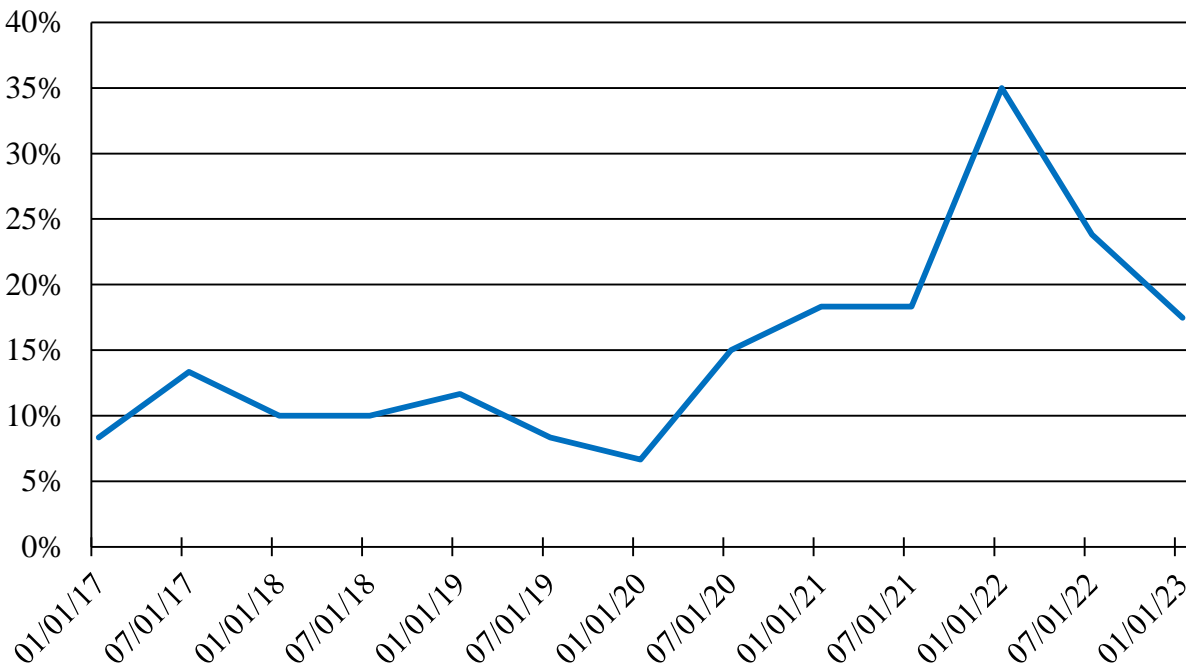
Turnover and Necessary Vacancies, Excluding New Positions	1.90	3.02%
Positions and Percentage Vacant as of 12/31/22	11.00	17.46%
Vacancies Above Turnover	9.10	14.44%

- The allowance includes 1.5 full-time equivalent (FTE) contractual positions for paralegal services. STO advises that it is handling more complex cases, especially related to police accountability claims, so additional staff is needed.
- There is also 1.0 FTE to train and develop the IT assistant director. The position is filled by a former State employee.
- The remaining contractual positions provide administrative support (0.5 FTE) and summer students to provide clerical support for recruitment (0.33 FTE).

Vacancy Rates Decline but Remain High

Exhibit 4 shows that vacancy rates at STO increased substantially at the beginning of the COVID-19 pandemic, as the vacancy rate more than doubled from 7% in January 2020 to 15% in July 2020. Vacancy rates increased again after July 2021 with the retirement of the former Treasurer. This led other eligible staff to retire, which increased the agency’s vacancy rate to 35%. The vacancy rate has come down as the new Treasurer hired staff, but there still are some long-term vacant positions. In January 2023, of the 11 vacant positions, 4 had been vacant for less than one year, 4 had been vacant between one and two years, and 3 had been vacant for over two years.

Exhibit 4
Vacancy Rates at the State Treasurer’s Office
January 2017 to January 2023



Source: Department of Budget and Management

The office has also updated personnel policies to reduce vacancies. A telework program was introduced in summer 2022 that allows employees to work virtually two days a week. Salaries were increased to make positions more competitive, and the Department of Budget and Management approved reclassifying the directors and creating a new, higher-grade class series for treasury management and insurance division positions.

Key Observations

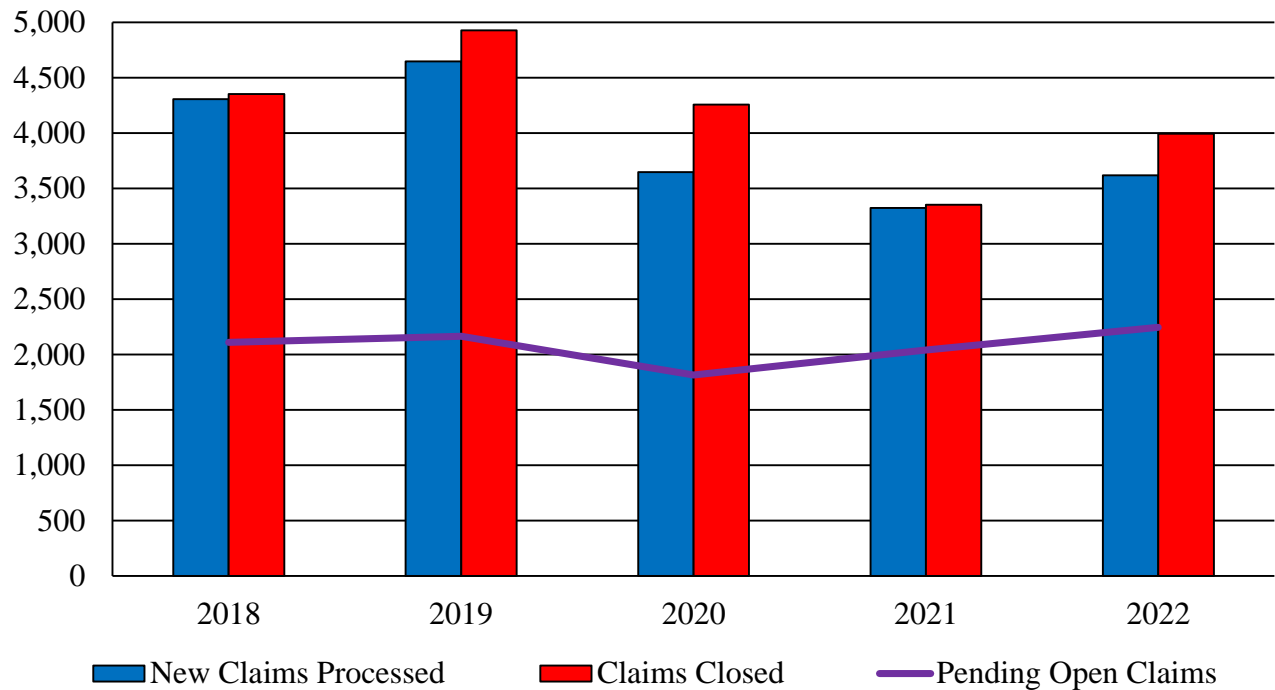
1. State’s Insurance Program

STO is responsible for administering the State’s Insurance Program, which is comprised of both commercial and self-insurance. The program covers catastrophic property and liability losses as well as other obligations derived from State contracts, statutes, and regulations. Self-insurance coverage includes State-owned real and personal property, vehicles, and liability claims covered under the MTCA. The State Insurance Trust Fund (SITF) is maintained by STO to pay claims filed against the State, its agencies, and employees and the costs associated with handling these claims. Self-insurance coverage is limited to \$2.5 million per incident; the State has purchased insurance to cover incidents that exceed \$2.5 million. Not all activities can be self-insured, and commercial insurance is purchased for those activities. Examples of this include the Port of Baltimore and the Baltimore/Washington International Thurgood Marshall Airport.

A tort is a civil act or omission that causes an individual to suffer loss or harm leading to legal liability. The legal doctrine of sovereign immunity allows the State to avoid legal liability. The MTCA waives the State’s sovereign immunity. The MTCA limits the State’s liability to \$400,000 for a single claimant from a single incident. BPW can authorize an award in excess of \$400,000, but it is uncommon for BPW to do this.

Reimbursable funds from State agencies support the SITF. Pricing is in two parts, a per head premium and a premium based on claims history. All agencies pay into the fund, while agencies with higher claims pay higher premiums. **Exhibit 5** shows that claims are still below prepandemic levels from fiscal 2019. STO advises that this is due to less activity and more people working from home during the pandemic. The office advises that, with respect to torts, (1) routine claims without injuries are usually processed within 90 days; (2) auto claims require three estimates and can take longer; and (3) bodily injury claims take the longest amount of time to process.

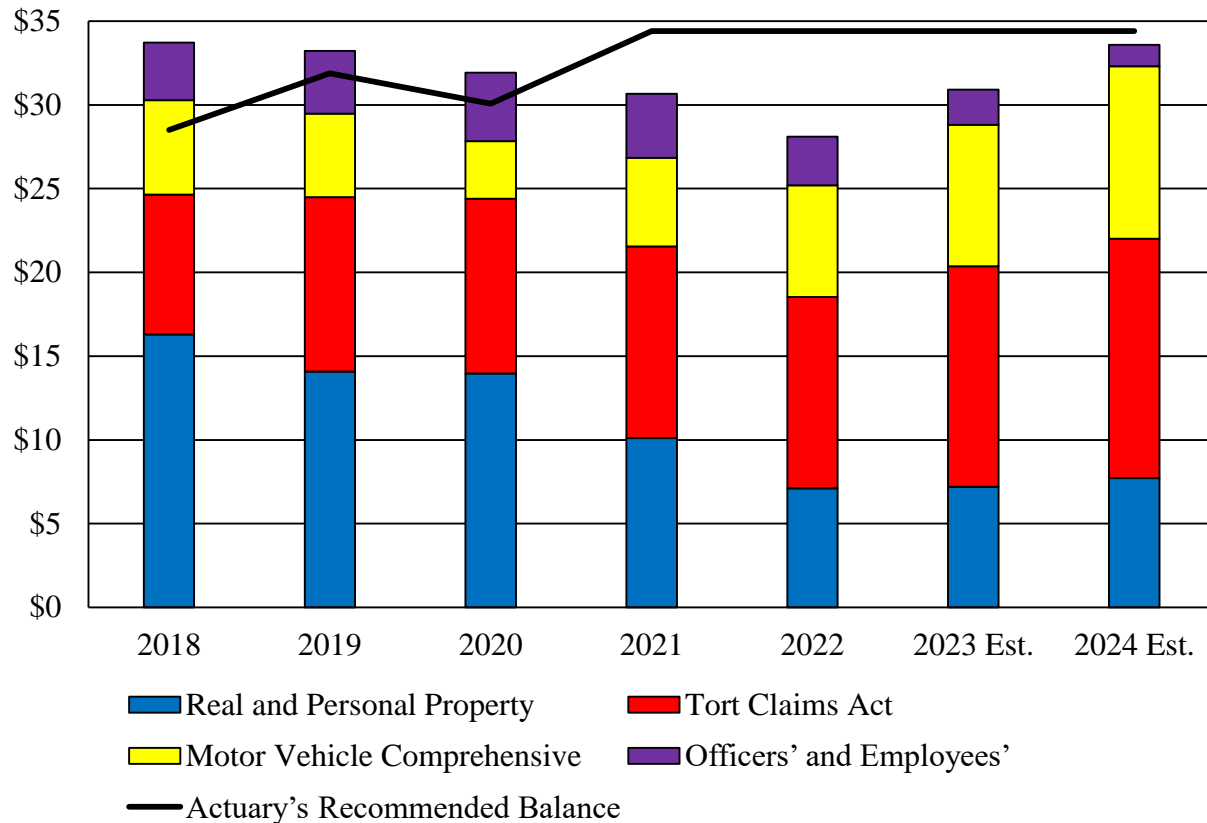
Exhibit 5
Insurance Claims Processed, Closed, and Pending
Fiscal 2018-2022



Source: Department of Budget and Management

Exhibit 6 shows that the fiscal 2021 closeout revealed that fund balances were below actuarial recommended levels. To address this, fiscal 2023 premiums were increased by \$1 million to reduce the deficit. In fiscal 2024, revenues remain level with fiscal 2023. Noteworthy is the decline in real and personal property balances, which is discussed in the next section.

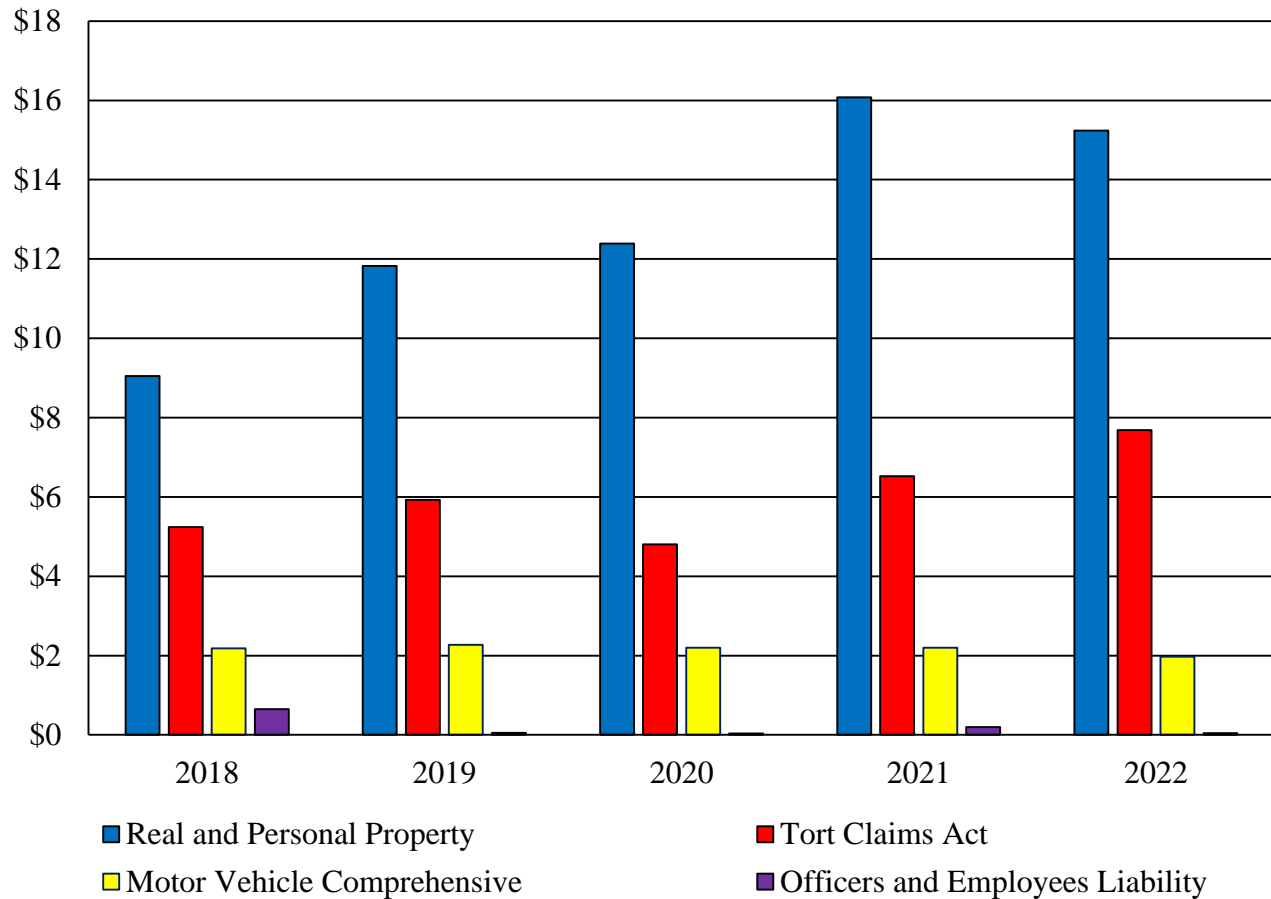
Exhibit 6
State Insurance Trust Fund Balance by Type of Liability
Fiscal 2018-2024 Est. Closing Balances
(\$ in Millions)



Source: State Treasurer's Office

Exhibit 7 shows that real and personal property losses and claims have increased since fiscal 2018. STO advises that there have been large losses directly linked to failure to properly keep up with building maintenance. For example, aging boilers and damaged roofs, windows, and doors can result in additional damage and claims to other property and equipment. Among the benefits expected from increased maintenance funding is reduced property insurance claims and premiums. The fund balance also includes excess policy coverage. This is additional fund balance available in case claims that are uncommonly large in a particular year need to be paid. **STO should be prepared to brief the committees on what it is doing to limit real and personal property losses and claims.**

Exhibit 7
State Insurance Trust Fund Losses and Excess Policy Coverage
Fiscal 2018-2022
(\$ in Millions)



Source: State Treasurer's Office

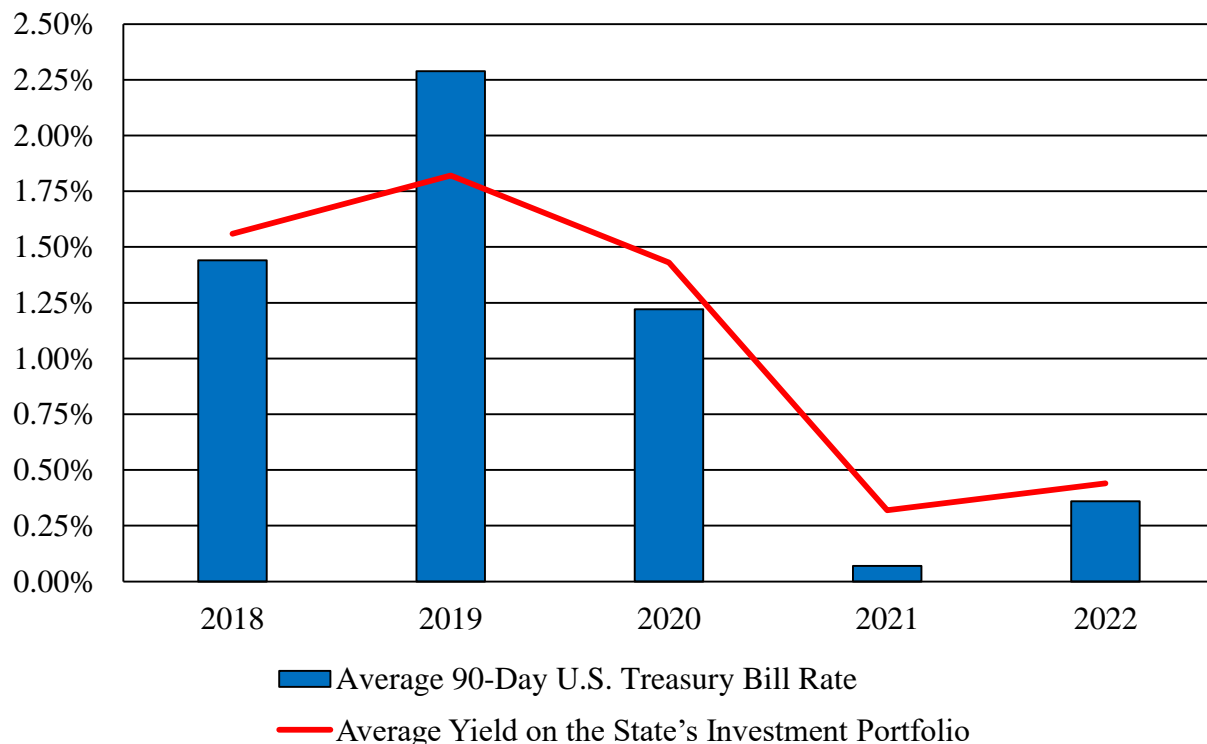
2. State's Investment Portfolio Earnings

The Treasury Management Division's Investment Department is responsible for the investment of unexpended State funds that are temporarily idle between the time revenue is collected and budgeted amounts are disbursed. This is a substantial sum; the STO website reports that the market value of the entire investment portfolio was \$20.6 billion at the end of December 2022. Investments are typically short term and designed to meet the cash flow needs of the State. Section 6-222 of the State Finance and Procurement Article governs the types of investments that may be made, and the State Treasurer's Investment Policy provides additional

guidance. The cautious nature of the Investment Department is highlighted by the restrictions placed on investments, which are limited to (1) secured bank accounts; (2) full faith and credit obligations of the federal government; (3) obligations of certain federal agencies or instrumentalities; (4) repurchase agreements (repos) collateralized by those securities; (5) certain money market mutual funds; and (6) limited amounts of highest rated commercial paper. Secured bank accounts require a 100% collateralization, and repos require 102% collateralization.

STO's Managing for Results goal is that the State's investment portfolio outperform the average 90-day U.S. Treasury Bill (T-bill) rate. The T-bill rate is the most secure security and generally accepted as the world's risk-free rate. Selecting this benchmark suggests that the portfolio's primary goal is to preserve capital. **Exhibit 8** shows the portfolio's yields exceeded the benchmark rate in all years except 2019. Underperformance in fiscal 2019 was attributable to steep interest rate increases. The portfolio included lower return coupon investments that lost value when interest rates rose. As was common with many portfolios, STO misjudged the likelihood of interest rate hikes.

Exhibit 8
Yield on the State's Investment Portfolio
Fiscal 2018-2022



Source: Department of Budget and Management

There were also substantial interest rate increases in fiscal 2022. However, STO was concerned about rising interest rates and shortened maturities as much as practicable; this included having unusually large shares of the portfolio mature overnight to a few weeks. STO advises that its weighted average maturity (WAM) for its portfolio is just over 1 year, compared to 1.8 years previously. As rates rose, maturing assets could be reinvested in higher interest-bearing assets. Having correctly anticipated higher rates keep returns modestly above the benchmark.

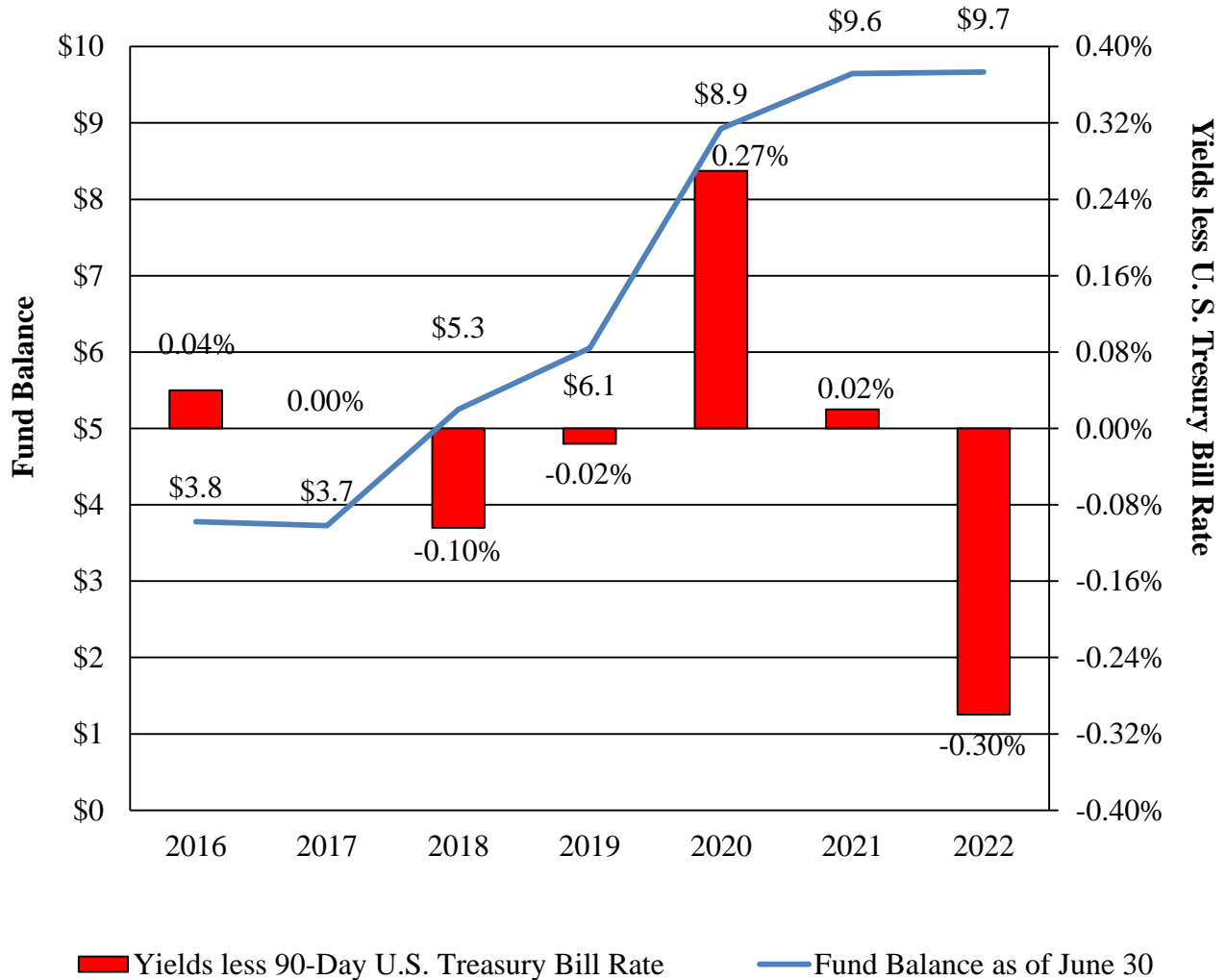
3. Maryland Local Government Investment Pool

The State Treasurer is responsible for administering the Maryland Local Government Investment Pool (MLGIP), which provides units of local government a safe investment tool for the short-term investment of funds. Management of MLGIP has been contracted to PNC Financial Services Group, Inc. The pool is audited annually. Participants benefit from professional money management, a diversified portfolio, and reduced investment costs. In September 2022, Standard and Poor's reaffirmed the MLGIP's AAAM rating, which is their highest rating.

Although MLGIP serves a similar purpose as the State's investment portfolio administered by STO, there are some key differences. MLGIP has, by design and legal requirements, a short WAM. The maximum maturity is 397 days. STO advises that the current WAM is 32 days. Usually, the yield curve is positive, which means that higher returns can be realized with longer maturities, so limiting maturities also limits returns. A second difference is that the MLGIP's investments are managed by external money managers, who charge fees for their services. As an internally managed portfolio, the State's investments do not charge fees. After comparing MLGIP returns to Standard and Poor's Rated GIP Index, the Department of Legislative Services observed that MLGIP's yields, while sometimes more and sometime less than the index, have generally been consistent with the industry.

Exhibit 9 shows how the fund balance has increased in recent years. Since the beginning of the COVID-19 pandemic, increased balances are primarily attributable to excess cash balances and a short-term need to move funds into liquid, high-quality investment instruments. Fund balances remained high in fiscal 2022. The exhibit also shows that, unlike the State's investment portfolio, the MLGIP's yields were less than the average 90-Day U.S. Treasury Bill rate in four of the last seven years. This is, in part, attributable to how the plan is managed. Limiting maturities reduces opportunities to realize higher yields, and fees reduce net earnings. With respect to MLGIP yields being 0.30% (30 basis points) below U. S. Treasury yields, STO advises that many funds stopped collecting fees during the pandemic, when returns were low and they did not want to have negative returns. Many of those funds have used the bounce back in interest rates in fiscal 2022 to recoup some of those amounts.

Exhibit 9
Maryland Local Government Investment Pool Fund Balance and Yields
Fiscal 2016-2022
(\$ in Billions)



Source: Department of Budget and Management

Operating Budget Recommended Actions

1. Concur with Governor's allowance.

Appendix 1
Financial System Modernization
Major Information Technology Project
State Treasurer’s Office

New/Ongoing: Ongoing								
Start Date: July 2017				Est. Completion Date: December 2023				
Implementation Strategy: Revised to be hybrid waterfall and agile								
(\$ in Millions)	Prior Year	2023	2024	2025	2026	2027	Remainder	Total
GF	\$6.426	\$2.551	\$2.974	\$1.151	\$0.000	\$0.000	\$0.000	\$13.102
SF	2.219	0.365	1.100	0.000	0.000	0.000	0.000	3.684
RF	3.091	1.377	0.000	0.000	0.000	0.000	0.000	4.467
Total	\$11.735	\$4.293	\$4.074	\$0.000	\$0.000	\$0.000	\$0.000	\$21.253

- Project Summary:** Replace the system that processes over 1 million State agency bank and accounting transactions daily. The new system should provide (1) new, cloud-based financial applications; (2) banking applications; (3) file transfer applications; (4) insurance-claims applications; (5) debt management capital lease management applications; (6) investment interest allocation applications; and (7) state-of-the-art application and infrastructure security systems to protect STO’s agency data and business applications.
- Need:** Replace the i5/As400 batch financial and insurance management system since its IBM hardware platform is end-of-life, and the applications and databases are no longer maintainable and cannot be functionally enhanced. The new system addresses cybersecurity concerns raised by the Legislative Auditor, which found that the legacy system was insufficiently robust to protect personally identifiable information.
- Observations and Milestones:** By December 2022, the insurance module’s live features included the Notice of Claim portal so that citizens can file claims, core features and capabilities for adjustors to manage, process and resolve claims, and the ability to make insurance payments that is fully integrate with the accounting module. Before the end of fiscal 2023, subrogation and deposit processes should be implemented, and the legacy system data migration should be complete. With respect to the banking module, planning should be completed by January 2023 with implementation starting shortly thereafter and continuing through the winter of calendar 2024.
- Changes:** The project has been delayed due to the pandemic and staffing changes. Total costs have increased by \$5 million.

E20B – State Treasurer

- **Concerns:** Risks include resource availability (challenges due to pandemic, retirements, and staffing changes), organizational culture (agency focused on existing system and business processes), technical (custom development of .NET need for cash management, which is then needed to be integrated with the accounting module), and implementation (staffing changes within IT and within agency management reduces the staff with institutional knowledge of the system and business processes).

Appendix 10
Object/Fund Difference Report
State Treasurer

<u>Object/Fund</u>	<u>FY 22 Actual</u>	<u>FY 23 Working Appropriation</u>	<u>FY 24 Allowance</u>	<u>FY 23 - FY 24 Amount Change</u>	<u>Percent Change</u>
Positions					
01 Regular	60.00	63.00	63.00	0.00	0%
02 Contractual	1.75	0.00	3.33	3.33	N/A
Total Positions	61.75	63.00	66.33	3.33	5.3%
Objects					
01 Salaries and Wages	\$ 6,073,508	\$ 8,177,972	\$ 8,646,596	\$ 468,624	5.7%
02 Technical and Special Fees	109,143	3,775	195,818	192,043	5087.2%
03 Communication	24,208	35,797	39,651	3,854	10.8%
04 Travel	8,444	10,002	10,002	0	0%
07 Motor Vehicles	113,743	2,630	2,630	0	0%
08 Contractual Services	8,941,286	11,128,757	8,936,425	-2,192,332	-19.7%
09 Supplies and Materials	222,856	196,302	196,302	0	0%
10 Equipment – Replacement	334,485	30,384	95,607	65,223	214.7%
11 Equipment – Additional	0	0	70,000	70,000	N/A
13 Fixed Charges	40,835,395	41,846,403	41,943,914	97,511	0.2%
Total Objects	\$ 56,663,068	\$ 61,432,022	\$ 60,136,945	-\$ 1,295,077	-2.1%
Funds					
01 General Fund	\$ 6,057,620	\$ 7,548,248	\$ 7,858,428	\$ 310,180	4.1%
03 Special Fund	2,155,349	3,315,938	3,477,675	161,737	4.9%
09 Reimbursable Fund	48,450,099	50,567,836	48,800,842	-1,766,994	-3.5%
Total Funds	\$ 56,663,068	\$ 61,432,022	\$ 60,136,945	-\$ 1,295,077	-2.1%

Note: The fiscal 2023 appropriation does not include deficiencies. The fiscal 2024 allowance does not include contingent reductions or cost-of-living adjustments.