SPENDING AFFORDABILITY COMMITTEE

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# Report of the Spending Affordability Committee

## Fiscal Year 2013

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*Baltimore County, Maryland*

*February 15, 2012*

## BALTIMORE COUNTY SPENDING AFFORDABILITY COMMITTEE

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Councilman, 1st District, Committee Chairman

Honorable Vicki Almond
Councilwoman, 2nd District

Honorable David Marks
Councilman, 5th District

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Professor, Department of Political Science, UMBC

Winston S. Sherman
Former Federal Government Administrator

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**SPENDING AFFORDABILITY COMMITTEE**

February 15, 2012

Honorable Members of the Baltimore County Council
Honorable Kevin Kamenetz, County Executive

I am pleased to submit the report of the Spending Affordability Committee, reflecting the Committee's fiscal policy recommendations for Baltimore County for fiscal year (FY) 2013.

For FY 2013, the Committee recommends a base spending guideline of $1,641,204,519, derived from a personal income growth rate of 2.98%. This guideline represents maximum potential growth of $47,492,615 over estimated FY 2012 base spending. The Committee further recommends that total debt outstanding not exceed 2.2% of FY 2013 estimated assessed property value and that debt service not exceed 9% of FY 2013 estimated General Fund revenues. These guidelines are meant to limit spending such that growth in the cost of government services does not exceed the growth in the County's economy. In making these recommendations, the Committee emphasizes that these guidelines do not represent targets but rather maximum levels not to be exceeded.

Given the proven long-term fiscal prudence and management of Chief Administrative Officer Fred Homan, Budget Director Keith Dorsey, and the Honorable County Executive Kevin Kamenetz—who served for 16 years on the Council prior to being elected as County Executive—the Committee trusts that the Executive Office will spend only what is absolutely necessary to meet current obligations—not one dollar more nor one dollar less than needed. Baltimore County Government recognizes that any dollar misspent is one dollar less for our schools, teachers, firefighters, police, community college, libraries, roads, and other critical local government functions. As we witnessed this past fiscal year, the County Executive's submitted budget came in roughly level to the previous fiscal year budget, even as the Spending Affordability Committee allowed additional flexibility in light of the pension transfer possibility. We are confident in the discernment of the Office of Budget and Finance along with the County Executive to continue in this long-standing tradition.

In determining its fiscal guidelines, the Committee reviewed current and projected conditions of the national, state, and local economies. This review disclosed slow economic recovery, with several downside risks regionally, primarily related to federal government cutbacks. At its January 11, 2012 meeting, the Baltimore County Economic Advisory Committee expressed a cautious near-term outlook. The Spending Affordability Committee shares this tone of caution and urges continued fiscal prudence in the upcoming years.

During this year's deliberations, important questions were raised regarding the General Fund's ability to sustain spending at the guideline level in FY 2013 and future years. While the Committee is confident that sufficient fund balance is available to support FY 2013 spending at the guideline level, a concern exists that projected revenue growth is insufficient to sustain this level of ongoing expenditures over the next few years. For FY 2013, the County is likely to absorb a significant portion of teachers' pension costs from the State, while various internal cost pressures, such as the general government's other post-employment benefits obligation and the County's debt burden, are mounting. Cost-cutting efforts are not just desirable but are necessary if the County is to hold the line with property and income tax rates.

The significant challenge of managing the County's fiscal balancing act is one that should be borne by the executive branch with active oversight by the legislative branch. In this regard, I would request that the Administration provide this legislative committee with more frequent fiscal updates on critical issues the County is facing, including debt, health insurance, and retirement cost pressures, as well as labor commitments—all of which could affect the ability of the County's revenue structure to afford the cost of government. Article 2, Title 3 of the Baltimore County Code charges the Spending Affordability Committee with determining an affordable level of spending based not only on the growth in the County's economy, but also on the projected ability of the revenue structure to sustain projected expenditures. To date, solely because of the existence of a healthy surplus balance, the Committee has not been faced with a need to scale back its guideline based on a projected imbalance. We advocate the maintenance of such strong levels of unassigned funds.

In addition to operating budget pressures, the County is faced with the prospect of approaching established debt guidelines in future years. It is imperative that the Administration keep the Committee promptly informed if plans to modify its debt policies are being considered.

In the near future, the Committee may review the personal income growth factor and examine other possible ways to assess affordability in overall spending growth for the County. While we embrace the five-year-average smoothing method, some members wonder if a broader measure of economic modeling might make sense given the challenging economic climate we face and the growing differential between spending guidelines and General Fund revenues. We will work closely and collaboratively with the County Auditor staff and the Budget Office as part of any such review to ensure that our recommended maximum levels of spending are appropriate, realistic, and prudent.

I would like to thank my fellow Council members who served on the Committee, the Honorable Council Chairwoman Vicki Almond and Councilman David Marks, for their time and thoughtful contributions to this year's process. I would also like to express gratitude to Dr. Roy Meyers, whose expertise in the field of public policy and government budgeting practices continued to benefit the Committee, and to Mr. Winston Sherman, for his participation in this important process. Thank you also to the Honorable Councilman Kenneth Oliver for providing additional support to the Committee.

Additionally, I would like to acknowledge the contribution of Mr. Anirban Basu, who again served the Committee this year both as its economic consultant and as the Chairman of the Baltimore County Economic Advisory Committee. Many thanks to all members of the Baltimore County Economic Advisory Committee for volunteering their time and providing their insights on the pulse of the local economy. Recognition is also due to County Auditor Lauren Smelkinson and the Fiscal and Policy Analysis Division of the County Auditor's Office for its diligent staff support to the Committee and to the Administration for its thoughtful communication in recent weeks. Finally, appreciation is due to County employees and labor unions for their spirit of cooperation and sacrifice over the years as the County has addressed its cost pressures in a fiscally sound manner.

We are hopeful that this report will be given careful consideration in the development and review of the County's operating and capital budgets for FY 2013.

Sincerely,

Tom Quirk
Chairman, Spending Affordability Committee
Councilman, 1st District

## INTRODUCTION

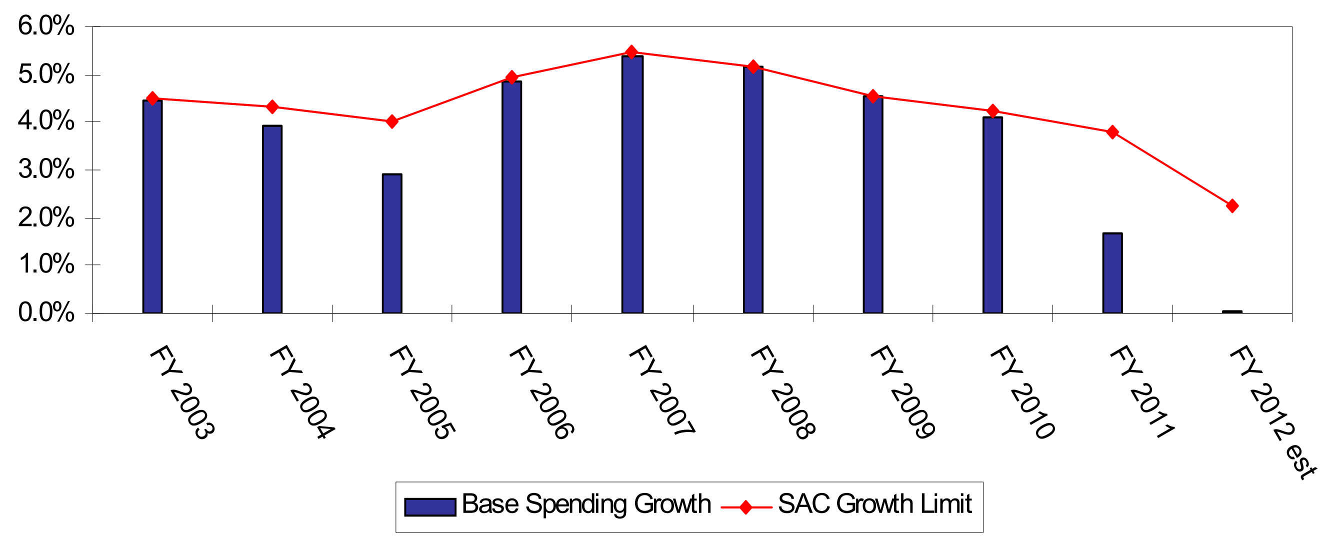
***The Baltimore County Spending Affordability Committee was established in order to limit growth in County government spending to a level that does not exceed the growth in the County's economy.***

In March 1990, the Baltimore County Council enacted legislation (Bill 33-90) that established a spending affordability law for Baltimore County to ensure that growth in County spending does not exceed the rate of growth of the County's economy (Baltimore County Code, Sections 2-3-101 to 2-3-107). The law mandates that the Spending Affordability Committee make a recommendation each fiscal year on a level of County spending that is consistent with the County's economic growth. The Committee has implemented this law by establishing both spending and debt guidelines. The spending guideline is a recommendation for the maximum level of General Fund spending for ongoing purposes, or "base spending." The debt guidelines are based on two common debt affordability indicators.

***The Spending Affordability Committee submits its report by February 15 of each year in order to provide timely input into the budgeting process.***

By law, the Spending Affordability Committee must submit its report to the County Council and County Executive by February 15 of each year. This reporting date allows the Executive ample time to consider the Committee's recommendations before formally presenting the proposed budget to the Council on or before April 16 of each year. The purpose of this report is to provide formal input to the County Council and the County Executive relative to the formulation of the County budget. Committee guidelines are intended to set recommended maximum amounts or growth levels for County spending that should not be exceeded (Figure 1); however, the law states that the County Council may exceed the Committee's recommendations if it provides a rationale for doing so.

**Figure 1. SAC Spending Growth Compliance, Most Recent 10 Years**



## SPENDING GUIDELINE

***The Committee recommends that base spending growth not exceed 2.98%, bringing the FY 2013 spending limit to $1,641.2 million.***

The spending guideline for a given fiscal year is calculated by multiplying the previous fiscal year's estimated base spending (as defined by the Committee) by the spending affordability growth factor (Figures 2 and 3). **For fiscal year (FY) 2013, the Committee recommends that base spending not exceed $1,641,204,519 based on an estimated County personal income growth rate of 2.98% applied to estimated final FY 2012 base-year spending of $1,593,711,904 (Figure 4). This guideline allows for maximum spending growth of $47,492,615 over estimated final FY 2012 spending.**

***The Committee utilizes a 5-year average of annual personal income growth rates to determine its personal income growth factor.***

In FY 2010 the Committee changed its measure of growth in the County's economy from a forecast of personal income growth for the upcoming fiscal year to the average of the annual growth forecasts for the upcoming and current fiscal years and the annual growth estimates for the 3 preceding fiscal years. There are a number of long-term advantages associated with this policy. Specifically, the use of 5-year averaging smoothes out economic fluctuations, stabilizing spending growth over time, and it corrects for revisions over time to current and prior year personal income growth forecasts.

***The Committee utilizes an "estimated final spending" methodology to determine base-year spending. Any "off-budget" expenditures are subject to the guideline for the year in which the spending occurs and become part of base-year spending for calculating the subsequent year's guideline.***

Committee policy further provides that base-year spending should reflect all approved and planned spending, or in other words, "estimated final spending," for the fiscal year. This methodology recognizes that certain adjustments in planned spending may occur after the budget is adopted. Such adjustments may include increases for supplemental appropriations or decreases due to planned expenditure reductions in response to detrimental economic events that are known or estimated prior to the adoption of the guideline. Additionally, Committee policy considers the expenditure of "off-budget" funds for general government purposes, including the "off-budget" expenditure of bond premium funds, as being subject to the guideline for the year in which the spending occurs. Accordingly, such "off-budget" expenditures are incorporated in base-year spending when calculating the guideline for the subsequent fiscal year. For the current fiscal year, no supplemental appropriations, significant reductions in planned spending, nor "off-budget" expenditures are anticipated.

***Presumably, the FY 2013 budget will be able to absorb any new State-transferred costs, such as a portion of teacher pension costs, within the confines of the spending guideline.***

Last year, the Committee felt compelled to consider the possibility that new costs could be passed to the County from the State (due to the State's budgetary imbalance) since such new costs potentially could affect the County's ability to comply with the spending guideline. The Committee approved the exclusion as a "one-time" allowance for FY 2012 and deferred the question of the multi-year implications of any such State cost transfer. Because significant new costs were not imposed in FY 2012, it was unnecessary for the Committee to address this question. Presumably, the FY 2013 General Fund budget will be able to absorb any new costs passed from the State within the confines of the spending guideline.

***Certain appropriations are not subject to the Committee's spending guideline because they do not represent ongoing County program obligations.***

It is important to note that the base spending amount to which personal income growth is applied excludes certain significant appropriations. These exclusions are made based on the premise that the expenditure is one-time/non-recurring in nature (such as certain contributions to the capital budget) or that the expenditure is required to support a State or Federal program (such as in the case of local share matching appropriations). In some cases, the appropriation may represent only a reserve of funds and not an earmarked expenditure. Given the nature of these appropriations, they should not be limited by the growth in the County's economy but rather by some other factor, such as available surplus or projected revenues. Accordingly, such appropriations are not subject to the Committee's spending guideline.

**Figure 2. Calculation of the Spending Guideline**

The spending guideline for the upcoming fiscal year is calculated by applying the spending affordability growth factor to the current year's estimated base spending (as defined by the Committee). Specifically, the recommended spending limit is calculated as follows:

General Fund Operating Budget Appropriations (current fiscal year)
\+ Supplemental Appropriations and Planned "Off-Budget" Spending
\- Estimated General Fund Reversion due to detrimental economic events
\- Appropriations not subject to growth in personal income (see Figure 3 for detail)
Base Spending (current fiscal year)
x Personal Income Growth Factor
Spending Guideline (upcoming fiscal year)

## SPENDING POLICY RECOMMENDATIONS

***The Committee is aware of a significant gap between projected ongoing revenues and expenditures for FY 2013 and urges continued cost-cutting efforts to reduce reliance on surplus for ongoing operations.***

During its deliberations, the Committee learned that ongoing County revenues will be insufficient to fund ongoing expenses in FY 2013, as in FY 2010 and FY 2011, and as anticipated by the FY 2012 budget. Prior to last year, the Committee recommended that the County Executive submit a General Fund budget that avoids the practice of funding ongoing operating expenses with one-time sources of funding. However, for FY 2012 the Committee acknowledged the occasional necessity of utilizing surplus for ongoing expenses during economic downturns. Accordingly, the Committee urges continued cost-cutting efforts to reduce reliance on surplus for ongoing operations, and it reaffirms its other longstanding fiscal policy recommendations, as follows:

***The Committee recommends that the County maintain a sufficient reserve on hand in case an unexpected revenue shortfall reoccurs in FY 2013 or future years. The Committee also recommends that the County Executive avoid underfunding essential items and minimize the use of one-time revenue sources to fund ongoing expenses.***

- The Committee recommends that the County maintain a sufficient reserve on hand in case an unexpected revenue shortfall reoccurs in FY 2013 or future years. Accordingly, the Committee endorses the Administration's adopted policy of striving to produce an unreserved General Fund balance (surplus) near 7% of revenues in these volatile economic times including a revenue stabilization reserve equal to 5% of revenues; establishing a floor level for surplus funds at 3% of revenues; and ensuring that the balance of surplus funds does not fall to the 3% floor level for 2 consecutive years.

- The Committee recommends that the County Executive avoid under-funding essential operating budget items in order to fund other initiatives.

- The Committee recommends that the County Executive strive to submit a General Fund budget that minimizes reliance on one-time sources of funding, such as surplus funds, for ongoing operating expenses.

**Figure 3. Spending Affordability Committee Definition of Base Spending**

Base spending: General Fund spending less appropriations not subject to personal income growth, as itemized below.

Appropriations not subject to personal income growth:

Local Matching Appropriations:

- Local Share—State and Federal Grants. The total required County General Fund match for all anticipated grants is based on the level (and match provisions) of grant funding. These funds support State and Federal programs (not County programs).

- Education—Federal/Restricted Program. The required County General Fund match for such funds in the Department of Education is similarly based on the level (and match provisions) of grant funding. These funds support a Federal program (not County programs).

Capital Project Appropriations:

- The General Fund contribution to the capital budget, if any, is determined annually based on funds that are available and not otherwise committed to supporting County services. Thus, such expenditures may be viewed as one-time outlays, not subject to personal income growth, provided these contributions are not dedicated to funding operating expenses.

Certain Reserve Fund Appropriations:

- Appropriations to the Revenue Stabilization Reserve Account (RSRA) do not represent expenditures but rather a reserve of funds available in case of an operating deficit. These funds are legally required to equal at least 5% of General Fund revenues.

- Contingency Reserve Appropriations are excludable to the extent they represent a reserve for unforeseen needs (e.g., emergencies) and are not earmarked for a specific purpose or program unless the specific purpose or program meets one of the other criteria for exclusion. If contingency reserve funds are spent, the nature of the expenditure must be examined to determine its effect on base spending (i.e., one-time vs. ongoing).

One-Time-Only Appropriations:

- Specific exclusions for extraordinary or special items that represent one-time, nonrecurring costs or revenues (such as spending by the Department of Education for items excluded from the State's maintenance of effort requirement) are determined on a year-to-year, case-by-case basis.

OPEB Accrued Liability (OAL) Appropriations:

- For fiscal years beginning after June 30, 2007, the County began funding its obligation for other post employment benefits (OPEB) on an accrual basis. Due to the significant unfunded accrued liability for OPEB, recognition of the additional annual required contribution resulting from the OPEB accrued liability will be phased-in over 10 years, in 10% increments, until the full amount is recognized by FY 2017. Actual funding in excess of the phase-in amount will be excluded from base spending.

**Figure 4. FY 2013 Spending Guideline**

| | | |
|---|---|---|
| FY 2012 Base Spending | | |
| General Fund Appropriations | $ | 1,603,784,784 |
| General Fund Supplemental Appropriations | | - |
| Appropriations Subtotal | | 1,603,784,784 |
| Estimated Off-Budget Expenditures | | - |
| Estimated Final Spending | | 1,603,784,784 |
| General Fund Exclusions: | | |
| Local Matching Appropriations | | |
| Local Matching Funds | | (6,792,237) |
| Federal Restricted Funds | | (48,428) |
| Capital Project Appropriations | | |
| PAYGO | | (636,805) |
| Reserve Fund Appropriations | | |
| Contingency Reserve | | (1,000,000) |
| One-Time-Only Appropriations | | |
| Baltimore County Public Schools State-Approved One-Time Costs | | (1,595,410) |
| OPEB Accrued Liability (OAL) Appropriations In Excess of Phase-In Amount | | - |
| Total Exclusions | | (10,072,880) |
| FY 2012 Base Spending | | 1,593,711,904 |
| Personal Income Growth 5-Year Average | x | 1.0298 |
| FY 2013 Spending Guideline | $ | 1,641,204,519 |
| ***Maximum Spending Growth*** | ***$*** | ***47,492,615*** |

**Calculation of the FY 2013 OPEB Accrued Liability Phase-in Amount**

FY 2013 is the sixth year of the 10-year phase-in period for recognizing the OPEB accrued liability (OAL) funding under the spending guideline. Therefore, the phase-in amount for FY 2013 is equal to 60% of the actuarial estimate of the annual OPEB accrued liability. Any FY 2013 General Fund OAL appropriations in excess of the 60% phase-in amount shall be excluded from spending subject to the guideline. If FY 2013 General Fund OAL appropriations are less than the 60% phase-in amount, the entire amount appropriated for OAL shall be included in spending subject to the guideline. The FY 2013 OAL phase-in amount is $37,925,400, calculated as follows:

| | | |
|---|---|---|
| Estimated Annual OPEB Accrued Liability (OAL) | $ | 63,209,000 |
| x FY 2013 OAL Phase-In Percentage | | 60% |
| FY 2013 OAL Phase-In Amount | $ | 37,925,400 |

## ECONOMIC GROWTH

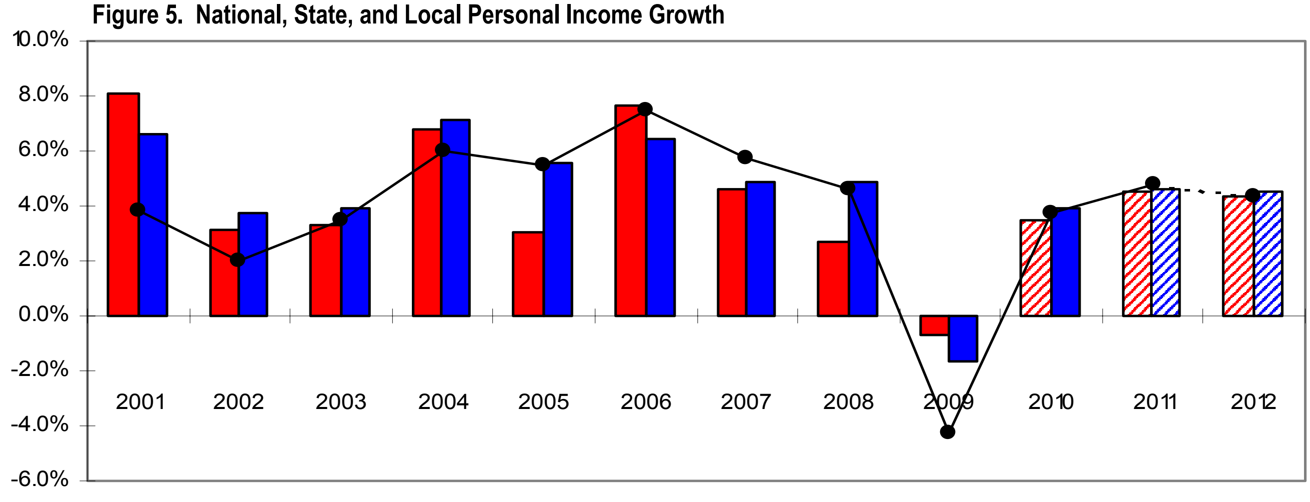
***Personal income growth estimates are rising for FY 2012 and FY 2013 and are approaching historic averages.***

Prior to adopting its FY 2013 personal income growth rate, the Committee reviewed current and projected economic conditions to gain an understanding of the basis for the consultant's personal income estimates and forecast. In its report dated January 13, 2012, the consultant (Sage Policy Group, Inc.) predicts that Baltimore County personal income will grow 4.00% in FY 2012, which is 10 basis points below its Maryland FY 2012 personal income growth forecast of 4.10%. Similarly, the consultant projects that FY 2013 personal income growth in the State (4.99%) will exceed the County personal income growth (4.80%) by 19 basis points. Over the 2001 to 2011 period, estimated County personal income increased at an average annual rate of 4.2%, compared to 4.6% and 3.9% in Maryland and the U.S., respectively (Figure 5).

***In light of the mixed performance among the various sectors represented on the Baltimore County Economic Advisory Committee, members expressed caution regarding the near-term economic outlook at their January 11, 2012 meeting.***

The January 11, 2012 meeting of the Baltimore County Economic Advisory Committee (BCEAC) provided further insight into local economic conditions. The BCEAC members predicted that the economy will continue to recover, albeit slowly, through the remainder of calendar year (CY) 2012. The panel reported that some companies are beginning to hire, and that even though unemployment will remain high by historical standards for the foreseeable future, the unemployment rate is trending downward. In addition, members noted that anecdotal data suggest a strong 2011 holiday season in the retail sector, which is a positive sign for the commercial real estate market. On the residential side, the panel reported that sales activity has risen in recent months; however, due to the large number of foreclosures that have not yet hit the market, prices in many areas are expected to remain low for the foreseeable future. The manufacturing sector, which is often considered a leading indicator for the overall economy, has been up and down in recent months, with many manufacturers reporting that it has been difficult to make sales. Members also observed several downside risks to the regional economy in CY 2012 and CY 2013, most notably federal government downsizing and cuts in defense spending, both of which would significantly impact local contractors that depend heavily on federal funds. In light of these mixed sentiments, members expressed a cautious near-term outlook for the local, regional, and national economies.

**Figure 5. National, State, and Local Personal Income Growth**




*Note: Lighter columns and dashed lines represent estimates.*

*Estimate Source: Sage Policy Group, Inc., January 2012*

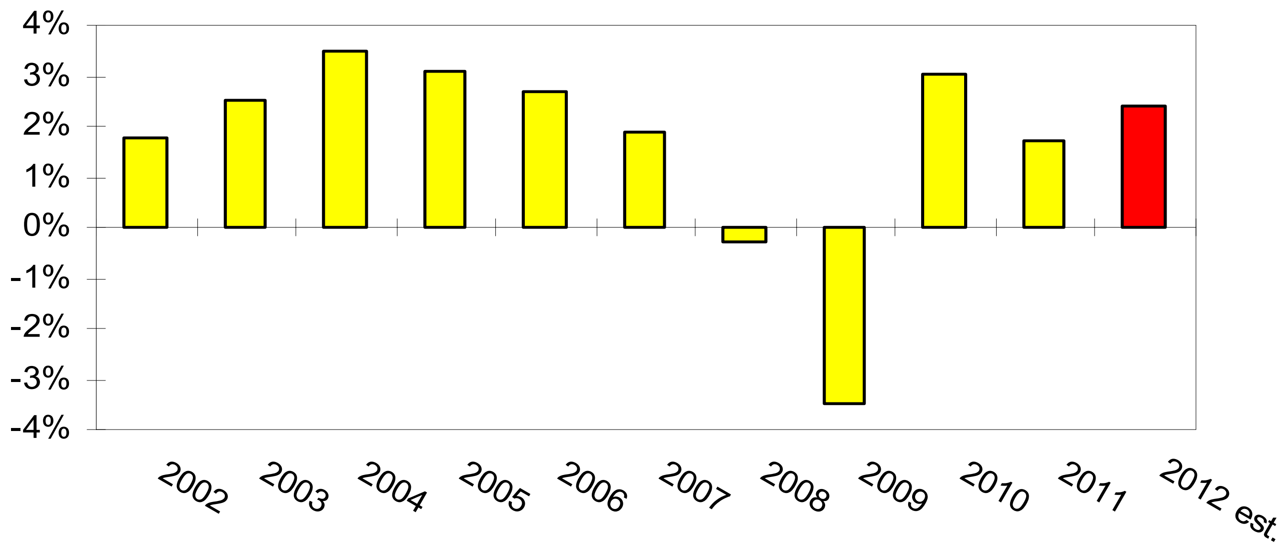
***Real Gross Domestic Product (GDP) grew at an average annual rate of 1.6% from CY 2002 to CY 2011. For CY 2012, real GDP is expected to increase by 2.4%.***

Projections for the local economy are influenced, to a large degree, by the underlying performance of the national and state economies. Nationally, both the housing market and household spending continue to be unpredictable. In CY 2012 consumer spending is expected to increase, albeit at a slightly slower pace, for the third consecutive year after falling in CY 2008 and CY 2009. However, unemployment remains well above pre-recession levels, and credit markets remain constrained despite government efforts to secure them. In addition, the future of federal spending continues to be a source of concern, particularly in this region. While the National Bureau of Economic Research determined that the recent U.S. recession ended in June 2009, the economy remains in recovery, and many sectors are still far from pre-recession performance levels. Over the last decade, real GDP grew by an average of 1.6% annually from CY 2002 to CY 2011, including contractions of 0.3% in CY 2008 and 3.5% in CY 2009. After growing 3.0% in CY 2010 and 1.7% in CY 2011, real GDP is projected to increase by 2.4% in CY 2012, according to the Federal Reserve Bank of Philadelphia's November 2011 *Survey of Professional Forecasters* (Figure 6).

***Employment has risen since this time last year, following 3 consecutive years of decreases.***

Employment increased by 0.7% among both Baltimore County and Maryland residents and by 1.2% nationally on a year-over-year annual average basis from CY 2010 to CY 2011, following 3 consecutive year-over-year decreases at all levels. While employment is finally on the rise, the pace of job growth is insufficient to replace the jobs that were lost in the last 3 years. Baltimore County's and Maryland's December 2011 unemployment rates were 6.9% and 6.5%, respectively, and averaged 7.5% and 7.0%, respectively, for all of CY 2011. Over the past 10 years, the annual unemployment rates in Baltimore County and Maryland were, on average, 140 and 150 basis points below the national rate, respectively. The *Survey of Professional Forecasters* projects a national unemployment rate of 8.8% in CY 2012 and 8.4% in CY 2013. If the trends between the national and local unemployment rates hold, Baltimore County and Maryland are already within the anticipated unemployment range for CY 2012 (7.4% and 7.3%, respectively), a positive sign for the local economy.

**Figure 6. Real Gross Domestic Product: Annual Percentage Change**




*Estimate Source: Federal Reserve Bank of Philadelphia's* Survey of Professional Forecasters, *November 2011*

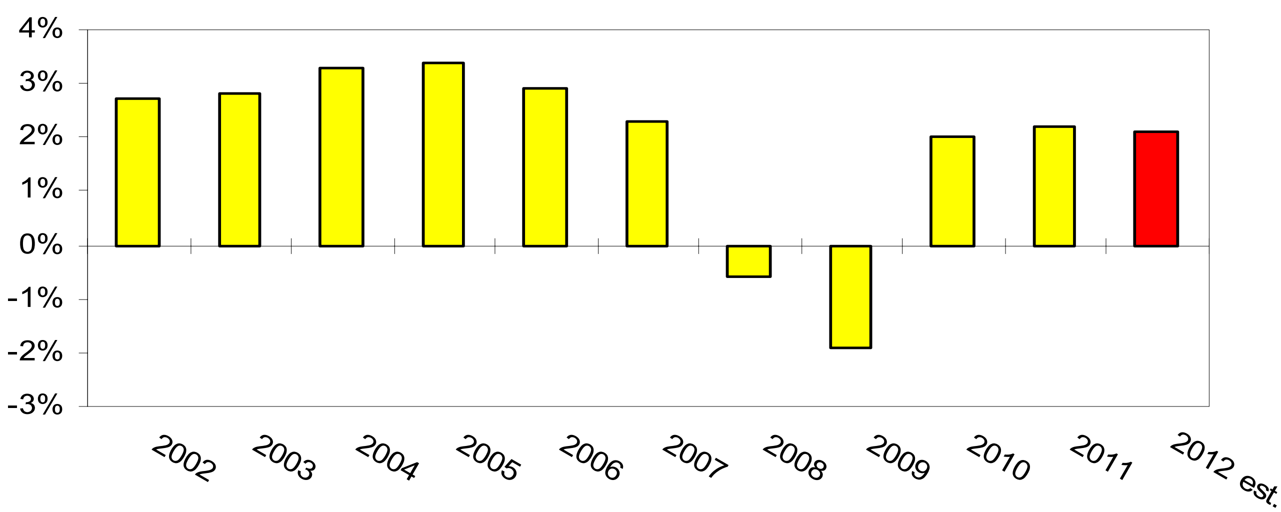
***Consumer spending increased at a rate of 2.2% in CY 2011, the second consecutive increase following two annual declines.***

Consumer spending, which typically accounts for slightly more than two-thirds of all U.S. economic activity, is the primary determinant of future economic performance (Figure 7). Consumer spending increased at a rate of 2.2% in CY 2011, the second increase following declines in CY 2008 and CY 2009. In January 2012, national unemployment reached its lowest level (8.3%) since February 2009, indicating some small impetus for increased consumer spending. Consistent with this employment report, based on a survey of 5,000 U.S. households by the Conference Board, consumer confidence posted strong gains in November and December 2011. However, consumer confidence retreated in January, with the "Present Situation" index experiencing the bulk of the decline and the "Expectations" index falling only slightly. The Conference Board signaled that consumers' view of current business and labor market conditions worsened, while over the short-term consumers are more up-beat about job availability but less optimistic about business conditions and their income prospects. The Conference Board further noted that the recent rise in gasoline prices may have consumers feeling less confident.

***Disparate economic indicators such as rising consumer spending and persistently high unemployment levels have led many to expect a continued slow recovery in CY 2012.***

The national economy's most significant challenge in the coming months is a persistently high unemployment rate. Forecasters participating in the Federal Reserve Bank of Philadelphia's November 2011 *Survey of Professional Forecasters* project 8.8% unemployment during CY 2012, reflective of the slow pace of recovery since the 26-year unemployment high of 10.0% in October 2009. The *Survey* anticipates continued growth in consumer spending and GDP in CY 2012 and future years, with GDP growth expected to reach 3.5% by CY 2014. However, the continued high unemployment rate, unstable housing market, and tight credit market will temper the positive effects of rebounding spending and GDP growth. The Maryland and Baltimore County economies are likely to continue to recover slowly along with the national economy, with the biggest threat to the regional recovery being the potential decline in federal spending. In this regard, the BCEAC concluded at its January 2012 meeting that while Baltimore County will see some signs of economic recovery in 2012, the recovery will be far from robust.

**Figure 7. Real Consumer Spending: Annual Percentage Change**




*Estimate Source: Federal Reserve Bank of Philadelphia's* Survey of Professional Forecasters, November 2011

## GENERAL FUND REVENUES AND SURPLUS

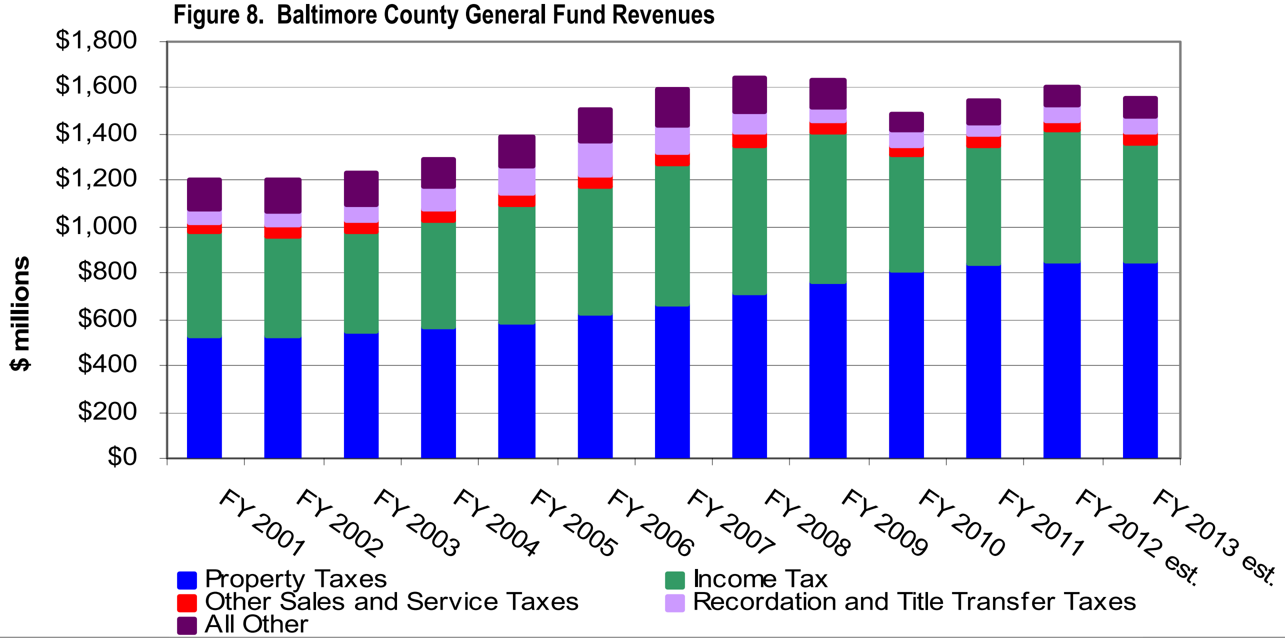
***FY 2012 General Fund revenues are projected to increase by $60.0 million, or 3.9%, over FY 2011 totals. This projection is $64.7 million higher than current-year budgeted revenues.***

FY 2012 projected revenues total $1,607.9 million, an increase of $60.0 million, or 3.9%, over FY 2011 revenues (Figures 8 and 9). This projection represents an increase of $64.7 million, or 4.2%, over FY 2012 budget estimates. The projected revenue increase is primarily due to higher-than-anticipated income tax revenues resulting from strong final payments and a decline in refunds at the State level for tax year 2010. In addition, property-related transaction tax revenues (i.e., title transfer and recordation tax revenues) are coming in slightly above expectations. Growth in property tax revenues has slowed significantly because the annual 4% growth limit pursuant to the local Homestead Property Tax Credit Program has caught up with declining assessed values. Higher-than-anticipated revenue collections, combined with various cost-cutting measures implemented by the Administration, are expected to allow the County to finish FY 2012 without drawing on the $60.6 million in surplus funds budgeted for FY 2012.

***FY 2013 General Fund revenues are projected to decrease by $50.3 million, or 3.1%, from the revised FY 2012 estimate.***

FY 2013 General Fund revenues are projected to reach $1,557.6 million, down approximately $50.3 million, or 3.1%, from the revised FY 2012 revenue estimate, but up $14.4 million, or 0.9%, over budgeted FY 2012 revenues. The projected decrease in FY 2013 General Fund revenues, which represents the first decline since FY 2010 and the third decline in the last two decades, primarily reflects an anticipated decline in income tax revenues in FY 2013 resulting from the State's method of distributing income tax revenues. In addition, growth in property tax revenues is expected to continue to slow due to falling assessments. Property-related transaction tax revenues are expected to show modest gains based on the expectation that the housing market has finally hit bottom and sales volume will continue to recover in FY 2013 while prices remain flat. The State aid reductions implemented in recent years (estimated at $44.3 million in FY 2012) are expected to continue in FY 2013 as a result of the State's budgetary challenges.

**Figure 8. Baltimore County General Fund Revenues**




*Sources: FY 2006 to FY 2011 Baltimore County Comprehensive Annual Financial Reports*

**Figure 9. General Fund Revenue Forecast, FY 2012-FY 2013**

($ Million)

| REVENUE SOURCE | FY 2011 Actual | FY 2012 Budget | FY 11 - FY 12 Bud. | FY 2012 Revised | FY 11 - FY 12 Rev. | FY 2013 Estimate | FY 12 Bud.- FY 13 | **FY 12 Rev.- FY 13** |
|---|---|---|---|---|---|---|---|---|
| Property taxes | $837.1 | $847.9 | 1.3% | $847.7 | 1.3% | $852.8 | 0.6% | 0.6% |
| Income taxes | 514.7 | 508.5 | -1.2% | 570.7 | 10.9% | 508.7 | 0.0% | -10.9% |
| Recordation & title transfer taxes | 54.0 | 61.0 | 13.0% | 63.7 | 18.0% | 68.2 | 11.8% | 7.1% |
| Other Sales and Service taxes | 43.1 | 46.0 | 6.7% | 43.8 | 1.6% | 43.8 | -4.8% | 0.0% |
| Intergovernmental aid | 34.2 | 31.6 | -7.6% | 31.5 | -7.9% | 32.5 | 2.8% | 3.2% |
| Services charges | 10.0 | 10.5 | 5.0% | 10.5 | 5.0% | 10.7 | 2.0% | 2.0% |
| Fines, forfeitures & penalties | 3.9 | 3.8 | -2.6% | 3.9 | 0.0% | 4.1 | 7.9% | 5.1% |
| Licenses & permits | 3.9 | 3.5 | -10.3% | 4.1 | 5.1% | 4.2 | 20.0% | 2.4% |
| Interest on investments | 0.8 | 1.7 | 112.5% | 1.0 | 25.0% | 1.3 | -22.9% | 31.0% |
| Other | 46.3 | 28.7 | -38.0% | 31.0 | -33.0% | 31.3 | 9.1% | 1.0% |
| **TOTAL** | **$1,547.9** | **$1,543.2** | **-0.3%** | **$1,607.9** | **3.9%** | **$1,557.6** | **0.9%** | **-3.1%** |

Note: Totals may not add due to rounding.

***The FY 2013 revenue projection is $84 million lower than the Committee's spending guideline.***

The FY 2013 revenue projection is approximately $84 million lower than the Committee's FY 2013 spending guideline. In light of this anticipated gap, the Committee fully expects the Administration to propose and implement a responsible financial plan that will both minimize the spending in excess of County revenues that is necessary to conduct County business and limit the use of fund balances.

***The FY 2011 General Fund surplus totaled $80.6 million, excluding $84.6 million of RSRA funds.***

As of June 30, 2011, the unassigned General Fund balance (surplus) totaled $80.6 million, or 5.0% of the FY 2012 General Fund budget. This amount does not include $84.6 million in the Revenue Stabilization Reserve Account (RSRA). In addition, $60.6 million of General Fund balance was assigned as a source of funding for the FY 2012 budget.

***The FY 2012 General Fund surplus is projected to total $144.9 million, excluding $85.0 million in the RSRA.***

The projected June 30, 2012 unassigned General Fund balance (surplus), assuming FY 2012 revenues of $1,607.9 million, totals $144.9 million, or 9.0% of projected FY 2012 revenues (Figure 10). This amount, plus an estimated $85.0 million in the RSRA, totals $229.9 million, or 14.3% of projected FY 2012 revenues. The unassigned surplus, which exceeds the gap between the FY 2013 revenue projection and the Committee's FY 2013 spending guideline, will be available as a source of funding for the FY 2013 budget. The Committee recognizes the necessity and prudence of using surplus funding during difficult economic times.

**Figure 10. Estimated General Fund Surplus, FY 2012**

($ in Millions)

| | | |
|---|---|---|
| **FY 2011 General Fund Surplus (excluding RSRA funds)** | | **$ 80.6** |
| FY 2012 Revenue Estimate (per Adopted Budget) | 1,543.2 | |
| FY 2012 Revision | 64.7 | |
| FY 2012 Revised Revenue Estimate | 1,607.9 | |
| FY 2011 General Fund Balance Designated to Fund FY 2012 Appropriations | 60.6 | |
| FY 2012 Total Funding | | 1,668.5 |
| FY 2012 Adopted Budget | | (1,603.8) |
| FY 2012 Interest Transfer to the RSRA | | (0.4) |
| **FY 2012 Estimated General Fund Surplus** | | **$ 144.9** |

## DEBT GUIDELINES

*The Committee adopts two debt guidelines, one pertaining to total debt outstanding and the other to debt service.*

The Committee's debt affordability recommendations provide an enhanced system of checks and balances, further demonstrating the County's fiscal responsibility to its citizens, bond-rating agencies, and others in the financial community. The debt guidelines are based on: (1) the County's total debt outstanding as a percentage of assessed property value; and (2) the County's level of debt service as a percentage of total General Fund revenues. Actual debt service expenditures and the amount of total debt outstanding have consistently remained below the Committee's guidelines.

During this year's deliberations, the Committee did not consider any changes to its maximum recommended debt ratios.

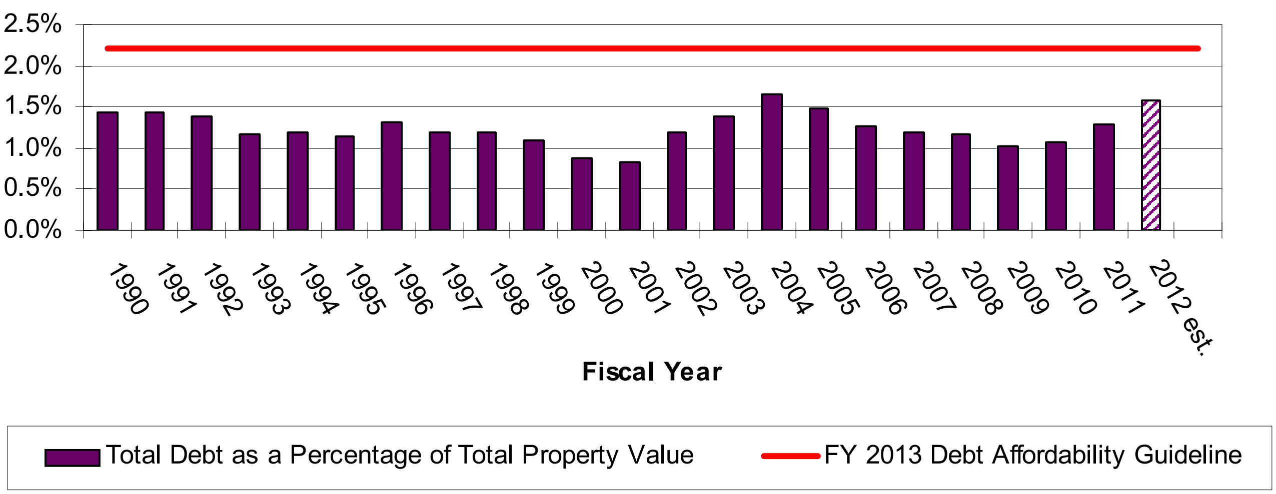
### Total Debt Outstanding Guideline

*The Committee recommends that total debt outstanding not exceed 2.2% of total assessed property value.*

The ratio of total debt outstanding to total assessed property value is a measure of debt affordability. Since 2004, the Administration's financial guidelines have set a target range of 1.8% to 2.2% for debt outstanding as a percentage of total assessed property value. Prior to FY 2007, the Committee's guideline was set at 2.0% and applied only to real property. Beginning in FY 2007, the Committee raised its limitation on total debt outstanding from 2.0% to 2.2% of total assessed property value, including real and personal property, based on a study prepared by the County's independent financial consultant. From FY 1990 to FY 2012, total debt outstanding has ranged from 0.8% to 1.7% of the County's total assessed property value (Figure 11). In recent years, the total debt outstanding ratio has been rising as the availability of General Fund Pay-As-You-Go contributions to the capital budget has decreased and the growth in assessable base has slowed.

In accordance with the Committee's policy that total debt outstanding should not exceed 2.2% of total assessed property value, **the Committee recommends that total debt outstanding during FY 2013 not exceed $1,777,191,460, or 2.2% of total assessed property value of $80,781,430,000.**

**Figure 11. Total Debt as a Percentage of Total Assessed Property Value**




Note: Excludes debt related to pension funding, metropolitan district bonds, and component unit capital leases not budgeted under Primary Government; FY 2012 debt outstanding is an estimate.

*Sources: Baltimore County Annual Budget Documents; Baltimore County Office of Budget and Finance; Maryland State Department of Assessments and Taxation*

## Debt Service Guideline

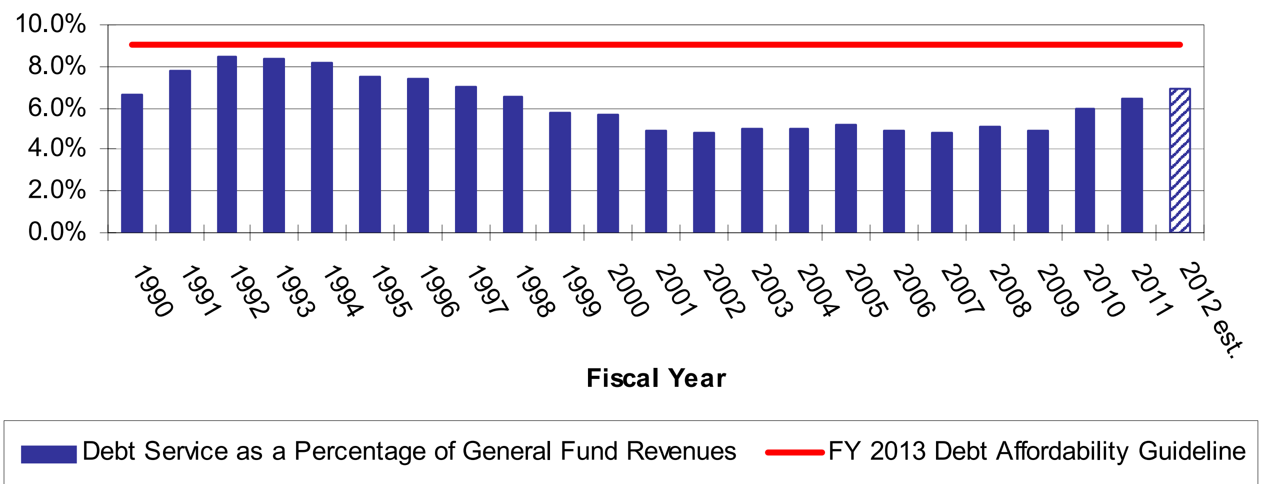
***The Committee recommends that debt service not exceed 9% of total General Fund revenues.***

The ratio of debt service to total General Fund revenues is a debt affordability indicator used not only by Baltimore County but by many other jurisdictions. Credit analysts generally concur that a ratio higher than 1:10 (i.e., over 10%) suggests that the debt burden is too heavy. The Administration's financial guidelines historically have set a target range for debt service expenditures at 8% to 9% of total General Fund revenues. From FY 1990 to FY 2012, the amount spent or budgeted for debt service ranged from 4.8% to 8.5% of total General Fund revenues (Figure 12). The Committee has established a policy that debt service should not exceed 9% of total General Fund revenues. **Accordingly, for FY 2013, the Committee recommends that debt service expenditures not exceed $140.2 million based on projected revenues totaling $1,557.6 million.**

***The recent rise in the ratio of debt service to total General Fund revenues reflects the challenging economic times, which have resulted in lesser availability of PAYGO funding and a lower General Fund revenues denominator.***

The ratio of debt service to total General Fund revenues from FYs 1990 through 2012 is shown below in Figure 12. The decrease in this ratio, beginning in the mid-to-late 1990s, is not reflective of a reduction in County capital spending, but rather is the result of increased usage of Pay-As-You-Go (PAYGO) operating budget funds to finance the County's capital budget. Such PAYGO usage also allowed the ratio to remain steady, hovering at around 5%, from FY 2001 to FY 2009, despite an aggressive capital budget over that period. In recent years the ratio has been rising, largely due to the challenging economic times, which have resulted in diminished General Fund revenues, and accordingly, less available PAYGO funding to offset the need for debt issuance.

**Figure 12. Debt Service as a Percentage of Total General Fund Revenues**




Note: Excludes debt service related to pension funding, metropolitan district bonds, and component unit capital leases not budgeted under Primary Government; FY 2012 ratio is an estimate.

*Sources: Baltimore County Annual Budget Documents; Baltimore County Office of Budget and Finance; Baltimore County Office of the County Auditor*