Maryland
STATE
TREASURER
Investing for Maryland's future.

TREASURER'S REPORT TO

LEGISLATIVE POLICY COMMITTEE

June 6, 2011

Nancy K. Kopp

State Treasurer

Section 5-104 of the State Government Article of the Annotated Code of Maryland provides that, *"The Treasurer shall address the Legislative Policy Committee of the General Assembly on a semi-annual basis and as necessary on issues of legislative importance, including the activities of the Board of Public Works, bond sales, and investment and procurement initiatives."* This Report is in fulfillment of that law and covers the period since the report of December 16, 2010. I invite and welcome further discussion with the Committee at your convenience.

The State Treasurer's activities and responsibilities are of particular concern to the Legislature. One of seven statewide Constitutional officers, and the only one elected by the General Assembly, the State Treasurer's duties are multifaceted and extend throughout State government and higher education. The Treasurer's duties include membership on the Board of Public Works and Board of Revenue Estimates and Chairmanship of the Capital Debt Affordability Committee. The Treasurer presently also serves as Chair of the Board of Trustees of the College Savings Plans of Maryland and the Board of Trustees of the State Retirement and Pension System. She is a member of the governing boards of the Teachers' and Employees' Supplemental Retirement Plans, the Maryland Health and Higher Education Facilities Authority, the Maryland Small Business Development Financing Authority and of the Maryland Agricultural Land Preservation Foundation. Several of these Boards work under the general oversight of legislative oversight committees which are in periodic receipt of reports and communications from the Office, as do the two legislative budget committees.

Due to the strength and diversity of Maryland's economy, the State's fiscal picture seems to be improving. While the State continues to face fiscal challenges, the Office continues to rely on the expertise of its small staff to work with agencies in improving their business processes. The Office continues to assist State agencies in many ways including expanding the use of innovative banking services such as remote deposit, negotiating reduced insurance premiums while enhancing coverage, and advising on procurements. We have also worked to improve our internal information technology programs to allow the Treasurer's staff to perform their functions more efficiently.

We continue to plan and conduct our bond sales effectively, while striving to maintain Maryland's coveted AAA bond rating. We monitor the market routinely to take advantage of savings as they become available in refunding our General Obligation Bonds or to issue new types of debt such as Qualified School Construction Bonds, Qualified Zone Academy Bonds and Qualified Energy Conservation Bonds. Lastly, we continue to invest State funds prudently and conservatively to minimize risk to the Maryland taxpayers.

While we continue to be fiscally constrained, the Office is working hard and achieving real results. The items set forth below detail a number of these achievements and we are always available to provide greater information or answer questions regarding these and other issues.

BOARD OF PUBLIC WORKS

Between November 17, 2010 and May 18, 2011, the Board of Public Works (BPW) acted on 947 items valued at $5,180,492,244.

Among the numerous contracts, wetland licenses, land and easement acquisitions and lease modifications approved during the past six months, the following represents the scope of actions overseen by the Maryland Board of Public Works, the only constitutionally mandated organization of its type in the nation:

- An Integrated statewide Public Safety Wireless Communications System at a cost of $345 million.
- The start of the State Center Project in Baltimore – The building of the parking garage that the State will eventually own and run will cost approximately $33 million.
- Design/Build Services for the relocation of Margaret Brent Hall at St. Mary's College of Maryland at a cost of $530,100.
- $40.9 million in Certificates of Participation for VLT's financing for Perryville in Cecil County and Ocean Downs Racetrack in Berlin in Worcester County.
- $264.6 million for the approval of the recommendations of the Interagency Committee on School Construction Program for FY 2011.
- $1 million for Pierce's Park Development in Baltimore City.
- Renovations to the Thomas Hunter Lowe House of Delegates Office Building at the cost of $9.9 million.
- The Dorsey Run Correctional Facility Design and Construction Project in Jessup at a cost of $22.5 million.
- Towson Center Arena Guaranteed Maximum Price project at a cost of $12.1 million.
- Rails-to-Trails (RTT) Park in Easton at a cost of $283,000.
- $171,237.50 for the acquisition of 200.12 acres in the Cedar Island Wildlife Management area.
- Phase II Energy Performance Contract at University of Maryland, College Park at the cost of $2.6 million.
- $686,551.51 for a 133.57-acres land acquisition in the Mid-Maryland Washington Rural Legacy Area in Washington County.
- Declaring as surplus, a portion of the Department of Housing and Community Development headquarters' site known as 100 Community Place in Crownsville in Anne Arundel County including an estimated 57.56 acres improved with office building and parking lot.

The Treasurer's Office communicates frequently with legislators and their staffs about the board agenda and items of specific interest to their districts. Feedback from legislators is essential to the Treasurer, as she represents the legislature on the Board of Public Works. The Treasurer's Office also receives comments and advice from the Department of Legislative Services to ensure that BPW agenda items are consistent with legislative policy.

INVESTMENT DIVISION

Once again, the Treasurer's conservative investment policy and practices have protected the portfolio through these continued volatile and unprecedented economic times. The par value of the General Fund investment portfolio for April 30, 2011 was $5,853,506,606.30 as compared to April 30, 2010 when it was $5,230,524,497.05. This is an increase of over $622 million dollars.

On April 30, 2011, the portfolio was earning an average of 2.512%, compared to 2.546% for the same date in 2010. The return reflects the impact of the Federal Open Market Committee maintaining the Fed Funds Target rate at .25% or less since December 16, 2008. For comparison, the three month constant maturity Treasury Bill averaged .15% since July 2010 as compared with .13% for the same time period in the previous fiscal year. The low rate environment combined with the highly conservative portfolio strategy focused on liquidity to offset unpredictable and volatile cash flows has resulted in continued moderate but positive interest earned.

The General Fund gross interest earnings received year-to-date for FY 2011 are $26,395,029 as compared with $43,268,247 received for the same time period in FY 2010. The over $16 million decline in interest received is directly attributable to the continued lower interest rate environment.

Total Interest Earned
% of Total Interest Earned Allocated to State Agencies

Fiscal Year	Net General Fund	Allocated to State Agencies	Total
2000	121,951,720	103,173,287	225,125,007
2001	136,981,074	144,249,899	281,230,973
2002	82,641,807	66,399,769	149,041,576
2003	37,205,637	42,240,523	79,446,160
2004	25,037,345	29,053,449	54,090,794
2005	52,886,074	54,538,463	107,424,537
2006	149,613,238	109,222,108	258,835,346
2007	150,798,001	205,589,917	356,387,918
2008	155,170,184	207,179,098	362,349,282
2009	102,768,740	142,619,087	245,387,827
2010	44,190,425	87,921,654	132,112,079
Apr-11	26,395,029	72,664,028	99,059,057

The Securities Lending Program continues to provide additional revenue. The program has earned $235,185.11 so far in FY 2011. This compares with $119,319.29 for the same period in FY 2010. The Federal Reserve and Federal Treasury programs designed to add liquidity to the financial markets which reduced borrowers' need for the securities in the State's portfolio is beginning to be scaled back.

The Office continues to increase Minority Business Enterprise participation in the investment of State funds. Nineteen MBE broker/dealers are on the Office's approved list for FY 2011 and they have handled investments of over $1 billion so far this fiscal year. This compares favorably to FY 2010, when the Office had 15 approved broker/dealers who handled over $527 million in investments by the end of April.

The Maryland Local Government Investment Pool (MLGIP) AAAm rating was reaffirmed by Standard and Poor's on March 28, 2011. The pool balance at April 30, 2011 was $2,594,709,558.11 compared with $2,476,891,571.33 for the same date in 2010. This is an increase of over $117 million dollars due to the lack of safe short term investment alternatives for investment pool members at a comparable yield. The MLGIP is paying .14% as of April 30, 2010 as compared with .18% last year. The MLGIP is in total compliance with the new Money Market rules and regulations.

The Office continues to invest according to the officially adopted State Treasurer's Investment Policy, which sets out investment goals, priorities and constraints. The overriding goal is to assure sufficient liquidity to maintain uninterrupted funding of State government and legislated payments. As revenues have become less predictable and more volatile, the strategy has been adjusted to ensure liquidity. The Office continues to review and compare our cash management and investment policies and practices with those of peer AAA-rated states to ensure best practices are followed and implemented.

BANKING SERVICES DIVISION

Maintaining the Banking Services Division's mission of providing efficient, accurate and timely banking services to all State agencies and external customers is essential in the current economic environment. We are driven to continually explore new financial products and improved data delivery methods that will create current efficiencies in State agencies' processes while anticipating the State's future banking needs. The Division must maintain the capacity to contain costs while accommodating for the growth, diversity, and complexity of banking transactions.

The Division's continual processing and reconciliation advancements allow the Treasurer's Office to be proactive in identifying and solving agency banking issues. These processes and controls ensure the timely, accurate, and completely documented reconciliation of the State's cash accounts. Current highlights of the results of the Division's efforts include:

- Total cash receipts and disbursements will each reach $175 billion for FY 2011.

- The State's bank accounts continue to be reconciled daily to the State's general ledger within two days of receiving all necessary bank data.

• There are no un-reconciled differences. We reconcile the State's cash accounts to the penny every day.

In spite of the recent turnover of several employees in the deposit reconciliation group, Banking Services has been unwavering in ensuring agencies' deposit posting processes remain timely and accurate. It is the responsibility of the Division to ensure bank deposits equal recorded general ledger deposits. Accurate outstanding deposit totals are vital to precise cash reconciliation.

Banking Services met its January 1st target date for implementation of the new Treasurer's Bank Account Information System (TBAIS). This system replaced the BAIS system previously maintained by the Comptroller's General Accounting Division. The new system allows for a more efficient set up and approval process for agency bank accounts. We continue working to enhance and further automate the management and control of the State's bank accounts, including the collateralization of State funds.

The efforts to convert recurring vendor check payments to electronic payments remains a joint focus of the Treasurer's Office and the Comptroller's Office. This is being done to increase controls and efficiencies in the disbursement process.

We continue to actively work with agencies to develop and strengthen their internal processes and to promote efficient banking services. We are working closely with Bowie State University and UMBC in their conversion of tuition refunds from checks to electronic payments. We are also working with Maryland Department of the Environment in setting up their ability to receive ACH and credit card payments through their web site.

To further our work and communications with State agencies, Banking Services presented at the January Maryland State Internal Auditor Forum as well as to a Motor Vehicle Administration quarterly managers meeting.

Finally, as noted in past reports, we are continually working on standardizing our tracking, processing, and reconciliation of bank related transactions for the State's cash accounts in order to ease the ability to change banks if required by market conditions or the procurement process.

INSURANCE DIVISION

The Insurance Division is responsible for administering the State's Insurance Program which is comprised of both commercial and self-insurance. Commercial insurance policies are procured to cover catastrophic property and liability losses, and other obligations derived from State contracts, statutes and regulations. Among the several exposures covered by commercial policies are State maintained toll bridges and tunnels, the Baltimore Washington International Thurgood Marshall Airport and the Port, rail operations, assorted professional liability exposures and student athlete accidents. The State also self-insures a significant portion of its exposures and maintains the State Insurance Trust Fund to pay claims and the costs associated with handling those claims. Self-insurance coverage includes State-owned real and personal property, vehicles, and liability claims covered under the Maryland Tort Claims Act.

The Insurance Division is comprised of three units: Underwriting, Loss Prevention, and Claims. The Division's goal is to provide Statewide risk management through loss protection (Underwriting), loss control (Loss Prevention), and loss restoration (Claims and Tort Litigation).

Underwriting

The Insurance Division procures broker services for the purchase of commercial insurance to protect the State Insurance Trust Fund from catastrophic loss, to meet statutory or regulatory requirements, and for compliance with agency contractual agreements. Underwriting highlights for the past six months include the following:

The State's FY 2011 Blanket Excess Property coverage renewed on April 1, 2011. The State's property values were up 4% this year over last. Nevertheless, the property insurance broker negotiated a **rate reduction of 5.3%, so that our annual premium actually decreased by $52,753.**

The Maryland State Police Aviation Command (MSPAC) benefited from "layup" credits accruing in FY 2011. Layup credits are earned for hours when aircraft are grounded for safety inspections and maintenance. In the past six months, MSPAC **earned a return premium of $33,763** as a result of that beneficial coverage provision.

The Underwriting Unit frequently addresses agencies' questions about commercial insurance and self insurance coverage and has worked with at least six agencies on special projects during the second half of FY 2011.

For example, the Director of the Insurance Division and the Underwriting Manager consulted with MDOT's Chief of Procurement on an upcoming RFP for the operation of the Brunswick and Penn Line commuter rails; with MPA regarding the 9-11 Memorial that will be placed in front of the World Trade Center; with DJS regarding an expansion of foster care services into Delaware; with MdTA about a planned "bridge" over I-95 in Cecil County; with UMCES about an autonomous underwater vehicle (AUV); and with SHA about their collaboration with State Farm Insurance to provide expanded emergency patrol services on Maryland highways.

Loss Prevention

On May 15, 2011, 85 flight crewmembers of Maryland State Police Aviation Command (MSPAC) completed an online training certification program on fatigue management. This program was arranged by the Loss Prevention Manager in conjunction with our insurance broker, to provide crewmembers with the knowledge, strategies and tools to achieve peak performance and safety through optimal sleep and alertness. This service was provided to MSPAC to address one of the safety recommendations made by the National transportation Board following the tragic crash on September 27, 2008, involving Trooper II.

Following the success of the historic valuation of the Maryland State House and the appreciation of the report with its recommendations for preservation by the Maryland Historic Trust and the Maryland Archives, the Loss Prevention Manager has arranged an historical valuation of Davidge Hall, located at the University of Maryland, School of Medicine. The facility is recognized as the oldest medical facility in the country in continuous use for medical education.

This period, the Loss Prevention Manager and Predictive Services Inc., the State's vendor for aerial infrared testing, have mapped all State buildings and determined the square footage of the roofing systems, to compile a plan for future testing.

The Loss Prevention Manager attended State boiler and pressure vessels' inspections with the risk engineer for boiler and machinery coverage. Inspections took place at the University of Maryland Chesapeake Bio Lab in Solomons Island, Maryland; Department of General Services' Annapolis Complex (Central Services, Legislative Library, Annapolis Data Center, Governor's Mansion, Jeffery Building, State House, Treasury Building, Miller Senate Building); and the State Highway Administration in Annapolis, Maryland. These inspections are conducted annually to ensure the equipment is properly maintained to meet intended operational conditions in accordance with State law.

In February 2011, the Loss Prevention Manager finalized the selection of agencies designated for infrared testing of electrical systems. Subsequently, a meeting was held with risk engineers and Infrared Testing Inc., the State's vendor for testing, to plan the program for the current year. Infrared testing of electrical systems is currently underway for the Department of General Services (Maryland State House, Louis Goldstein Treasury Building, William Donald Schaefer Towers, and Martin District Court), the Department of Juvenile Services (Cheltenham Youth Facility), the Department of Public Safety and Correctional Services (Eastern Correctional Institute and Western Correctional Institute), the Maryland Stadium Authority (Camden Yards, M&T Bank Stadium, and the Hippodrome Theatre), Morgan State University (Murphy Fine Arts Center), the Maryland Port Administration (Locust Point Marine Terminal and the World Trade Center), and the Maryland African American Museum Corporation (Reginald Lewis Museum). This testing identifies hot spots in the electrical distribution system so that appropriate action can be taken before costly repairs and down time are incurred.

Claims

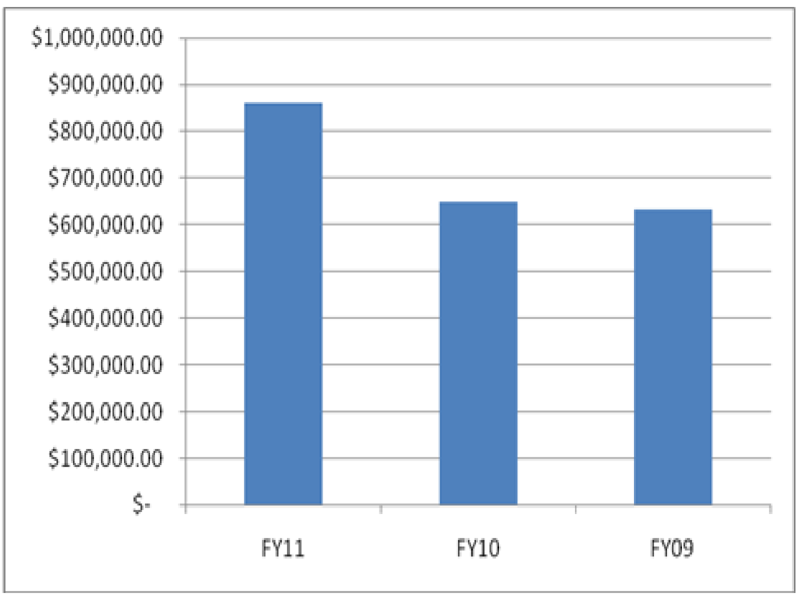
The Insurance Division's Claims Unit investigates and resolves liability claims filed under the Maryland Tort Claims Act, Md State Gov't Code Ann. §§12-101 *et seq.* The Unit also handles claims for damage to State-owned property arising from sudden and accidental perils such as collision and comprehensive losses to autos, and a number of other perils such as fire, hail, lightning, and wind which may cause damage to State structures, equipment, and contents.

In addition to adjusting claims filed under the Maryland Tort Claims Act, the Unit is also charged with recovering the cost of damage to State automobiles and property caused by others. This subrogation recovery process helps to offset State Insurance Trust fund liabilities and positively affects the fund's solvency. Since 2007, the Claims Unit has focused on increasing subrogation recoveries by designating specific claims personnel to pursue these debts.

In December, 2010, the Unit hired a Casualty Claims Adjuster whose primary responsibility is to pursue subrogation recoveries. This strategy yielded remarkable results. Year-to-date **recoveries in FY 2011 of $860,211** surpassed both FY 2009's recovery total of $632,398 and FY 2010's recovery total of $648,963 by over 30%.

The highest single recovery also occurred in FY 2011. A high value library van was damaged as a result of the negligence of a third party. The Unit recovered the full cost of repairs which amounted to $44,038.

Claims Subrogation Recoveries



Cost-effective professional development

As part of the Division's commitment to professional development, in April 2011, the Claims Unit adjusters participated in training developed by the Maryland Automobile Insurance Fund (MAIF). The three-hour course was designed to show adjusters how to recognize fraud indicators in low-velocity collisions. Technical issues such as "unibody frame displacement" and mitigating crash impact design changes on late model vehicles were discussed. The adjusters also gained knowledge in the fine points of evaluating injury claims arising from low-velocity collisions.

Continuous customer service improvements

In keeping with the Division's commitment to continuously improve its operations, members of the Claims Unit met with representatives from the State Highway Administration (SHA) to discuss how to further improve communication between the motoring public, SHA, and the State Treasurer's Office when road hazard claims are filed.

The goal of improved communication is to reduce the response time of road repair crews and the processing time of road hazard claims. SHA and the Claims Unit are exploring the feasibility of expanding the use of SHA's Customer Care Management System (CCMS). Programming changes in the CCMS technology may yield a more accurate, rapid, and reliable exchange of information between SHA maintenance shops and the Claims Unit. The changes may also reduce or even eliminate the need for multiple phone calls, faxes, or emails which are currently being used to exchange information.

Tort Litigation

The Litigation Manager works closely with the Office of the Attorney General to proactively resolve these matters by investigating and evaluating cases, providing settlement authority or when necessary, by briefing the Insurance Review Committee on high dollar value settlements, and by attending settlement conferences and other court mandated activities. The Litigation Manager also works closely with the claims adjusters to provide feedback on investigations conducted by the adjuster. The Litigation Manager may also brief an adjuster on the status of certain litigation claims of interest.

In FY 2011, the Litigation Manager began tracking the reason for or actual method of disposition of all cases closed since July 1, 2010. The disposition reason or method of each case as of May 19, 2011 is noted in the following table:

Disposition	Reason or Method	Count
Dismissal	Motions granted	25
	Notice of claim not provided	1
	State not served	0
	Non – State	2
	Voluntary w/o prejudice	4
	Voluntary w/prejudice	4
Verdict	Adverse	4
	State	5
Settlement	Pre trial settlement	9
	Pre trial settlement conference	9
	Mediation	3
	Settlement at trial	0
	Post trial settlement	0
TOTAL CASES CLOSED SINCE JULY 1, 2010		66

INFORMATION TECHNOLOGY DIVISION

The Information Technology Division (IT) provides a platform of integrated systems to support the State Treasurer's Office's (STO) operations. During the first half of 2011, the IT Division worked with the Office's Divisions and our State agency clients to support many changes and upgrades.

One of many projects that were completed was the Treasurer's Bank Account Information System (TBAIS). This system co-developed by the Banking and IT Divisions replaced the BAIS system hosted by the Comptroller's General Accounting Division (GAD). The new TBAIS system has two unique components. The first is a web based form that allows agencies to request authorization to open or close bank accounts and electronically routes the request via a secured email to Banking and GAD for authorization or denial. Authorized accounts are then added to the second component that includes a menu driven account database application, hosted on our IBM i5 System.

Two system upgrades were rolled out successfully. The first upgrade migrated our existing email over to new hardware hosting Microsoft Exchange 2007. The new email offers many improvements which include more system tools for IT and larger mailboxes for the clients. The second critical upgrade involved a complete rewrite and design of our website. The site went live in February and has a fresh look, is better organized and provides easier navigation throughout the site.

Disaster Recovery (DR) planning is an important responsibility to the State Treasurer's IT Division. In February of this year, the IT Division executed a disaster recovery test at our DR vendor's office. This test, like many in the past, always results in new ideas and methods to better prepare the Office for an actual disaster.

The IT Division continued to process disbursements for General Accounting Division (GAD), Revenue Administration Division (RAD), Child Support, CARES, Retirement and Central Payroll. Our support of these disbursement processes frequently requires upgrades and changes. The first half of the year was no exception and included updating of Department of Human Resources Child Support and CARES check signatures, changes to include additional departments to RAD's custom deposits file, and adding a message encouraging Direct Deposit to the GAD check advice.

Numerous enhancements to the IBM i5 were made to provide additional reporting for the Administration Division's insurance accounting process and the payment processing menus. Improvements were made to the Banking Services Division's wire reconciliation and R*STARS postings by logically matching incoming deposit file wire transactions against our validation table and automatically encoding the transaction with the required accounting information.

DEBT MANAGEMENT DIVISION

Maryland is one of eight states with AAA ratings from all three rating agencies. The states are Maryland, Delaware, Virginia, North Carolina, Georgia, Missouri, Iowa and Utah.

The State Treasurer's Office maintains frequent contact with the rating agencies and schedules conference calls with each of them prior to every bond sale as we did on February 11, 2011 just prior to the sale of 2011 First Series General Obligation Bonds. Participating in the most recent conference call were the Treasurer, Comptroller, Secretary of Budget and Management, Director of the Bureau of Revenue Estimates, Executive Director of the Maryland State Retirement Agency, and the Director of Policy Analysis for the General Assembly and staff.

The State Treasurer's Office sends copies of the ratings reports for each bond sale to all members of the General Assembly. The recent reports are generally uniform in their assessment of Maryland's credit and cite Maryland's history of prudent, moderate debt and budget management, its protected Rainy Day Fund and other reserves, its Capital Debt Affordability and Spending Affordability processes, its 15-year General Obligation bond terms and other strong evidence of prudent stewardship. However, while they note the State's recent revenue stabilization and projected modest revenue growth, the agencies also cite Maryland's continuing budget pressure in out years. All three rating agencies have reported the pension as underfunded and Moody's has privately expressed concern that Maryland's pension funding level and the corridor method do not correspond with other AAA states.

In 2011 there has been an increased focus on pensions by the rating agencies. In its report "Combining Debt and Pension Liabilities of U.S. States Enhances Comparability", Moody's noted "Large and growing debt and pension burdens have been, and will continue to be, contributing factors in rating changes. However, unfunded pension liabilities have grown more rapidly in recent years because of weaker-than-expected investment results, previous benefit enhancements and, in some states, failure to pay the full annual required contribution (ARC). Moreover, pension liabilities may be understated because of current governmental accounting standards." Using various measures, Moody's now ranks states by long term liabilities which combine debt *and* pension liabilities. In all categories, Maryland's combined pension and long-term debt liabilities ranking is in the highest third of all states.

Analysts from Fitch Ratings, Standard & Poor's and Moody's Investors Service will be in Annapolis on Wednesday, June 29 and Thursday, June 30 to attend meetings prior to rating the 2011 Second Series General Obligation Bonds. Issuance for these bonds is scheduled for late July. The State Treasurer's Office extended this invitation to the rating agencies to highlight the progress made in the last Session on the structural deficit and pension sustainability. Typically the rating agencies review the State's credit by phone prior to each sale but periodically a personal visit is scheduled. The last such visit was in the summer of 2007.

Working sessions on June 29 will include presentations on the Economy and Revenues, Video Lottery Terminals (VLTs), Budget, Pension and Retiree Health Reforms, Legislative Updates and Debt Issuance plans. To demonstrate the positive impact of BRAC on the Maryland economy, the rating agencies will tour Ft. Meade and the surrounding areas on June 30.

Closed Financing - General Obligation Bonds

Since our last report, there has been one General Obligation Bond Sale. The 2011 First Series totaled $485,000,000, closed on March 22, 2011 and had two series:

Series A - $130.8 million in tax-exempt bonds sold in a negotiated sale with first priority to Maryland citizens

Series B - $354.2 million in tax-exempt bonds sold in a competitive sale primarily to institutions

Closed Financing – Certificates of Participation

To finance video lottery terminals in Perryville and Ocean Downs, the State issued $40,900,000 in Taxable Certificates of Participation Series 2011 A on January 20, 2011. My Office accomplished the goals it established for this financing:

1. **Lowest cost of capital:**
   To achieve the lowest possible interest expense, the State Treasurer's Office (with the approval of the Board of Public Works and the statutorily-required prior notification to the Legislative Policy Committee) structured this financing as Certificates of Participation (COPs) instead of using the State's lease program to finance the VLTs. COPs are a method of structuring capital leases to attract multiple investors in a rated, public offering.

   By using COPs, the Treasurer's Office calculates that the State achieved almost $1.6 million in present value savings compared to using a conventional lease-purchase financing for the VLTs. The rate estimated by the State's financial advisor for a taxable lease-purchase agreement on the same date was 3.95%, compared to the average coupon on the Certificates of 2.29%.

   These desirable rates were achieved in part due to the solid AA+, AA+ and Aa1 ratings from Fitch, S&P and Moody's, respectively. These ratings are one notch below the AAA rating which reflects the full faith and credit of the State. The ratings on the COPs are the highest possible ratings for appropriation backed debt.

2. **Inclusion of minority firms:**
   The total costs of issuance, underwriters' discount, and underwriter's counsel fees for the 2011 A COPs are estimated at approximately $274,000. The State Treasurer's Office projects that approximately 45% of these costs will be paid to the two minority investment banking firms who were the sole underwriters of these Certificates and a Maryland minority financial advisor who also participated in the sale.

3. **Transparency:**
The State Treasurer's Office invited interested persons to listen to market commentary and to observe the sale which took place on January 11. The State's financial advisor also conducted a market evaluation of the rates on the Certificates and they compared very favorably to other municipal issuers' recent taxable sales.

Closed Financing - Leases

The Capital Lease-Financing Program allows State agencies to acquire equipment and pay for those items over a three, five, or ten year time frame. Between December 15, 2010 and May 15, 2011, $2,969,700, in capital equipment (primarily IT equipment) was lease purchased by State agencies through the State Treasurer's Office.

The Treasurer's Office also finances Energy Performance Leases in cooperation with the Department of General Services (DGS), providing funding for energy conservation at State facilities. The program finances significant up-front investments in conservation projects and the lease is paid for using the savings in operating costs. One Energy Lease in the amount of $25,587,813 was financed between December 15, 2010 and May 15, 2011.

2011 Financing Plans

At this time, the Office is structuring the July 2011 General Obligation Bond issue. Tentatively, the sizing will be approximately $510 million comprised of $15 million of Qualified Zone Academy bonds (QZABs), $5 million of Qualified Energy Conservation Bonds (QECBs), and $490 million of tax-exempt bonds. The QZABs and QECBs will be taxable bonds with a 100% and 70% direct interest subsidy from the US Treasury respectively. The Office is also planning a retail component of the tax-exempt bonds with first priority to Maryland citizens.

Throughout the year, the Office monitors interest rates to gauge refunding opportunities that meet present value savings criteria in our officially adopted debt policy. There may be a refunding possible in this next sale although this could change in the weeks prior to the sale as market conditions continue to be volatile in 2011.

The Office encourages legislators and all interested persons to attend the pricing calls for the negotiated sale on July 22 and July 25 and/or the competitive sale on July 27. Please contact the State Treasurer's Office if you are interested in the locations and times.

Status of the Annuity Bond Fund

Debt service on General Obligation Bonds is paid from the Annuity Bond Fund (ABF) and the primary source of revenue for this fund is real property tax receipts. The Commission on State Debt met and released its annual report on April 14. In fiscal year 2012, no appropriations from the General Fund are necessary to support General

Obligation debt service. At this time however, a General Fund subsidy may be necessary to support debt service beginning as early as 2013.

Capital Debt Affordability Committee (CDAC)

CDAC's meetings are scheduled throughout the summer on July 6, August 12 and September 13 to review the size and condition of State and Higher Education debt, the State's capital program and rating agency reports. The affordability analysis will also be ongoing to determine the level of future debt authorizations that comply with the benchmarks of 4.0% of tax-supported debt outstanding to personal income and 8.0% tax-supported debt service to revenues. Based on recent analysis, the State Treasurer's Office expects continued pressure on the debt service to revenues ratio of 8.0%. Meeting materials and the final 2011 CDAC Report will be available on the Treasurer's website.

At the final meeting on September 21, 2011, the Committee will recommend the total amount of new State debt that prudently may be authorized for the next fiscal year and the annual increase for future years. The Committee will also recommend the amount of new bonds for academic facilities for the next fiscal year by the University System of Maryland, Morgan State University, St. Mary's College of Maryland and the Baltimore City Community College.

As noted in the opening section of this Report, present revenue and market conditions continue to impact the operations and achievements of the State Treasurer's Office in many ways. The Treasurer appreciates the opportunity to provide this report to the Legislative Policy Committee on a regular schedule. A copy of this report is also available on the State Treasurer's website: www.treasurer.state.md.us. If the Committee or its members would care to pursue further these or other STO developments, or any other aspects of the Treasurer's activities, please call the Treasurer at (410) 260-7160 or Chief Deputy Treasurer Bernadette T. Benik at (410) 260-7390.