



**TREASURER'S REPORT TO  
LEGISLATIVE POLICY COMMITTEE**

**June 8, 2012**

**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 13, 2011. 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.

While the State’s fiscal picture seems to be improving slightly due to the strength and diversity of Maryland’s economy, the State continues to face fiscal challenges. The Office’s experienced staff 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 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, such as by refunding our General Obligation Bonds or issuing 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 do more with less, the Office is implementing improvements 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 December 1, 2011 and May 31, 2012, the Board of Public Works (“BPW”) met 12 times to consider State procurements, expenditures of capital appropriations, the acquisition, use and transfer of State assets, issuances of licenses to dredge and fill wetlands, and the acquisition of land and easements in support of Program Open Space, the Conservation Reserve Enhancement Program, the Rural Legacy Program and the Agricultural Land Preservation Program.

During this timeframe, the following items worthy of note were considered by the Board of Public Works:

### Capital Equipment Lease-Purchase Financing

- The Legislative Policy Committee (“LPC”) approved the request of the State Treasurer periodically to lease-finance equipment acquisitions in an aggregate amount not to exceed \$40 million over a two-year period beginning July 1, 2011 and ending June 30, 2013. The BPW approved the following lease-purchase equipment financing consistent with this authorization:
  1. **December 2011** Tax-Exempt Equipment Lease-Purchase Agreement for financing the acquisition of approximately **\$1.76 million of capital equipment** for the Department of Public Safety and Correctional Services, Maryland Department of the Environment, and Maryland Department of Health and Mental Hygiene. (12/7/11)
  2. **April 2012** Tax-Exempt Equipment Lease-Purchase Agreement for financing the acquisition of approximately **\$1.67 million of capital equipment** for the Department of Public Safety and Correctional Services and Maryland Department of Health and Mental Hygiene. (04/18/12)
  3. **June 2012** Tax-Exempt Equipment Lease-Purchase Agreement for financing the acquisition of approximately **\$1.17 million of capital equipment** for the Department of Public Safety and Correctional Services, Maryland Department of the Environment, Maryland Department of Health and Mental Hygiene, Department of Information Technology, and Maryland Public Television. (05/23/12)
  
- Following the most recent financing (June 2012), the remaining balance of the \$40 million authorized by LPC for equipment lease-purchase financing is approximately \$35.4 million.

### Public School Construction

- I. **State School Construction – Capital Improvement Program for FY 2013:**

Approval of allocations totaling \$349.2 million (05/23/12)

  - Incorporates \$187.5 million approved by the BPW on January 25, 2012.
  - Additional projects in the amount of \$136.7 million were approved at the May 23, 2012 BPW meeting, including \$2.8 million for a project at the Maryland School for the Blind.

- Reserved \$25 million for projects that improve energy efficiency of schools, with a priority given to projects that maximize leverage, such as incremental costs required to achieve the highest levels of energy performance.
- Uses \$326.4 million of new bond authorizations and \$22.8 million in reverted funds from the Statewide Contingency Account.

**II. Aging School Program for FY 2013:** Approval of allocations totaling \$32,046,424. (05/23/12)

**III. Qualified Zone Academy Bond Program for FY 2013:** Approval of allocations totaling \$27,213,951. (05/23/12)

**IV. Supplementary Appropriation - Alcoholic Beverages Tax Increase**

During the 2011 Legislative Session, legislation (HB 1213/ Chapter 572) was passed to increase the tax on alcoholic beverages from 6% to 9%. The bill requires a **supplementary appropriation** of **\$47.5M** in FY12 for public school construction projects in local jurisdictions. The BPW is required to approve the individual projects for each local jurisdiction based upon criteria set forth in the legislation. The following requests were approved:

- **Eastern Shore Region: \$1.25 million.** (01/25/12)
  - **Caroline County Public Schools: \$148,737** for three backup power generator projects at Denton Elementary School, Greensboro Elementary School, and North Caroline High School.
  - **Dorchester County Public Schools: \$137,109** to improve the energy efficiency at Maces Lane Middle School and Hurlock Elementary School.
  - **Kent County Public Schools: \$104,177** to make improvements to the electrical, lighting, and sound systems for the auditorium at Kent County High School.
  - **Queen Anne's County Public Schools: \$179,000** to modernize instructional technology at Centreville Middle School.
  - **Talbot County Public Schools: \$135,198** to rebuild the existing HVAC system and chiller at Easton High School.
  - **Somerset County Public Schools: \$114,027** for renovations at the Promise Academy located at Marion Sarah Peyton School.
  - **Wicomico County Public Schools: \$267,221** for energy efficient lighting upgrades at Pittsville Elementary and Middle School.
  - **Worcester County Public Schools: \$164,535** for four projects at Berlin Intermediate School, Pocomoke Middle School, Snow Hill Middle School, and Stephen Decatur High School.
- **Baltimore City: \$9 million** for 20 projects addressing deferred capital maintenance. Seventeen of the 20 projects improve energy efficiency or incorporate green building principles. (01/25/12)

- Projects fell into the following categories:
  1. Fire alarm system replacements: Hilton Elementary School, Johnston Square Elementary/Middle School, and Chinquapin Building;
  2. Roof replacement: Gardenville Elementary School and Bay Brook Elementary/Middle School;
  3. Boiler/Chiller/Mechanical Equipment replacements: Frederick Elementary School, Robert Poole Building, Walter P. Carter Elementary/Middle School, and Garrett Heights Elementary/Middle School;
  4. Window/Door replacements: Dr. Bernard E. Harris, Sr. Elementary School, Govans Elementary School, Westside Elementary School, Thomas Johnson Elementary/Middle School, Medfield Heights Elementary School, Alexander Hamilton Elementary School, and Hilton Elementary School; and
  5. Window replacements: Callaway Elementary School, Langston Hughes Elementary School, Woodhome Elementary/Middle School, and Rosemont Elementary/Middle School.
  
- **Howard County:** reallocated **\$4 million** for four projects at Atholton High School, Hammond High School, Dunloggin Middle School, and Wilde Lake Middle School. (01/25/12))
  
- **Western Maryland Region: \$750,000.** (02/08/12)
  - **Allegany County Public Schools: \$124,125** to address safety concerns at Northeast Elementary School.
  - **Carroll County Public Schools: \$174,225** to install backup power generators at William Winchester Elementary School and Sykesville Middle School.
  - **Frederick County Public Schools: \$231,750** to complete a feasibility study for the Frederick High School.
  - **Garrett County Public Schools: \$48,675** for exterior repairs at Broad Ford Elementary School.
  - **Washington County Public Schools: \$171,225** for boiler replacement at Sharpsburg Elementary School.
  
- **Prince George's County: \$9 million** for eight projects at High Point High School, Bladensburg Elementary School, Bradbury Heights Elementary School, Gladys Noon Spellman Elementary School, Tall Oaks Vocational, Forestville Military Academy, Friendly High School, and Oxon Hill High School. (02/22/12)
  
- **Southern Maryland Region: \$1.25 million.** (05/23/12)
  - **Calvert County Public Schools: \$410,000** for refurbishing metal roofs at Sunderland Elementary School, Patuxent High School, Plum Point Elementary School, and Patuxent Elementary School.
  - **Charles County Public Schools: \$550,000** for improvements to the F. B. Gwynn Educational Center.

- **St. Mary's County Public Schools: \$290,000** for installation of high efficiency lighting at multiple secondary schools in the County.

### **Facilities and Services of State Agencies**

- Approval of lease of approximately 2 acres of land at Eastern Correctional Institute ("ECI") to ECOCORP, Inc. for the purpose of construction and operation of a 1MW **Anaerobic Digester Facility**, a renewable energy source, that will "digest" chicken manure and produce methane gas that will be used to produce electricity to meet a portion of the electricity needs of ECI. Approval was also given to a 20-year power purchase agreement between ECOCORP and the Maryland Environmental Service, the agency undertaking this initiative. (12/21/11)
- Approval of **Public Private Partnership** Lease and Concession Agreement (P3) between the Maryland Transportation Authority ("MDTA") and Areas USA MDTP, LLC for the refurbishment and operation of the **I-95 Travel Plazas** (Maryland House and Chesapeake House). (03/07/12)
- Approval of the procurement of **EZ Pass transponders** through an intergovernmental cooperative purchasing agreement that will enhance an interstate interoperability toll program. Under the new contract, the cost of transponders for users will be \$9, down from previous cost of \$21. (04/04/12)
- Approval of a contract to implement **cell phone managed access services at the Department of Corrections' MD Transition Center** to eliminate illegal cell phone use. Instead of using a jamming technology, the contractor, Tecore Networks, will differentiate between authorized and unauthorized cellular devices within the target area. (04/18/12)
- Award of a construction contract to build a new **athletic team building** on the East Campus of **Salisbury University** to Harkins Contracting, Inc. (05/02/12)
- To better serve the mass transit needs of Southern Maryland and to support commuter bus service to Washington, DC, approval was given for the construction of the **Charlotte Hall Park & Ride Facility** and for the acquisition of property necessary for construction of the **Dunkirk Park & Ride Project**. (05/02/12)
- Approval of a construction management contract for a new **youth detention center at Cheltenham Youth Center** in Prince George's County. A Project Labor Agreement is one of the assessment factors for this contract. (05/23/12)
- **State Employee/Retiree Health Care:** Approval was given for a 5-year, \$2.43 billion contract with Express Scripts, Inc. to provide pharmacy benefits management and **prescription coverage** for State of Maryland employees and retirees. (02/08/12)

- **Prisoner Health Care:** Action was taken on three health care contracts for inmate health services for:
  - Medical Care and Utilization Management Services contract award with Wexford Health Sources, Inc.: 5 year contract (05/02/12)
  - Mental Health Services contract award with MHM Correctional Service of MD, Inc.: 5 year contract (05/02/12)
  - Refusal by the BPW to award a new contract to Diamond Pharmacy Services in the face of a protest (12/21/11), and the extension of the existing Pharmacy Program contract with Correct Rx Pharmacy Services for six months pending determination of a protest at the Maryland State Board of Contract Appeals. (01/25/12)

### **Information Technology**

- Approval for the Maryland State Lottery Commission to **lease 4719 Video Lottery Terminals** (“VLTs”) for the Anne Arundel County slots facility at a cost of \$168 million. (12/21/11)

### **BWI Marshall Airport**

- Approval for \$100M expedited procurement with a phased construction schedule for improvements at BWI Marshall to facilitate the merger between Southwest and AirTran Airlines. Improvements will include a new security checkpoint at lower level Concourse A to add screening capacity and efficiency and to increase the throughput of passengers through security and an expansion of the existing terminal between Concourses B and C creating a continuous airside connector for Concourses A, B and C. (12/07/11)
- Approval of the reimbursement of costs related to the relocation of the Silver Diner in order to accommodate the merger of Southwest and AirTran Airlines by creating a connector between Concourses B and C that would allow passengers to travel between the two without having to go through a security checkpoint and expanding Concourse C. Silver Diner, located at the top of Concourse B, will be affected by the Concourse B/C. Maryland Aviation Administration may be paying up to \$3,534,848 in order to keep Silver Diner as a tenant at BWI and to relocate Silver Diner to accommodate the Southwest/AirTran merger improvements. (03/07/11)
- Approval of the award of a contract to BWI Taxi Management, Inc. for the exclusive right to operate and manage the **airport taxicab ground transportation concession service** at BWI Airport. BWI Taxi Management, Inc. is the incumbent provider of these services. Under the terms of the lease and concession contract, there will be no change in the number of cabs operating at BWI Marshall or in the percentage of owner-operated cabs as compared to leased cabs. (04/18/12)

### **State Property Tax Rate**

- Set the State Real Property Tax Rate based upon the recommendation of the Commission on State Debt. The Rate remained unchanged at 11.2 cents per \$100 of the full assessed value of real property other than that of public utilities and 28.0 cents per \$100 of the full assessed value of real property of public utilities. (04/18/12)

### **Bonds**

- Adoption of a Resolution for the sale of \$736,340,000 of State of Maryland General Obligation Bonds:
  1. Negotiated Sale: \$56,085,000
  2. Competitive Sale: \$543,915,000
  3. Refunding Bonds: \$136,340,000 (03/07/12)
- Authorized the sale of \$105 million in refunding bonds by the Maryland Stadium Authority that resulted in:
  - Removing \$82 million in variable rate debt;
  - Terminating an interest rate swap agreement with AIG; and
  - Savings from the refunding equal to \$1.7 million. (12/07/11)
- Adopted Resolutions authorizing the issuance and sale by the Maryland Department of Transportation of its Consolidated Transportation Bonds, Series 2012 in an amount not to exceed \$260 million at a public sale to occur on or before June 30, 2012.

## **INVESTMENT DIVISION**

The Treasurer's conservative investment policy and practices have protected the investment portfolio through these continued volatile and unprecedented economic times. It is a true accomplishment in this environment to report that all principal is intact and a modest but continuous return has been earned on the portfolio. The par value of the General Fund investment portfolio for May 31, 2012 was \$4,811,128,892.46 as compared to May 31, 2011 when it was \$5,299,320,073.06. This is a decrease of over \$488 million dollars.

On May 31, 2012, the portfolio was earning an average of 1.042%, compared to 2.185% for the same date in 2011. The lower 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 .046% from July 2011 until the end of May 2012 as compared with .124% 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 2012 are \$65,546,816 as compared with \$121,431,955 received for the same time period in FY 2011. The over \$55 million decline in interest received is directly attributable to the continued lower interest rate environment combined with the increased liquid balances which earn a lower return.

The following chart tracks the impact of the legislation passed last fiscal year to reduce the number of individual Agency accounts that receive an interest allocation from the total interest earned on the investment portfolio. It should be remembered that as the total General Fund portfolio decreases, the proportion of Agency Funds to General Funds increases and therefore their allocated share increases.

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

<b>Fiscal Year</b>	<b>Net General Fund</b>	<b>Allocated to State Agencies</b>	<b>Total</b>	<b>% of Total Allocated to State Agencies</b>
<b>2000</b>	121,951,720	103,173,287	225,125,007	46%
<b>2001</b>	136,981,074	144,249,899	281,230,973	51%
<b>2002</b>	82,641,807	66,399,769	149,041,576	45%
<b>2003</b>	37,205,637	42,240,523	79,446,160	53%
<b>2004</b>	25,037,345	29,053,449	54,090,794	54%
<b>2005</b>	52,886,074	54,538,463	107,424,537	51%
<b>2006</b>	149,613,238	109,222,108	258,835,346	42%
<b>2007</b>	150,798,001	205,589,917	356,387,918	58%
<b>2008</b>	155,170,184	207,179,098	362,349,282	57%
<b>2009</b>	102,768,740	142,619,087	245,387,827	58%
<b>2010</b>	44,190,425	87,921,654	132,112,079	67%
<b>2011</b>	53,002,765	87,698,955	140,701,720	62%
<b>May-2012</b>	24,044,082	41,502,734	65,546,816	63%

The Securities Lending Program continues to provide additional revenue. The program has earned \$416,491.78 so far in FY 2012. This compares with \$269,869.96 for the same period in FY 2011. 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 being scaled back.

The Office continues to increase MBE participation in the investment of State funds. Twenty-two MBE broker/dealers are on the Office's approved list for FY 2012 and they have handled investments of \$718 million so far this fiscal year. This compares

with FY 2011, when the Office had 19 approved MBE broker/dealers who handled \$839 million in investments by the end of May.

The Maryland Local Government Investment Pool (MLGIP) AAAM rating was reaffirmed by Standard and Poor's on March 26, 2012. The pool balance at May 31, 2012 was \$3,037,720,182.80 compared with \$2,930,626,885.08 for the same date in 2011. This is an increase of over \$100 million dollars due to the lack of safe, short-term investment alternatives for Investment Pool members at a comparable yield. The MLGIP is paying .13% as of May 31, 2012 as compared with .12% 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 STO 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.

## **DEBT MANAGEMENT DIVISION**

### **Ratings**

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 13, 2012 just prior to the sale of 2012 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 Department of Legislative Services and staff.

In late February 2012, Moody's Investors Service, Standard & Poor's (S&P) and Fitch Ratings all affirmed the State's AAA rating. Moody's retained the assignment of a negative outlook due to the State's macroeconomic linkages to the U.S. government (to which Moody's has also assigned a negative outlook). S&P and Fitch have also expressed concerns about the effect of federal budget reductions on Maryland's credit but have also noted the State's response to any such impacts will affect their assessment.

### *Excerpts from Ratings Reports*

Generally, there is consensus among the rating agencies in evaluating the State's credit strengths and weaknesses. All three agencies cite Maryland's economy and fiscal management as a credit positive. The State's unfunded pension liability continues to be a

credit challenge, although each agency recognizes the State's recent reform efforts. The following summarizes the most recent reports:

Fitch Ratings, in assigning the AAA rating and stable outlook, noted:

- *Debt oversight is strong and centralized, and the debt burden is moderate. The State has policies to maintain debt affordability, and the constitution requires GO and transportation bonds to amortize within 15 years.*
- *Pension funding levels have deteriorated, although the State is undertaking extensive pension and other post-employment benefit (OPEB) reforms.*
- *The State has a diverse, wealthy economy, benefiting from its proximity to the nation's capital.*
- *Financial operations are conservative, and the State maintains a Rainy Day Fund to manage revenue cyclicity. The State took repeated action during the course of the recession to address projected budget gaps, including raising tax revenues, cutting spending, and using Rainy Day and other balances.*

Moody's cited the following factors that could lead to a downgrade:

- *Economic and financial deterioration that results in deficits and continued draw downs of reserves without a plan for near-term replenishment.*
- *Failure to adhere to the State's tradition of conservative fiscal management.*
- *A State economy that does not rebound in tandem with the rest of the country.*
- *Failure to adhere to plans to address low pension funded ratios.*

S&P's rating rationale notes the following:

- *Diverse, broad-based economy, which has historically outperformed the national economy;*
- *Strong wealth and income levels, coupled with unemployment that remains below the national average through economic cycles;*
- *Long history of prudent fiscal management, including making difficult decisions to restore structural budget balance; and*
- *Moderate debt burden; enhancing this are a clearly defined debt-affordability model limiting annual issuance and the maintenance of ratios within reasonable limits, including a constitutional 15-year debt maturity schedule.*

The State Treasurer's Office sends copies of the ratings reports for each bond sale to all members of the General Assembly and current reports are also available on the Treasurer's website at [www.treasurer.state.md.us](http://www.treasurer.state.md.us).

### *Discussions with Rating Agencies*

As of the date of this report, there have been no further rating actions. The Treasurer's Office has provided the rating agencies regular updates on the fiscal year 2013 budget package and the 2012 Special Session. The next conference call with the rating agencies is expected on July 10, 2012, prior to the sale of the 2012 Second Series General Obligation Bonds.

### **Closed Financing - General Obligation Bonds**

Since our last report, the State completed the successful sale of \$738.4 million of General Obligation Bonds in three series. The Series A bonds, totaling \$56.1 million, were sold exclusively to retail investors with first priority to Maryland citizens and \$543.9 million of Series B bonds were sold in a competitive sale primarily to institutions. The Series A and Series B bonds provided \$600.0 million, at a historically low TIC (True Interest Cost) of 2.40%, to finance investments in capital projects critical to our State. The Series C bonds totaled \$138.4 million to advance refund certain outstanding General Obligation Bonds. The refunding bonds saved taxpayers \$10.2 million in interest costs.

### **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. Since December 1, 2011, \$4.6 million in capital equipment was leased by State agencies through the State Treasurer's Office. On June 5, 2012, the State Treasurer's Office will finalize the financing of another equipment lease totaling \$1.2 million.

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; the lease is paid using the savings in operating costs. Two energy leases totaling \$10.8 million have been financed since December 1, 2011.

### **2012 Financing Plans**

The next General Obligation Tax-Exempt financing of approximately \$540 million is planned for late July – early August 2012. The sale is expected to include \$20 million of taxable bonds and, including \$15 million of Qualified Zone Academy Bonds (QZABs), is planned for late July – early August 2012. The State Treasurer's Office expects to again offer 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 debt policy. If these benchmarks are met, refunding bonds could also be issued.

The Treasurer's Office encourages legislators and all interested persons to attend the pricing calls for the negotiated sales which are tentatively scheduled for July 27 and

July 30, 2012 and/or the competitive sale on August 1. Please contact the State Treasurer's Office for the locations and times if you are interested.

### **Status of the Annuity Bond Fund**

Debt service on General Obligation Bonds is paid from the Annuity Bond Fund 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 16, 2012. In fiscal year 2013, no appropriations from the General Fund are necessary to support general obligation debt service. Assuming current property tax rates of 11.2 cents per \$100 of assessed value of real property, other than that of public utilities, and 28 cents per \$100 of assessed value of real property of public utilities are maintained and other assumptions remain as currently estimated, a General Fund subsidy is projected for fiscal years 2014 through 2017. The complete report is available on the Treasurer's website at <http://www.treasurer.state.md.us/debtmanagement/csd-reports.aspx>.

### **Capital Debt Affordability Committee (CDAC)**

CDAC meetings are scheduled on July 16 and August 22 to review the size and condition of State and Higher Education debt, the State's capital program and rating agency reports. Throughout the summer the Committee will conduct an affordability analysis to review projected debt authorizations in light of the affordability benchmarks that tax-supported debt outstanding should not exceed 4% of personal income and tax-supported debt service should not exceed 8% of revenues. Based on prior analyses, the State Treasurer's Office expects continued pressure on the debt service to revenues ratio of 8.0%.

CDAC is scheduled to meet on September 24 to 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. Meeting materials and the final 2012 CDAC Report will be available on the Treasurer's website.

## **BANKING SERVICES DIVISION**

The primary mission of the Banking Services Division (BSD) is to manage and control relationships with vendors providing banking services for the State of Maryland, to anticipate agency banking requirements and respond timely to agency requests.

The Division is directly responsible for managing the banking needs for all agencies of the State. Over the past six months, BSD continued to be actively involved in the conversion of lockbox processing to the new statewide lockbox provider, Citibank N.A. The initial phase of this transition is nearing completion with the first two agencies, the Comptroller's Revenue Administration Division and the Department of Labor, Licensing and Regulation's Contributions Division, scheduled to implement with their

first lock boxes with Citibank during June 2012. These two agencies represent approximately 60% of total statewide lockbox volume. Utilizing Citibank's enhanced imaging capabilities and on-line, real-time access; both agencies anticipate a significant decrease in the amount of "exception" processing. Agency personnel will now be able to review, research, and resolve most exception items on-line. The result will be faster processing of exception deposits and reduced paper flow between the lockbox provider and agencies. The remaining 24 agencies will be converted during the second half of 2012.

Banking Services continues to ensure the accurate and timely recordation of State funds and the reconciliation of the State's bank accounts to the State's R\*STARS accounting system. The Division must account for the receipt of all warranted deposits and the disbursement of all warranted payments. To meet these responsibilities, a comprehensive daily cash reconciliation is performed which allows Banking services to proactively resolve agency banking issues. Even as the volume of transactions has increased, the processes and controls developed by BSD continue to result in a timely, accurate, and well documented reconciliation of the State's cash accounts. For FY 2012, total cash receipts and disbursements each exceeded \$140 billion through May 31<sup>st</sup> and the State's bank accounts continued to be reconciled to the penny on a daily basis to the State's general ledger.

In addition to the reconciliation duties, the Division performs daily operational functions that are critical to the movement of funds into and out of the State's bank accounts and to the recordation of these transactions in R\*STARS. These include:

- Processing the drawdown of funds from federal programs and grants
- Initiating Fed wire payments
- Managing foreign currency transactions
- Processing check stop payments, cancellations and reissues
- Initiating replacement checks for failed ACH payments
- Providing transaction research assistance to State agencies
- Managing the Unpresented and Undeliverable Check Funds
- Recordation in R\*STARS of all bank adjustments
- Maintenance of tables to allow for accurate posting of electronic receipts

During the past six months, BSD worked with several agencies in streamlining their receivables collection processes through implementation of the Bank of America Payment Collection Gateway (PCG) service:

- Maryland Insurance Administration (MIA) implemented PCG as part of an initiative to allow insurance companies to file and pay their premium taxes on the MIA website.
- Maryland Department of Natural Resources (DNR) began utilizing PCG to process collections from their sports license vendors. This allowed DNR to transition from an older telephone based voice response system. Additionally, DNR began collecting licensing fees over the internet and at their regional service centers.

- Maryland Port Administration (MPA) and Department of General Services (DGS) have begun initiatives to implement on-line collections of parking fees from cruise passengers at the cruise terminal parking facility and the online auctioning of surplus State property.

BSD continued to work with the Department of Information Technology (DoIT) and NIC USA (NIC), on the implementation of self-funded eGovernment applications using a centralized web portal. The Department of Agriculture was the first agency to begin using these services to collect fees from the waste kitchen grease disposal program. The Motor Vehicle Administration began testing in anticipation of collections for driver and vehicle record information.

The Division is assisting the Comptroller's Revenue Administration Division (RAD) in implementing Bank of America Image Cash Letter (ICL) Service. The ICL service will allow RAD to deposit tax check receipts via transmission of an image file vs. the physical delivery of paper checks to the bank. Once completed, this service will result in faster availability of funds and a reduction in armored courier fees.

Another responsibility of the Division is to ensure protection of all State funds on deposit with financial institutions through monitoring of bank account and collateral balances. Utilizing the Treasurer's Bank Account Information System (TBAIS) Banking, Services monitors over 1,800 agency bank accounts at 23 financial institutions. Total posted collateral as of March 31, 2012 was \$479 million.

The Banking Services continues to serve as the State's authority for the development, control and maintenance of statewide policies and procedures for banking products and services. We continually strive to stay at the forefront of changes in banking products and services offered in the financial industry. The Division will continue to explore new financial products and improved data delivery methods that will increase its capabilities to provide efficient, cost-saving, banking services to Maryland State agencies.

## **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, 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 four units: Underwriting, Claims, Tort Litigation Management and Loss Prevention. The Division's goal is to provide statewide risk management through loss protection (Underwriting), loss restoration (Claims and Tort Litigation Management), and loss control (Loss Prevention).

## **Underwriting**

The Underwriting Unit in 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 Unit highlights for the past six months include the following:

The Maryland Port Administration (MPA) has a liability policy that renewed on January 31, 2012. The primary coverage was renewed with Allianz, and the total renewal premium was \$660,812 plus the broker fee, **saving MPA \$34,760**. This was a very good renewal especially in light of the fact that Allianz paid a large loss of \$400,000 during the past year that occurred in the 2009/10 policy term.

The Unit buys commercial marine liability insurance to cover State-owned watercraft. In the January 1, 2012 renewal the broker was able to negotiate the addition of towing and labor coverage. The expiring premium was \$40,082 for 990 vessels, and the renewal premium with improved coverage is \$43,855 for 1046 vessels.

The statewide excess property coverage renewed April 1, 2012. The insurance carriers were seeking rate increases of 15%-20% because of 2011 world-wide catastrophic losses.

The Unit provided the broker additional details on State-owned buildings to help minimize the anticipated rate increase, and the broker successfully negotiated with the insurance carriers to limit the rate increase to 11.7%. Other factors affecting the renewal pricing was a large fire loss with estimated damages of \$5,000,000 in November 2011 as well as property values going up 10.9%. The renewal also includes ten property inspections provided by the insurance carrier which will help prevent future claims. The expiring premium was \$3,461,782 and the renewal premium is \$4,264,194.

The Underwriting Unit frequently addresses agencies' questions about commercial insurance and self-insurance coverage and has worked on special projects with at least six State agencies.

- An annual meeting was held in March to include the Maryland Aviation Administration, our insurance broker, the insurance carrier and representatives of the State Treasurer' Office Insurance Division, in advance of the August 2012 policy renewal. The meeting was held at the BWI Fire and Rescue building and included a briefing on fire and rescue operations on and off airport premises. There was a video shown of a fire suppression training exercise, and both the

history and future plans were discussed. Open claims, and available loss control services for both BWI and Martin State Airport were reviewed and discussed.

- The meeting with the Maryland State Police Aviation Command (MSPAC) was held in March at their headquarters, and included our insurance broker, insurance carrier, and representatives of the State Treasurer's Office Insurance Division. The meeting was held to provide an open forum for MSPAC to present their accomplishments and future plans directly to the insurance carrier and the Insurance Division. MSPAC has worked closely with the Federal Aviation Administration to exceed the minimum safety requirements. The contract for new helicopters is being finalized with the first delivery expected in 2012. The meeting topics included but were not limited to operational and training updates, a possible flight simulator purchase, new dispatch software, new maintenance tracking software, medical insurance provider billing study, a review of the number of bases needed, and the final response to the National Transportation Safety Board recommendations after the tragic crash in 2008. The information supplied is in advance of the June 30, 2012 renewal.
- The Underwriting Manager worked with the Maryland Transit Administration (MTA) regarding insurance requirements in the final phase of the RFP for operations and maintenance on their Camden and Brunswick lines. A conference call included MTA staff and the insurance broker.
- The Unit received requests from three State agencies including DGS, UMCES, and Towson, to assist them with the insurance requirements in agreements with other public entities, and for leasing State-owned land and facilities to others.

The Underwriting Unit had two good opportunities to meet with insurance brokers and insurance carriers in the first half of 2012. The first was in March when an Aon London broker was in town to discuss the London insurance market and how it would affect the MTA liability renewal in July. The second was a rare opportunity for the Underwriting Manager, two of our local brokers, and the President and CEO of Aon Bermuda, to meet with three foreign and domestic insurance carriers to discuss recent and future renewals. The insurance carrier representatives in this meeting either insure or participate in insuring five State insurance liabilities with annual insurance premiums totaling over \$13,818,000.

## **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.

### Greenhouse Explosion at UMES

A build-up of noxious gases from the tenant's improper storage of peat moss in a hydroponic greenhouse at the University of Maryland, Eastern Shore, resulted in a major explosion just days after Thanksgiving. Damage estimates approach \$5 million. The University's restoration efforts will continue into FY13.

The Claims Unit and the commercial carrier are working to help the University restore the damage under the State's self-insurance and the commercial coverage. They are also collaborating to recover the damage expenses from the tenant who is domiciled in China.

The Claims Supervisor supported the Loss Prevention Manager's efforts in providing the University with strategies and loss control measures designed to prevent future greenhouse losses.

### Post Catastrophe Updates

#### Hurricane Irene

Nearly one year has passed since Hurricane Irene struck Maryland. The Claims Unit and the commercial carrier adjusters determined that 14 State agencies suffered approximately \$779,000 in damage. By contrast, in September, 2003, over 20 agencies sustained approximately \$5,000,000 in damage from Tropical Storm Isabel. The Department of Natural Resources suffered the majority of the State's damage (approximately \$500,000) when Irene destroyed several State park structures such as boat ramps and pavilions. Other agencies reported damage to buildings and contents caused by flooding, wind and wind driven water. To date, approximately \$113,500 has been reimbursed from the State Insurance Trust Fund and seven agency claims have been closed.

#### Earthquake

Inspections continue to State-owned property as agencies discover more damage from the 5.8 magnitude earthquake that shook Maryland last summer. The commercial carrier and the Claims Unit have engaged structural engineers and other experts to evaluate the extent of the damage reported statewide. The Claims Unit and commercial carrier are working to derive an aggregate damage estimate. At this time, it appears unlikely that the damage will exceed the State's \$2,500,000 self-insured property coverage.

### **Tort Litigation Management**

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.

The Litigation Manager tracks the reason for or actual method of disposition of all cases closed. The Tort Unit handles a rolling docket of 120 suits at any one point in time. The disposition reason or method of each case disposed of between July 1, 2011 and May 31, 2012, is noted in the following table:

Disposition	Reason or Method	Count
Dismissal	Motions granted	30
	Notice of claim not provided	0
	State not served	0
	Non – State	0
	Voluntary w/o prejudice	4
	Voluntary w/prejudice	4
Verdict	Adverse	3
	State	5
Settlement	Pre trial settlement	11
	Pre trial settlement conference	9
	Mediation	4
	Settlement at trial	0
	Post trial settlement	0
<b>TOTAL CASES CLOSED AS OF MAY 31, 2012</b>		<b>70</b>

### Loss Prevention

The Division often receives requests from State agencies for information about how to determine what type or how much insurance is required for various reasons including, when entering into contracts, Requests for Proposal, and lease agreements. In response to these requests, the Loss Prevention Manager developed a “Minimum Insurance Requirements” guidance document to assist State personnel. The Division consulted with the State’s insurance brokers and with the Office of the Attorney General to develop the guidelines.

A 5-year loss analysis of State colleges and universities was completed in March 2012. The University of Maryland, College Park, University of Maryland, Baltimore, University of Maryland, Baltimore County, and University of Maryland Eastern Shore were selected for further examination due to their high hazard and/or high severity property claims. The following month, the Insurance Division met individually with the University of Maryland, College Park, University of Maryland Baltimore, and the University of Maryland Baltimore County; and discussions were held with University of Maryland Eastern Shore in response to the greenhouse fire. Each discussion centered on property claims trends, loss control, and the corrective actions taken to minimize future losses.

The State's insurance carrier provided a free live-webcast on flood planning. An invitation was extended to the colleges and universities, due to repetitive water damage claims caused by heavy rain events and localized flooding on various campuses. The webcast provided tips to help entities reduce damage and downtime so that operations can be quickly restored following a flood event. The webcast topics included facility audits, pre-planning, and elements of a flood emergency plan; precautions to take before, during and after a flood, and claim reporting.

In April 2012, Bowie State University participated in the Aerial Infrared Testing program. The university requested the service after learning about it during the State insurance program workshop last November. The purpose of testing is to identify the location of moisture penetration of roofing systems before there are visible signs, structural damage or business interruption. With the results of this analysis and implementation of preventive measures, State agencies, colleges and universities can significantly extend the life of roofing structures while reducing maintenance expenditures and potential property-related claims.

The Electrical Infrared Testing program for 2012 began in May, with the University of Maryland Eastern Shore and Frostburg State University. These inspections provide valuable information on the condition of equipment in State agency facilities. Thermographic imaging identifies potential equipment failures and loose connections that create heat that can be imaged to show the exact location of a threat so that appropriate action can be taken before costly repairs and downtime are incurred.

## **INFORMATION TECHNOLOGY DIVISION**

The Information Technology (IT) Division provides a platform of integrated systems that include midrange, server, and web based hardware hosting customized and industry standard applications and communications that support the State Treasurer's Office's (STO) operations.

Over the last six months, the IT Division worked with the Office's Divisions and our State agency clients to support many changes and upgrades. The IT Division added enhancements to the Treasurer's Bank Account Information System (TBAIS) including a Stat Dashboard, a utility to globally change Bank ID's due to bank mergers, added a bank account notes feature, and added the Web X-1 number field to TBAIS for cross reference and tracking. Additional programming is currently in progress and will bring new functionality to bank collateral and account interest reporting and tracking.

Other projects included adding R\*STARS information to the Investment Division's Interest Allocation process, automation of Annual Loss Queries and creation of new programs to link Urepresented and Undeliverable checks in FMIS. The IT and Investment Division worked with the Department of Information Technology (DoIT) to create a new daily report for Investments that will identify the total dollars and specific large dollar payments that are pending in FMIS. The hope is that this report will complement the Investments Division's existing process for estimating and funding daily disbursements. A Task Order RFP (TORPF) was completed for programmers to assist

with the maintenance of programs that support the State's disbursement operations, Banking Division's reconciliation of deposits and disbursements, Investment Division's reporting and the Insurance Division's Claim Management application.

IT continued to work to enhance operations with State agencies by implementing a more streamlined communications process for Quik Pay checks that shortens the processing time and ensures same day reconciliation and adding a Direct Debit option for vendor payments of Admissions & Amusement fees.

The Network Services staff maintained their support of all network, firewall, email, web, file and application server hardware and software for the agency. Additional responsibilities include maintaining reliable PC hardware and software built via a standard image. This standard provides the staff with the ability to utilize automated scripts for the deployment of security, anti-virus and application patches. They also maintain all custom software utilized within the agency, including, but not limited to, Mun-ease, Sungard, LAS (Leave Accounting System), M&T Check Viewer, Matter Tracker, PTX Viewer, Rumba, J-Walk, NGS Query, Orgplus and the entire MS Office Suite including MS Project. Recent accomplishments include upgrades of network server spam, antivirus, backup software, and the installation of updated server hardware drivers and firmware that ensures the continuation of a reliable infrastructure. Recent projects include the support of another successful retail (BuyMarylandBonds.com) and competitive bond sale in March 2012.

Disaster Recovery (DR) planning is an important responsibility of the Division. In March of this year, the Division executed a Disaster Recovery test at our DR vendor's office. The DR Team replicated an actual workday that included the retrieval, processing, printing and transmission of the files from the ADC mainframe to the disbursement bank. The test system was a mirror copy of our production system that included all of our customized programs and software that are necessary to keep the money moving. Other testing included the receipt and formatting of State deposit files from our depository bank and the generation of reconciliation reports. This test, like many in the past, always results in new ideas and streamlined methods to better prepare the Office for an actual contingency.

***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](http://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.***