



PRELIMINARY REPORT

FEBRUARY 2016

February 2016

Redis C. Floyd
Clerk of the Council
Prince George's County Council
County Administration Building, 2nd Floor
14741 Governor Oden Bowie Drive
Upper Marlboro, Maryland 20772

Dear Ms. Floyd:

On behalf of the *Blue Ribbon Commission on Addressing Prince George's County's Structural Deficit* ("The Commission"), I write to submit the Commission's preliminary report.

The Commission consists of representatives of business groups, organized labor and the public at-large – a true cross-section of the residents of Prince George's County. I am proud of the work done by this group of committed county leaders.

Since the Commission was created in June 2015 under CR-26-2015, we have met 5 times and gathered significant information on understanding the structural budget problems impacting the county. On behalf of the Commission, I look forward to continuing this important work and making recommendations in our final report for addressing these challenges.

Sincerely,



Earl Adams, Jr., Esq.
Chair

BLUE RIBBON COMMISSION MEMBERS

We would like to thank and acknowledge the following individuals for their service on the Commission:

Commission Chair

Earl Adams Jr., Esq.
Fort Washington

County Auditor

David Van Dyke, *County Auditor*
Prince George's County Council

Turkessa Green, *Assistant County Auditor*

Prince George's County Council

Prince George's County Council

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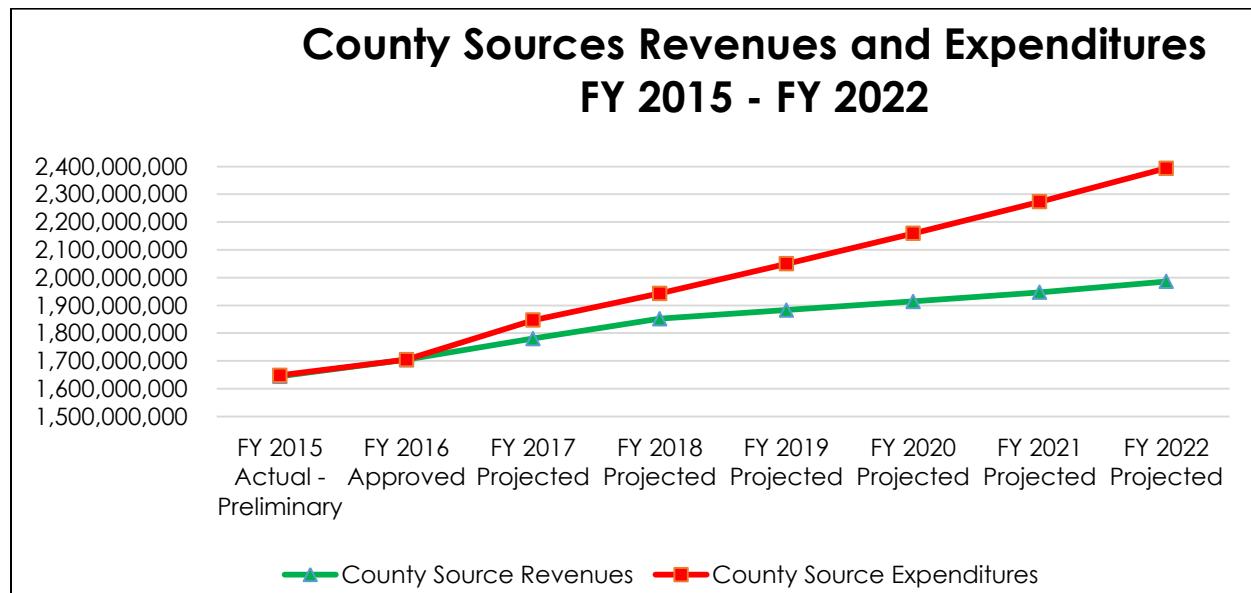
Blue Ribbon Commission on Addressing Prince George's County's Structural Deficit

Preliminary Report

(February 2016)

Part I. Introduction

Prince George's County (the "County") is facing a dire scenario with respect to its long term fiscal health. Based on current forecasts, and absent any intervention, the County will have an annual budget shortfall of between \$65 and \$250 million dollars beginning in Fiscal Year ("FY") 2017 through FY 2022. This gap, more aptly referred to as a "structural deficit," has been looming for several years and was caused by significant reductions in County revenue while annual expenditures continued to increase (See chart below).



Over the next five (5) years, the County's projected revenue growth is expected to be \$40 million to \$75 million dollars per year, however expenditures are projected to increase between \$90 million and \$200 million dollars per year. A significant portion of the County's expenditures are

necessary for the efficient operation of government and the delivery of services; however, the spending trend, absent intervention, is not sustainable.¹ Determining the proper balance of priorities and long-term fiscal obligations with the reality of reduced revenue growth requires immediate action to ensure the fiscal stability of Prince George's County.

To aide in the process of identifying solutions to this crisis, the County Council created the *Blue Ribbon Commission on Addressing Prince George's County's Structural Deficit* ("Commission"). The Commission is comprised of fifteen (15) voting members and two ex-officio (non-voting) members, all of whom are experienced community leaders and stakeholders. Between September 2015 through January 2016, the group met five (5) times. Each of the meetings was dedicated to a different topic to help Commissioners in developing an in depth understanding of the County's fiscal landscape. The topics touched on several items, including: (i) comparative budget data and information relating to the County's fiscal health and similar jurisdictions; (ii) policies and practices that impact Prince George's County's revenue structure and the strength of its tax base; and (iii) structural and fiscal dynamics of the County's government. Presentations were made by: (i) the Prince George's County Office of Management and Budget ("OMB"); (ii) the Office of Audits and Investigations ("A&I"); (iii) the County Financial Advisor Lester Guthorn; (iv) members of the County's Spending Affordability Committee; and (v) the County's Office of Human Resources Management.

The following Report summarizes the Commission's initial findings regarding the primary forces that have contributed to the County's current fiscal condition. It provides both a historical and contemporary perspective on how and when the County's revenues and

¹ The major expenditure drivers are debt service, Maintenance of Effort ("MOE") contribution to the County's Board of Education, employee benefits costs (i.e., pensions, healthcare, worker's compensation), cost of living adjustments ("COLA")/merits increases required under collective bargaining agreements, and public safety (e.g., overtime and new recruitment classes).

expenditures diverged over the past several years. Although this Report contains some recommendations, the majority of the recommendations will be presented in the Commission's Final Report. Part I of this Report discusses the revenue challenges impacting the County; Part II looks at the County's most significant expenditure obligations; and Part III closes the Report with a discussion on the regulatory limitations in place that restrain County government.

i. **Current Fiscal Year Outlook (FY 2016 and FY 2017)**

Based on the 1st quarter revenue and spending projections, there will be a \$400,000 deficit between revenues and expenditures in FY 2016. The forecast projects actual revenues will exceed the budget by \$16.7 million, totaling \$2.967.1 billion.² Strong performance in these revenue sources offset lower estimates in telecommunications, admissions and amusement, highway user revenue and permits collections. Actual expenditures are projected to total \$2.967.5 billion and will exceed the budget by \$17.1 million.³ This is primarily due to excess overtime spending, unfunded State mandates, operational service needs and the inability of several agencies to meet the 2% spending control measures included in the budget. OMB officials report that this is manageable and can be corrected by the end of the fiscal year.

The FY 2017 expenditure forecast is \$186.3 million above the FY 2016 budget (\$169.2 million above the FY 2016 estimated level). The higher forecast for FY 2017 reflects the following: 1) the anticipation of awarding compensation enhancements (merit increases) to employees; 2) fringe benefit cost growth (6% annually) and operating expense adjustments; 3) annual public safety classes; 4) additional staffing for certain general government agencies; 5) education sector contribution increase of 3% for the Board of Education, 4% for the Community

² This is primarily driven by stable year-to-date collections in real property, income, energy and transfer and recordation tax collections.

³ This is primarily due to excess overtime spending, unfunded State mandates, operational service needs and the inability of several agencies to meet the 2% spending control measures included in the budget.

College and 2% for the Library; 6) purple line and new hospital obligations in debt service costs; 7) \$4 million for worker's compensation obligations; and 8) an increase in non-departmental items. As required by law, the County will align revenues and expenditures and present a balanced budget.

ii. **Outlook for FY 2017 through FY 2022**

The picture for FY 2017 through FY 2022 is not positive. Based on preliminary projections, revenues for FY 2017 are projected to grow by \$113.2 million, but, as stated in the prior section, expenditures are forecasted to increase more rapidly to \$186.3 million. This results in a County Source budget gap of \$73.1 million.⁴ Further, this pattern multiplies for the next five years (FY 2018 through FY 2022) leading to potential annual shortfalls of \$98.1 million, \$145.1 million, \$195.1 million, \$246.7 million, and \$250.3 million, respectively.⁵

Part II. Preliminary Findings

a. Revenue

County revenues have lagged for several years. As an example, since FY 2006, annual growth has averaged approximately 1.76% a year as compared to the Consumer Price Index

⁴ County Source Budget is defined as the portion of the County budget that is funded by County Source Revenue, which is revenue that is primarily generated from County taxes, penalties, fees and investment income.

⁵ **Assumptions Underlying Forecasts.** These projections are based on the following revenue and expenditure assumptions:

Revenue Assumptions

1. Moderate growth of 4% in County Source revenue in FY17 and FY18 primarily related to increase in property tax, income tax receipts, and initial influx of new additional revenues generated by MGM Grand Casino.
2. Between FY19-FY22, revenue projected to slow and return to normal growth rate of 1.5%-2% annually.
3. No growth in Maryland aid to support Health Department, Police Department and Highway User revenues. Important note that County could be negatively impacted as Maryland addresses projected \$1.7 billion shortfall in FY 2016
4. Drop in miscellaneous revenues due to decreased revenues in automated speed cameras.

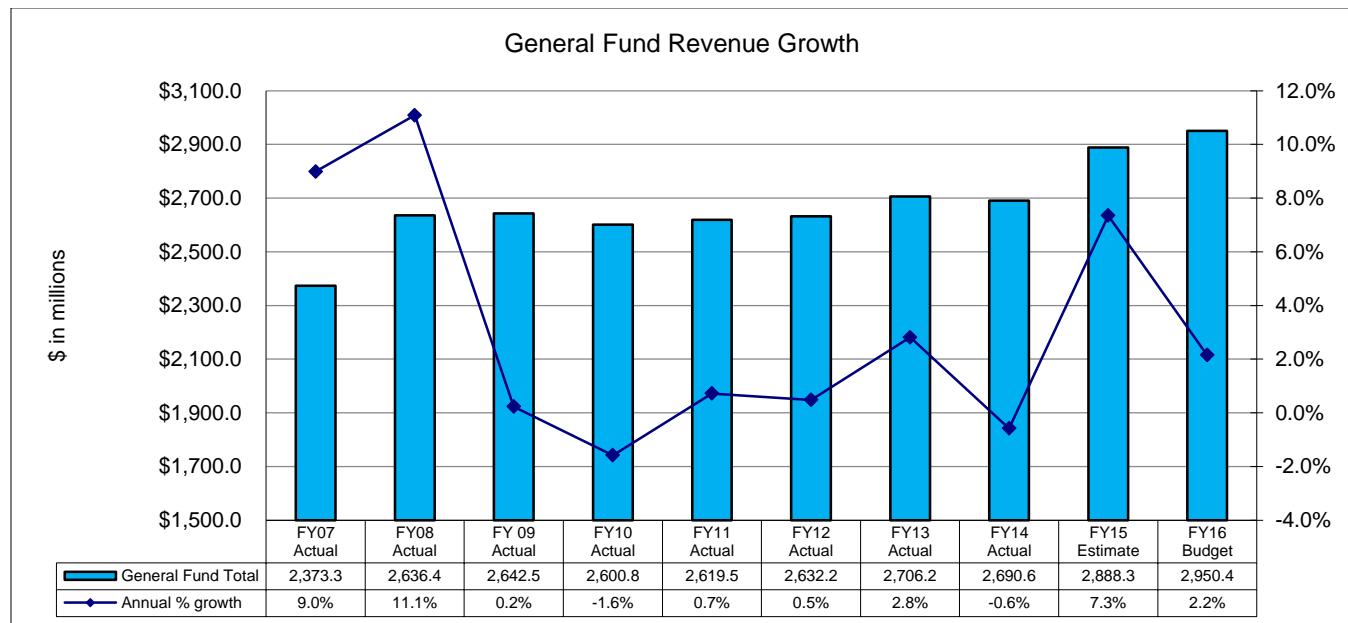
Expenditure Assumptions

1. Annual increases in employee compensation (merit and cost-of-living adjustments (COLA).
2. Annual increases in fringe costs (6%) and operating expenses (2.3%).
3. Increases in Public Safety Classes.
4. Additional staffing for County, Circuit Court, State's Attorney Office (SAO), Sheriff, Homeland Security, Health and Human Services, Environment and Infrastructure, and Development.
5. Annual increases for Board of Education (3%), Community College (4%), and Libraries (2%).
6. Purple Line and new hospital obligations in Debt Service.
7. \$4 million for Other Post-Employment Benefits (OPEB/Worker's Compensation).
8. Reduction in Non-Department Grants/Transfers (2.5%) and other (3%).

(“CPI”) which has averaged approximately 2.1% from FY 2006 to FY 2015. The following section discusses some of the factors impacting revenue growth in the County.

1. Historical

As with the majority of local governments, County revenues began to flatten in FY 2008 due to the Great Recession. Total General Fund revenues for FY 2007 were \$2.4 billion, \$2.636.4 billion in FY 2008, \$2.642.5 billion in FY 2009, and then dropped to \$2.600.8 billion in FY 2010 (See chart below).⁶ County source revenues showed a similar pattern. In FY 2007, they were \$1.48 billion, rising to \$1.49 billion in FY 2008, and then going down to just below \$1.48 billion in FY 2009. At the same time, a closer look reveals that the County’s revenues actually began to decline in FY 2007.



One particular issue contributing to the revenue lull was the loss of significant amounts of outside state funding. Specifically, beginning in FY 2003, the County received a significant amount of state-based aide for education, as a result of the “Bridge to Excellence” funding

⁶ General Fund is defined as the principal operating fund for the County government. It is used to account for all financial resources except those required by law, County policy and Generally Accepted Accounting Principles to be accounted for in another fund.

program totaling more than \$10 billion over the course of 13 years. In essence, this funding contributed to an artificial perception that the County was supporting its educational obligations when in fact outside sources were a contributing factor.

2. Income Taxes

Relative to its population of roughly 900,000 residents, Prince George's County lags significantly behind comparable jurisdictions in what it collects in income taxes. (See chart on page 7). For example, Montgomery County, which has a similar number of residents, collects approximately \$1,391 per capita in income tax compared to \$584 in Prince George's County.⁷ Income taxes accounted for 17.9% of the County's total budget, including outside sources, in FY 2016 compared to 28.2% for Montgomery County in the same year. The County currently applies the maximum permissible tax rate on income (also known as the "piggyback" tax), and in 2013 (which is the most reliable data available) the total net taxable income for Prince George's County exceeded approximately \$15 billion dollars, ranking it fourth in the state. However, when that total is adjusted for the County's overall population (also referred to as "per capita net taxable income"), the County's ranking drops to 16th in the state.⁸ These statistics demonstrate that the County is not as wealthy as it may appear, and that there is perhaps a misconception regarding the wealth profile of County residents.

⁷ The County is 20th in the state for the amount of incomes taxes paid on returns over \$150,000.

**NET AND PER CAPITA TAXABLE INCOME
CALENDAR YEAR 2013**

SUBDIVISION	Estimated Population July 2013 ¹	Total Net Taxable Income ²	Rank	Per Capita Net Taxable Income	Rank
ALLEGANY	73,521	883,324,281	19	12,015	23
ANNE ARUNDEL	555,743	15,636,875,234	3	28,137	4
BALTIMORE CITY	622,104	8,336,453,230	6	13,400	22
BALTIMORE COUNTY	823,015	21,287,945,539	2	25,866	5
CALVERT	90,484	2,298,278,397	13	25,400	8
CAROLINE	32,693	444,086,756	21	13,584	21
CARROLL	167,564	4,272,854,810	9	25,500	6
CECIL	101,913	1,824,523,665	14	17,903	15
CHARLES	152,864	3,251,745,193	10	21,272	12
DORCHESTER	32,660	447,355,915	20	13,697	20
FREDERICK	241,409	6,150,452,048	7	25,477	7
GARRETT	29,889	429,605,220	22	14,373	18
HARFORD	249,215	5,926,992,757	8	23,783	10
HOWARD	304,580	10,972,456,432	5	36,025	2
KENT	19,944	419,493,814	23	21,034	13
MONTGOMERY	1,016,677	38,036,993,408	1	37,413	1
PRINCE GEORGE'S	890,081	15,047,432,585	4	16,906	16
QUEEN ANNE'S	48,517	1,218,705,721	16	25,119	9
ST. MARY'S	109,633	2,479,551,035	11	22,617	11
SOMERSET	26,273	207,793,663	24	7,909	24
TALBOT	37,931	1,111,304,912	17	29,298	3
WASHINGTON	149,588	2,477,483,140	12	16,562	17
WICOMICO	100,896	1,400,850,656	15	13,884	19
WORCESTER	51,620	990,978,118	18	19,198	14
TOTAL IN STATE	5,928,814	145,553,536,529		24,550	
OUT OF STATE		4,393,936,077			
TOTAL		\$149,947,472,606			

¹ Maryland Department of Legislative Services, October 2015

² Comptroller of the Treasury, Revenue Administration Division, "Income Tax Summary Report, Tax Year 2013"

3. Homestead Tax Credit

Maryland law provides a tax credit to help homeowners deal with significant increases in the tri-annual tax assessments for their principal residences. The effect of this credit on the County's budget is that it loses revenue associated with its largest source—property taxes. The County's Charter Section 812, which sets how the credit is calculated, has not been amended since 2002. According to presentations by both OMB and A&I, as a result of this tax credit, the County has not seen any increase in the amount it collects in property taxes, notwithstanding the increase in housing assessments, since 2012. In real terms, the lost revenue dollars total approximately \$215.2 million over the last four (4) years (See chart below).

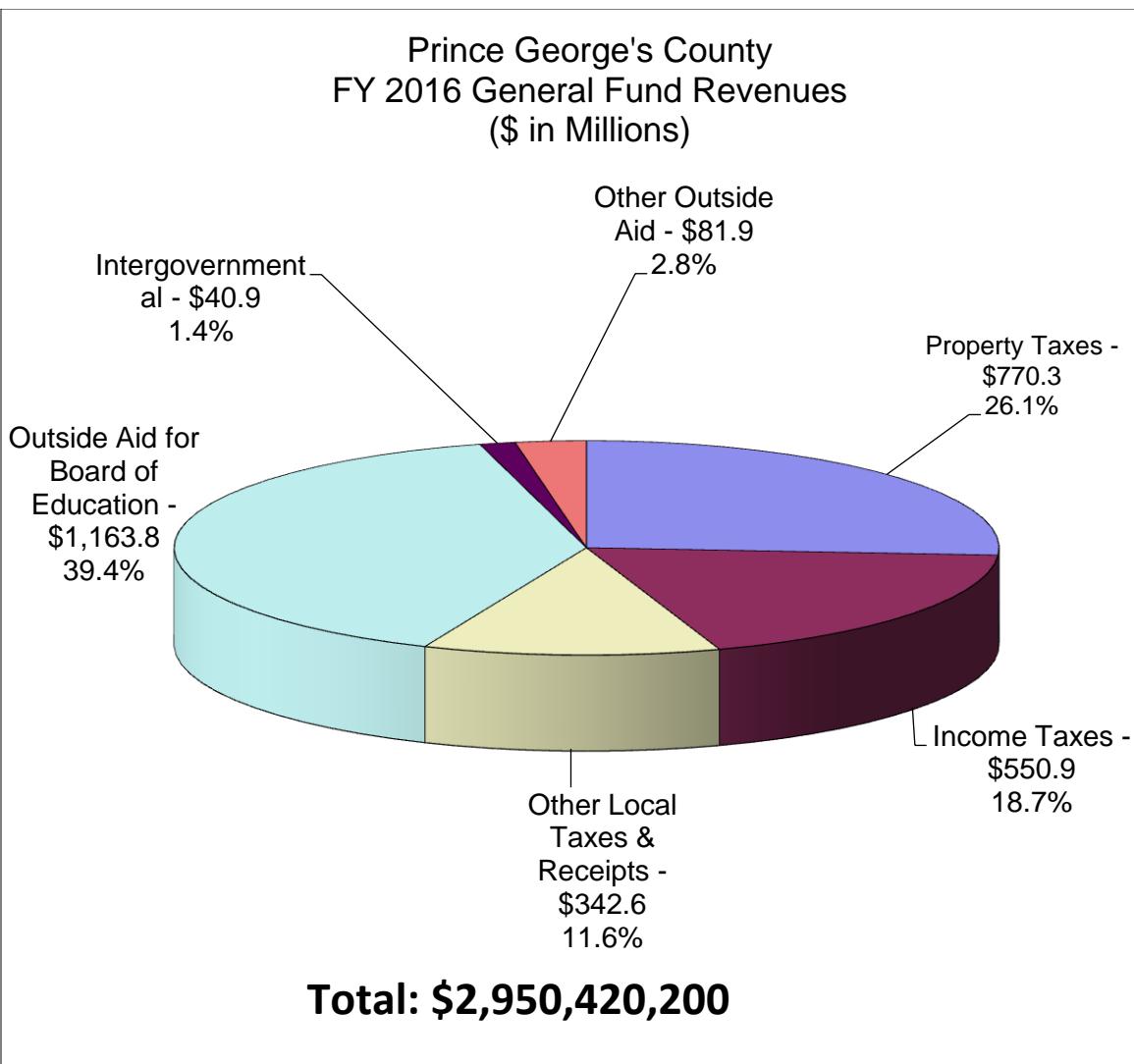
Period	Homestead Tax Credit Percentage	Homestead Tax Credit Assessments	Revenue Loss
FY 2012	101%	\$ 11,426,952,310	\$ 109,698,742
FY 2013	104%	5,498,575,692	52,786,327
FY 2014	102%	2,924,502,956	28,075,228
FY 2015	102%	2,562,541,732	24,600,401
FY 2016	102%	2,443,269,495	24,432,695

SOURCE:
Maryland State Department of Assessments and Taxation (November Projections) and Office of Management and Budget

The Homestead Tax credit is an important tool to prevent dramatic increases in County residents' tax bills. At the same time, Maryland permits jurisdictions to determine how the tax credit is to be calculated. However, Prince George's County has not taken any steps to attempt to address the impact of this restriction.

4. Outside Aid

Outside Aid represents the one positive component of the County's revenue picture. In 2016, the County received approximately \$1.245.7 billion from outside state aid to provide funding for (i) the Prince George's County Public School ("PGCPS") system; (ii) the Prince George's Community College; and (iii) the Prince George's County Public Library System. Over the last 40 years, outside aid to the County to help fund operations has doubled from approximately 21.8% to 42.2% of the total budget (See chart on page 10). In comparison, outside aid accounts for approximately 20.5% of Montgomery County's total budget. The import of this distinction is that Prince George's County is far more reliant on outside aid than comparable counties.



b. Expenditures

Despite the lag in County revenues, expenditures have continued to increase by 22.9%, or \$548.8 million, over the last 10 years. However, the majority of the County's spending is required, including costs for personnel and public education. During the Commission's first five (5) meetings, it focused on understanding how the mandatory spending obligations impact the budget.

1. Personnel

As with every jurisdiction in Maryland, including state government, personnel costs are a significant portion of County expenditures. Prince George's County has 5,970 full-time equivalent ("FTE") employees, and over the last two (2) years, the size of the workforce has decreased by 1.5%. When compared to comparable jurisdictions like Baltimore County (6,040), Baltimore City (12,033) and Montgomery County (8,244), the County's workforce is the smallest of the aforementioned jurisdictions.

The County's workforce can be divided into two main categories – Public Safety and Non-Public Safety. There are currently 14 Collective Bargaining Agreements ("CBA") covering County employees absent General Schedule employees. For informational purposes, the County's workforce breaks down as follows:

PUBLIC SAFETY GROUP (SWORN Employees)

- 1) Number and percentage of overall FT workforce: 2,825 or 45%
- 2) Distinct features of the CBAs (e.g., timing, significant increases in benefits, percentage of overall personnel costs, etc.)
 - For at least the last 20 years in Prince George's County, all public safety employees had full retirement benefits after 20 years of creditable service. The County recently negotiated, among other things, a 25-year retirement benefit for deputy sheriffs and correctional officers with less than five years of service, and for all new hires, which anticipates creating a savings of approximately \$656,900 annually.

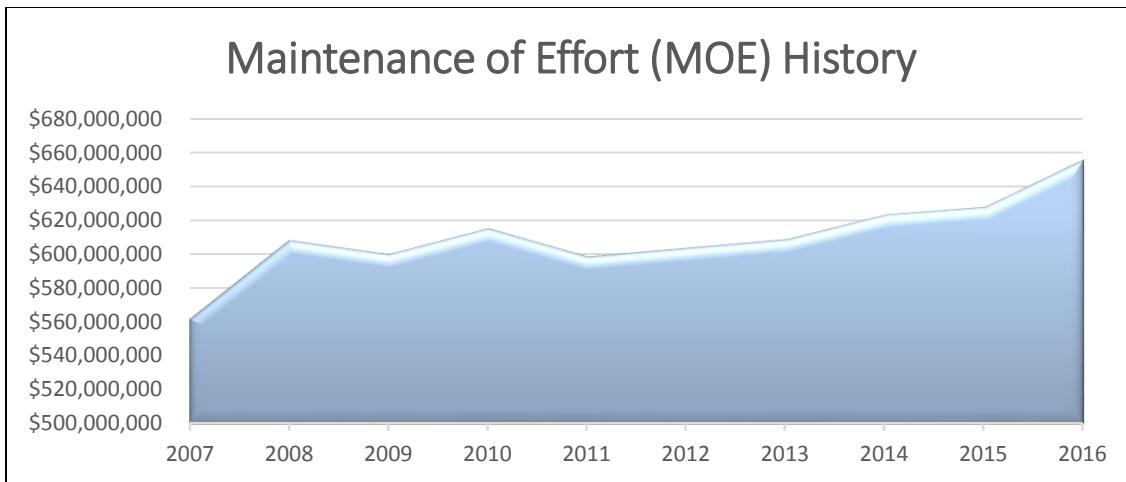
NON PUBLIC SAFETY Employees

- 1) Number and percentage of overall FT workforce: 3,449 or 55%
- 2) Two CBAs have been recently renegotiated.⁹
- 3) Distinct features of the CBAs (e.g., timing, significant increases in benefits, percentage of overall personnel costs, etc.)
 - Previous civilian contracts covered 2 years. In times of fiscal constraints, the County has had one year contracts.
 - Contracts agreed to by AFSCME and PCEA contain no merit increases for FY 2016, and provision for cost of living increases only if the County's undesignated revenues increase by 103.5% over the estimate made by the Spending Affordability Committee.

2. Education

In FY 2016, expenditures for the Board of Education constitute 62% of the County's budget or \$1.8 billion. Much of this expenditure is mandated by state law and requires the County to continue funding for schools at the same level set in the prior year. Said differently, any additional monies given to the Board of Education by the County in one year must be given in subsequent years. This requirement is referred to as "maintenance of effort" (MOE). Since FY 2007, the County's MOE requirement for education spending has increased by approximately \$100 million dollars (See chart on page 13), and for FY 2017 the school board is proposing an additional \$182 million over its FY 2016 approved budget. The Commission takes no position on whether these increases are necessary or prudent, but strongly notes that once set, the spending represents an ongoing obligation that may or may not be sustainable without continued overreliance on state aid.

⁹ The majority of civilian employees can be represented by one of the following unions: AFSCME Master (Locals 1170, 2462, 2735, 3389); Police Civilian (PCEA); Deputy Sheriffs Civilian (DSA); Corrections Civilian (PGCOA); Fire Civilian (IAFF); or General Schedule (non-union employees)



c. Limitations

Voter mandated limitations are a major force impacting the County's fiscal condition and ability to raise revenue. Prince George's County is not the only jurisdiction in Maryland that operates under such restrictions and the Commission has decided to reserve judgment on their efficacy at this point. Nevertheless, it is imperative for policy makers and residents to understand the impacts these limitations have on the County's ability to right-size itself during this current fiscal crisis.

1. Regulatory

With respect to the County's ability to raise revenue, there are three distinctive legislatively-created and voter-supported limitations: (i) Tax Reform Initiative by Maryland ("TRIM"), (ii) Question I, and (iii) Binding Arbitration. As discussed below, TRIM and Question I, in their own way, limit County government from raising revenue to fund its obligations and operations while Binding Arbitration limits the ability to control expenditures.

i. TRIM

In 1978, Prince George's County voters approved a charter amendment that prevented the government from increasing the property tax rate beyond FY 1979 levels without seeking prior voter approval. As a result of this provision, Prince George's County has only raised its property tax one time over the last 38 years. The artificial cap on the County's primary revenue source—property tax—has created significant challenges for the County. Currently, the County's real property tax rate is \$1 per \$100 dollars of assessed value. Four other Maryland jurisdictions have this provision in their local charters (Anne Arundel County, Montgomery County, Talbot County, and Wicomico County).

ii. Question I

This ballot question targeted certain other taxes and fees levied by the County and mandated that any proposed increase in the fee or tax had to be approved by voters. Again, as with TRIM, policy makers appear to be reluctant to raise fees or taxes given the unlikely prospect that residents will vote affirmatively to increase fees or taxes supporting certain goods or services they receive. No other Maryland jurisdiction has such a provision in law.

iii. Binding Arbitration

One final regulatory item that impacts County government personnel costs is binding arbitration. In 1980, and as amended in 1988, County voters passed a referendum requiring binding arbitration to resolve any wage or work condition disputes with the County's sworn police officers, uniformed firefighters, correctional officers and deputy sheriffs. The legitimate policy objective behind the charter amendment was to prevent unnecessary strikes or other work stoppages. The challenge is that in 2013 the County was subject to a binding arbitration award

that mandated that the Fraternal Order of Police be awarded four merit increases at one time that amounted to \$14 million in annualized cost. The Commission does not take a position on the prior arbitration awards; rather, this is a prospective warning that such awards can have a significant impact on the County's budget for years.

Part III. Conclusion

As the foregoing details, several factors have contributed to creating the County's current fiscal situation. County revenues have continued to be stagnant and there is no obvious path to increases in those revenues in the short term.¹⁰ Additionally, although some County expenditures can and must be reduced, mandatory spending related to personnel and public education will continue to apply downward pressure on the County's budget. Lastly, even with a disciplined approach to restricting spending, the regulatory limitations restricting the County's ability to raise revenue, represent a significant challenge for the County.

The Commission expects to continue its comprehensive review of the County's fiscal condition and will make several recommendations as required by the County Council's resolution. At this point, the Commission has determined that the voter-mandated limitations must be closely examined to determine their long-term viability given the County's fiscal condition.

The remaining meetings of the Commission will focus on strategies for solving the fiscal issues. The Commission will hear presentations focusing on the following: (i) the County's economic development strategies; (ii) fiscal impact of current land-use policies in the County; (iii) creative commercial revenue opportunities that have worked in other jurisdictions; (iv)

¹⁰This is the case even with projected revenues of \$35-\$41 million annually to be realized from the expanded National Harbor complex for FY 2017.

approaches to identifying greater efficiencies in the County's organizational structure; (v) and strategies for improving capital investments and procurement policy. Lastly, there will be three (3) public hearings in the northern, central and southern regions of the County to receive input from the public on the issues raised by this Report.