MARYLAND ASSOCIATION OF COUNTIES, INC.

May 14, 2012

The Honorable Edward J. Kasemeyer
Chair
Senate Budget and Taxation Committee
Miller Senate Office Building, 3 West Wing
11 Bladen Street
Annapolis, MD 21401

RE: Budget Reconciliation and Financing Act of 2012 and the State and Local Revenue and Financing Act of 2012

Dear Senator Kasemeyer:

The Maryland Association of Counties (MACo) appreciates the opportunity to express its concerns regarding the Budget Reconciliation and Financing Act of 2012 (BRFA) and the State and Local Revenue and Financing Act of 2012. As you know, MACo opposed the BRFA during the session and did not take a position on the revenue bill. Now that a number of the teacher pension shift offsets have been included in the revenue bill, MACo would also like to comment on components of this legislation.

The past month has been a difficult one for county governments. The passage of a “doomsday” budget and the uncertainty of whether that budget would be replaced by a proposal approved by the budget conference committee during a special session has forced counties to pull together a number of very different budget scenarios for FY 2013. Under these scenarios, a number of counties may increase property taxes and/or significantly reduce county services. However, the level and long term consequences of these actions will be set by the budget that is before you today.

When comparing the “doomsday” budget to the one that is before you, the outcomes are very different. Doomsday represents a one year reduction that can be restored in FY 2014. The budget before you represents a shift of increasing on-going costs for which counties will be responsible for years to come. While MACo appreciates the work of both the House and Senate to minimize the effects of the pension shift through a phase-in and by providing a number of offsets, it is still concerned with the policy direction and long term effect such a shift will have on county governments and their citizens.

Teacher Pension Shift – The proposal before you includes a massive shift in teacher pension costs to county governments. While most attention has been focused on the effects in the immediate budget year ahead, this cost shift will grow from approximately $137 million in FY 2013 to $216 million in FY 2016, with the net effect landing squarely onto county governments. While a variable range of offsets are being provided to lessen the effect of this cost shift, these offsets do not grow commensurate with the costs being shifted, and some will not generate as much revenue after the first year ultimately leaving counties to cover even more of these new mandated costs.

Counties disagree that shifting funding responsibility in this manner does anything to improve the sustainability of state pension funding, it simply relocates these cost burdens – away from the level of government that has complete control over benefit levels and investment decisions; and has deliberately guided policy toward wage increases, and toward the level of government that has played the far lesser role in these cost changes. Counties also differ with the claim that a "sharing of retirement costs will incentivize locals to consider the impact of salary decisions on retirement benefits." County governments have no control over the setting of teacher salaries, and do not even have a seat at the table to negotiate benefits and terms.

MACo would argue that there are three cost drivers for pensions: benefit design/employee cost sharing, investment performance, and growth in teacher salaries. None of these elements are within county government control.

Benefit Design/Employee Cost Sharing – Plan design and employee contribution rates are entirely a creation of state law. A DLS presentation provides a historical overview of what has occurred in these areas over the years. Although new plans were created in the early 1980's to control costs, many benefit enhancements were made through legislation. The most recent benefit enhancement occurred in 2006 adding $1.9 billion to the system's actuarial accrued liabilities. Local governments had no control or say in enacting these benefit enhancements.

Investment Performance – The State Retirement and Pension System (SRPS)'s investments are managed by a state-appointed Board. As the SRPS became fully funded by the end of FY 2000, the system experienced significant losses in FY 2001 and 2002. With the economic downturn of 2008, the SRPS experienced a 22% decline in asset value and a -20% return on investments in FY 2009. A DLS presentation on the funding of Maryland's SRPS refers to 2000 – 2010 as "The Lost Decade." The SRPS earned annualized returns of 2.1% during this timeframe. Again, local governments played no role in making these investment decisions.

Growth in Teacher Salaries – Teacher salaries have been fueled by state funding formulas. A very clear policy direction was set by the State to better recruit and retain qualified teachers, to reduce classroom sizes, and to improve the share of fully certificated classroom teachers. The Bridge to Excellence legislation ("Thorton") was enacted in 2002 to achieve gains in public education equity and adequacy by altering and increasing education funding significantly from FY 2002 to FY 2008. During this time frame, state funding increased by 78.9%, or $2.2 billion. It should be no surprise that staff employed by local systems increased by 8,274 positions, or 15.5%. Whereas, local funding also increased during this time frame, that was the expectation of the State.

County Offsets – A series of actions have been included in the proposal before you to offset some portion of the pension costs newly shifted onto local governments. Again, MACo appreciates the work of the House and Senate to provide for these offsets and for listening to its concerns with respect to out-years costs. However, counties must reiterate some its concerns raised with these offsets during the session:

Forgives repayment on income tax reserve – MACo has advocated for the elimination of this requirement, however not as an offset to teacher pension costs. Counties have always argued that repayment of this fund was unnecessary.

Changes to income tax personal exemptions – These tax changes are being proposed to address the state's budget deficit and generate local revenues to offset teacher pension costs. Revenues generate from this proposal is based on 18 months for FY 2013 and will drop roughly by a third in FY 2014 and beyond leaving counties to cover a larger share of costs in the out years. Any analysis focusing only on the FY 2013 effects of this revenue change will thoroughly overstate the new county revenues arising from it, despite the permanent and increasing pension costs.

Recordation Tax and Indemnity Deeds of Trusts – MACo has advocated for the closing of this loophole, as a more general matter of providing greater tax fairness for the many individuals and business that currently pay recordation taxes on secured borrowing. The transactions subject to the proposed tax law would vary greatly from one year to the next, making it very difficult to build a budget on these figures. Contemplating these highly variable county-by-county revenue figures suggests unwise budgeting practices.

MACo would also like to express concern with the following components of the BFRA:

Funding for Court Judgments – A recent Court of Appeals opinion found that the State is responsible for satisfying court judgments against a school board. However, the BRFA is shifting this funding responsibility to local governments and precludes local governments from reducing those items in the proposed school budget. This represents another shift in funding responsibility to local governments where they have no say or control over actions of a school board.

Other Changes Affecting Local Governments – Lastly, MACo is concerned with language in the BRFA that is amending two Maryland Department of the Environment Programs, the Community Right-to-Know Funds and the Recycling Trust Fund to give MDE greater flexibility in funding emergency response activities of the department and the land management administration. Local governments currently receive funding from these programs to fund local emergency planning committees and improvements in recycling programs. These actions, combined with others that may be carried out administratively by State agencies, places increased burdens on local governments at a time when they can least afford them.

Again, MACo would like to thank you for the opportunity to speak today. Please contact us if we can provide additional information or respond to questions.

Respectfully yours,

Michael Sanderson
Executive Director

cc: Members, Senate Budget and Taxation Committee
Committee Staff