SPENDING AFFORDABILITY COMMITTEE
Anne Arundel County
January 12, 2016

The Hon. Steve Schuh, County Executive
The Hon. Derek Fink, Chairman, County Council
Mr. Mark Hartzell, Chief Administrative Officer
Mr. John Hammond, Budget Officer
Mrs. Julie Mussog, Controller
The Arundel Center, 44 Calvert Street
Annapolis, Maryland 21401

This report of the Spending Affordability Committee (SAC) for FY2017 is hereby submitted to you in accordance with Section 610 of the Anne Arundel County Charter. This section requires in part that "The Committee shall make advisory recommendations to the Office of the Budget, the County Executive, and the County Council relating to spending affordability including County spending levels to reflect the ability of the taxpayer to finance County services and long-term debt." Section 610 also tells the Spending Affordability Committee to "examine" current capital projects, the five-year capital improvement program, per capital wealth, debt service, pay-as-you-go funding and alternative sources of funding.

Committee Recommendation

The SAC has followed the past practice of previous committees and determines that "spending affordability" can best be determined by estimating the growth in personal income of County residents in FY2017. For example, if personal income of our residents should only increase one percent, then County spending should not increase more than that one percent.

As discussed below, the SAC is estimating that personal income will grow about three percent during FY2017. As shown in the following table, applying the three percent growth rate to the approved FY2016 budget as adjusted means that the Committee is recommending that the maximum FY2017 appropriation not exceed $1,386,888,820 for an increase of about $40 million. Further, the SAC is recommending that the FY2017 General Fund Debt Limit be limited to $1,117,344,000, or almost $21 million less than FY2016.

Current Expense Budget Recommendation	
(Adjusted Base Budget for Current Year x Estimated Personal Income Growth Rate for Budget Year)	
Approved FY2016 Budget	$1,366,527,500
- Appropriated Fund Balance	(18,033,500)
- Rainy Day Fund Contribution	(2,000,000)
Committee's Adjusted Base Budget - FY2016	$1,346,494,000
Estimated Increase in County Personal Income (FY16 to FY17)	3.00%
FY2017 General Fund Appropriation Limit (customary manner)	**$1,386,888,820**
Capital Budget Recommendation	
(Personal Income Forecast for Current Year x Estimated Personal Income Growth Rate for Budget Year x Standard)	
Average of RESI (Regional Economic Studies Institute of Towson University)	
Quarterly Forecasts for County Personal Income - FY2016	$36,160,000,000
Estimated Increase in County Personal Income (FY16 to FY17)	3.00%
Forecast Personal Income - FY2017	$37,244,800,000
Standard Applied in County's Debt Affordability Model	3.0%
FY2017 General Fund Debt Limit (customary manner)	**$1,117,344,000**

Background

Anne Arundel County and the State of Maryland have historically contracted with about four econometric firms (economic modeling) to provide estimates of personal income and other data for the United States and more specifically Maryland. One of these four firms, RESI of Towson University also provides data for Anne Arundel County. Personal income estimates are based on data collected by the Bureau of Labor Statistics, U. S. Department of Labor.

In recent years, the Maryland State Board of Estimates and their four econometric firms have had to revise downward their estimated personal income growth for Maryland. As shown in the following table, their November 2014 estimates were 4.7, 5.4 and 5.4 percent respectively for fiscal years 2015, 2016, and 2017. This past December 2015 they revised their estimates downward to 4.0, 4.8, and 4.8. Out contractor, RESI of Towson, has been lower and more on target than the State-wide firms and estimates. Hence, the SAC believes that a more prudent approach would be to adopt an estimate closer to the lower estimates of personal income growth.

Also supporting a lower estimate is a national economy that has continued to fall short of most expectations, the decline in the usually dependable growth of Federal jobs in our County, the large number of Presidential candidates with varying policies, Congress' continuing reliance to fund the Federal Budget via short-term appropriations, rapidly changing energy prices, potential terrorist attacks…and the list can go on. These and other factors account for arguably the most uncertain economic environment in many years thereby dampening the willingness to spend and invest.

The lowest estimate of the econometric firms for the State of Maryland was developed by RESI that also estimates our only county-level personal income. RESI estimates for the County's personal income growth in FY 2016 is 3.1 percent and 3.3 percent in 2017. Nevertheless, the Committee recommends for FY 2017 a slightly lower estimate of 3.0 percent. At the State-level, the Bureau of Revenue Estimates met in December 2015 and adopted personal income growth estimate of 4.9 percent for FY2016 and 4.8 percent in FY2017 respectively, accompanied by the statement that "Our expectation is for economic growth, but at a rate lower than in comparable periods of economic expansion."

Comparison of Personal Income Forecasts (Fiscal Years)

	2014	2015	2016	2017
State of Maryland				
Board of Revenue Estimates (Dec)	4.0%	4.4%	4.9%	4.8%
Sage Policy Group (Nov)	4.0%	4.6%	5.2%	5.2%
Moody's (Nov)	4.0%	4.7%	5.6%	6.0%
Global Insight (Aug)	3.6%	4.2%	4.8%	5.2%
RESI of Towson University (Dec)	1.5%	2.3%	3.6%	2.9%
This year's average Dec 2015 estimates	3.4%	4.0%	4.8%	4.8%
have been substantially reduced from				
From last year's average Nov 2014 estimates	3.0%	4.7%	5.4%	5.4%
Anne Arundel County				
RESI of Towson University (Dec)	2.0%	3.0%	3.1%	3.3%

Please see Appendix A for further detail and factors affecting growth in Anne Arundel County.

Committee Concerns

For the past several years, the Committee has expressed concern over a number of budgetary issues. Underfunding of the capital budget remains a continuing concern. In last year's SAC Recommendation letter, the committee again expressed concerns regarding the state of the county capital assets. The accumulated deficit for the maintenance and renovation of capital assets, including schools, roads, and other essential County infrastructure, was highlighted in the SAC report for FY2010 as approaching $2 billion and growing at a rate of nearly $100 million per year. The proposed increase in capital spending FY 2016-2021 is a great start provided it is mostly spent on aging assets as opposed to new items. In addition, the impact fees charged still remain below 100 percent of the calculated costs with roads being the worse at just over 50 percent based on the 2008 Impact Fee study. The SAC recommends that the County move towards 100 percent of calculated costs (adjusting for inflation) for Impact Fees. This is consistent with the 2008 Report by the Impact Fee Advisory Committee.[1]

A second area of concern is the County's fee structure. The SAC discourages any reduction to or the waiving of hookup fees that may negatively affect the ability to meet the debt service obligations for the Utility Enterprise Fund. If the Fund cannot service the debt

[1] April 21, 2008 Report of the Impact Fee Advisory Committee required by Resolution No. 13-08.

obligation at 100 percent, it would have to be subsidized from other areas of the budget.

The above two practices perpetuate the underfunding of the real cost of supporting the County's infrastructure. This underfunding is ultimately passed onto and paid by County taxpayers.

A third area of concern is the overall decline in average weekly salaries in our County. While County employment has increased over the past five years from 230 thousand in 2010 to 263 thousand in 2015, the average salary, when adjusted for inflation, has fallen from about $1,147 to $1,021 per week.[2] This means that we are replacing better paying jobs with lower paying jobs. This also suggests that the rise of the "Gig Economy" is impacting Anne Arundel County as well as the rest of the U. S. The Gig Economy is where workers holding long-term, regular employment are being replaced by workers who hold multiple types of flexible employment (gigs) known as part-time or contingent jobs. This trend was identified by RESI. This drift toward lower paying jobs reduces the strength of our tax base.

Finally, the Committee, as required by our enabling legislation, plans to "...examine ... alternative sources of funding" as well as review other budgetary issues over the coming calendar year with a view toward minimizing the burden upon our taxpayers.

Closing

The Committee once again extends its heartfelt appreciation to our County employees, especially to Assistant Budget Officer Hujia Hasim and Budget Officer John Hammond. The quality of governmental services that they provide is second to none. We sincerely hope that the evidence assembled for this report will help manage expectations and inform fair and just analysis of the difficult choices facing our elected leaders.

The Committee's membership is listed in Appendix B.

Sincerely,

John W. Spencer, Chair

[2] Based on various data from the U. S. Department of Labor's Bureau of Labor Statistics QCEW database.

Appendix A
Economic Outlook and Recommendations for Spending Affordability

In the report on Estimated Maryland Revenues from December 15, 2015, the Maryland Board of Revenue Estimates stated: *"…the economic picture has not changed much, accordingly our outlook remains subdued relative to normal periods of economic expansion. It must be stressed that our outlook calls for improving employment and wages as the economic expansion continues, just not at the rates of growth witnessed throughout the expansionary periods of the 1990s and 2000s."*[3]

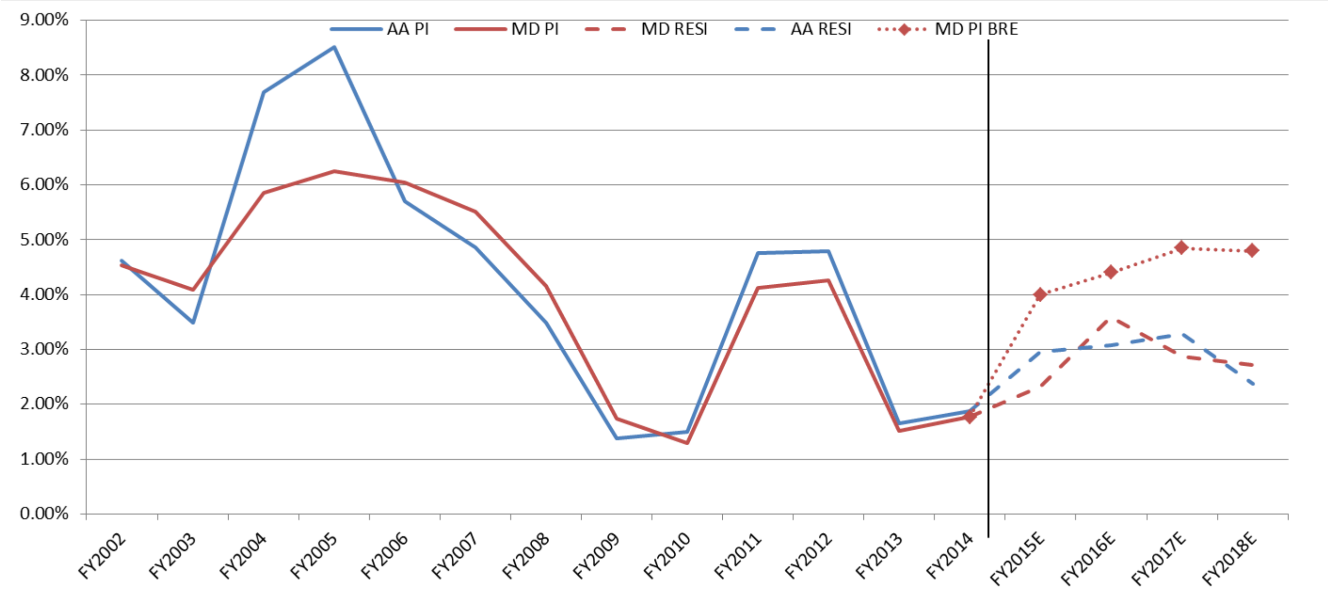
Thus looking forward, Figure 1 below shows that both State and County employment are to grow, but only in the one percent range. Note that Anne Arundel County has experienced employment growth rates of almost five percent in 2004, 2012, and 2013.

Figure 1
County and State Employment Growth and Forecasts

As shown in Figure 2, the Maryland Board of Revenue Estimates expects that the State's Personal Income growth to remain moderately strong for the near future, that is, in the range of four to five percent. Our consultant RESI forecasts weaker growth for both the State and Anne Arundel County, that being in the range of three percent, or markedly less than Maryland Board of Revenue Estimates. This is consistent with the SAC's recommendation for a 3.0 percent growth in personal income in FY2017.

[3] Report of the Maryland Board of Revenue Estimates on Estimated Maryland Revenues, fiscal year ending June 30, 2016 and June 30, 2017, submitted to Lawrence J. Hogan, Jr. Governor, December 15, 2015, on page 1.

Figure 2
County and State Personal Income Growth and Forecasts



Appendix B
Mission and Membership of Spending Affordability Committee

Mission

The Spending Affordability Committee was established through a Charter amendment approved by the voters of Anne Arundel County at the General Election in November 1990. The Committee is charged with making advisory recommendations to the Office of the Budget, the County Executive, and the County Council relating to spending affordability including County spending levels to reflect the ability of the taxpayer to finance County services and long-term debt.

Consistent with this mission, the Committee has historically provided the Office of the Budget, the County Executive, and the County Council with a recommended General Fund Current Expense Budget appropriation limit and a recommended General Fund debt limit. In addition to these recommended spending affordability limits, the Committee has also provided comments on various issues related to the County budget, County operations, and the County's capital infrastructure.

Membership

The Spending Affordability Committee consists of seven residents, one from each County Council district who are knowledgeable in the field of economics, finance, fiscal planning, or a related field. These residents are appointed to the Committee by the County Executive and confirmed by resolution of the County Council. The Committee members elect their own chairman. The district memberships consist of staggered four- year terms, and a person may not serve for more than two successive terms. The current membership is shown below (need to confirm years below:

District	Name	Resolution #	Appointed on	Term Expires
1	Debi Sandlin	42-15	October 1, 2015	December 1, 2018
2	Joseph Robert Sapp	66-12	December 1, 2012	December 1, 2016
3	John W. Spencer, Chair	52-13	December 2, 2013	December 1, 2017
4	Aaron Klebanoff	52-13	December 2, 2013	December 1, 2016
5	J. Timothy Connolly	42-15	October 1, 2015	December 1, 2018
6	Jerry L. Pesterfield	42-15	October 1, 2015	December 1, 2018
7	Jason C. Johnson	21-14	July 1, 2014	June 30, 2018