Agenda Item 5
April 8, 2019

MEMORANDUM

April 4, 2019

TO: County Council

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SUBJECT: Overview – FY20 Operating Budget

I. INTRODUCTION

The Executive's FY20 Operating Budget proposes to increase the Total Budget for all funds by $142 million (2.5%) to $5,722,955,614. Tax Supported Funds would increase by 2.3% to $4,996,234,180. Based on the Executive's recommendation, the County Government funding is proposed to increase by 3.9% and the Washington Suburban Sanitary Commission (WSSC) by 4.6%, Montgomery County Public Schools (MCPS) by 1.6% and the Maryland-National Park and Planning Commission (M-NCPPC) by 0.8% and 0.8% and Montgomery College's funding is proposed to decrease by 1.2%.

The review of the budget will give the Council the opportunity to determine whether it shares the Executive's priorities as to how best to serve the residents of the County and make tradeoffs among worthy but competing choices. The upcoming public hearings are likely to identify programs and functions which residents believe require additional resources, particularly since 3 outside agencies were not funded at the levels they requested. The Council may also determine that certain funding in the Executive's recommended budget does not match its priorities and choose to reallocate it to other purposes. Over the next 7 weeks, the Council will have numerous decisions to enable it to budget for its priorities in a fiscally sustainable framework.

This memorandum describes the Recommended Budget's assumptions regarding revenues and recommendations for Expenditures (including agency allocations, compensation, changes in workforce) and for the implementation of fiscal policies related to reserves, pay as you go (PAYGO) and Other Post Employment Benefits (OPEB). Attached on © 1-30 are the highlights of the different agency budgets as presented in their transmittal letters.

II. REVENUES

Page 5-17 of the budget (attached at © 33) displays the budgets estimates of revenue in FY19, FY20 and beyond to FY25. FY19 **total** revenue is now estimated to be $29.9 million below the FY19 approved budget, and $36.9 million below December's estimate. Property and income taxes are the greatest sources of revenue and the combined estimates are **reduced by $64.2 million for FY19** (property tax by $21.9 million and income tax by $42.3 million), while other revenue sources stay level or increase with the exception of total revenues from Montgomery College tuition, which is projected to decrease.

REVENUE SUMMARY TAX SUPPORTED BUDGET ($ Millions)					
Revenue Category	**App. FY19 (5/18)**	**Est. FY19 (3/19)**	**% chg FY19 App. Vs. Est**	**Rec. FY20**	**% Chg. FY 19-20**
Property Tax	1,808.4	1,786.5	-1.2%	1,836.8	1.6%
Income Tax	1,585.2	1,542.9	-2.7%	1,640.3	3.5%
Transfer/Recordation Tax	162.9	180.6	10.9%	182.8	12.2%
Other local taxes (energy,telephone, hotel, admissions, e-cigarette	273.7	278.3	1.7%	283.2	3.5%
Intergovernmental Aid	880.5	884.9	0.5%	903.6	2.6%
Fees and Fines	193.0	195.4	1.2%	193.0	0.0%
Miscellaneous	24.6	29.8	21.1%	27.3	11.0%
TOTAL REVENUES	**4,928.3**	**4,898.4**	**-0.6%**	**5,067.0**	**2.8%**

FY20 tax revenue projections have also changed significantly ($41.5 million less in the March 15 budget than in the May 2018 projection, and $33.7 million below the projection from this past December).

Revenue projections are inherently difficult given the number of factors affecting revenue, the limited information available, and the timing of data releases. Changes to economic fundamentals and demographics, as well as changes to the policy landscape (such as the Tax Cuts and Jobs Act of 2017), exacerbate those challenges. Locally, property tax revenue has fallen short of projections for each year since FY17. Income tax revenue has fallen short of projections for each year since FY15.

a. Property tax

The County Executive's budget assumes that property tax revenue will be at the Charter Limit with a property tax credit of $692. His budget assumes property tax revenue of $1,836.8 million in FY20, which is $28.4 million above the FY19 approved budget and $50.3 million above the FY19 estimate (a 2.8% increase).

A seventh consecutive year of rising assessments has relieved pressure on property tax rates. The County Executive recommends a General Fund property tax rate of $0.7202 per $100, and a weighted average property tax rate of $0.9786 per $100, which is $0.0028 per $100 below the weighted average rate in FY19.

b. Income tax

FY19 income tax revenue is now estimated at $1,542.9 million, which is $42.3 million below the amount assumed when the FY19 budget was approved last May. This unexpected current year decline in income tax revenue has the most significant impact on the change in total revenues.

The recommended budget assumes FY20 income tax revenue of $1,640.3 million, which is $42.7 million below the FY20 projection from last May. The recommended FY20 income tax revenue is up by 3.5% from the approved FY19 budget; it is estimated to increase 6.3% from the March estimate ($97.4 million). As noted earlier, the County's projections for income tax have fallen short since FY15, and during that period, the Council approved five savings plans.

Income tax revenue volatility is a fact of life for Montgomery County. The volatility of income tax revenue from year to year, and within any year, presents challenges for fiscal planning. In the pre-recession years (FY05-08), revenue rose 37% from $941 million to $1,291 million. Income tax revenue was flat in FY09 before falling 19% to $1,042 million in FY10. Income tax revenue bottomed in FY11 at $1,039 million before rising 21% in FY12 to $1,255 million. For FY18, it had been projected to reach $1,558 million, but the year ended $88.7 million below that number. FY19 incomes are now projected to come in $42.3 million less than anticipated last May.

To a large degree, that volatility is the result of the year-to-year variations in the capital gains income of a small number of County residents. In FY18, income tax revenue has fallen short of projection in large part because of a sharp decline in the 2016 capital gains of the County's top 50 taxpayers. In 2015, the top 50 taxpayers realized capital gains of $1.2 billion. In 2016, the capital gains income of those same taxpayers was reduced by half. Similarly, a review of tax return data published by the Comptroller indicates that roughly 1.8% of Montgomery County returns report income of $500,000 or greater. On average, these returns explain more than half of any year-to-year increases in income tax revenue and more than 100% of any year-to-year declines in income tax revenue.

Other forces impact the County's income tax revenue situation including: (1) the *Wynne* case; (2) H.R. 1 (the Tax Cuts and Jobs Act of 2017); and (3) the national and local economy. The U.S. Supreme Court's 2015 decision ***Maryland State Comptroller of the Treasury v. Brian Wynne, et ux.*** which requires that the County begin to provide a credit of county income tax for income taxes paid to other states. The Finance Department has determined that the cost of repaying the State for past claims is now estimated at $143.3 million ($14.3 million in FY21, $28.7 million in FY22-25 and $14.3 million in FY26). **In addition to the repayment obligations, there will be ongoing annual revenue loss from *Wynne* of $30 million per year, resulting in total costs of $44.3 million in FY21, $58.7 million in FY22-25 and 34.3 million in FY26 and $30 million each year thereafter.**

Over the long term, the Tax Cuts and Jobs Act of 2017 and Maryland legislative reactions to the federal changes will impact Montgomery County's income tax revenue, but impacts are still unclear. Due to the uncertainty, Finance based FY20 income tax estimates on the December 2018 income tax estimate by the Board of Revenue Estimates.

Finally, national and regional economic trends will impact income tax revenues. There are mixed and recently negative signs regarding the national economy. While the unemployment remains low at 3.8%[1] and wages had their biggest annual increase since 2008 (2.9% between September 2017 and September 2018), the recent sharp decline in interest rates on long-term United States government bonds

[1] The unemployment rate in February 2019 was 3.8%, compared to 4.1% a year earlier and 10% at the end of 2009.

to below short-term rates is seen as a signal of a slowdown in economic growth and possible recession[2]. Last month the Federal Reserve left interest rates unchanged indicating that economic growth was slowing more than expected (2.1% down from an earlier estimate of 2.3% and last year's 2.9%) and the stock market has had a turbulent few months.

The March 2019 "Washington Economic Watch" prepared by the Stephen S. Fuller Institute for Research on the Washington Region's Economic Future indicates some troubling signs for the local economy as well. The Washington Leading Index (which is designed to forecast the performance of the metropolitan area economy six to eight months in advance) declined by 1.18% in January on a monthly over-the-year basis. The Leading Index has now only increased once since mid-year 2018 and is forecasting slower economic growth over the next several quarters. While Suburban Maryland had added 15,200 new jobs in 2017, it only added 3,000 jobs in 2018, down 80.3%.

Additional information on local demographic and economic trends appears in Chapter 5 of the budget and is summarized in the chart on page 5-15.

c. *Fuel/Energy tax*[3]

Fuel/energy tax revenue is up $3.9 million (2%) in FY19. The County Executive did not recommend any change to rates in FY20. **The fuel/energy tax—the County's third largest tax revenue source—generates 5.0% of local tax revenue.** Revenue from this tax depends on consumption, and consumption is affected by weather conditions, economic conditions, and other public policy interventions that are intended to reduce fuel/energy consumption.

d. *Transfer and recordation taxes*

Revenue from both the transfer tax and the recordation tax are generally volatile. From FY17 to FY18 revenues decreased by $22.3 million (11.5%); for FY19, the current estimate is $17.7 million (10.9%) above the approved FY19 budget. Transactions which generate transfer and recordation tax revenues have fluctuated greatly over time and primarily reflect shifting trends in the real estate market, primarily due to changes in large commercial transactions.

III. EXPENDITURES – AGENCY ALLOCATIONS

Total tax supported expenditures of $5,082.9 million is recommended for FY20, 2.4% above FY19. This amount includes $517.2 million in non-agency expenditures (debt service, PAYGO and CIP current revenue, changes to reserves and other set asides). Agency tax supported budgets are up 2.3% overall. Montgomery County Government is up 3.9% over FY19, MCPS is up 1.6%, and M-NCPPC is up 0.8% while Montgomery College is 1.1% **below** FY19.

With a tax supported budget of $2483.7 million, MCPS represents more than half (54.3%) of the recommended budget. Tax supported debt service, including debt service on Park bonds, is $430.5 million, or 8.5% of total tax supported expenditures—more than the combined tax supported allocations

[2] A fall in long-term bond rates below yields on short-term bonds – a yield curve inversion – has preceded every recession over the last 60 years (New York Times 3/22/19 and Federal Reserve Economic Letter 3/5/18)

[3] The tax is imposed on providers of electricity, fuel oil, gas, steam, or liquefied petroleum gas. Providers then pass the cost of the tax on to their customers. One-third of revenue is from energy provided to residential users and two-thirds is from energy provided to non-residential users. Electricity accounts for the lion's share of revenue, with the smaller amount of revenue from natural gas.

to Montgomery College ($262.4 million, or 5.7%) and M-NCPPC ($129.3 million, or 2.8%). County Government, at $1,690.4 million excluding debt service, represents 37% of the total tax supported budget. A full listing of expenditures by agency, fund, function and department can be found in the budget in Schedule B on pages 70-3 to 70-13.

AGENCY TAX SUPPORTED BUDGETS FY19 and FY20 (Appropriations excluding debt service) and FTEs[4]				
	FY19		FY20	
FUNCTION	Appropriation ($ millions)	FTEs	Appropriation ($ millions)	FTEs
Montgomery County Public Schools	2,444.1	21,254	2,483.7	21,650
Montgomery County Government	1,627.2	8441	1,690.4	8,531
Montgomery College	265.5	1,810	262.4	1,803
M-NCPPC	128.3	923	129.3	942[5]
Total All Agency Tax Supported	*4465.1*	*32,428*	*4565.7*	*32,926*

MCPS

The Executive recommends a total budget of $2.648 billion for MCPS, which is a 2.0% increase from FY19 but $14.5 million below the Board of Education's request of $2.662 billion. The Executive's recommended County contribution is also $14.5 million below the Board's request, and $2.5 million over the required Maintenance-of-Effort (MOE) funding level.

Summary MCPS Budget Recommendations	BOE Request	CE Recommendation	Difference
Total Request (All Funds)	$2,662.0 million	$2,647.5 million	**($14.5 million)**
Change from FY19	*2.5%*	*2.0%*	***(0.5%)***
County Contribution	$1,735.1 million	$1,720.6 million	**($14.5 million)**
Change from FY19	*1.5%*	*0.7%*	***(0.8%)***
Amount over MOE	$17.0 million	$2.5 million	**($14.5 million)**

The Executive's budget notes two issues related to the funding gap compared to the Board's request:

- $1.0 million in the Early Care and Education NDA will be used to support the expansion of MCPS pre-K programs. This would reduce the gap to $13.5 million and would also impact the amount of funding over MOE.
- Additional State Aid from the Kirwin bill could increase overall funding for MCPS. The Council will know whether additional State dollars are available prior to taking its final budget action.

[4] See page 5-18 of the recommended budget, (©34).
[5] The Executive's budget significantly decreases the M-NCPPC requested funding but not the requested FTEs, even though it would be impossible to fund an increase in FTEs with the recommended budget.

MCPS enrollment continues to grow, with projected enrollment for FY20 of 164,477, an increase of 1,183 students or 0.7%. As a result, the County contribution must increase by $9.5 million under the MOE law. Any increase to the County contribution of new dollars above MOE adds to the base calculation for the next year and cannot be reduced in future years (absent a waiver). The most significant cost associated with MOE is not the annual increases tied to enrollment growth, but rather the long-term effects of exceeding it.

Additional recommended support for MCPS totaling $315.5 million comes from the budgets of other departments and agencies. This critical support is outside of the MCPS budget and beyond the County's MOE obligations. It includes: $154.9 million for debt service on school construction bonds; $78.5 million for pre-funding retiree health benefits; $71.3 million for support services (such as School Health Services, Linkages to Learning, School Resource Officers, and crossing guards); and $10.7 million for technology modernization.

Montgomery College

The Executive recommends a budget of $310.4 million for Montgomery College, which is a 1.1% decrease from FY19 and $3.1 million below the College's request of $313.5 million. The decrease compared to FY19 is primarily due to a reduction in tuition and fee revenue. The Executive's recommended County contribution of $144.5 million did not change from the FY19 funding and is the minimum amount required under the College MOE law. The College's requested County contribution is $147.6 million.

M-NCPPC

M-NCPPC's tax supported budget request is $134.7 million. The Executive recommends $129.3 million, including $97.5 million for the Park Fund (excluding debt service) and $31.8 million for the Administration Fund, up 0.8% and 0.6% respectively compared to FY19, but in both cases the Executive's recommendation is well below the agency's request. ($5.4 million or 4%)

County Government Allocations

The changes in the FY20 budget for County Government reflect the priorities of the new County Executive with increases of $63.2 million in tax-supported appropriations and 90 FTEs. No tax-supported functional area has decreased in appropriation of funding from FY19.

FY19 and FY20 (Appropriations and FTEs)				
	FY19		FY20	
FUNCTION	Appropriation (millions$)	FTEs	Appropriation (millions$)	FTEs
Public Safety	590.6	3,996	616.9	4,024
Health and Human Services	240.1	1,237	244.8	1,246
General Government	192.0	1,149	201.5	1,167
Transportation	178.3	1,115	185.1	1,144
Libraries, Culture, and Recreation	81.3	856	82.6	859
Community Development & Housing	13.0	64	14.7	64
Environment	2.8	16	3.1	16
Other governmental (non-departmental)	329.2	4	341.6	6
Total MCG Tax Supported	1,627.2	8,440.0	1,690.4	8,530.0

The recommended budget sets aside $11.4 million for the County's weather-related costs in FY20, including $3.5 million in the Department of Transportation's budget and $7.9 million in the Snow Removal and Storm Cleanup NDA, an increase of $5 million over FY19.

While last year's budget represented a same services budget with few increases, the new County Executive has chosen to make his imprint on his first budget with several new initiatives including a new Innovation Fund NDA ($2 million), Flash bus service on US29 ($1.5 million), a Regional Business Service Hub Program ($786,324), and a County-based Kitchen Incubator/Food Hall ($40,740). In addition, he was able to allocate $7 million in a new Early Care and Education Non-Departmental Account (NDA) to indicate his intent to partner with the Council President in the implementation of her recommended 4-year action plan for an Early Care and Education Initiative.

The budget also recommends increased funding for several existing programs including the following:

- $5 million increase in the Snow Removal and Storm Cleanup to bring contingency funding closer to historical actual funding
- $2.64 million general fund increase for the Housing Initiative Fund
- $2.4 million to begin funding actual overtime in Fire and Rescue
- $2 million in Corrections and Rehabilitation to restore lapse increases, address medical and food expense, and electronic monitoring expenditures
- $1.6 million increase in Health and Human Services to budget for actual IT expenditures
- address the structural deficit in the mandated Community First Choice: Nurse
- $1.8 million increase in DTS - $0.8 million in compensation adjustments, and $1.0 million in program expansions
- $1 million increase in Services to End and Prevent Homelessness
- $0.8 million to address overtime and lapse issues in facility management and fleet services
- $0.8 million increase for the Device Client Management (DCM) NDA, restoring computer replacement cycles.

IV. COMPENSATION: EMPLOYEE PAY INCREASES

This section provides an overview of recommended FY20 pay increases. On April 23, the Council will receive a more detailed presentation of compensation costs including both pay and benefits. In addition, on April 23, staff will present an analysis of the on-going sustainability of recommended compensation cost increases.

a. County Government

This year, the Executive negotiated new one-year agreements with each of the three bargaining units representing County Government employees. The table below shows the FY20 general wage adjustments and service increments recommended by the County Executive. This Fall, the Executive will enter into new negotiations for contracts covering FY21 (and possibly future years) pay increases.

Executive Recommended FY20 County Government General Wage Adjustments and Service Increments				
Employee Group	**General Wage Adjustment**	**Service Increment**	**Past Year Service Increment**	**Maximum Cumulative**
MCGEO	2. 4%	3.5%	3.5% (from FY11)	9.4%
FOP	None	3.5%	3.5% (from FY12, FY13)	7.0%
IAFF	2.4%	3.5%	None	5.9%
Non-Represented	2.0%	3.5%	None	5.5%

The Executive recommends other pay adjustments, including:

- New Longevity Adjustments: The agreement with MCGEO includes a new longevity increment of 2.5% at 24 years of service for Correctional Officers and Deputy Sheriffs (in addition to the existing adjustment of 3.5% at 20 years of service). The agreement with the FOP includes a new longevity increment of 3.5% at 16 years of service for Police Officers (in addition to the existing adjustment of 3.5% at 20 years of service).
- Lump Sum Payments: The agreement with MCGEO includes a one-time lump sum payment of \$1,200 for employees (including those at top of grade) who are not eligible for a service increment in FY20. The agreement with the FOP includes a one-time lump sum payment of \$1,000 for employees who do not receive a previous year service increment or additional longevity increase in FY20.
- Performance-Based Pay: Employees in the Management Leadership Service are eligible for a general wage adjustment of 2.0% and a performance-based pay increase in lieu of service increments.
- Miscellaneous Pay Adjustments: The negotiated agreements include various miscellaneous pay adjustments including increases in Fire Marshal stand-by pay, Advanced Life Support Provider salary differential and transit subsidies.

The following table shows that the pay adjustments recommended by the Executive will have a combined FY20 cost of \$32.7 million (\$24.6 million tax supported). These estimates include the salary and wage costs as well as employee benefit costs borne by the employer. However, as many of the pay adjustments take effect several months into the fiscal year, the amount budgeted for FY20 does not reflect the full annualized cost (that is, the 12-month cost) of the Executive's recommendations. The annualized cost of the FY20 pay adjustments is $41.5 million ($31.0 million tax supported). The annualized cost of the pay adjustments exceeds the FY20 cost by almost $8.8 million ($6.4 million tax supported). These costs will become part of the FY21 budget base.

Estimated Cost of Executive Recommended FY 20 Pay Adjustments ($ millions)				
	Total Cost		Tax Supported Cost	
	FY20	Annualized	FY20	Annualized
General Wage Adjustments	$12.8	$17.5	$9.8	$13.3
Service Increments	$7.6	$14.1	$6.0	$11.2
Past Year Service Increments	$2.4	$4.0	$2.0	$3.1
Other	$8.1	$5.8	$6.8	$5.0
TOTALS	**$31.0**	**$41.5**	**$24.6**	**$32.7**

b. MCPS

Last year, the Board of Education negotiated new two-year agreements with its employee bargaining units. The general wage adjustments and service increments shown in the table below reflect the second-year pay increases in those agreements. This Fall, MCPS will enter into new negotiations with its employee bargaining units for contracts covering FY21 (and possibly future years) pay increases.

FY20 MCPS General Wage Adjustments and Service Increments			
Employee Group	**General Wage Adjustment**	**Service Increment**	**Maximum Cumulative**
MCEA	1.0%	Ranges from 1.5% to 5.5% (average of 3.5% for eligible employees)	4.5% (average)
SEIU			
MCAAP / MCBOA			

c. Other Agencies

Montgomery College, M-NCPPC, and WSSC are each in the process of contract negotiations with their employee organizations. The operating budget requests for each agency include a placeholder for compensation increases:

- The FY20 Montgomery College budget request includes $5.3 million for pay adjustments.
- The Montgomery County portion of M-NCPPC's FY20 budget request includes $2.1 million for employee pay increases as well as an additional $0.5 million for possible employee reclassifications.
- The FY20 WSSC budget request includes $5.2 million for employee pay increases.

V. CHANGES IN WORKFORCE

Total net FTE changes in FY20 are up 497.7 (1.5%) from FY19, with close to an 80% of the increase due to the MCPS workforce. Tax supported FTE increases include: MCPS (+395.5), County Government (+90.3), M-NCPPC[6] (+18.65), and Montgomery College (-6.75). Non-tax supported FTEs for MCPS is up by 19.35 and a decrease for the other three agencies (County Government down by 5.48, Montgomery College down by 8.0 and M-NCPPC down by 4.9).

TAX SUPPORTED FTEs BY AGENCY – FY18-FY20 RECOMMENDED					
	FY18	***Chg.***	**FY19**	***Chg.***	**FY20 Rec.**
Total Four Agencies					
Tax Supported	**32,192.10**	***236.06***	**32,428.16**	***497.70***	**32,925.86**
Non Tax Supported	**3,326.10**	***13.77***	**3,339.87**	***(0.03)***	**3,339.84**
County Government					
Tax Supported	8,384.47	*56.13*	8,440.60	*90.30*	8,530.90
Non Tax Supported	1,851.16	*8.75*	1,859.91	*(5.48)*	1,854.43
MCPS					
Tax Supported	21,090.64	*163.71*	21,254.35	*395.50*	2,1649.85
Non Tax Supported	1,193.69	*4.22*	1,197.91	*19.35*	1,217.26
Montgomery College					
Tax Supported	1,802.10	*8.00*	1,810.10	*(6.75)*	1,803.35
Non Tax Supported	115.50		115.50	*(8.00)*	107.50
M-NCPPC (Montgomery)					
Tax Supported	914.89	*8.22*	923.11	*18.65*	941.76
Non Tax Supported	165.75	*(0.20)*	165.55	*(4.90)*	160.65

During the **15 years** from FY05 to FY19, the County's population has grown by 14%, the number of households has increased by 10%, and K-12 enrollment increased by 17%. Understandably, this growth has created additional demand for services, and has resulted in growth in the size of the tax supported workforce. From FY05 through FY15, total tax supported FTEs across all agencies increased by 15%. During that period, workforce growth varied by agency: Montgomery College's workforce increased by 21%; County Government by 17%; MCPS by 15%; and M-NCPPC by less than 1%.

Changes in Demographics and FTEs – FY05-FY19			
	FY05	**FY19**	**% Change**
Population	948,000	1,078,700	13.8%
Households	350,000	383,600	9.6%
K-12 Enrollment	139,300	163,100	17.1%
FTEs	31,116	35,768	15.0%
College	1,591	1,926	21.0%
MCPS	19,601	22,452	14.5%
MCG	8,837	10,301	16.6%
M-NCPPC	1,087	1,090	0.3%

[6] See footnote 5.

While the growth in the tax-supported Montgomery County Government workforce is not large at 90.3 FTEs (1.1%), it is significant if the goal of the Executive is to decrease the size of the workforce. Notable changes include the following: Transit Services (+26.5 FTEs), Fire and Rescue (+20 FTEs), Health and Human Services (+12.23 FTEs), Police (+7.31 FTEs), Community Engagement Cluster (+6.0 FTEs), Fleet Management Services (+6.0 FTEs), and Liquor Control (-14.5 FTEs).

Workforce size at MCPS and Montgomery College has generally tracked their enrollment trends – steady enrollment increases and workforce growth at MCPS, in contrast to the College's uneven pattern of large enrollment and workforce growth in the aftermath of the Great Recession, followed by a period of declining enrollment. For FY20, MCPS FTEs increase by 415, over double the increase from FY18 to FY19 (167.94). While other agencies grew from 14.5 to 21%, M-NCPPC staffing has not grown in the 15-year period.

VI. RESERVES, PAYGO, AND OPEB

The County allocates substantial resources each year to pay for costs already incurred or set aside resources for known future obligations. The County's rigorous standards for sound financial management are outlined in Resolution No. 16-1415, (See ©45-47) *Reserve and Selected Fiscal Policies* (June 29, 2010), which the Council adopted during the depth of the Great Recession. The Council added specific annual reserve targets in Resolution No. 17-312 (See ©56-59).[7]

a. Reserve

Our difficult experience during the recession confirmed that a large reserve, consisting of unrestricted General Fund reserve and the Revenue Stabilization Fund, is essential to sound financial management. Without it, funds for core County services may not be available when residents need them most. Before the recession our policy called for a 6% reserve. Under current policy, the target rises until it reaches 10% for FY20 and after.

This budget revises the FY19 target to 9.7% or $507.2 million up from the 9.4% target when the 2019 budget was adopted (page 5-19). The County Executive recommends reserves at the policy level for FY20, including $361.0 million in the Revenue Stabilization Fund and $172.2 million in unrestricted General Fund reserve.[8] In the current fiscal plan, the FY20 target (10%) is $533.2 million—this is $213 million more than would have been required under the previous 6% reserve policy.

The County's reserve policy is essential to maintaining the County's AAA bond rating. For more than four decades, Councils and Executives have given top priority to maintaining the AAA bond rating, even in the face of extreme fiscal pressures. A memorandum detailing the history and rationale for the reserve policy is (attached at 36-65).

[7] The resolution also called for the annual adoption of a fiscal plan that is balanced in each year of the six-year period. The Council approved the first such plan in June 2010 and has done so each June since then. See Resolution 17-312: https://www.montgomerycountymd.gov/council/resources/files/res/2011/20111129_17-312.pdf

[8] As an additional reserve starting in FY12, there is a Snow and Storm Cleanup Non-Departmental Account to supplement the amounts budgeted for the Departments of Transportation and General Services. The Executive recommends $7.9 million, an increase of $5 million over the approved budget for the NDA in FY19.

b. PAYGO

Resolution No. 17-312 also states: "The County should allocate to the CIP each year as PAYGO [cash] at least 10% of the amount of general obligation bonds planned for issue that year." PAYGO was $33.0 million in FY19, and following the Council's actions to reduce general obligation borrowing, **FY20 PAYGO is $32.0 million.**[9]

c. Pre-funding OPEB (Other Post-Employment Benefits)

While many jurisdictions have made little progress towards pre-funding retiree health benefits, the County began fully funding its actuarially determined contribution in FY15. **The Executive's recommended FY20 budget includes $121.1 million in tax supported OPEB pre-funding, fully meeting the actuarily determined contribution.**

The Executive has recommended an FY19 savings plan to reduce approved OPEB pre-funding for County Government, MCPS, and Montgomery College by a combined $89.6 million (see © 31-32). A similar (but smaller in terms of total dollars) savings plan was approved in FY18. The Executive's recommendation does not impact the approved PAYGO funding for any agency and current retirees would see no change to their retiree health benefits.

In addition to the recommended pre-funding, the agency requests also include full funding of $83.9 million for PAYGO costs. **Overall, retiree health costs account for approximately 4% of all tax supported spending across the agencies.**

Tax Supported FY19-20 Retiree Health Funding (all agencies, $'s in millions)				
	FY19			
All agencies	Approved	CE Savings Plan	Difference	FY20 CE Recommended
PAYGO funding	$83.2	$83.2	--	$83.9
Pre-funding	$128.8	$39.2	($89.6)	$121.4
Total	**$212.0**	**$122.4**	**($89.6)**	**$205.3**

d. Debt Service

Debt service represents 8.5% of the FY20 tax supported budget, $430.5 million — far more than the total funding for Montgomery College, M-NCPPC, or any department of County Government. Debt service is projected to rise steadily to $485.9 million by FY25.

The debt service budget and its current trajectory reflect decisions already made. The County's capital improvements program (CIP) has been much more robust than that of most other jurisdictions. While other counties rarely provide more local funding than is needed to match their State school construction aid, the County is funds significant portions of school and road construction projects. The County also has a significant program to add, replace, or renovate fire stations, police stations, libraries, recreation centers, parks, bridges, hiker-biker trails, and public amenities.

As the size of the County's CIP has grown, operating budget expenditures for debt service and other spending related to capital projects has grown as well. This spending places pressure on the

[9] The cost of this fiscal policy is driven by the amount of GO debt to be issued. Assuming that GO debt issued in FY20 is $320 million (down from $330 million), then PAYGO will be $32 million (rather than $33 million).

County's ability to provide services in the operating budget. Beginning with the FY19-FY24 CIP, the Council decided to address this increasing pressure by slowly ratcheting back the size of the debt-funded CIP.

VII. COUNCIL'S ROLE AND NEXT STEPS

The Council's five public hearings on the budget will be held on April 8-10. Committee worksessions are scheduled to start on April 11; Council worksessions will start on May 6. Revenue day and reconciliation day are tentatively scheduled for May 15 and 16. Our budget tracking system, which records all Committee and Council actions, will prepare regular updates through May 23, the date for final budget approval.

As the County's final budget authority under the Charter, the Council has historically viewed the budget recommended by the Executive as a strong starting point and re-shaped it with its own initiatives. Each year the Council also makes extensive changes in the budgets, to reflect its priorities and initiatives. The Council's annual Reconciliation List has historically provided more support than the recommended budget proposes in certain key areas such as education and health and human services. Examples of significant changes made by the Council include the following: Examples of significant changes made by the Council include: ensuring continued Fire and Rescue funding for Hyattstown, Germantown, Hillandale, and Burtonsville, funding Parks at a level needed to avoid reduction in service and maintain new and expanded parks, providing an inflationary adjustment for non-profit contracts, expanding half day Pre-K, expanding Head Start, supporting additional Police Department staffing, and contributions to the Public Election Fund. In FY17 the Council changed both compensation and tax rates to enable a reduction in MCPS class size and address the achievement gap. The Committees' review of the budget is likely to identify meaningful changes for FY20.

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OFFICE OF THE COUNTY EXECUTIVE
ROCKVILLE, MARYLAND 20850

Marc Elrich
County Executive

MEMORANDUM

March 15, 2019

TO: Nancy Navarro, President, Montgomery County Council

FROM: Marc Elrich, County Executive

SUBJECT: FY20 Recommended Operating Budget and Public Services Program FY20-FY25

I am pleased to submit to you my Fiscal Year 2020 Operating Budget, my first recommended budget. The total FY20 budget request is $5.723 billion in all funds, with a 2.3 percent increase in tax-supported dollars.

FY20 Recommended Budget by Agency

Agency	Total Budget	Tax Supported
Montgomery County Government	$2,043,314,959	$1,571,753,169
Montgomery County Public Schools	2,647,536,627	2,483,699,617
Montgomery College	310,382,217	262,402,381
M-NCPPC (including Debt Service)	155,471,285	133,723,257
Retiree Health Insurance	127,026,286	121,417,116
Debt Service (MCG)	439,224,240	423,238,640
TOTAL	5,722,955,614	4,996,234,180

OVERVIEW

This budget is a progressive and prudent plan reflecting the values of Montgomery County. This budget also begins to deliver on the promises I made to our residents during the campaign.

To that end, I am proposing a down payment on expanding access to quality early childhood education so that

Montgomery County's young children have a future of opportunity regardless of their family's economic circumstances. I am increasing our investment in a strong, multimodal transportation system that can serve as the backbone of a growing economy. I am focusing our economic development programs on the small businesses of our County to foster long-lasting wealth for our community. Finally, I am proposing several budget modifications to correct several long-term structural deficiencies while simultaneously satisfying the County's longstanding goal to provide 10 percent of total adjusted governmental revenues in reserve. Balancing these competing priorities was not an easy task.

The last decade has been an extremely challenging period for governments across the country - and particularly in the National Capital region. During this time, Montgomery County has been buffeted by the 2008 global economic meltdown and the painful 2013 regional recession, the ripple effects of which are still felt. Solid economic growth is in a dance with lingering uncertainty. The new federal tax law has introduced more uncertainty and volatility in revenue forecasting for all governments. Repeated needless shutdowns of the federal government, including one of historic length just weeks ago, hurt families and businesses across our region. Trade disputes with countries across the globe and inhumane federal immigration enforcement policies at home have derailed and delayed important financial decisions in our community. Finally, the Supreme Court's Wynne decision has permanently reduced income tax revenues by an estimated $30.0 million annually.

As a result of these trends, within days of taking office, I was presented with the troubling news that the final closeout of Fiscal Year 2018 had turned up an unexpected gap of $44 million due to an underperformance of revenues and higher spending than budgeted in Transit and Fire and Rescue Services (FRS). FY18 revenue growth unexpectedly slowed to an anemic 0.3 percent or $14.5 million over FY17 actuals. Income tax revenue estimates flatlined due to the massive changes to Federal tax law. Property tax receipts underperformed due to unanticipated reductions in commercial property valuations. Finally, transfer and recordation taxes fell as the square footage of new construction dropped. Unexpected increases in motor fuel prices and vehicle maintenance costs lead to higher than anticipated spending in operating expenses for FRS and Transit, while increased overtime utilization drove higher spending for personnel expenses particularly in FRS.

Unfortunately, the volatility of the income tax has continued into FY19 and FY20. Estimated quarterly payments were down by more than 30 percent in the final quarter of Calendar Year 2018. This necessitated a downward revision of income tax estimates of $85 million across the two fiscal years. This decline is in line with recent downward revisions in State income tax receipts made by the Maryland Board of Revenue Estimates. The combination of steady job growth with declining quarterly payments suggests volatility in the highest income brackets caused by fluctuations in capital gains. I am hopeful our revenues will regain equilibrium as our residents get through the first tax year cycle with the new Federal tax code.

To address the gap in the current fiscal year, the County Council and I worked together to enact a $45.7 million savings plan in January. Unfortunately, the decline in revenue estimates requires additional action. Therefore, I am proposing we forgo our contribution to the OPEB Trust Fund for FY19. Instead, I am directing these funds into our reserve accounts to satisfy our longstanding fiscal policy goal of holding 10 percent of adjusted governmental revenues in reserve as protection from additional economic shocks. Quite frankly, we do not have the revenues available at this time to satisfy both our OPEB funding policy and our reserves funding policy without making substantial reductions in current services. I will not layoff or furlough current employees to pay for their future retirement healthcare benefits.

The decision to delay OPEB funding for a year is, I believe, the most prudent course of action with just months left in the fiscal year. It is important to note that this action does not alter our commitment to current or future retirees. Their healthcare benefits are fully funded in this budget. However, this action will allow us to closeout our FY19 budget with 9.7 percent in reserve. It also allows me to propose an FY20 budget that funds services, provides a fair compensation increase for our dedicated County employees as fully bargained with their representatives, adheres to our adopted fiscal policies, and addresses some of the structural budget problems which have plagued County government over the last few years.

I intend to put County government on a more sustainable path, and this budget begins that process. I have already directed my senior management team to develop a 10-year financial plan that is grounded in reality and sustainability. As I learned from my own formative years as a manager with a once-iconic department store chain, organizations that do not plan adequately for the future do not have a future. I envision a plan that details the challenges our community faces and presents affordable ways to address them. This budget provides funding to correct several long-term deficiencies. The budget provides new resources to a variety of departments from FRS and Corrections to Health and Human Services to address budget conditions that drive expensive overtime expenditures and to fix chronic underfunding of programs where appropriations have not kept pace with demands for services. The budget recognizes that computer systems and data storage needs must be adequately funded, or else other programs are cannibalized to pay the bills and snow removal must be accounted for properly. Almost all new programmatic funding in the budget is offset by an equal amount of reductions. Most other new funding in the budget for County government is to cover expenses related to fixed costs and legal obligations ranging from debt service and risk management to employee contracts and healthcare.

In fulfillment of recently concluded labor negotiations, I am including funding for compensation adjustments for the County's workforce. These increases include general wage adjustments of 2.4 percent for employees in the Municipal and County Government Employees Organization (MCGEO) and International Association of Fire Fighters (IAFF) bargaining units (effective November 2019), and 2 percent for non-represented employees (effective July 1, 2019). There is also funding for service increments and longevity steps for eligible employees, as well as performance-based increases for employees in Management Leadership Services and Police Leadership Services. I have also included funding for a deferred service increment for eligible employees in the FOP and MCGEO bargaining units.

THRIVING YOUTH AND FAMILIES

As I indicated during my inaugural address, one of the primary goals of my Administration will be to significantly expand early childhood education. As a former teacher, I know firsthand that the biggest barriers to student success are poverty and economic inequality. Evidence shows that an upfront investment in early childhood education yields large dividends in the future - for both children and society.

My Administration's FY20 recommended budget includes $7 million for an Early Care and Education Initiative, a joint effort of the County Government, Montgomery County Public Schools, and Montgomery College to ensure that the achievement gap gets closed. We will increase the number of seats in school-based classroom and family- and center-based child care settings, improve access to child care, expand training and professional development opportunities for the childcare workforce, and establish a workgroup to resolve barriers to quality childcare in the County.

Closing the achievement gap is not only accomplished in those critical early years, but also during a child's school-age years. In addition to the Early Care and Education Initiative, my FY20 recommended budget includes a total of $2.6 billion for the Montgomery County Public School System (MCPS) - a 2.0 percent increase over FY19 approved. Our County contribution to MCPS increases by $12.0 million and is $2.5 million above the State's Maintenance of Effort level. In addition, MCPS will receive $1 million from the new Early Care and Education Fund. This amount, when combined with an increase in State education funding means that the MCPS budget will increase by $51.1 million in FY20. Despite difficult fiscal conditions, it is imperative that we continue to make investments in K-12 education, including new initiatives to reduce elementary school class sizes and improve programming for special education students and English Language Learners. I remain hopeful that the General Assembly will increase State aid beyond current levels. If current fiscal estimates hold true, this new, higher level of State Funding would provide MCPS resources beyond their requested FY20 budget.

Our children and families also need access to top-notch library and recreational facilities in order to thrive. That's why my FY20 recommended budget includes over $800,000 to ensure that the Wheaton Library and Recreation Center opens on-time and adequate staffing in late summer 2019.

During my time on the County Council and as County Executive, my appreciation for the County's nonprofit community has deepened, as these organizations provide quality services to our residents. I'm recommending over $9.1 million in grants for individual human services programs through community grants. Among other things, services offered by these organizations help address poverty, provide emergency services, serve disconnected youth in our community, bolster services for seniors and those with disabilities, and help ensure that our immigrant neighbors can access services to become thriving members of our community and defend themselves against unwarranted deportation. The FY20 recommended budget also preserves funding for the County Council's community grants.

A GROWING ECONOMY

The County's economy is at a crossroads. Many of our communities are facing challenges beyond our control, like an aging population, shrinking Federal budgets, and increased poverty. But we are also presented with opportunities to foster continuous economic growth in the County by focusing efforts on starting and expanding local businesses. I believe successful modern economies are built on a foundation of vibrant entrepreneurship, efficient infrastructure, a world-class workforce, and sensible regulations to promote and protect growth opportunities for all. Good neighborhoods, strong schools, and a good quality of life are the result of a healthy economy and the hallmark of Montgomery County for the last 75 years.

My first recommended budget begins paving the way to support opportunities that will create, retain, and attract good jobs by helping businesses grow in our County. My FY20 budget recommendations include the creation of a Regional Business Service Hub Program that will proactively interact and reach out to local businesses and entrepreneurs for assistance needed to grow and expand jobs. We will start developing a County-based Kitchen Incubator/Food Hall to help entrepreneurs translate their great ideas into successful products and to train a workforce to for the County's vibrant food and hospitality industry. Locating the small business solutions teams in our Regional Service Centers allows for additional boots on the ground and more direct in-person access to residents and business Countywide.

While local redevelopment efforts provide greater economic opportunities for our communities, many local businesses are facing difficult challenges thriving during the construction phase. My FY20 recommended budget will add funds to continue providing technical and financial support through the Small Business Assistance Program and the Impact Assistance Fund to eligible small businesses adversely impacted by County-led redevelopment projects. Funding for the Microlending Program will allow continued financial and technical assistance to County entrepreneurs. I will also continue supporting the MOVE Program to attract new businesses and expand local ones to reduce the County's vacant office space.

For growing an innovative economy in the 21st century, Montgomery County has a competitive advantage over other areas because of our proximity to major Federal research and development organizations, including the National Institute of Health (NIH), Federal Drug Administration (FDA), the National Institute of Standards and Technology (NIST), and many others. Over the past decade, we have witnessed the steady growth of key strategic industries like biotech, life sciences, cybersecurity, and health tech in the County.

My budget recommendations continue needed funding to expand the County's bioscience and high-tech industries at all talent levels. The budget retools the County's business incubator system to better serve start-ups and early-stage technology companies with technical mentorship and capital access opportunities. It provides County matching funds to local recipients of Federal Small Business Innovation Research and Small Business Technology Transfer (SBIR/STTR) grants from the NIH, and it continues the UltraMontgomery Initiative to provide a high-speed fiber network that connect people with opportunities and drives economic growth by linking our business, academic and Federal institutions, and transit-oriented smart-growth communities.

County's funding support for two economic development and workforce organizations will continue in FY20. The Montgomery County Economic Development Corporation (MCEDC) will continue leading the County's efforts in growing and diversifying the local economy through marketing, business attraction and retention, and cultivating a local ecosystem of entrepreneurship and innovation. Through collaborative partnerships among public institutions, and our nonprofit and business partners, the County will prepare our students with needed skills and job experience, while also providing unemployed and underemployed residents with in-demand job-ready skills.

A GREENER COUNTY

Montgomery County must be a leader on environmental issues. My Administration recognizes the urgency of global warming and will take concrete steps to address climate change by exploring creative and common-sense ways to address greenhouse gas emissions at the local level - through clean energy, energy efficiency, enhanced building design, reduction of waste, and better transit options that get cars off our roads. My Administration's FY20 recommended budget begins to accomplish these goals by funding a number of targeted initiatives to help move our environmental objectives forward.

I believe climate change is the defining environmental issue of our time and my Administration is committed to reducing the County's greenhouse gas emissions and impact on climate. Transportation is one of the largest greenhouse gas emissions contributors and my FY20 recommended budget aims to mitigate this impact by including $1.5 million for the new limited stop FLASH service on US 29 to bolster public transportation options. In addition, the Department of Transportation will purchase ten electric Ride On buses in FY20 and continue its efforts to convert street lights to more energy efficient Light Emitting Diode (LED) fixtures through the capital budget. My recommended budget continues support for the Department of General Services program to install solar and other clean energy technologies on County facilities. To date, the program has produced enough clean energy to power more than 800 homes.

EASIER COMMUTES

Congestion continues to be a significant issue for County residents. My Administration's FY20 recommended budget includes funds to continue implementation of a new limited stop, high frequency FLASH bus service on US 29 between the Burtonsville Park-and-Ride Lot and the Silver Spring Transit Center. The new service will open in May 2020. The line will include 18 new state-of-the art stations and a fleet of sixteen 60-foot articulated buses. The FLASH will improve mobility and transit reliability on the corridor with 7.5-minute headways in the morning and afternoon peak periods and 15 minutes at other times. It supports my commitment to improve transit equity in a corridor where 65 percent of residents are minorities, 31 percent speak a language other than English at home, 30 percent of households earn less than half of the area median income, and 12 percent of households have no car. This service will improve travel times along the corridor and provide a higher level of service, but I am also interested in doing more to develop Bus Rapid Transit (BRT) on US 29. A study, expected to be concluded in 2019, is underway to identify modifications that can be made to US 29 between Tech Road and Downtown Silver Spring to enhance the performance of the FLASH bus system and the overall corridor. The study is exploring options to minimize traffic bottlenecks, reduce travel time, improve safety, expand walking access to the FLASH stations, and improve travel time reliability.

Work on other critical transit projects continue as well. This summer a Recommended Alternative will be selected for this BRT on the MD355 corridor. My budget includes funding for environmental studies necessary to move this project forward. After many discussions with State officials, the Maryland Department of Transportation has agreed to reengage on the Corridor Cities Transitway and our County's Department of Transportation is looking at adding additional road capacity (for cars and transit) to upper parts of MD355. In total these improvements will address some of the major bottleneck in Upcounty.

In addition, my FY20 budget continues investment in other critical transportation infrastructure, committing over $30 million to road resurfacing programs and $14 million to bridge maintenance and construction. It is my intention to propose additional funding for street paving should extra dollars remain in our FY19 set asides. Out of an abundance of caution, I have not programmed these Funds until after the winter weather has passed.

A MORE AFFORDABLE AND WELCOMING COUNTY

We have a moral obligation to create a more economically and socially just society. To do so means that we must focus on providing access to safe and affordable housing for our residents.

Within weeks of taking office my Administration launched a housing code enforcement campaign to protect tenant rights and address troubled properties. Rigorous inspections of rental units are critical to safe, affordable housing. To address this issue, my FY20 recommended budget for the Department of Housing and Community Affairs includes over $500,000 in budget enhancements to bolster inspections and tenant rights - including $218,000 in additional funding for the Renter's Alliance to provide information and services to tenants, $144,450 to fund two vacant housing code inspector positions, $102,647 for tenant advocacy services, $100,000 to enhance the Housing Code Inspections Delivery System, and $74,365 for tenant-landlord outreach and educational activities. In addition, a Deputy Director position is being created to focus on preservation and the creation of more affordable housing. To help offset the costs for these enhancements, we are proposing a small ($3.00) increase to rental license fees.

In addition to working for tenant rights as part of an affordable and welcoming community, my Administration continues to support efforts to expand affordable housing and we continue to strive to end chronic homelessness in the County. In FY20, I am recommending a $41.3 million budget for the Montgomery Housing Initiative Fund (HIF), a 16 percent increase ($5.7 million) from the FY19 approved budget. Part of this increase is an additional $2.6 million transfer from the General Fund to HIF. Furthermore, $4.8 million in loan repayments have been added in FY19 and $17 million in funding is planned for FY20 for the Affordable Housing Acquisition and Preservation CIP Project.

I am also recommending funding for the creation of a Senior Home Sharing Pilot Program. This innovative program will connect senior home providers who have a spare room with home seekers interested in a long-term housing option. This home sharing arrangement can work when renters find it difficult to find affordable rental housing and home providers either need extra income or prefer living with another person who can offer social connection and/or assist with tasks, errands, and costs related to property maintenance.

Thanks to prior efforts of the Council, Montgomery County was one of the first jurisdictions in the Country to reach functional zero for veteran homelessness. We've been able to sustain this status due to the County's ongoing commitment to ending homelessness. The County is now aiming to end chronic homelessness in our community. To that end, I am recommending an additional $1 million in the Services to End and Prevent Homelessness budget to help us continue on this path to reach functional zero chronic homelessness in Montgomery County.

SAFE NEIGHBORHOODS

One of my highest priorities while in office is to ensure every neighborhood in the County is a safe neighborhood, not just safe from crime but safe for pedestrians to walk and move about. I am paying close attention to pedestrian safety by overseeing Vision Zero implementation and the County's plans for short- and long-term improvements for the busiest County-maintained roads. Areas with traffic calming improvements like these have seen significant declines in pedestrian collisions.

To ensure those who break the law are held accountable for their actions, I recommend adding funds for the Gang Unit of the State's Attorney's Office and for a new forensic scientist in the Crime Lab to ensure DNA and other evidence is analyzed in a timely manner.

To ensure the public trust, I also recommend adding funds to purchase 250 new dashboard cameras for our Police patrol cars and adding a position to process public information requests for footage created by those cameras and the Police

Department's body-worn camera program. My budget additionally funds the full annual contract for Next Generation 911 service, which will expand the ways people can seek assistance from just a phone call to text and video.

My Administration is building a sustainable and realistic budget. Towards that goal, I am adding twenty positions in FRS to begin closing the structural budget deficiency identified in our analysis of the Net Annual Work Hours. I am also increasing the overtime budget to address actual wages that in previous years had not been used in calculating overtime, leading to an underestimate of what overtime would actually cost. I am also adding overtime to address failures to respond during the periods in the morning and evening when our career personnel are being replaced by our community's volunteers, who cannot always match the career shift hours when transitioning from the work that supports their families to the unpaid work that supports our community.

EFFECTIVE, SUSTAINABLE GOVERNMENT

As County Executive, it is my goal to make County government work better for its residents. This means that government must operate more cost effectively and ensure that the programs it implements are back by evidence of success. It also means that we must implement a budget process that is more transparent and one where public input in the process is encouraged.

In order to get to a more effective and sustainable government; however, we must true up our budget to reflect where actual expenditures occur. To this end, my FY20 recommended budget resolves several long-standing budget deficiencies in several departments. Without resolving these issues, these Departments must either spend beyond their approved budget level or use funding intended for other programs to pay for those obligations. Due to fiscal constraints, we were not able to fully resolve all of these structural issues; however, I am recommending a total of $12 million in increases to address many of them as described below:

- Snow Removal and Storm Cleanup NDA: $5 million to bring our contingency funding closer to historical actual expenditures;
- Fire and Rescue Service: $2.4 million to begin to fund actual overtime wage rates;
- Correction and Rehabilitation: $2.0 million to restore lapse increases, address medical and food expenses, and electronic monitoring expenditures;
- Health and Human Services: $1.6 million to budget for actual IT expenditures; address the structural deficit in the mandated Community First Choice: Nurse
- Monitoring Program; align the budget for translation services to reflect actual demand;
- General Services and Fleet: $836,391 to address overtime and lapse issues in facilities management and fleet services; and
- County Attorney's Office and Sheriff's Office: $174,329 to address structural budget deficiencies in these offices.

Over the coming months, I look forward to working with Council in implementing a number of changes to the way that County government operates. My Administration will align budgets and our budget decision-making process to our Key Priority Outcomes. Similar to the Capital Improvements Program, the development of the County's operating budget and Public Services Program should occur on a two-year basis. It is my intent that the FY20 budget will be the final one-year operating budget for the County. Moving to a two-year budget cycle will provide more stability for our County departments, agencies, and nonprofit partners; and it will provide us with time to evaluate the effectiveness of programs to ensure that limited tax dollars are being spent in the most efficient way possible.

While my recommended budget ensures that the County meets its policy of holding 10 percent of adjusted governmental revenues in reserve, we intend to reevaluate our reserve policy and move us toward a risk-based reserve policy. In addition, we will be examining the way we estimate our revenues to implement an approach to which mitigates revenue volatility.

Finally, I have left $10 million set aside for the County Council to allocate for the budget reconciliation process. I tried to address our shared priorities within this constrained budget, but I know there's more to be done and I know other issues will arise. Therefore, I wanted to make sure the Council had resources to address those needs during the appropriations process.

As promised, my budget includes no tax increases. In fact, the property tax rate is decreased slightly to stay within the Charter Limit. However, some property owners will see an increase in their property tax bill due to increased property assessments. The property tax for each owner-occupied residence will include a credit of $692 to limit the burden on homeowners and to maintain a progressive property tax structure in the County.

In order to encourage the implementation of creative ways to strengthen both program performance and customer service for County residents, we have established a new Innovation Fund as a non-departmental account. This fund will be a revolving loan fund internal to County government that will be administered by the Office of Performance and Innovation (formerly CountyStat) and will complement the County's new Lean business process improvement initiative. Loans will be made from the fund on a rolling basis to projects with strong potential to improve customer service and performance results while at the same time reducing costs or generating new County revenue within three to five years. There will be a rigorous application process, and the review committee will be comprised of Administration and Council representative, and members of the community who will make recommendations to the Chief Administrative Officer.

While I am recommending no change to the Water Quality Protection Charge in FY20, I am recommending small increases in the solid waste charges for County residents. These rates have not changed for several years, despite rising costs; the increases are needed to finally address those costs and cover growing operational needs.

In addition, I recommend you approve the FY20 operating budget for the Washington Suburban Sanitary Commission (WSSC) as proposed by the Commission, including the 5 percent increase to the water and sewer rates paid by WSSC ratepayers.

Given the volatility of the capital gains taxes, we cannot simply assume one year's tax revenue forecasts will form an accurate basis for the following year. This year we will begin work in earnest on lean business processes, procurement reform, working toward optimal efficiency, and making sure we get the best value for the dollars we spend.

In conclusion, I look forward to working with you, your Council colleagues, and your outstanding staff in passing this budget. The resources of the Executive Branch are at your disposal as you begin the next phase in the budget process.

MONTGOMERY COUNTY PLANNING BOARD
THE MARYLAND-NATIONAL CAPITAL PARK AND PLANNING COMMISSION

January 15, 2019

The Honorable Marc Elrich
Montgomery County Executive
Executive Office Building
101 Monroe Street
Rockville, MD 20850

The Honorable Nancy Navarro
President, Montgomery County Council
Stella B. Werner Council Office Building
100 Maryland Avenue
Rockville, MD 20850

Dear Mr. Elrich and Ms. Navarro:

Pursuant to §18-104 of the Land Use Article of the Annotated Code of Maryland, the Montgomery County Planning Board is pleased to transmit the FY20 Proposed Budget for the operations of the Maryland-National Capital Park and Planning Commission in Montgomery County. This comprehensive document is presented at the budget appropriate departmental and divisional levels, including lists of the programs and services provided by each division.

We have been made aware of the County's fiscal challenges, both in the current year and in FY20. Consequently, we have adopted a savings plan for FY19. However, our budget development and submission calendar did not allow for adequate and timely consideration of the direction provided to the County's internal departments and agencies, and therefore this document is submitted as proposed.

Although we have proposed increases where needed to address critical needs, we fully understand the ongoing economic challenges and will work with the Council and Executive to incorporate adjustments as needed.

On-going Service Provision

The Commission's primary mission remains unchanged: providing clean and safe parks, and delivering a timely, comprehensive development review program, key master plans, and other critical planning programs which drive economic development. It is our goal to continue to give our customers/residents excellent service. We are proud to have been awarded the National Gold Medal Award for excellence in Parks and Recreation Management in 2015. This is the sixth time we have been so recognized by the American Academy for Park and Recreation Administration in partnership with the National Recreation and Park Association. In addition, our Planning efforts were recognized in 2018 with awards from the National Capital Area Chapter of the American Planning Association for the Bethesda Downtown Plan and for our outreach efforts on the Veirs Mill Corridor Plan.

Cognizant of the limited resources available, we will continue to work with the County to reach an appropriate balance with service delivery demands. The FY20 Proposed Budget focuses on maintaining service levels, responding to federal/state/local mandates, and addressing a limited number of critical needs. The FY20 Proposed Budget includes increases related to necessary planning studies, legislative mandates, and operating costs of new parks.

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The FY20 proposed tax-supported operating budget is $145.2 million. This is $7.6 million more than the FY19 adopted budget, a 5.5 percent change, reflecting both critical needs requests and the additional costs of the new Wheaton Headquarters building. The total proposed budget, including Enterprise operations, Property Management, Park Debt Service and Special Revenue funds, is $171.2 million, an increase of $5.2 million or 3.1 percent from the FY19 adopted budget.

Summary of FY20 Proposed Operating Budget Expenditures
(net reserves, ALARF, Internal Service Funds, and Capital Projects Funds)

	FY19 Adopted	FY20 Proposed	$ Change	% Change
Montgomery Funds				
Administration (1)	$ 31,767,007	$ 33,424,912	$ 1,657,905	5.2%
Park (2)	103,860,211	109,701,294	5,841,083	5.6%
ALA Debt	2,024,928	2,088,800	63,872	3.2%
Subtotal Tax Supported	**137,652,146**	**145,215,006**	**7,562,860**	**5.5%**
Enterprise (3)	13,871,959	10,234,402	(3,637,557)	-26.2%
Property Management	1,528,240	1,566,600	38,360	2.5%
Special Revenue	6,519,833	7,084,740	564,907	8.7%
Park Debt	6,461,285	7,124,410	663,125	10.3%
Total Montgomery	**$166,033,463**	**$171,225,158**	**$ 5,191,695**	**3.1%**

(1) Includes transfer to Special Revenue Fund in FY20
(2) Includes transfer to Park Debt Service and Capital Projects
(3) Includes transfer to Capital Projects

Fiscal challenges remain at all levels of government, including the Commission. Although for FY20 there are several positive indicators - assessable base is projected to grow at a rate of about 4.29 percent; the Economic and Revenue Update from the Montgomery County Department of Finance released in December 2018 shows a drop in unemployment from 3.3 percent in October 2017 to 3.1 percent in October 2018, an increase in resident employment, and an estimated 4.4 percent increase in wage and salary income for 2018 – the County experienced a shortfall in anticipated reserves in FY18 that is necessitating a retrenchment of expenditures in FY19, and which will also impact the FY20 budget process.

Costs, however, continue to grow at higher rates than the revenues that support them. National Pollutant Discharge Elimination System (NPDES) and American with Disabilities Act (ADA) mandates and Operating Budget Impacts (OBI) from previously approved CIP projects impact the base budget. Maintenance needs are more expensive to address the longer they are deferred. With property tax revenue making up more than 94 percent of operating revenues, growth, although modest, means the Commission must manage its resources carefully to sustain a stable financial position.

The following table begins with our FY19 adopted budget total and adds each of the elements that make up the proposed General Fund increase, totaling 5.5 percent.

M-NCPPC
Summary of FY20 Proposed Budget Major Changes
Montgomery County General Fund Accounts
Administration and Park Funds (excludes property management and reserves)

	Budget Amount	% Change
FY19 Adopted Budget	**$ 135,627,218**	
FY20 Major Changes- increase (decrease)		
Major Personnel Cost Changes		
OPEB Paygo and prefunding	(320,755)	
Health Insurance	1,844,843	
Pension (ERS)	(2,248,149)	
Employee Compensation Marker	2,105,692	
Reclassification Marker	(102,429)	
Subtotal Major Personnel Changes	**1,279,202**	**0.9%**
Major Non-Personnel Cost Changes		
Debt Service	663,125	
Transfer to Development Review	500,000	
One Time Reductions	(481,000)	
Park- NPDES	77,564	
OBI	1,466,101	
Investment in Critical Needs	2,364,981	
Operating Major Known Commitments	1,629,015	
Subtotal FY20 Major NonPersonnel Changes	**6,219,786**	**4.6%**
Total Dollar Change for Major Changes	**7,498,988**	**5.5%**
TOTAL FY20 Proposed Budget	**$ 143,126,206**	**5.5%**

OVERVIEW OF BUDGET DEVELOPMENT AND ASSUMPTIONS

The Commission is putting forth a budget for FY20 that includes increases for major known commitments and investments in critical needs, and seeks to continue to rebuild service levels.

The Proposed Budget includes the following major known commitments for personnel costs in FY20:

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- Medical insurance and benefit costs;
- Full funding of OPEB PayGo and Pre-Funding as determined by the actuarial study;
- Full funding of pension contribution as determined by the actuarial study; and
- Dollar markers to adjust employee compensation, and possible position reclassification due to a multi-year classification study of the workforce.

In recent years, the Commission has taken a number of pro-active steps to reduce or slow the growth of benefit costs. These have included instituting a new pension plan and adopting a credited service model for retiree medical benefits for new hires; new health related initiatives such as incentives for annual exams and offering a lower cost health plan, while continuing to ask our employees to share more of the cost. These actions continue to free up resources to support our delivery of services.

As shown in the following table, personnel expenses reflect an increase of $1.28 million.

FY20 Proposed Budget
Summary of Changes in Major Personnel Costs
Montgomery County Administration Fund and Park Fund

	FY19 Adopted	FY20 Proposed	$ Change	% Change
OPEB				
OPEB Paygo & Prefunding	$ 8,008,035	$ 7,687,280	$ (320,755)	-4.0%
Pension (ERS)				
Pension (ERS)	10,177,683	7,929,534	(2,248,149)	-22.1%
Health and Benefits(1)				
Employee Health Benefits	12,398,210	14,243,053	1,844,843	14.9%
Subtotal Personnel Costs	**$ 30,583,928**	**$ 29,859,867**	**$ (724,061)**	**-2.4%**
Employee Compensation				
Marker for Changes to Employee Comp.		2,105,692	2,105,692	-
Marker for Possible Reclassifications	603,553	501,124	(102,429)	-17.0%
Total Major Personnel Costs			**$ 1,279,202**	

(1)Health and Benefits includes medical insurances (health, dental, vision, prescription), long-term disability, accidental death and dismemberment, and life insurance.

The compensation marker represents the largest cost increase, followed by the increased cost for health insurance. Health costs are increasing due to increased utilization and cost trends.

The net change for total OPEB costs is a decrease of $321,000, or 4.0 percent. Total OPEB funding is $7.93 million. OPEB is shown in the Non-Departmental accounts in individual funds rather than being allocated to each department.

As determined by the actuary, pension costs will decrease by 22.1 percent in FY20, representing a savings of $2.25 million from the FY19 budget. Health benefit costs are projected to increase by 14.9 percent, resulting in additional cost of $1.84 million over the FY19 Budget.

As for employee compensation, the budget includes a dollar marker of $2.1 million in the General Fund. The Commission will be in the second year of our contract with MCGEO, with a wage and health benefit re-opener scheduled this year, and in full contract negotiations with the FOP for FY20, the results of which will be presented for approval at the Joint County Council Meeting in May 2019. Also included is $500,000 for possible reclassification adjustments based on the multi-year classification study that is under way.

Investing to Meet Critical Equipment, Maintenance, and Essential Service Needs

Included in the funding levels of the Administration Fund and Park Fund is a funding request of approximately $2.4 million to address critical maintenance, equipment, and essential service needs. Each department's budget sections provide detailed information on how this increased investment is proposed to be used. The following is a summary of the requests by department.

Fund	Department	Essential Needs Investment Amount
Administration	Planning	$ 808,400
Administration	Commissioners' Office	24,000
Administration	DHRM	-
Administration	Legal	49,628
Administration	Finance	101,391
Administration	Inspector General	-
Administration	Corporate IT	19,401
Administration	Share of CIO/CWIT Initiatives	120,367
Park	Parks	1,241,794
Total		**$ 2,364,981**

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Summary of FY20 Proposed Budgets for General Fund

The following table provides a comparative summary of the FY20 proposed budget to the FY19 adopted budget for the General Fund. Specific changes in each of the departments are explained in full detail in the Department sections of the Budget Book.

Summary of FY20 Proposed Budget General Fund Accounts
By Fund by Department (excludes reserves)

	FY19 Adopted	FY20 Proposed	$ Change	% Change
Administration Fund				
Commissioners' Office	$ 1,247,346	$ 1,273,938	$ 26,592	2.1%
Planning Department Operating	20,030,266	20,360,503	330,237	1.6%
CAS	8,217,502	8,627,506	410,004	5.0%
Transfer to Development Review	-	500,000	500,000	-
Grants	150,000	150,000	-	0.0%
Non-Departmental (1)	2,121,893	2,512,965	391,072	18.4%
Subtotal Admin Fund	**31,767,007**	**33,424,912**	**1,657,905**	**5.2%**
Park Fund				
Park Department Operating	90,081,579	94,040,953	3,959,374	4.4%
Transfer to Debt Service	6,461,285	7,124,410	663,125	10.3%
Transfer to Capital Projects	350,000	350,000	-	0.0%
Grants	400,000	400,000	-	0.0%
Non-Departmental (1)	6,567,347	7,785,931	1,218,584	18.6%
Subtotal Park Operating	**103,860,211**	**109,701,294**	**5,841,083**	**5.6%**
Montgomery Operating Subtotal	**135,627,218**	**143,126,206**	**7,498,988**	**5.5%**
Property Management	1,528,240	1,566,600	38,360	2.5%
Montgomery General Fund Total	**$ 137,155,458**	**$ 144,692,806**	**$ 7,537,348**	**5.5%**

(1) Non-Departmental for both years include OPEB prefunding and OPEB paygo, and a budget marker for compensation adjustments.

PROGRAM HIGHLIGHTS

We are committed to a FY20 work program that helps achieve our goal of maintaining Montgomery County as one of the nation's best places to live. Below are some highlights of the program budget focus in each of the departments. A more detailed discussion of department budgets is provided in each Department's section of the Budget Book.

Parks Department

The Department of Parks will focus on delivering core services to properly operate, maintain and protect our park system.

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The Commission continues to develop and maintain one of the largest and most diverse park systems in the nation with over 36,800 acres in 421 parks. Montgomery Parks has balanced the dual roles of providing developed parkland for active and passive recreational opportunities that promote healthy, active life styles, and serving as stewards and interpreters of Montgomery County's natural and cultural resources by conserving parkland. From playgrounds and sports fields to park benches and trails, parks offer opportunities for people of all ages to communicate, compete, interact, learn and grow. Proximity to parks has been shown to increase property values.

Montgomery Parks seeks to provide quality recreational and educational opportunities through its operation, construction, development, and maintenance of a wide variety of facilities to meet the varied needs and interests of the County's residents. Montgomery Parks' Vision 2030 plan, prepared together with the County's Department of Recreation, is a comprehensive planning effort to develop long range plans and serves as a guide for future park development and resource protection to better address changing needs and growth forecasts through 2030.

The Department's FY20 budget includes increases for:

- Compensation adjustments;
- Unfunded Operating Budget Obligations, including Operating Budget Impacts from Capital Improvement Projects;
- Known operating commitments;
- Debt service on general obligation park bonds, capital equipment, and Commission-wide information technology initiatives;
- National Pollutant Discharge Elimination System (NPDES) mandates; and
- Wheaton Headquarters operating budget impact.

In addition, the FY20 budget includes funding to address identified deficiencies in our work program as well as emerging trends aimed at meeting the future needs of the department such as:

- Improving the quality and playability of ballfields;
- Improving fleet management;
- Improving data managemet and enterprise systems; and
- Addressing a maintenance backlog to reduce costly system replacements.

Together, we have created a highly popular, valued, and nationally-recognized park system. Our entire team remains committed to honoring our core vision to provide "...an enjoyable, accessible, safe, and green park system that promotes a strong sense of community through shared spaces and experiences and is treasured by the people it serves." We will continue to aggressively seek new funding opportunities and to improve work program efficiencies. We remain committed to forming viable partnerships and strong relationships with our stakeholders and within our communities.

The FY20 budget request will enable us to continue to provide safe, clean parks, keep our programs and facilities accessible and affordable, and maintain the quality of life for which Montgomery County is renowned.

Planning Department

The Planning Department continues to deliver its core services to improve the quality of life in Montgomery County by conserving and enhancing both natural and man-made environments for current and future generations. Central to this role, the Department develops master plans, reviews development applications, and researches, analyzes and presents information to the community and public officials to aid in planning for Montgomery County's future.

In addition to the FY20 work plan that is detailed in the Department's budget section, the following critical needs are proposed:

One-Time projects:

- Pedestrian Master Plan Support
- Rustic Roads Functional Master Plan Update
- General Plan Update Support
- Ten-Year Check-up on the White Flint Sector Plan's Metrorail Station Area
- Architectural Field Surveys
- Archival Assistance
- Data for Vision Zero
- Affordable Housing Preservation and Redevelopment Feasibility
- Preserving Community Value of Ethnically Diverse Retail Centers

On-going projects:

- Project Dox Upgrade
- Comprehensive Park and Planning Placemaking Initiative

Other Initiatives:

- Wheaton Headquarters operating budget impact
- Operating Transfer to the Development Review Special Revenue Fund

Central Administrative Services (CAS)

For FY20, CAS Departments' work priorities will center on continuing to meet the needs of the operating departments. Critical needs are proposed as follows:

- Finance Department:
  - One career position to provide additional accounting resources to the CIP.
  - One career position to augment payroll processing.
- Legal Department: Restoring the previous year's budget for professional services.
- Corporate IT Division: Funding to expand a regular computer replacement schedule.
- Chief Information Officer:
  - One career position to provide IT project management, currently provided by contractors.

- Funding for the following IT initiatives
  - Budget software replacement
  - Intranet upgrade
  - Remediation of security assessment findings
  - Next phase of the Microsoft Active Directory project, which manages permissions and access to email, network storage, and other network resources
  - Feasibility study for Enterprise Content Management, which would allow for access to and the management of the Commission's information, wherever stored.

Commissioners' Office

The role of the Commissioners' Office staff is to support the Chair and Planning Board in the performance of their official duties, serve as the point of contact for meeting related issues, and coordinate prompt responses to issues and inquiries from agencies and the general public. This also includes preparing and web posting the Board's meeting agenda; producing and preserving records of official Board proceedings; and managing correspondence between the Board and other agencies and the public.

In addition to known operating commitments, the FY20 Proposed Budget for the Commissioners' Office includes increased training funds for the Commissioners, and freezes a part-time position in order to fund a full-time administrative position.

Capital Budget

This transmittal also includes the Capital Budget (the second year of the six year Capital Improvements Program (CIP), since the County adopts the CIP every other year). Highlights of this budget can be found within the Department of Parks detail pages.

TAX RATES AND LONG-TERM FISCAL SUSTAINABILITY

Beyond meeting the immediate FY20 challenges, the Commission continues to strive for long-term fiscal sustainability. Property taxes comprise more than 94 percent of operating revenue in the tax-supported funds. The Commission, in proposing this budget, is requesting a change in the property tax rates for both the Administration Fund and the Park Fund. The requested increase in the real property tax rate is 0.19 cent for the Administration Fund and 0.38 cent for the Park Fund. At this level, the total tax rate is still below what it was in FY08.

The FY20 Proposed Budget reflects a total tax rate for property tax supported funds of 7.53 cents real property and 18.83 cents personal property. The breakdown by fund is:

- Administration Fund: 1.75 cents real and 4.38 cents personal, an increase of .19 and .48, respectively;

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- Park Fund: 5.68 cents real and 14.20 cents personal, an increase of .38 and .95, respectively; and
- Advanced Land Acquisition Fund: 0.10 cents real and 0.25 cents personal, unchanged.

At these tax rates, the Commission will have sufficient property tax revenues to meet the proposed expenditures and reserve requirements for the Administration Fund and the Park Fund although both funds will continue to utilize fund balance in FY20.

MONTGOMERY COUNTY PROPERTY TAX RATES (Cents per $100 of assessed value)

FUNDS	ACTUAL FY08	ACTUAL FY09	ACTUAL FY10	ACTUAL FY11	ACTUAL FY12	ACTUAL FY13	ACTUAL FY14	ACTUAL FY15	ACTUAL FY16	ACTUAL FY17	ACTUAL FY18	ADOPTED FY19	PROPOSED FY20
Administration Fund													
Real	1.90	1.90	1.80	1.50	1.70	1.80	1.80	1.70	1.80	1.70	1.72	1.56	1.75
Personal	4.70	4.70	4.50	3.80	4.30	4.50	4.50	4.25	4.50	4.25	4.30	3.90	4.38
Park Fund													
Real	5.80	5.30	5.00	4.50	4.80	5.40	5.30	5.60	5.52	5.48	5.54	5.30	5.68
Personal	14.50	13.20	12.50	11.20	12.00	13.50	13.25	14.00	13.80	13.70	13.85	13.25	14.20
Advance Land Acquisition Fund													
Real	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Personal	0.30	0.30	0.30	0.30	0.30	0.30	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Total Tax Rates (Cents)													
Real	7.80	7.30	6.90	6.10	6.60	7.30	7.20	7.40	7.42	7.28	7.36	6.96	7.53
Personal	19.50	18.20	17.30	15.30	16.60	18.30	18.00	18.50	18.55	18.20	18.40	17.40	18.83

CONCLUSION

The Proposed 2020 Budget is respectfully submitted for your consideration. In this document, we are proposing a budget that not only moves us forward incrementally, but allows us to address several critical needs and planning and parks initiatives. We continue to explore potential collaborative efforts across departments and counties in our effort to provide efficient, effective quality service, while maintaining our fiscal responsibility and commitment to the community we serve.

We continue to strive to find new ways to save taxpayer dollars while providing quality service and achieving progress in our many areas of focus. We look forward to working with you and your staffs on this budget. Working together, we will do everything in our power to ensure that taxpayer dollars are invested wisely in our collective future.

Respectfully Submitted,

Casey Anderson
Chair

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Board of Education

MONTGOMERY COUNTY BOARD OF EDUCATION

850 Hungerford Drive ◆ Room 123 ◆ Rockville, Maryland 20850

Malcolm Baldrige National Quality Award
2010 Award Recipient

March 1, 2019

The Honorable Marc Elrich, County Executive
Executive Office Building
101 Monroe Street, 2nd Floor
Rockville, Maryland 20850

The Honorable Nancy Navarro, President,
and Members of the Montgomery County Council
Stella B. Werner Council Office Building
100 Maryland Avenue, 6th Floor
Rockville, Maryland 20850

Dear Mr. Elrich, Ms. Navarro, and Councilmembers:

I am pleased to submit the Montgomery County Board of Education's Fiscal Year (FY) 2020 Operating Budget Request for Montgomery County Public Schools (MCPS). It is a result of the internal and external feedback coupled with extensive analysis of our programs and our outcomes.

The Board of Education is requesting an operating budget of $2,662,004,234 for MCPS for FY 2020. This is an increase of $65,562,515, or 2.5 percent, compared to the current FY 2019 Operating Budget. This increase is necessary to fund the same level of services for a growing number of students enrolled in MCPS, rising costs, and strategic accelerators to intensify efforts to close the persistent opportunity gap and improve academic excellence for all students. This budget will continue to build on the foundation and structure that are needed to ensure that all MCPS students are able to achieve at high levels.

The MCPS tax-supported operating budget (excluding grants and enterprise funds) for FY 2020 is $2,498,155,224, an increase of $54,075,062, or 2.2 percent, compared to the current FY 2019 tax-supported budget. This budget assumes Montgomery County will continue to fund $27,200,000 of MCPS retiree health benefits costs from the County's Consolidated Other Post-employment Benefits Trust Fund. In the event we chose to decrease this amount, we would need to increase the operating budget accordingly.

State law requires the County to provide, at a minimum, $9,489,140 in increased funding for MCPS based on the Maintenance of Effort law to account for enrollment growth. However, the need is greater in FY 2020, and the Board's budget request seeks $16,955,607 more than the minimum funding level required by the state law. This additional investment is essential if we are to maintain the quality of our school system and address the much needed work to improve the educational outcomes for all MCPS students.

Governor Lawrence J. Hogan's FY 2020 budget submitted to the Maryland General Assembly on January 18, 2019, reflected a total of $735,398,464 for MCPS. This is an increase of $27,429,716 compared to FY 2019. The Governor's budget increased the state's K–12 education funding by $176.0 million, or 3.1 percent compared to the previous year's budget. In addition, $210.0 million was set aside for recommendations of the Kirwan Commission. Our enrollment increase in the 2018–2019 school year used to calculate state aid in FY 2020 was the second largest in the state and represented 42.1 percent of the statewide increase.

This budget also assumes that it will be funded, in part, by end-of-year MCPS fund balance. The amount projected to be available to fund the FY 2020 budget is $25,000,000. This is the same amount used to fund the FY 2019 budget.

In order to manage our anticipated student growth in FY 2020, the budget adds 139.827 Full-time Equivalent (FTE) positions and $12,052,871. While there is an overall increase of students, there is a decrease in student enrollment in elementary schools, as was the case in FY 2019. Growth in elementary schools in prior years has moved on to secondary schools. These resources also support additional services for special education and our English language learners. We also are adding 10.250 positions $1,567,033 to open the new Clarksburg Cluster Elementary School (Clarksburg Village Site #2 Elementary School) in September 2019.

The Board's budget includes targeted, strategic accelerators for key bodies of work totaling 185.650 FTE positions and $19,575,364. The strategic accelerators include resources for reducing class size, providing alternative pathways for graduation, adding additional leadership positions in our schools, and providing additional differentiated and program support to our students receiving special education services and our English language learners. We also are implementing extended year programming at two elementary schools, expanding prekindergarten programs, adding Focus teachers in highly impacted schools, and increasing world language experiences at elementary schools through volunteers, online resources, and after-school programs. This FY 2020 budget expands dual enrollment opportunities for students at all three campuses of Montgomery College and expands the Northwest and Northwood high schools' Middle and Early College programs. Finally, the budget adds counselor positions and implements a new platform to put into place an improved physical, social, and psychological support framework and strengthen school safety and student security with improved background checks of staff.

At the same time, we have closely reviewed the MCPS operating budget and identified program efficiencies, reductions, and other adjustments totaling 8.125 FTE and $1,672,699 in FY 2020. The majority of this funding reduction, or $1,376,611, is from central services.

As in the past, this FY 2020 Operating Budget request was developed through a variety of collaborations. The Board held two public hearings on January 9 and 16, 2019, and heard testimony from approximately 80 individuals. The Board held two work sessions on the budget on January 17 and 24, 2019. Board members spent a great many hours analyzing the budget and submitted a number of formal questions to MCPS staff that eventually led to the Board's tentative adopted budget request on February 12, 2019.

The top priority of this budget is to maintain the high levels of achievement that we have for many of our students and eliminate those opportunity gaps that most heavily impact our Black or African American students, our Hispanic/Latino students, children who live in poverty, English Language Learners, and our students who receive services through an Individualized Education Program. We want our school system to be defined by its capacity to ensure the success of all students and we will not be satisfied until we have eliminated disparities in opportunities and performance among our entire student population. The Board of Education looks forward to working with you in the coming weeks and months to fund an operating budget for MCPS for FY 2020 that meets the needs of all our students.

Sincerely,

Shebra L. Evans
President

SLE:JRS:ND:jp

Enclosure

BOARD OF TRUSTEES

February 12, 2019

The Honorable Marc Elrich County
Executive
Executive Office Building
101 Monroe Street
Rockville, Maryland 20850

The Honorable Nancy Navarro President,
Montgomery County Council
Stella B. Werner Council Office Building 100
Maryland Avenue
Rockville, Maryland 20850

Dear Mr. Elrich and Ms. Navarro:

On behalf of the entire College community, we are grateful for the County's steadfast support of our mission and our students.

With keen awareness of the County's generosity and the current state of fiscal affairs, we seek a total appropriation of $313,448,186—a decrease of 0.82 percent from last year, which includes a request to increase the County contribution by $3.1 million, the lowest contribution request in seven years.

Again, thank you for your enduring commitment which enables the College to empower *all* who need their community's college—be they veterans, immigrants, apprentices, recent high school graduates—to help them grasp opportunity. Together, we can continue to build a thriving and just community—a place where education is truly the great equalizer.

Recent graduates like Glenn, Avanti, Kevin, and Kim know the power of a locally provided, high quality, affordable postsecondary education.

- Glen, *a veteran*, who turned to the College after serving in the US Army, and now, at age 26, attends the University of Maryland after earning his degree at MC;

- Avanti, *a recent high school graduate*, who enrolled at MC for the support and education she knew she needed so she could reach her goal to become a physician's assistant and help people in need in our County. Now 20 years old, she is pursuing her bachelor's degree at Towson University;

- Kevin, *an apprentice*, who got on-the-job skills training required for employment. Today, at 27, he works as an HVAC technician in Rockville; and

- Kim, *an immigrant* born in Vietnam who now attends Towson University at age 22, to pursue her dream to be an accounting professor and own a math learning center here in Montgomery County.

When we see students like these filled with pride and hope as they cross the stage at commencement, we see our county's future—we see Montgomery County.

It is clear to us: Montgomery College *is* Montgomery County!

This makes our work—empowering students like Glenn, Avanti, Kevin, and Kim to change their lives so they may become the next generation of entrepreneurs, health care providers, professors and technicians—crucial to the success of our community and the individuals who are Montgomery.

Affordability matters—it is crucial to access.
Our important work is possible because you continue invest in the College—investments that make affordable tuition a reality. You do so because you know economic disparity—not aptitude, ability, or aspiration—is the number one barrier to the completion of a college degree. Nationally, high school graduates from the lowest income quartile do not complete a degree in a timely fashion. Yet, an education is the surest path to economic mobility. As disparities grow locally, protecting access to education for all of Montgomery is more important than ever.

The pursuit of equity requires radical inclusion.
Thanks to your investments, we can also embrace and enhance our efforts for student success. Our mission must grow and evolve—we cannot be about *access for all and* success *for some*—instead we must be about *success for every student*.

That is why we have placed an emphasis—not on closing the *achievement* gap—but on closing the *opportunity* gap. We view our work through a "promise" lens—our students are standing on the threshold of their promise—not "at risk." This lens compels us to embrace an attitude—an imperative where we demand and expect equitable outcomes for every student. Together, from trustee to professor, our one pursuit is radical inclusion—to ameliorate the impact of opportunity gaps—so that all students, no matter their zip code, economic status, country of origin, or race can realize their own promise.

Radical inclusion requires a commitment to outcomes and measurement.
To advance these efforts, the College will continue to deepen our commitment to outcome measurement. Thanks to our faculty and staff, the College's Student Success Scorecard shows we are making progress: the fall-to-fall retention rate is at an all-time high at 66 percent for 2016 to 2017. The three-year graduation/transfer rate (for students who started in 2014) is at a peak and stands at 46 percent, which exceeds the national average.

To continue to make progress, we must routinely scrutinize how we use our resources to serve our students to make sure we are meeting their needs: to achieve equity, we must listen to the evidence. That's why, in 2016, we readily joined Achieving the Dream (ATD), a national non-profit that champions evidence-based improvements in community colleges. As an ATD institution, we aim to nurture a culture of evidence with a practice of data-informed decisions around minimizing institutional barriers and maximizing opportunities to access, success, and completion to help our students overcome opportunity gaps, and consistently improve achievement—so all students can meet their promise. Guided by ATD coaches, we look at our work—and our data—with fresh eyes to see what truly advances student success. As a result, the College implemented an ongoing effort to reduce the DFW rates (the number of students earning Ds, Fs or withdrawing from a class) in gateway courses. The Achieving the Promise Academy (ATPA), to which you appropriated funds, is a program designed to tackle the DFW rate and enhance overall student success metrics like fall to spring retention. Early data say the faculty and the APTA efforts are making a difference.

The board, too, is deeply committed to student success and recently established bold student success goals. Set in June of 2018 and beginning with the fall 2018 new student cohort, the board asked the College to aim for 30 percent of the cohort to obtain a credential—degree or certificate—by 2022. The trustees also set the goal that 50 percent of the cohort transfer to a four-year school within four years of beginning at MC. Finally, the board hopes that 38 percent of the cohort members will obtain a baccalaureate within eight years of their initial enrollment at the College.

The College's current student success metrics as described above are similar to—and, in some cases, exceed—other community colleges across the state and nation. Nonetheless, the board recognizes the College must push our institution to excel—to deliver the education that is in fact the great equalizer. Radical inclusion requires us to strive to live up to our mission more fully—again, we cannot be about access for all and success for some if we hope to help all who need their community's college to grasp the ladder of opportunity and meet the workforce needs of our dynamic knowledge-based economy.

BUDGET PRIORITIES

With this lean budget, we look forward to continuing to work with you to pursue equity and opportunity.

In FY20 College, the College will continue our efforts to expand access, protect affordability and drive student success and completion. With your support, the College can provide compensation increases for our employees, who are crucial to student success. In addition, with this appropriation, we can increase scholarship funds and add more financial aid counselors to help more students afford their education; expand the Early College program to enable more high school students to enroll at MC early and earn a college degree at a lower cost; and, finally, open two buildings.

Fiscal prudence is a guiding principle.
We closed our projected budget gap for FY20 by almost 84 percent—or $15.7 million—through reductions and reallocations of existing resources, increased state aid, and a student tuition increase, and use of an increase in state aid. A County contribution of $3.1 million will balance the budget and contribute to the cost of wage adjustments for our faculty and staff.

Budget reductions totaled $8.0 million. For example, to address long-term fiscal sustainability, we implemented a new compensation model that produced positive budget impacts—our base compensation cost is down $2.9 million. The academic affairs division reduced instructional salaries by $1.2 million to reflect enrollment contractions and continued to realize savings through seat utilization strategies that maximize space and talent. In addition, the College continues to experience a downward trend for utility costs, which reduced our budget by $975,000. A college wide response by our units resulted in budget reductions of $1.3 million. These reductions include a decrease of our staff complement by 6.25 full time equivalent (FTE) positions and our administrator complement by 2.0 FTE, as well as other unit operational costs. In addition, our salary lapse increased by $1.6 million with intentional hiring decisions balanced with enrollment.

The $2.8 million yielded from savings will support FY20, as requested and approved by the Council on January 29, 2019, as part of the County's FY19 savings plan.

Furthermore, we made changes to our employee health plans that eliminated approximately $900,000 in potential expenditures.

In FY20, we will open the Student Services Center on the Rockville Campus and the expanded and renovated Student Affairs and Science Building on the Germantown Campus. However, we made the difficult decision to forgo hiring 10 new staff such as building service workers to support the opening of new buildings, which eliminated the potential expense of $291,000. The budget does include some minor additional expenses for operational costs, cleaning supplies, for example—associated with opening a building.

Equity requires investments in excellence, affordability, and quality programs.
Compensation
The College's most important asset in our efforts to deliver on the promises of student success: our excellent faculty and staff who rise to meet the needs of all students to complete a postsecondary education. Our award-winning faculty provide extraordinary teaching and our staff support students in countless ways—cleaning classrooms, preparing lab materials, organizing mobile food markets, shoveling snow, tutoring, mentoring, leading math workshops, and more—to help students get to-and-through college. We have an employee agreement with our part-time faculty. While the economic terms of our two other employee agreements are not definitive, in order to plan for the FY20 operating budget, we have included $6.7 million to support all employee agreements.

Affordable tuition
Affordability remains critical to ensure equitable access to opportunity. As you well know, the community looks to us for affordable postsecondary education. One in four MC students receives Pell grants, federal financial aid. The average household income for Pell grant recipients is $20,000—in a County where a family of four needs $90,000 a year to subsist without help. Your continued investment helps keep the College affordable so all residents can access education and thrive. With your support of this proposed budget, students will contribute 28.7 percent of our operating costs through tuition—down from 40 percent in FY13, a reflection of your commitment to our students.

Scholarships
Yet, even with affordable tuition, scholarships are crucial for many students to access their community college. Attending part-time is not the answer to affordability challenges. Only 7.8 percent of part-time students, nationally, complete an associate's degree within four years of high school graduation. As a result, the budget includes an increase of $160,000 in scholarship funds to keep pace with increased tuition. Scholarship applications for credit students have increased from 2,271 to 4,395 in the last three years while WDCE scholarship applications have increased by 44 percent in the same time-period.

Historical data tells us that when the College runs out of scholarship funds students do not enroll. When last measured, 7000 students—the equivalent of the combined student population at Clarksburg, Montgomery Blair and Walter Johnson high schools—who qualified for grants but did not receive one *did not enroll* at the College. Additionally, we know that more than 80 percent of the students who receive a scholarship do enroll.

Clearly, students need financial support.

As a result, the College looks forward to the implementation of the Maryland Community College Promise Scholarship Program. We are pleased with the initial statewide appropriation of $15 million annually to provide last dollar scholarships for students in need entering one of the 16 Maryland community colleges within two years of receiving their high school diploma. Community colleges across the state are looking forward to analyzing the impact of the program on access after the initial implementation. Given the complexity of the law and the pace of the issuance of implementation directions, it is nearly impossible to predict the impact in advance. One issue that has already arisen: students who are ineligible to fill out the Free Application for Federal Student Aid (FAFSA) must complete a new Maryland financial aid application introduced this month. Gaining access to this form has already proven to be difficult for Dreamers and DACA students—which could be an enormous deterrent to these vulnerable students. All applicants using this Maryland form will have to participate in a verification process—another hurdle.

It is important to note the vast majority of our students will not qualify for the Promise Scholarship—the average age of our students is 26 and 65 percent of our students attend part-time. Many students work and attend part-time to cover the costs of housing, transportation, and groceries—the Promise scholarship likely will not be sufficient to eliminate the need to work and attend part-time. Nonetheless, given that we cannot meet the current demand for financial support, we look forward to some additional resources to help those that will qualify afford their community college.

Financial aid staff
With increased scholarship offerings, the complexities of implementing the Promise scholarships, and the rising number of scholarship applicants, we plan to use $100,000 to hire additional financial aid counselors to help more students get the help they need to access financial aid. Two full-time counselors and one part-time counselor will conduct outreach and coordinate applications for the Promise scholarships, work with newly eligible students for Maryland state scholarships, and ensure athletic scholarship awards comply with the National Junior College Athletic Association regulations. Importantly, the part-time counselor will work with students at risk of not meeting federal satisfactory academic progress (SAP) standards—who consequently may lose their Pell grant and be forced to drop out. Recall the average household income of a Pell grant recipient is $20,000. Equity demands additional support for Pell students on the verge of "SAPing out" to help drive student completion.

Early College and summer bridge programs
In addition to scholarships and counselors, we will widen the path to postsecondary education by expanding our Early College effort in partnership with Montgomery County Public Schools (MCPS). In the fall of 2018, we launched the Early College program on the Rockville Campus. In this dual enrollment program, high school students from all MCPS high schools can attend classes on our campus to complete their high school requirements while simultaneously earning a college degree. Students reduce the time to complete a degree by two years. During this kickoff year, 49 students enrolled. Notably, almost 50 percent of the inaugural class is African American, Black, or Latino. These students will graduate with an associate of arts in teaching in mathematics or an associate of arts in mathematics: we are helping grow the next generation of MCPS math teachers.

Based on the overwhelming interest and success of this first year, we plan to open Early College on the Germantown Campus and the Takoma Park/Silver Spring Campus. With $185,000, we will hire two full-time coordinators to oversee the campus programs and we will also implement a summer bridge program so students are oriented to the college experience before classes begin. We anticipate more than 300 students to participate in the fall 2019—365 students have already applied with 59 percent of applicants who are African American or Latino. By fall 2020, we expect to enroll 600 students. Students can earn degrees in business, biological science, computer science, cybersecurity, diagnostic medical sonography, nursing, physical therapist assistant, radiologic technology, and surgical technology. With Early College expansion and other dual enrollment programs combined, we anticipate over 1,000 new full-time students by the fall of 2020.

FISCAL BACKGROUND

Enrollment

Our student body reflects the County's population—over 75 percent are students of color and come from every high school, Whitman to Wheaton. The College is a large postsecondary education institution with 54,000 students, including 21,720 credit students. We continue to have the largest enrollment of all community colleges in Maryland and are one of the largest higher education institutions in Maryland—only University of Maryland College Park and University of Maryland University College enroll more undergraduate students. Each fall term since 1988, we have consistently enrolled more than 20,000 credit students. Our WDCE course enrollments exceed 40,000 each fiscal year.

As seen in the attached performance measures, individuals enrolling in WDCE programs steadily increased by 3.2 percent in the last three years. More students are enrolling through incumbent worker training, apprenticeship program like our HVAC technician program, and credential programs, such as certification in health career programs like pharmacy technician. It is evident that our County needs relevant education and training programs that fuel—or refuel—residents with new skills and credentials needed to move up the career ladder, improve the productivity of local employers, and contribute to a thriving County.

Currently, 22.5 percent of MCPS graduates enroll at MC the fall semester directly after high school. Our performance measures indicate a 10 percent increase in dual enrollment students, largely due to the implementation of the Early College program in FY19. With the planned expansion of Early College, we expect this number to continue to rise.

As we finalize the College's next strategic plan, MC2025, we are creating a strategic enrollment management plan based on guidance from the American Association of College Admission Officers and Registrars. The plan will address student recruitment, onboarding student processes, course scheduling, advising, financial aid assistance, and retention. Strategic enrollment management will support our commitment to access.

Each year, we carefully examine historical and projected data regarding enrollment because these figures guide many institutional decisions including tuition rates, personnel and operations, and, especially, programs outside the classroom. Our analysis predicts an enrollment increase in fall 2023, following the enrollment contraction of approximately 2,300 students in the last three years. The College will continue to implement strategies to lower operational costs where appropriate with enrollment contractions while we continue to provide critical, equity-infused, wrap-around services needed by so many of our students.

Ultimately, credit-hour enrollment determines our tuition revenue. In FY20, credit hour enrollment of 410,929 hours is the basis for the calculation of the College's tuition revenue.

Revenue

State aid—$45,200,000

The College's budget includes the John R. Cade Funding Formula allocation in the Governor's FY20 budget, $45.2 million, of which $37.2 million is allocated to the Current Fund and $8.0 million is allocated to the WDCE Fund. Final action by the Maryland General Assembly on the State's budget will occur in April.

Tuition—$75,900,000
The budget, as adopted by the Board of Trustees on January 24, anticipates a $4/$8/$12 per-credit-hour increase in tuition for in-county/in-state/out-of-state students. The board acts on tuition rates in April. The consolidated fee charged to students will also increase because it is calculated as a percentage of tuition. With these proposed increases, the average full-time student will pay $5,322 next year, a 2.8 percent increase from last year. Tuition and related fees are expected to generate $75.9 million.

County savings plan—$2,800,000

Child care center sale proceeds—$160,000
Last year, the College sold its child care center property in Takoma Park. The board designated these funds to award $160,000 in scholarships over four years.

Auxiliary fund transfer—$500,000
We anticipate the revenue from the Follett Higher Education Group contract for bookstore retail operations to be $500,000.

Workforce Development & Continuing Education Fund transfer—$1,000,000

County support—$145,200,000
The College's budget reflects County support of $145.2 million which includes a $3.1 million County contribution increase request.

EXPENDITURES

The following is a summary of new expenditures and initiatives, described above, included in our FY20 budget:

Employee compensation—$6,700,000

New building operational costs—$216,000

Early College coordinators and a summer bridge program—$185,000

Student financial aid scholarship counselors—$100,000

Scholarships—$160,000

OTHER FUNDS

Emergency Plant Maintenance and Repair Fund—$300,000
The Emergency Plant Maintenance and Repair Fund is a tax-supported fund including a County contribution. We request a total appropriation equal to last year's appropriation of $250,000 of County funds plus the authority to use $35,000 in fund balance. This crucial funding supports our emergency maintenance needs.

Workforce Development & Continuing Education Fund—$18,400,000
We request appropriation authority to spend $18.4 million. State aid and student tuition are the sources

for this fund. This amount is a 3.9 percent increase over last year because of the previously noted increase in WDCE enrollment.
WDCE students access career programs and certifications in the health sciences, trades, cybersecurity, and management, as well as programs for personal enrichment and lifelong learning. The College also serves adults earning high school equivalency, adult basic education, and English for speakers of other languages.

Auxiliary Enterprises Fund—$1,700,000
We request appropriation authority to spend $1.7 million for the Auxiliary Enterprises Fund. This covers expenditures associated with the Parilla Performing Arts Center, the Cultural Arts Center, the student-operated Macklin Business Institute Café, the Summer Dinner Theatre program, other facility rentals, and athletic camps for County resident youth.

Cable TV Fund—$1,800,000
We request appropriation authority to spend $1.8 million. The County's cable plan is the source of revenue.

The Cable TV fund continues to provide opportunities for student involvement in MCTV productions using varied media platforms for student recruitment and expanded programming. MCTV supports community outreach by increasing multicultural and foreign language programming in the six most common languages used in the County.

Grants Fund—$20,300,000
We request grant appropriation authority to spend $20.3 million. Of this amount, $400,000 is requested in County funds for the Adult English for Speakers of Other Languages (ESOL), Adult Basic Education, and General Equivalency Degree (GED) program. The $400,000 is the same amount as appropriated last year.

The College uses grant funds to support several important initiatives including English as a Second Language (ESL), adult education and literacy programs, as well as innovative workforce development training programs for information technology, cybersecurity, biotechnology, transportation, early childcare, nursing, and science, technology, engineering, and mathematics (STEM) programs.

Transportation Fund—$4,200,000
We request appropriation authority to spend $4.2 million. This fund is comprised entirely of user fees from students and employees, including parking enforcement revenue. The revenue funds transportation alternatives for students—Ride On bus service and the MC shuttle bus. It also underwrites the finance costs of the construction for the Takoma Park/Silver Spring West Parking Garage and the Rockville North Garage.

Major Facilities Reserve Fund—$2,000,000
We request appropriation authority to spend $2.0 million to pay the Montgomery College Foundation for the cost of The Morris and Gwendolyn Cafritz Foundation Arts Center. This fund is entirely comprised of user fees and no county funds are requested.

In FY20, $2.0 million will be transferred to the capital budget for the continued renovations of the physical education buildings and to complete the conversion of a baseball field on the Rockville Campus to a soccer stadium, which will support the College athletic program. It will be transferred to the capital budget as a non-mandatory transfer.

CONCLUSION

On behalf of the Montgomery College Board of Trustees, we respectfully request a total appropriation authority of $313,448,186.

Again, thank you for your enduring commitment to help us to empower *all* who need their community's college—be they veterans, immigrants, apprentices, recent high school graduates—to help them grasp opportunity. Empowering students like **Glenn, Avanti, Kevin, and Kim** to change their lives—to become the next generation of entrepreneurs, health care providers, professors, and technicians—is crucial to the success of our community and the individuals who are Montgomery.

Together, we can continue to build a thriving and just community—a place where education is truly the great equalizer.

Thank you for your support.

Sincerely,

Michael J. Knapp

Michael J. Knapp
Chair, Board of Trustees

DeRionne P. Pollard

DeRionne P. Pollard, PhD
President

Personnel

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OFFICE OF THE COUNTY EXECUTIVE
ROCKVILLE, MARYLAND 20850

Marc Elrich
County Executive

RECEIVED
MONTGOMERY COUNTY
2019 MAR 15 AM 11:21

MEMORANDUM

March 15, 2019

TO: Nancy Navarro, President, County Council

FROM: Marc Elrich, County Executive

SUBJECT: FY19 Savings Plan: NDA – Retiree Health Benefits Trust ($34,562,660); NDA – Consolidated Retiree Health Benefit Trust – College ($2,845,000); and NDA – Consolidated Retiree Health Benefit Trust – MCPS ($52,205,000)

My FY20 Recommended Operating Budget includes additional FY19 expenditure savings needed to fully restore current year reserves to the level assumed in the FY19 Approved Budget and to meet our commitment to fund reserves at 10 percent of revenues by FY20. Please find attached my recommended FY19 savings plan to achieve those goals. In total, these expenditure reductions will increase the FY19 General Fund reserve by $89.6 million.

As you are aware, the savings plan approved by the County Council in January only partially closed the current year budget gap of more than $40 million. After updating our revenue forecast in late February, additional expenditure reductions were necessary to close a significantly wider gap. The current fiscal situation is not the result of a declining economy; it is likely caused by changes in taxpayer behavior driven by speculation about federal tax reform. Within this context, it is appropriate to isolate this corrective action to the current year.

The recommended expenditure savings reduce FY19 Other Post-Employment Benefits (OPEB) prefunding by $89.6 million. As noted above, given the unexpected shortfall in current year revenues, this approach is intended to be a one-time departure from our policy of prefunding retiree health insurance benefits. My FY20 Recommended Operating Budget restores prefunding consistent with our fiscal policy, as well as contributes an additional $9 million on behalf of MCPS. It should be noted that retirees will see no change to their benefits as a result of my recommendation, and their benefit claims will continue to be paid as they have been in the past.

It is important that the Council join me in this approach as it is aligned with our reserve funding target. Quite frankly, it is our best option for closing our FY19 gap without limiting services for our residents in FY20 and beyond. My staff is available to assist the Council in its review of the attached proposal.

ME:cbo

Attachment: Recommended FY19 Savings Plan Montgomery County Government

County Executive's Recommended FY19 Savings Plan
Montgomery County Government
March 2019

NDA	AMOUNT	DESCRIPTION
NDA - Retiree Health Benefits Trust	-34,562,660	Reduce spending to restore General Fund reserve
NDA - Consolidated Retiree Health Benefit Trust - College	-2,845,000	Reduce spending to restore General Fund reserve
NDA - Consolidated Retiree Health Benefit Trust - MCPS	-52,205,000	Reduce spending to restore General Fund reserve
TOTAL	**-89,612,660**	

REVENUE SUMMARY
TAX SUPPORTED BUDGETS
($ Millions)

	KEY REVENUE CATEGORIES	App. FY19	Est. FY19	% Chg. FY19-20	Rec. FY20	% Chg. FY20-21	Projected FY21	% Chg. FY21-22	Projected FY22	% Chg. FY22-23	Projected FY23	% Chg. FY23-24	Projected FY24	% Chg. FY24-25	Projected FY25
	TAXES	5-24-18	3-15-19	Rec/App	3-15-19										
1	Property Tax	1,808.4	1,786.5	1.6%	1,836.8	3.1%	1,893.8	3.1%	1,951.9	3.5%	2,020.5	3.5%	2,091.4	3.3%	2,160.7
2	Income Tax	1,585.2	1,542.9	3.5%	1,640.3	3.8%	1,702.9	3.5%	1,762.6	4.6%	1,843.2	4.8%	1,930.8	4.7%	2,021.1
3	Transfer Tax	109.5	124.8	15.3%	126.3	0.5%	127.0	2.1%	129.7	3.0%	133.6	4.9%	140.1	4.5%	146.4
4	Recordation Tax	53.4	55.8	5.7%	56.5	0.5%	56.8	2.1%	58.0	3.0%	59.7	4.9%	62.6	4.5%	65.4
5	Energy Tax	194.0	197.9	2.5%	198.9	-2.0%	195.0	2.0%	198.9	-2.1%	194.8	2.1%	198.9	-1.3%	196.3
6	Telephone Tax	53.3	53.3	5.8%	56.3	-0.8%	55.8	-0.3%	55.7	0.3%	55.9	-0.1%	55.8	-0.1%	55.7
7	Hotel/Motel Tax	22.2	22.1	1.8%	22.6	0.8%	22.8	0.8%	23.0	0.8%	23.2	0.8%	23.3	0.8%	23.5
8	Admissions Tax	3.6	3.6	9.1%	3.9	7.6%	4.2	7.9%	4.5	7.9%	4.9	7.9%	5.3	7.9%	5.7
9	E-Cigarette Tax	0.7	1.4	120.3%	1.4	3.8%	1.5	3.7%	1.5	3.6%	1.6	3.5%	1.7	3.5%	1.7
10	**Total Local Taxes**	**3,830.2**	**3,788.3**	**2.9%**	**3,943.1**	**3.0%**	**4,059.7**	**3.1%**	**4,185.8**	**3.6%**	**4,337.3**	**4.0%**	**4,509.8**	**3.7%**	**4,676.7**
	INTERGOVERNMENTAL AID														
11	Highway User	3.8	3.8	118.3%	8.2	0.0%	8.2	0.0%	8.2	0.0%	8.2	0.0%	8.2	0.0%	8.2
12	Police Protection	14.2	14.2	0.0%	14.2	0.0%	14.2	0.0%	14.2	0.0%	14.2	0.0%	14.2	0.0%	14.2
13	Libraries	6.4	6.4	3.9%	6.7	0.0%	6.7	0.0%	6.7	0.0%	6.7	0.0%	6.7	0.0%	6.7
14	Health Services Case Formula	4.6	4.6	0.0%	4.6	0.0%	4.6	0.0%	4.6	0.0%	4.6	0.0%	4.6	0.0%	4.6
15	Mass Transit	40.3	41.3	2.5%	41.3	0.0%	41.3	0.0%	41.3	0.0%	41.3	0.0%	41.3	0.0%	41.3
16	Public Schools	706.9	706.9	3.9%	734.6	0.0%	734.6	0.0%	734.6	0.0%	734.6	0.0%	734.6	0.0%	734.6
17	Community College	36.6	36.6	1.7%	37.2	0.0%	37.2	0.0%	37.2	0.0%	37.2	0.0%	37.2	0.0%	37.2
18	Other	67.7	71.1	-16.1%	56.8	-29.5%	40.0	-0.2%	39.9	0.0%	39.9	0.0%	39.9	0.0%	39.9
19	**Total Intergovernmental Aid**	**880.5**	**884.9**	**2.6%**	**903.6**	**-1.9%**	**886.8**	**0.0%**	**886.7**	**0.0%**	**886.7**	**0.0%**	**886.7**	**0.0%**	**886.7**
	FEES AND FINES														
20	Licenses & Permits	13.1	12.8	1.6%	13.3	1.5%	13.5	1.5%	13.7	1.5%	13.9	1.5%	14.1	1.5%	14.3
21	Charges for Services	72.7	72.2	-6.7%	67.8	2.0%	69.2	2.2%	70.7	2.2%	72.2	2.2%	73.8	2.2%	75.3
22	Fines & Forfeitures	29.1	35.0	23.7%	36.0	1.6%	36.6	1.6%	37.1	1.6%	37.7	1.6%	38.3	1.6%	38.9
23	Montgomery College Tuition	78.2	75.4	-3.0%	75.9	2.0%	77.4	2.2%	79.1	2.2%	80.8	2.2%	82.5	2.2%	84.3
24	**Total Fees and Fines**	**193.0**	**195.4**	**0.0%**	**193.0**	**1.9%**	**196.6**	**2.0%**	**200.6**	**2.0%**	**204.6**	**2.0%**	**208.7**	**2.0%**	**212.9**
	MISCELLANEOUS														
25	Investment Income	5.3	8.1	61.3%	8.6	0.0%	8.6	0.1%	8.6	0.0%	8.6	0.0%	8.6	0.0%	8.6
26	Other Miscellaneous	19.2	21.7	-2.77%	18.7	2.5%	19.2	2.7%	19.7	2.7%	20.2	2.7%	20.8	2.7%	21.3
27	**Total Miscellaneous**	**24.6**	**29.8**	**11.1%**	**27.3**	**1.7%**	**27.8**	**1.9%**	**28.3**	**1.9%**	**28.8**	**1.9%**	**29.4**	**1.9%**	**29.9**
28	**TOTAL REVENUES**	**4,928.3**	**4,898.4**	**2.8%**	**5,066.9**	**2.1%**	**5,170.9**	**2.5%**	**5,301.4**	**2.9%**	**5,457.5**	**3.2%**	**5,634.6**	**3.0%**	**5,806.3**
	Calculation for Adjusted Governmental Revenues														
29	**Total Tax Supported Revenues**	**4,928.3**	**4,898.4**	**2.8%**	**5,066.9**	**2.1%**	**5,170.9**	**2.5%**	**5,301.4**	**2.9%**	**5,457.5**	**3.2%**	**5,634.6**	**3.0%**	**5,806.3**
30	**Capital Projects Fund**	**187.2**	**187.2**	**-22.2%**	**145.7**	**-15.0%**	**123.9**	**1.2%**	**125.4**	**1.3%**	**126.9**	**1.7%**	**129.1**	**0.0%**	**129.1**
31	**Grants**	**118.5**	**118.5**	**0.4%**	**119.0**	**2.5%**	**122.0**	**2.7%**	**125.3**	**2.7%**	**128.7**	**2.7%**	**132.2**	**2.7%**	**135.7**
32	**MCG Adjusted Revenues**	**5,234.0**	**5,204.1**	**1.9%**	**5,331.7**	**1.6%**	**5,416.8**	**2.5%**	**5,552.1**	**2.9%**	**5,713.1**	**3.2%**	**5,895.9**	**3.0%**	**6,071.1**

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County Executive's Recommended FY20-25 Public Services Program

Tax Supported Fiscal Plan Summary

($ in Millions)

		App. FY19	Est. FY19	% Chg. FY19-20	Rec. FY20	% Chg. FY20-21	Projected FY21	% Chg. FY21-22	Projected FY22	% Chg. FY22-23	Projected FY23	% Chg. FY23-24	Projected FY24	% Chg. FY24-25	Projected FY25
		5-24-18	3-15-19	App/Rec	3-15-19										
	Total Revenues														
1	Property Tax	1,808.4	1,786.5	1.6%	1,836.8	3.1%	1,893.8	3.1%	1,951.9	3.5%	2,020.5	3.5%	2,091.4	3.3%	2,160.7
2	Income Tax	1,585.2	1,542.9	3.5%	1,640.3	3.8%	1,702.9	3.5%	1,762.6	4.6%	1,843.2	4.8%	1,930.8	4.7%	2,021.1
3	Transfer/Recordation Tax	162.9	180.6	12.2%	182.8	0.5%	183.7	2.1%	187.7	3.0%	193.3	4.9%	202.7	4.5%	211.8
4	Other Taxes	273.7	278.3	3.5%	283.2	-1.4%	279.3	1.6%	283.7	-1.2%	280.3	1.6%	284.9	-0.7%	283.0
5	Other Revenues	1,098.1	1,110.1	2.3%	1,123.9	-1.1%	1,111.2	0.4%	1,115.6	0.4%	1,120.2	0.4%	1,124.8	0.4%	1,129.6
6	**Total Revenues**	**4,928.3**	**4,898.4**	**2.8%**	**5,066.9**	**2.1%**	**5,170.9**	**2.5%**	**5,301.4**	**2.9%**	**5,457.5**	**3.2%**	**5,634.6**	**3.0%**	**5,806.3**
7															
8	**Net Transfers In (Out)**	**34.9**	**26.1**	**-54.2%**	**16.0**	**2.5%**	**16.4**	**2.7%**	**16.8**	**2.7%**	**17.3**	**2.7%**	**17.8**	**2.7%**	**18.2**
9	**Total Revenues and Transfers Available**	**4,963.3**	**4,924.4**	**2.4%**	**5,082.9**	**2.1%**	**5,187.3**	**2.5%**	**5,318.3**	**2.9%**	**5,474.8**	**3.2%**	**5,652.4**	**3.0%**	**5,824.5**
10															
11	**Non-Operating Budget Use of Revenues**														
12	Debt Service	420.0	416.5	2.5%	430.5	4.4%	449.4	2.7%	461.7	3.3%	476.9	0.0%	477.1	1.8%	485.9
13	PAYGO	33.0	33.0	-3.0%	32.0	-3.1%	31.0	-3.2%	30.0	0.0%	30.0	0.0%	30.0	0.0%	30.0
14	CIP Current Revenue	35.6	26.3	3.6%	36.9	137.3%	87.5	-14.3%	75.0	30.4%	97.8	0.8%	98.7	0.0%	98.7
15	Change in Other Reserves	-37.3	-17.8	40.4%	-22.2	100.8%	0.2	-2.9%	0.2	15.2%	0.2	6.0%	0.2	-0.7%	0.2
16	Contribution to General Fund Undesignated Reserves	21.1	63.7	-72.6%	5.8	23.5%	7.1	-26.2%	5.3	6.1%	5.6	20.1%	6.7	15.2%	7.7
17	Contribution to Revenue Stabilization Reserves	29.7	32.1	-31.8%	20.2	-80.2%	4.0	91.2%	7.6	25.0%	9.6	27.6%	12.2	-15.6%	10.3
18	Set Aside for other uses (supplemental appropriations)	-4.0	-4.0	450.0%	14.0	42.9%	20.0	0.0%	20.0	0.0%	20.0	0.0%	20.0	0.0%	20.0
19	**Total Other Uses of Resources**	**498.2**	**549.8**	**3.8%**	**517.2**	**15.9%**	**599.2**	**0.1%**	**599.8**	**6.7%**	**640.1**	**0.8%**	**644.9**	**1.2%**	**652.8**
20	**Available to Allocate to Agencies (Total Revenues+Net Transfers-Total Other Uses)**	**4,465.1**	**4,374.6**	**2.3%**	**4,565.7**	**0.5%**	**4,588.1**	**2.8%**	**4,718.5**	**2.5%**	**4,834.7**	**3.6%**	**5,007.5**	**3.3%**	**5,171.7**
21															
22	**Agency Uses**														
23															
24	Montgomery County Public Schools (MCPS)	2,444.1	2,425.9	1.6%	2,483.7										
25	Montgomery College (MC)	265.5	261.2	-1.2%	262.4										
26	MNCPPC (w/o Debt Service)	128.3	126.5	0.8%	129.3										
27	MCG	1,627.2	1,560.9	3.9%	1,690.4										
28	**Agency Uses**	**4,465.1**	**4,374.6**	**2.3%**	**4,565.7**	**0.5%**	**4,588.1**	**2.8%**	**4,718.5**	**2.5%**	**4,834.7**	**3.6%**	**5,007.5**	**3.3%**	**5,171.7**
29	**Total Uses**	**4,963.3**	**4,924.4**	**2.4%**	**5,082.9**	**2.1%**	**5,187.3**	**2.5%**	**5,318.3**	**2.9%**	**5,474.8**	**3.2%**	**5,652.4**	**3.0%**	**5,824.5**
30	**(Gap)/Available**	**0.0**	**0.0**		**0.0**		**0.0**		**0.0**		**0.0**		**0.0**		**0.0**

Assumptions:

1. Property taxes are at the Charter Limit with a $692 credit. Other taxes are at current rates.
2. Reserve contributions are consistent with legal requirements and the minimum policy target.
3. PAYGO, debt service, and current revenue reflect the County Executive's Amendments to the FY19-24 Capital Improvements Program and additional proposed current revenue amendments.
4. State Aid, including MCPS and Montgomery College, is not projected to increase from FY20-25.

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County Executive's Recommended FY20-25 Public Services Program

Tax Supported Fiscal Plan Summary

($ in Millions)

		App. FY19	Est. FY19	% Chg. FY19-20	Rec. FY20	% Chg. FY20-21	Projected FY21	% Chg. FY21-22	Projected FY22	% Chg. FY22-23	Projected FY23	% Chg. FY23-24	Projected FY24	% Chg. FY24-25	Projected FY25
31	Beginning Reserves			App/Rec											
32	Unrestricted General Fund	133.0	102.7	25.1%	166.4	3.5%	172.2	4.1%	179.3	2.9%	184.6	3.0%	190.2	3.5%	196.9
33	Revenue Stabilization Fund	308.3	308.7	10.6%	340.8	5.9%	361.0	1.1%	365.0	2.1%	372.7	2.6%	382.3	3.2%	394.5
34	Total Reserves	441.2	411.4	15.0%	507.2	5.1%	533.2	2.1%	544.4	2.4%	557.3	2.7%	572.5	3.3%	591.4
35															
36	Additions to Reserves														
37	Unrestricted General Fund	21.1	63.7	-72.6%	5.8	23.5%	7.1	-26.2%	5.3	6.1%	5.6	20.1%	6.7	15.2%	7.7
38	Revenue Stabilization Fund	29.7	32.1	-31.8%	20.2	-80.2%	4.0	91.2%	7.6	25.0%	9.6	27.6%	12.2	-15.6%	10.3
39	Total Change in Reserves	50.8	95.8	-48.8%	26.0	-57.2%	11.1	16.0%	12.9	17.3%	15.2	24.9%	18.9	-4.6%	18.0
40															
41	Ending Reserves														
42	Unrestricted General Fund	154.1	166.4	11.8%	172.2	4.1%	179.3	2.9%	184.6	3.0%	190.2	3.5%	196.9	3.9%	204.7
43	Revenue Stabilization Fund	338.0	340.8	6.8%	361.0	1.1%	365.0	2.1%	372.7	2.6%	382.3	3.2%	394.5	2.6%	404.8
44	Total Reserves	492.0	507.2	8.4%	533.2	2.1%	544.4	2.4%	557.3	2.7%	572.5	3.3%	591.4	3.1%	609.4
45	Reserves as a % of Adjusted Governmental Revenues	9.4%	9.7%		10.0%		10.0%		10.0%		10.0%		10.0%		10.0%
46	Other Reserves														
47	Montgomery College	4.7	7.5	-3.8%	4.5	0.0%	4.5	0.0%	4.5	0.0%	4.5	0.0%	4.5	0.0%	4.5
48	M-NCPPC	4.3	5.6	14.1%	4.9	3.1%	5.1	3.1%	5.3	3.5%	5.4	3.5%	5.6	3.3%	5.8
49	MCPS	0.0	25.0	n/a	0.0	n/a	0.0	n/a	0.0	n/a	0.0	n/a	0.0	n/a	0.0
50	MCG Special Funds	0.8	-5.8	-18.1%	0.7	4.1%	0.7	2.9%	0.7	3.0%	0.7	3.5%	0.8	3.9%	0.8
51	MCG + Agency Reserves as a % of Adjusted Govt Revenues	9.6%	10.4%		10.2%		10.2%		10.2%		10.2%		10.2%		10.2%
52	Retiree Health Insurance Pre-Funding														
53	Montgomery County Public Schools (MCPS)	79.4	27.2		78.5		85.0		89.2		88.2		87.7		81.1
54	Montgomery College (MC)	2.8	0.0		5.4		5.5		5.6		5.4		5.3		5.2
55	MNCPPC	3.0	3.0		2.8		2.7		2.6		2.6		2.5		2.5
56	MCG	43.6	9.0		34.7		34.5		34.3		31.7		29.9		28.6
57	Subtotal Retiree Health Insurance Pre-Funding	128.8	39.2		121.4		127.7		131.6		128.0		125.5		117.4
58	Adjusted Governmental Revenues														
59	Total Tax Supported Revenues	4,928.3	4,898.4	2.8%	5,066.9	2.1%	5,170.9	2.5%	5,301.4	2.9%	5,457.5	3.2%	5,634.6	3.0%	5,806.3
60	Capital Projects Fund	187.2	187.2	-22.2%	145.7	-15.0%	123.9	1.2%	125.4	1.3%	126.9	1.7%	129.1	0.0%	129.1
61	Grants	118.5	118.5	0.4%	119.0	2.5%	122.0	2.7%	125.3	2.7%	128.7	2.7%	132.2	2.7%	135.7
62	Total Adjusted Governmental Revenues	5,234.0	5,204.1	1.9%	5,331.7	1.6%	5,416.8	2.5%	5,552.1	2.9%	5,713.1	3.2%	5,895.9	3.0%	6,071.1

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M E M O R A N D U M

April 1, 2019

TO: County Council

FROM: Marlene Michaelson, Executive Director MM

SUBJECT: Reserve Policy

This memorandum summarizes the recommendation in the Executive's proposed FY20 budget regarding reserves and provides information on prior Council's decisions regarding the reserve policy. Reserve polices were established by resolution and law in 2010 and revised in 2011. (Prior to this time, reserve policy goals were included in the operating budget and fiscal plan.) Any change to those policies should only occur after careful consideration by the Council and Executive with accompanying changes to County law.

FY20 Budget

The Executive's FY20 budget proposes to use funds that would otherwise have been used for Other Post-Employment Benefits (OPEB) to fund contributions to the reserve in FY19 and FY20. He proposes to reduce the FY19 contribution to the OPEB Trust Fund by $89.6M (from 128.8M to 39.2M) through a Saving Plan submitted on March 15 for the Council's approval. The budget proposes to add $63.5M to the FY19 General Fund Undesignated Reserve (compared to the December fiscal update) and $5.8M to the FY20 General Fund Undesignated Reserve. If the Council supports the additional Saving Plan or identifies other sources of funding, the reserve would reach 9.7% reserve by the end of FY19 and 10.0% by the end of FY20. **Staff strongly supports the Executives recommendation to achieve the reserve targets consistent with County law and Council Resolution.** The Council should determine during its budget review whether redirected OPEB funds are the best way to achieve this goal.

Background on Reserve Policy Changes

Significant changes to the reserve policy were made in 2010 after the Great Recession led to precipitous declines in the reserve and negative reactions from the bond rating agencies. In FY10 the County experienced reductions in income and property tax revenues and state aid at the same time it experienced extraordinary expenditures associated with the H1N1 flu virus and successive and historic winter blizzards.

To balance the FY10 budget, the reserve target was reduced from 6% to 5% and reserves continued to fall during FY10.[1] The dire fiscal situation led then County Executive Leggett to propose two savings plans prior to his transmission of the FY11 budget and significant reductions and tax increases in the proposed budget. In April 2010, he recommended additional reductions just one month after submitting his March 15 budget. To balance the budget, the County increased the Fuel Energy tax and telephone tax, created an ambulance fee, shifted current revenue and pay-as-you-go financing (PAYGO) from the capital budget, eliminated general wage adjustments and step increases for all agencies and removed retiree health insurance pre-funding for all agencies. It also made very large reductions in agency spending: $125 million for County Government, $41 million for Montgomery County Public Schools (MCPS), $15 million for the College and $16 million for the Maryland-National Capital Park & Planning (M-NCPPC).

In April 2010 Moody's Investors Service placed the County on a watchlist for a possible ratings downgrade, citing the County's need to "stabilize and replenish reserve levels and to restore financial flexibility." Moody's action was based on the deterioration in the County's financial position, most notably a three-year decline in its Fund Balance. Stanford & Poor and Fitch also highlighted the County's weakened financial conditions and their credit concerns in written reports. **The Council's final action on the FY11 budget in May 2010 closed a budget gap of nearly $1 billion; the budget was the first in at least 40 years to show a decline from the previous year's budget.**

At the same time the County was working to close the gap in the FY11 budget, the County hired Public Financial Management, Inc. (PFM) to review the County's Fund Balance Policy, its Revenue Stabilization Fund (RSF) legal provisions and other related policies to determine if these policies were adequate and, if not, to suggest alternative policies for the County's consideration. PFM understood the challenge of recommending an appropriate Fund Balance policy that would be satisfactory to rating agencies, while not overstating the necessary level of reserves.

The Executive Summary of the PFM report appears on ©1-5. Their 4 key recommendations were as follows:

1. Act swiftly and decisively as part of the FY 2011 budget process to significantly restore target fund balance levels to the 5% General Fund Balance and 1% RSF balance.
2. Amend law with respect to the RSF provide for a mandatory contribution to the RSF (until the 10% target for the combined fund balances is achieved) and define Adjusted Governmental Fund Revenues.[2]
3. Establish and meet targets for the combined ending General Fund and RSF balance of 10% by FY 2020.
4. Strengthen its budget policy requiring the County to adopt a structurally balanced budget and to eliminate the ability to treat accumulated fund balance as revenue for the purpose of determining structural balance.

Recommendation 3 focused on the need to restore the General and RSF Fund balances in FY11 and to target and maintain a combined reserve balance equal to 10% of "Adjusted Governmental Fund Revenues" by 2020. Their recommended 10% fund balance was equal to approximately 36 days of revenues for all governmental funds. PFM believed this reserve level was appropriate since the one year drop in tax revenues experienced by the County in 2010 was equal to 16 days of Adjusted Governmental Fund

[1] By the end of FY10 the General Fund reserve was drawn down to $0 and the Revenue Stabilization Fund (RSF) to $74.9 million (a reduction of 40%).

[2] Adjusted Governmental Fund Revenues are defined in the PFM report as "revenues of all tax-supported County governmental and agency revenues, including operating grant and capital project revenues".

Balance. PFM further noted that the County had experienced a 20% drop in income tax revenue in a single year and this volatile revenue stream makes it very difficult to budget reliably and thus requires a larger fund balance that other governments with less volatile revenue streams.

The Council adopted a comprehensive resolution on reserve and select fiscal policies in June 2010, implementing the recommendations of PFM (see ©6-8). The resolution addresses building reserve levels to 10% of Adjusted Governmental Revenues by 2020, maintaining PAYGO at 10% of annual general obligation bond issuance, and other goals. At the same time the Council amended the County Code to make similar changes, indicating the importance of these goals and the need to more formally guide the actions of future Councils and Executives (see Bill 36-10 at ©9-16). Subsequently, all three rating agencies confirmed the County's AAA bond rating. The resolution was updated in November 2011 to further strengthen and clarify the portion of the resolution addressing reserves and establish annual goals to reach the 10% target (see ©17-20).

The County has held a AAA rating since 1973 and is currently one of a select number of local governments nationwide with a AAA rating from all three rating agencies. A memorandum from the Finance Department prepared in 2018 outlines in concrete terms the dollars-and-cents importance of maintaining the AAA rating, quite apart from its symbolic importance (see ©21-22).

Guidance on Reserve Policy

The County considers a range of factors in setting reserve policy, including the guidelines of the Government Finance Officers' Association (GFOA), the reserve levels of comparable highly-rated AAA jurisdictions, cash flow requirements and the volatility of revenues. GFOA "recommends, at a minimum, that general-purpose governments, regardless of size, maintain unrestricted budgetary fund balance in their general fund of **no less than two months** of regular general fund operating revenues or regular general fund operating expenditures." This is approximately 16% of revenues.

Moody's recommends the "available" fund balance to be **30% or more** of revenues (December 16, 2016 report of the Moody's Investor Service entitled Rating Methodology U.S. Local Government General Obligation Debt). The "available" fund balance is determined from financial reporting done as part of the Comprehensive Annual Financial Report (CAFR). Moody's uses these numbers as a basis for examining different jurisdictions in a comparable manner and does not use our definition of budgeted reserve. The available fund balance is larger than the budgeted reserve because it includes funds that have already been appropriated for future expenditures.

The comparison with other AAA jurisdictions indicates that in 2017 the County's **available** fund balance of **16.5%** was significantly less than the National AAA County Median (28.5%) and less than the Peer County Median of 23.5%. The County ranked 14th among the 20 counties with AAA ratings. Continued efforts to increase the reserve have had a positive impact and in 2018 the County had a **20%** available balance. While this was still less the National and Peer Median, it was measurably closer; the County tied for a rank of 13th out 20. Charts showing the available fund balances of other AAA counties in 2017 and 2018 appear on ©23-25.

Each jurisdiction has a different risk profile and its reserve policies should reflect those risks. The County Executive has previously indicated his intent to "complete a risk-based reserve study and adjust the General Fund reserve target based on the results to ensure that we can sustain basic services during emergencies and recessions" further noting that this analysis could lead to an increase or reduction from the current level. Staff welcomes this analysis but believes it must be done carefully and with the input of financial experts who understand how rating agencies evaluate reserves. The time needed to do this properly suggests it should be done after the adoption of the FY20 budget.

Other Factors Impacting Bond Ratings

While fund balance is only one of several factors considered in establishing a jurisdiction's bond rating, it is arguably the most important credit factor that a rating analyst considers. The factors used by Moody's are shown on ©26 and include Economy/ Tax Base, Finances (including fund balance and fund balance trend), Management, and Debt/Pensions. The County's rating is bolstered by a strong economy, tax base, management and pension policies. Fund balance, however, was the focus of prior rating agency concerns due to the fact that the County's current fund balance level remains below both national and peer medians for other AAA-rated credits. In addition, while the County currently remains under its self-imposed policy of 10% of Adjusted Governmental Revenues, it has communicated to the rating agencies (since establishment of this policy in 2010) that it would meet this benchmark by FY20. The proposed budget (assuming adoption of the Savings Plan or another funding source) would achieve that objective.

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Report to Montgomery County, Maryland

Regarding Recommendations For Unreserved Undesignated Fund Balance And Revenue Stabilization Fund

May 21, 2010

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The PFM Group

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Report to Montgomery County, Maryland

Regarding Recommendations for Unreserved Undesignated Fund Balance and Revenue Stabilization Fund
May 21, 2010

Table of Contents

I. Executive Summary

A. Rating History and Recent Rating Action

Montgomery County, Maryland is one of 23 Counties in the Country (as of April 30, 2010) who have been awarded a triple-A rating from all three major rating agencies. This rating category is reserved for the most financially secure, economically wealthy, best run governments. By virtue of its long-term demonstration of prudent financial management practices and the long-term strength of the local and regional economy, Montgomery County has been rated triple-A by Moody's since 1973, Standard & Poor's since 1974 and Fitch since 1993. The County highly values its ratings because it helps the County obtain the lowest cost of capital and most favorable borrowing terms, and assures the County of a ready market for its bonds.

Recently, on April 2 the County was placed on negative watch by Moody's Investors Services. This "Watchlist Negative" category means that Moody's has put the investor community and the County on notice that it intends to take a rating action within 90 days from the date the County was placed on Watch list. Ninety days from April 2 is July 1. While Moody's seeks to take action in 90 days – the practical reality is that the 90 days is a "targeted" period. This will be after the County's fiscal year-end and after the County will have passed its FY 2011 budget, both of which will be a factor in the Moody's analysis and will impact the action to be taken. The rating action taken could be either (1) to remove the County from "Watchlist Negative" and reaffirm the stable outlook, or (2) to downgrade the County, most likely to the Aa1 level. Technically, Moody's could continue the "Watchlist Negative" status (or reaffirm it) if it concludes there is additional near-term information which might meaningfully affect the outcome of the rating review.

A key reason for Moody's actions is the adverse impact the recession has had on the County's revenues, leading to a deterioration of the County's financial position, most notably a three year decline in its Fund Balances. We note that Standard & Poor's and Fitch have also indicated in their written reports that the County's weakened financial condition has highlighted credit concerns. While they have not yet taken a formal action to alter the County's rating status, the two other rating agencies are clearly watching as well to see what actions the County will take in the next few months. Any actions the County takes to protect its Moody's rating will positively affect the Standard & Poor's and Fitch ratings as well.

B. Report Objective

Montgomery County has developed a series of fiscal policies in order to guide management and elected officials in their policy and financial decision making. It is clear that the recession has exposed some areas in the County's fiscal policies which should be re-evaluated and strengthened. In light of the Moody's Watchlist action and concerns regarding the County's reserves raised by all three rating agencies, PFM has been asked to review the County's Fund Balance Policy, Revenue Stabilization Fund (RSF) legal provisions and other related policies in order to determine if these policies are adequate and if not, to suggest alternate policies for the County's consideration. Higher fund balance levels will clearly help preserve the County's Aaa rating; our challenge is to recommend a level that is adequate for the County's specific needs, but not greater than necessary. We understand that in any community there are pressures to limit the size of fund balance; the objective of this report is to identify the appropriate level of fund balance necessary to address Montgomery County's specific needs and in light of these other pressures, to not overstate the level necessary to maintain the Aaa rating.

C. Summary of PFM Recommendations

In order to prepare our report, we have reviewed the County's historical and most recent audited financial statements, proposed FY 2011 Budget, credit ratings reports published by Moody's, Standard & Poors and Fitch and other financial materials provided to us by the County Office of Management and Budget and Finance Department. We have also evaluated the County relative to other Aaa rated counties and have provided that analysis in Exhibit A attached hereto.

Based on our review of the economic volatility of key County revenue streams: the Income Tax, the recordation tax and the transfer tax, and on the average monthly level of cash flow expenditures, PFM is of the opinion that the County should:

#1) Act swiftly and decisively as part of the FY 2011 budget process to significantly restore target fund balance levels

- The combined fund balances of its unreserved, undesignated General Fund Balance and Revenue Stabilization Fund ("RSF") in FY 2011 should be restored to its current policy goal of 6% of tax supported resources.
- Simultaneously, the County should institute a multi-year plan to phase in a new policy which establishes higher unreserved undesignated General Fund Balance and Revenue Stabilization Fund to levels which reflect the County's specific liquidity needs given its cash flow and economically sensitive revenue streams.

#2) Amend local law with respect to the RSF (Please refer to Exhibit C for the section of the County Code that establishes the RSF.)

- Remove the provision which establishes a maximum amount permitted in the RSF.
- Provide for a mandatory contribution to the RSF equal to 0.5% of "Adjusted Governmental Fund Revenues". This provision would require a budgeted annual contribution until the combined ending balances of the General Fund and the RSF equals 10% of Adjusted Governmental Fund Revenues. "Adjusted Governmental Fund Revenues" are defined as revenues of all tax-supported County governmental and agency revenues, including operating grant and capital project revenues and explicitly excludes reserves applied to fund future expenditures.

#3) Establish and meet targets for the combined ending General Fund and RSF balance by FY 2020

- FY 2011 General Fund balance must be restored to 5% of prior year General Fund revenues.
- FY 2011 RSF must be restored to at least 1% of Adjusted Governmental Fund Revenues.
- Establish a planned annual contribution.
- Further, PFM recommends that the County needs to target and maintain a reserve balance (made up of unreserved, undesignated General Fund reserves and the Revenue Stabilization Fund) equal to 10% of Adjusted Governmental Fund Revenues.
- The County should plan to reach the reserve balance target no later than 2020.

#4) Strengthen its budget policy requiring the County to adopt a structurally balanced budget and to eliminate the ability to treat accumulated fund balance as revenue for the purpose of determining structural balance

D. Key Findings

These recommended target reserve levels will provide the County with sufficient reserves to protect itself from both intra-year cash flow shortfalls, as well as multi-year economic downturns similar to the levels experienced without having to resort to a mid-year tax increase.

#1) The proposed combined fund balance goal of 10% of Adjusted Governmental Fund Revenues is equal to approximately 36 days of revenues for all governmental funds. This is a minimum amount to maintain given that the one year drop in tax revenues experienced by the County in 2010 before consideration of the energy tax increase is equal to 16 days of Adjusted Governmental Fund Revenues, or 5.9% of prior year tax revenues.

#2) The County has undertaken an analysis of its economically volatile revenue streams; this analysis shows that the standard deviation during a five year period, which is the longest appropriate period to evaluate, is 5.8% of those revenues. The second largest revenue stream, the income tax, has experienced a 20% drop in a single year, and has a 15.5% standard deviation. This makes it very difficult to budget reliably, and thus requires a larger fund balance than other governments with less volatile revenue streams.

II. Comment on the Moody's, Standard & Poor's and Fitch Reports

All three rating agencies reserve their triple-A rating for the best run governments. The focus of this discussion will be Moody's, however we will also include some observations and concerns raised by the other two rating agencies. It is clear that the other two rating agencies, like Moody's, take negative trends seriously. Moody's analytic approach to rating General Obligation credits is outlined it its October 2009 publication "Moody's U. S. Public Finance Rating Methodology: General Obligation Bonds issued by U.S. Local Governments." This publication outlines the four rating factors Moody's considers and identifies the weighting assigned to each:

- Economic Strength: 40%
- Financial Strength: 30%
- Management & Governance: 20%
- Debt Profile: 10%

The rating agencies key concerns are highlighted below, with a quote from rating reports to substantiate our view of this as an important concern:

Rating Agency Comment #1 - Downward Pressure on the Rating

The County has been rated Aaa by Moody's investors service for 37 years. Based on a review of the Moody's report, we believe they are focusing their concerns on the second and third factors shown in the four bullet points. In taking its April 2nd action to place the County on Watchlist Review for Possible Downgrade Moody's indicated this could affect both the outstanding $1.8 billion of County General Obligation bonds as well as any future debt issued by the County. Moody's made the following statement:

> *"Placement on Watchlist for possible downgrade reflects deterioration of the County's financial position driven primarily by income tax revenue shortfalls, which is expected to result in the use of a significant portion of the County's General Fund and Revenue Stabilization Fund as of fiscal 2010 (year ends June 30th). Future rating reviews will factor (a)*

Resolution No:	16-1415
Introduced:	May 27, 2010
Adopted:	June 29, 2010

COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND

By: Council President at the Request of the County Executive

SUBJECT: Reserve and Selected Fiscal Policies

Background

1. Fiscal policy corresponds to the combined practices of government with respect to revenues, expenditures, debt management, and reserves.

2. Fiscal policies provide guidance for good public practice in the planning of expenditures, revenues, and funding arrangements for public services. They provide a framework within which budget, tax, and fee decisions should be made. Fiscal policies provide guidance toward a balance between program expenditure requirements and available sources of revenue to fund them.

3. As a best practice, governments must maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. Fund balance levels are a crucial consideration, too, in long-term financial planning. Credit rating agencies monitor levels of fund balance and unrestricted fund balance in a government's general fund to evaluate a government's continued creditworthiness.

4. In FY10, the County experienced an unprecedented $265 million decline in income tax revenues, and weathered extraordinary expenditure requirements associated with the H1N1 flu virus and successive and historic winter blizzards. The costs of these events totaled in excess of $60 million, only a portion of which was budgeted and planned for.

5. In a memorandum dated April 22, 2010, the County Executive recommended that the County Council restore reserves first to the current 6% policy level for FY11 and also to revise and strengthen policy levels in order to more appropriately position the County to weather economic cycles in the future, and to achieve structural balance in future budgets.

6. The County's financial advisor has recommended that the County strengthen its policy on reserves and other fiscal policies to ensure budget flexibility and structural stability, and has provided specific recommendations, which are reflected below.

Action

The County Council for Montgomery County, Maryland, approves the following policies regarding reserves and other fiscal matters:

1. Structurally Balanced Budget

   Montgomery County must have a goal of a structurally balanced budget. Budgeted expenditures should not exceed projected recurring revenues plus recurring net transfers in minus the mandatory contribution to the required reserve for that fiscal year. Recurring revenues should fund recurring expenses. No deficit may be planned or incurred.

2. Reserves

   Montgomery County must have a goal of achieving the Charter §310 maximum for the reserve in the General Fund of 5% of General Fund revenues in the preceding fiscal year, and of building up and maintaining the sum of Unrestricted General Fund Balance and Revenue Stabilization Fund Balance to 10% of Adjusted Governmental Fund revenues, as defined in the Revenue Stabilization Fund law. This goal must be reflected in the Revenue Stabilization Fund law.

3. Use of One-Time Revenues

   One-time revenues and revenues in excess of projections must be applied first to restoring reserves to policy levels or as required by law. If *the County determines that reserves have been fully funded, then one-time revenues should be applied to non-recurring expenditures which are one-time in nature, PAYGO for the CIP in excess of the County's targeted goal, or to unfunded liabilities. Priority consideration should be given to unfunded liabilities for Retiree Health Benefits (OPEB) and Pension Benefits Prefunding.*

4. PAYGO

   The County should allocate to the CIP each fiscal year as PAYGO at least ten percent of the amount of general obligation bonds planned for issue that year.

5. Fiscal Plan

   The County should adopt a fiscal plan that is structurally balanced, and that limits expenditures and other uses of resources to annually available revenues. The fiscal plan should also separately display reserves at policy levels, including additions to reserves to reach policy level goals.

6. Reports to Council

The Executive must report to the Council:

a. the prior year reserve and the current year reserve projection as part of the November fiscal plan update;
b. current and projected reserve balance in the Executive's Annual Recommended Operating Budget;
c. any material changes expected to have a permanent impact on ending reserve fund balance; and
d. current and projected reserve balances in any proposed mid-year savings plan.

This is a correct copy of Council action.

Mary Anne Paradise

Mary Anne Paradise, Acting Clerk of the Council

Bill No. 36-10
Concerning: Finance - Revenue Stabilization Fund – Amendments
Revised: June 28, 2010 Draft No. 4
Introduced: May 27, 2010
Enacted: June 29, 2010
Executive: July 7, 2010
Effective: October 4, 2010
Sunset Date: None
Ch. 33, Laws of Mont. Co. 2010

COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND

By: Council President at the Request of the County Executive

AN ACT to:

(1) repeal the limit on the size of the Revenue Stabilization Fund;
(2) modify the requirement for mandatory County contributions to the Revenue Stabilization Fund; and
(3) generally amend the law governing the Revenue Stabilization Fund.

By amending
Montgomery County Code
Chapter 20, Finance
Article XII
Sections 20-65, 20-66, 20-68, 20-69, 20-70, 20-71 and 20-72

By repealing
Montgomery County Code
Chapter 20, Finance
Article XII
Section 20-67

Boldface	*Heading or defined term.*
Underlining	*Added to existing law by original bill.*
[Single boldface brackets]	*Deleted from existing law by original bill.*
Double underlining	*Added by amendment.*
[[Double boldface brackets]]	*Deleted from existing law or the bill by amendment.*
* * *	*Existing law unaffected by bill.*

The County Council for Montgomery County, Maryland approves the following Act:

Sec. 1. Sections 20-65, 20-66, 20-68, 20-69, 20-70, 20-71 and 20-72 are amended and Section 20-67 is repealed as follows:

20-65. Definitions.

In this Article the following terms have the following meanings, unless the context clearly indicates a different meaning:

[(a)] *Actual total revenues* means the combined total of income tax, real property transfer tax, recordation tax, and investment income, as reported in the County's annual financial report.

Adjusted Governmental Revenues means tax-supported County Governmental Funds revenues, plus revenues of the:

(1) County Grants Fund;

(2) County Capital Projects Fund;

(3) tax supported funds of the Montgomery County Public Schools, not including the County's local contribution;

(4) tax supported funds of Montgomery College, not including the County's local contribution; and

(5) tax supported funds of the Montgomery County portion of the Maryland-National Capital Park and Planning Commission.

[(b) *Certified revenues* means revenues derived each fiscal year from the income tax, real property transfer tax, recordation tax, and investment income of the General Fund as certified by the Director on or before June 15.]

[(c) *Debt Service Fund* means the fund used to accumulate funds to pay general long-term debt principal, interest and related costs.]

[(d)] *Director* means the Director of the Department of Finance.

Excess revenue means the amount, if positive, by which actual total revenues from the income tax, real property transfer tax, recordation tax, and investment income of the General Fund for the fiscal year exceed the original projections for these amounts.

[(e)] *Fund* means the Revenue Stabilization Fund created under this Article.

[(f)] *General Fund* means the general operating fund of the County which is used to account for all revenues and expenditures, except revenues and expenditures required to be accounted for in another fund.

[(g)] *Income tax* means the County income tax imposed under state law.

[(h)] *Investment income of the General Fund* means income from the investment of revenues that is reported in the General Fund.

[(i)] *Original projection* means the projection of total General Fund revenues for the next fiscal year approved by the County Council in the "Schedule of Revenue Estimates and Appropriations" resolution or any similar resolution.

[(j)] *Real property transfer* tax means the tax imposed under Sections 51-19 et. seq.

[(k)] *Recordation tax* means the tax imposed under Sections 12-101 et. seq., Tax-Property Article, [Annotated Code of] Maryland Code.

[(l)] *Revised forecast* means any revised projection of total General Fund revenues for the next fiscal year prepared by the Department of Finance.

Total reserve means the sum of the reserve in the Fund plus the Unrestricted General Fund Balance.

Unrestricted General Fund Balance means the residual portion of the General Fund fund balance that has not been reserved, restricted, or encumbered for later years' expenditures.

20-66. Revenue Stabilization Fund.

(a) The Director may establish a Revenue Stabilization Fund to support appropriations which have become unfunded.

(b) The Fund is continuing and non-lapsing.

(c) The Fund is in addition to any surplus that is accumulated under Section 310 of the County Charter.

20-67. [Fund sources and maximum size.] Reserved.

[(a) The Fund must not exceed 10 percent of the average aggregate annual revenue derived from the income tax, real property transfer tax, recordation tax, and investment income of the General Fund in the 3 preceding fiscal years.

(b) The Director must compute the maximum amount of the Fund annually and report that amount to the County Council not later than June 15.

(c) The Fund is in addition to any surplus that may be accumulated under Section 310 of the County Charter.]

20-68. Mandatory contribution to Fund.

[(a) Subject to the limit set in Section 20-67(a), the] The mandatory annual contribution to the Fund must equal the greater of:

(a) [50 percent of the product of the certified revenues estimated for the current fiscal year times the difference between:

(1) the annual percentage increase in the certified revenues projected for the next fiscal year, and

(2) the average annual percentage increase in the certified revenues collected in the 6 fiscal years immediately preceding the next fiscal year.] 50 percent of [[the]] any excess revenue [[amount

by which actual total revenues from the income tax, real property transfer tax, recordation tax, and investment income of the General Fund for the next fiscal year exceed the original projections for these amounts]]; or

(b) an annual amount [[that does not exceed]] equal to the lesser of 0.5 percent of the Adjusted Governmental Revenues [[for the current year, but which does not result in the sum of the current year-end projected Unrestricted General Fund Balance and the Fund to exceed]] or the amount needed to obtain a total reserve of 10 percent of the Adjusted Governmental Revenues.

[(b) A growth or decline in certified revenues which results from either an increase or decrease in County tax rates must be:

(1) excluded from revenues projected for the next fiscal year, and

(2) phased in in the average annual percentage increase calculation in the third, fourth, fifth and sixth years.

(c) If actual total revenues from the income tax, real property transfer tax, recordation tax, and investment income of the General Fund for the next fiscal year exceed the original projection, then 50 percent of the excess must be transferred to the Fund if doing so will not result in the 10 percent limit in Section 20-67(a) being exceeded.]

20-69. Discretionary contributions to Fund.

The County Executive may recommend and the County Council may by resolution approve additional contributions to the Fund [if doing so will not result in the 10 percent limit in Section 20-67(a) being exceeded].

20-70. Transfer of contributions.

The Director must transfer the mandatory contributions required by Section 20-68 and any discretionary contributions under Section 20-69 from the General [fund] <u>Fund</u> to the Fund at the end of each fiscal year.

20-71. Interest.

All interest earned on the Fund must be added to the Fund. [However, the Director must transfer interest earned on the Fund when the Fund exceeds 50 percent of the maximum Fund size authorized by Section 20-67(a) to the Debt Service Fund as an offset to the approved issuance of general obligation debt.]

20-72. Use of Fund.

[[(a) After holding a public hearing and seeking the recommendation of the Executive, and if the Council finds that reasonable reductions in expenditures are not sufficient to offset the shortfall in revenue, the Council may by resolution approved by the Executive transfer an amount from the Fund to compensate for no more than half of the difference between the original projection of total General [fund] <u>Fund</u> revenues for that fiscal year and a revised forecast of the General Fund revenues projected for the same fiscal year. If the Executive disapproves a resolution within 10 days after it is transmitted and the Council readopts it by a vote of 6 Councilmembers, or if the Executive does not act within 10 days after it is transmitted, the resolution takes effect.]]

[[(b) However, a transfer must not be approved unless 2 of the following conditions are met:

(1) The Director estimates that total General Fund revenues will fall more than 2 percent below the original projected revenues.

(2) Resident employment in the County has declined for 6 consecutive months compared to the same month in the previous year.

(3) The [local] most recent regional index of leading economic indicators, published by the Center for Regional Analysis, George Mason University, or a successor index determined by the Department of Finance, has declined for 3 consecutive months.]]

[[(c) The cumulative transfers from the Fund in any single fiscal year must not exceed half of the balance in the Fund at the start of that fiscal year.]]

[[(d) The funds transferred may only be used to support appropriations which have become unfunded.]]

[[(e)]] By an affirmative vote of 6 Councilmembers, the Council, after holding a public hearing, reviewing relevant economic indicators, and seeking the recommendation of the Executive, may transfer [[amounts]] any amount from the Fund to the General Fund [[without regard to the limits and conditions in subsections (a)-(c)]] to support appropriations which have become unfunded.

Approved:

6/30/10

Nancy M. Floreen, President, County Council — Date

Approved:

July 7, 2010

Isiah Leggett, County Executive — Date

This is a correct copy of Council action.

July 12, 2010

Linda M. Lauer, Clerk of the Council — Date

Resolution No: 17-312
Introduced: November 29, 2011
Adopted: November 29, 2011

COUNTY COUNCIL
FOR MONTGOMERY COUNTY, MARYLAND

By: Government Operations and Fiscal Policy Committee

SUBJECT: Reserve and Selected Fiscal Policies

Background

1. Fiscal policy corresponds to the combined practices of government with respect to revenues, expenditures, debt management, and reserves.

2. Fiscal policies provide guidance for good public practice in the planning of expenditures, revenues, and funding arrangements for public services. They provide a framework within which budget, tax, and fee decisions should be made. Fiscal policies provide guidance toward a balance between program expenditure requirements and available sources of revenue to fund them.

3. As a best practice, governments must maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. Fund balance levels are a crucial consideration, too, in long-term financial planning. Credit rating agencies monitor levels of fund balance and unrestricted fund balance in a government's general fund to evaluate a government's continued creditworthiness.

4. In FY10, the County experienced an unprecedented $265 million decline in income tax revenues, and weathered extraordinary expenditure requirements associated with the H1N1 flu virus and successive and historic winter blizzards. The costs of these events totaled in excess of $60 million, only a portion of which was budgeted and planned for.

5. In a memorandum dated April 22, 2010, the County Executive recommended that the County Council restore reserves first to the current 6% policy level for FY11 and also revise and strengthen policy levels in order to more appropriately position the County to weather economic cycles in the future, and to achieve structural balance in future budgets.

6. The County's financial adviser recommended that the County strengthen its policy on reserves and other fiscal policies to ensure budget flexibility and structural stability, and provided specific recommendations, which are reflected below.

7. On June 29, 2010 the Council approved Resolution No. 16-1415, *Reserve and Selected Fiscal Policies*. This Resolution established a goal of achieving the Charter §310 maximum for the reserve in the General Fund of 5% of General Fund revenues in the preceding fiscal year, and of building up and maintaining the sum of Unrestricted General Fund Balance and Revenue Stabilization Fund Balance to 10% of Adjusted Governmental Revenues (AGR), as defined in the Revenue Stabilization Fund law.

8. The County's reserve policy should be further clarified and strengthened. This resolution replaces the reserve policy established in Resolution No. 16-1415.

Action

The County Council for Montgomery County, Maryland approves the following policies regarding reserve and selected fiscal matters:

1. *Structurally Balanced Budget*

Montgomery County must have a goal of a structurally balanced budget. Budgeted expenditures should not exceed projected recurring revenues plus recurring net transfers in minus the mandatory contribution to the required reserve for that fiscal year. Recurring revenues should fund recurring expenses. No deficit may be planned or incurred.

2. *Use of One-Time Revenues*

One-time revenues and revenues in excess of projections must be applied first to restoring reserves to policy levels or as required by law. If the County determines that reserves have been fully funded, then one-time revenues should be applied to non-recurring expenditures that are one-time in nature, PAYGO for the CIP in excess of the County's targeted goal, or unfunded liabilities. Priority consideration should be given to unfunded liabilities for retiree health benefits (OPEB) and pension benefits prefunding.

3. *PAYGO*

The County should allocate to the CIP each fiscal year as PAYGO at least 10% of the amount of general obligation bonds planned for issue that year.

4. *Fiscal Plan*

The County should adopt a fiscal plan that is structurally balanced, and that limits expenditures and other uses of resources to annually available revenues. The fiscal plan should also separately display reserves at policy levels, including additions to reserves to reach policy level goals.

5. *County Government Reserve*

(a) **County Government Reserve.** The County Government Reserve has three components. The components of the budgeted reserve at the end of the next fiscal year are:

(i) **Reserve in the General Fund**. The County's goal is that this reserve will be the maximum permitted by §310 of the Charter, which is 5% of revenues in the General Fund in the previous fiscal year;

(ii) **Reserve in the Revenue Stabilization Fund (RSF).** This budgeted reserve at the end of the next fiscal year is the reserve at the beginning of the year, plus interest on the fund balance, plus a mandatory transfer from the General Fund, as defined in the Revenue Stabilization Fund law, plus a discretionary transfer if the Council approves one. The actual amount of the mandatory transfer is calculated in accordance with §20-68 of the Montgomery County Code; and

(iii) **Reserve in the other tax supported funds in County Government.** The budgeted reserve at the end of the next fiscal year for the following funds – Fire, Mass Transit, Recreation, Urban District, Noise Abatement, Economic Development, and Debt Service – and any other tax supported County Government fund established after adoption of this resolution, should be the minimum reserve possible (as close as possible to zero, but not negative), since the Council sets the property tax rate to the nearest one tenth of 1¢.

(b) **Calculation of budgeted reserve as a percent of Adjusted Governmental Revenues.** The target reserve as a percent of Adjusted Governmental Revenues is the sum of the reserves in the General Fund and the Revenue Stabilization Fund divided by Adjusted Governmental Revenues, as defined in the Revenue Stabilization Fund law. The reserves in the other tax supported funds in County Government are not included in this calculation.

(c) **Budgeted reserve as a percent of Adjusted Governmental Revenues.** To reach the County's goal of 10% of AGR in 2020, the annual minimum target goals are:

FY13	6.4%
FY14	6.9%
FY15	7.4%
FY16	7.9%
FY17	8.4%
FY18	8.9%
FY19	9.4%
FY20 and after	10.0%

The Council may make a discretionary transfer each year from the General Fund to the Revenue Stabilization Fund, if necessary, to reach the target goal for each year. The 10% goal for FY20 and after must be reflected in the Revenue Stabilization Fund law.

6. *Reserves in other agencies*

The reserves for the Montgomery County Public Schools (MCPS), the Maryland-National Capital Park and Planning Commission (M-NCPPC), and Montgomery College (MC) are not included in the target reserves for County Government. The County's reserve policies for these agencies are:

(a) **MCPS.** The Council should not budget any reserve for the MCPS Current Fund.

(b) **M-NCPPC.** The reserve in the Park Fund should be approximately 4.0% of budgeted resources. The reserve in the Administration Fund should be approximately 3.0% of budgeted resources. The reserve in the Advance Land Acquisition Debt Service Fund should be the minimum reserve possible, since the Council sets the property tax rate to the nearest one tenth of 1¢.

(c) **Montgomery College.** The reserve in the Current Fund should be 3.0% - 5.0% of budgeted resources minus the annual contribution from the County. The target reserve in the Emergency Plant Maintenance and Repair Fund – as stated in Resolution No. 11-2292, approved by the Council on October 16, 1990 – "may accumulate up to $1,000,000 in unappropriated fund balance, such goal to be attained over a period of years, as fiscal conditions permit."

7. *Reports to Council*

The Executive must report to the Council:

(a) the prior year reserve and the current year reserve projection as part of the annual November/December fiscal plan update;
(b) current and projected reserve balance in the Executive's annual Recommended Operating Budget;
(c) any material changes expected to have a permanent impact on ending reserve fund balance; and
(d) current and projected reserve balances in any proposed mid-year savings plan.

This is a correct copy of Council action.

Linda M. Lauer

Linda M. Lauer, Clerk of the Council

The Financial Impact of a Credit Rating Downgrade

April 2018

Prepared by the Montgomery County Department of Finance

A credit rating reflects a nationally recognized statistical rating organization's independent opinion of the creditworthiness of an issuer of bonds and the likelihood the issuer will make timely and required debt service payments on outstanding bonds. The question as to the relative costs associated with being downgraded from an AAA rated county is not answered with a simple mathematical calculation. Below, we attempt to both define and quantify the impacts of a downgrade in the County's general obligation bond rating on various components of the County's financial operations, and especially on its borrowing and transaction costs.

Nearly every single financial transaction that the County enters into with a financial institution has some element of risk for that institution and that risk has a price associated with it. So from a more subjective standpoint, a lower rated county pays more for banking services and credit card merchant fees, receives less interest on investments, pays higher lockbox fees, has a less lucrative P-card rebate program, pays higher fees for financial advisors and bond counsel, pays higher underwriting and remarketing fees, etc.

It would be difficult, if not impossible, to quantify all of the additional costs associated with being a lower rated county. Too many subjective and objective attributes are calculated and considered in pricing certain financial services. However, as a triple AAA rated issuer of debt, and one of the top 250 counties in the nation issuing debt, it is highly probable that Montgomery County is paying some of the lowest fees for its financial services and, more importantly, has one of the lowest costs of funds.

It is not difficult to quantify in dollars some of the more obvious differences in higher and lower rated general obligation debt. For example, if the County priced its $687 million of general obligation bonds sold on October 31, 2017 as an AA+ rated issuer, over the 20-year life of that bond issue, the County would pay approximately $7.0 million more in interest expense. In the current market the average spread between AAA and AA+ interest rates is about 15 basis points (0.15%). To place this additional cost in the context of the County's 6-year $4.521 Billion CIP program, if one assumes equal future annual borrowings; debt service would increase by about $36 million.

The County maintains standby liquidity facilities to back its $670 million variable rate note programs. These programs include the County's $500 million commercial paper program (BANs) and its $170 variable rate demand obligation program. Based on information provided by the County's financial advisor, as an AA+ rated issuer of short-term notes, the County would pay an additional 20 basis points for its lines of credit. In real terms, the additional annual fee would be $1.34 million. Again, that is an annual fee for programs, which at different amounts, have been in place since 1988.

Typically, debt issued by the County that is subject to annual appropriation, including lease revenue bonds and certificates of participation, is rated one or two notches below the County's AAA rated general obligation bonds. Each rating notch costs approximately 15 basis points in the current market. Therefore, if the general obligation bonds are downgraded from AAA to AA+, the appropriation backed debt would also be downgraded from AA+ or AA to AA or AA-.

The average basis point spread over the last year between an AA+ bond and an AA bond with a maturity of 10 years is about 11 basis points. The County issued certificates of participation for about $24.8 million in July 2016. The certificates were rated Aa1; had they been rated Aa2, the additional debt service cost over the life of the certificates would have been about $275,000.

Another example of the benefit of the AAA rating is the access to the credit markets. During and after the Great Recession and financial crisis, the County was able to maintain its access to a liquidity facility for its commercial paper program because of its strong credit rating. During this same time period other lower rated municipalities were not able to access the credit markets or paid significant premium for market access.

The last few examples of costs associated with being a lower rated county are probably some of the most obvious and expensive examples. Since FY12 the County has been able to save over $112.7 million in long term debt service savings through bond refundings. This level of savings would not have been possible without the County's strong credit rating. The County has a $70 million master lease program, through which over the last 12 years it has leased various assets such as computer equipment, fire trucks, ambulances, and buses. The County also has a $40 million master lease line of credit to finance energy performance savings contracts. Without question, the cost of these leases would have been higher if the County had lower ratings. Over the last few decades, the County frequently issued debt that did not fall into the categories described above. The County issued development district bonds, various varieties of revenue bonds, term notes, short term debt for bus, safety apparatus, and equipment financings, and acted as a conduit issuer for not-for-profit borrowers. Suffice it to say, all those terms would have been more costly had the County been lower rated.

Finally, one should remember that a credit rating downgrade has an adverse impact on the price and yield of debt offered in the primary market, but it also has an adverse impact on the price and yield on existing debt in the secondary market. After a credit rating downgrade, the investor who owns a AAA rated County bond, now owns a lower rated security that is worth less than before the credit rating downgrade. Credit rating downgrades, or the perceived risk of a potential credit rating downgrade, are viewed negatively by investors and typically result in lower bond prices and higher interest rates paid by the County.

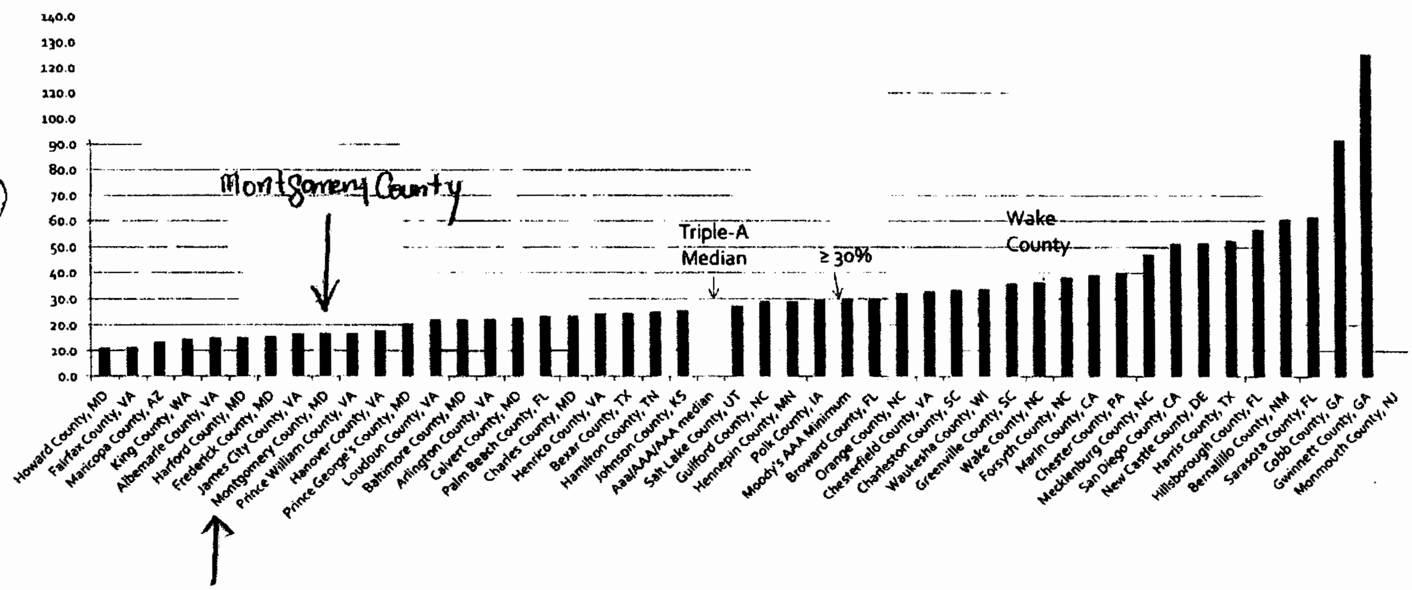
For decades, the County has enjoyed and benefited from having the highest ratings from all three rating agencies. In the municipal bond market, the name Montgomery County, Maryland is synonymous with the highest quality bonds. County bonds often trade at levels equal in price and yield to similarly rated state bonds. There are only 46 other counties in the United States enjoy AAA ratings from all three rating agencies and only 14 of those have populations greater than 900,000 people. While it is difficult to achieve and maintain that status, from a financial perspective the rewards are voluminous.

Fund Balance

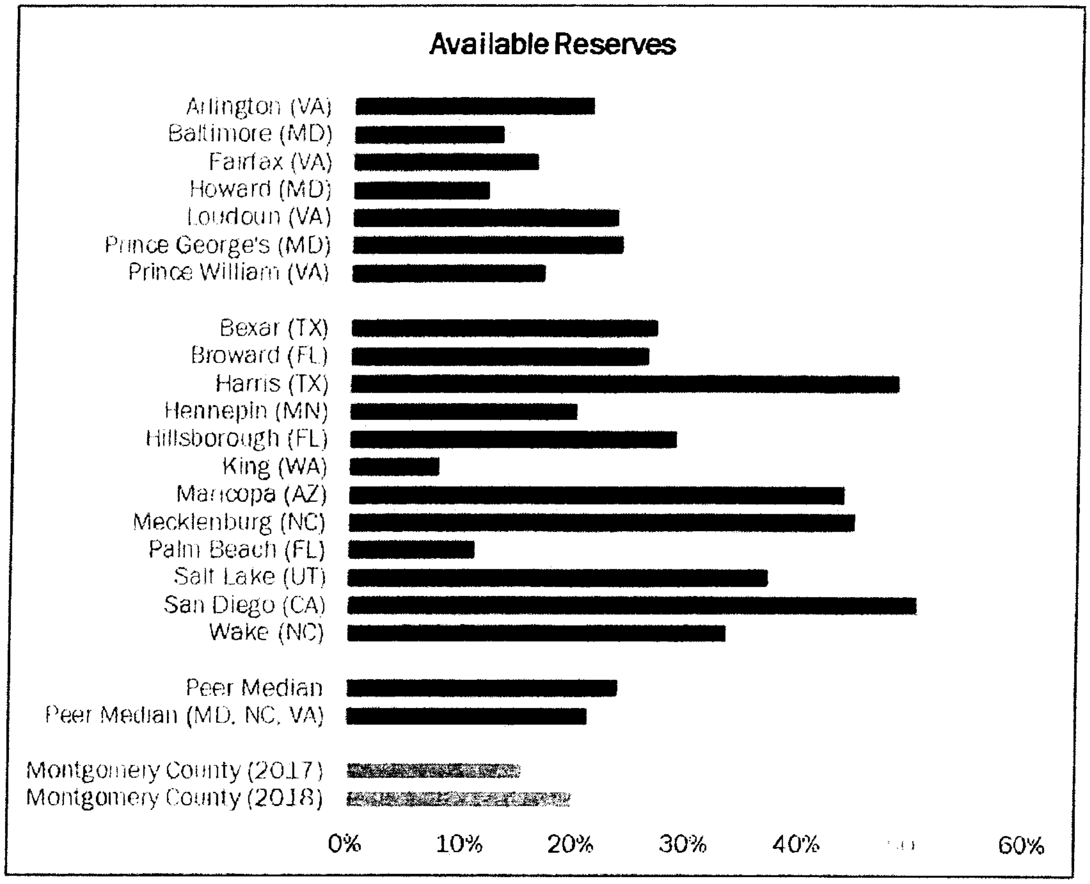
- Adequate Reserves That Meet Standards of Aaa/AAA/AAA Counties
- We define this value for Wake County as ≥ 30% Combined General Fund and Debt Service Fund Revenues

Aaa/AAA/AAA Counties: Operating Funds Balance as % of Revenues

23



	Population	Available Fund Balance as % of Revenues
Montgomery County, MD	**1,017,859**	**16.6%**
National Aaa County Median	452,369	28.5%
Peer County Group Median	1,128,722	23.5%
Arlington County, VA	223,945	22.3%
Baltimore County, MD	822,959	21.0%
Bexar County, TX	1,825,502	23.5%
Broward County, FL	1,843,152	25.6%
Fairfax County, VA	1,128,722	15.5%
Harris County, TX	4,356,362	28.3%
Hennepin County, MN	1,197,776	27.6%
Hillsborough County, FL	1,302,884	28.3%
Howard County, MD	304,115	10.4%
King County, WA	2,045,756	14.4%
Loudoun County, VA	351,129	22.1%
Maricopa County, AZ	4,018,143	50.8%
Mecklenburg County, NC	990,288	47.4%
Palm Beach County, FL	1,378,806	11.2%
Prince George's County, MD	892,816	12.3%
Prince William County, VA	437,271	15.5%
Salt Lake County, UT	1,078,958	26.0%
San Diego County, CA	3,223,096	43.9%
Wake County, NC	976,019	36.3%



Source: Moody's MFRA Database
Prepared by Davenport & Company LLC

The scorecard outcome will not match the actual rating in every case, for a number of reasons including the following:

» Our methodology considers forward-looking elements that may not be captured in historical data

» The scorecard is a summary that does not include every rating consideration

» In some circumstances, the importance of one factor may escalate and transcend its prescribed weight in this methodology

EXHIBIT 1

Scorecard Factors and Weights

Local Governments

Broad Rating Factors	Factor Weighting	Rating Sub-factors	Sub-factor Weighting
Economy/Tax Base	30%	Tax Base Size (full value)	10%
		Full Value Per Capita	10%
		Wealth (median family income)	10%
Finances	30%	Fund Balance (% of revenues)	10%
		Fund Balance Trend (5-year change)	5%
		Cash Balance (% of revenues)	10%
		Cash Balance Trend (5-year change)	5%
Management	20%	Institutional Framework	10%
		Operating History	10%
Debt/Pensions	20%	Debt to Full Value	5%
		Debt to Revenue	5%
		Moody's-adjusted Net Pension Liability (3-year average) to Full Value	5%
		Moody's-adjusted Net Pension Liability (3-year average) to Revenue	5%

Our scorecard metrics are limited to major rating drivers that are common to most issuers. Outside of these drivers, we may adjust the scorecard outcome for a variety of "below-the-line" adjustments, which are more idiosyncratic factors that are likely not to apply to all issuers, but that can impact credit strength. The adjusted scorecard outcome is based quantitatively on the "above-the-line" factors, combined with any "below-the-line" notching adjustments. The adjusted scorecard outcome is a guideline for discussion, but does not determine the final rating. The final rating is determined by a committee, which considers, but is not bound by, the adjusted scorecard outcome.

About the Rated Universe

A local government is a subdivision of a state, most commonly a city[2], county, or school district. The provisions establishing local governments are typically enumerated in each state's constitution. Most states have local government laws governing the authorities and responsibilities of the political subdivisions within each state.

Local governments provide public services such as police and fire protection, courts, property records, public works maintenance, and water and sewer services. Cities or counties can also be responsible for

[2] We use the term "city" interchangeably with terms such as Town, Township, Village, and Borough.