COMPTROLLER of MARYLAND
Serving the People

Peter Franchot
Comptroller

Sandra Zinck
Interim Director
General Accounting Division

August 31, 2017

The Honorable Peter Franchot
Comptroller of Maryland
Comptroller's Office
80 Calvert Street
Annapolis, Maryland 21404

Dear Comptroller Franchot:

Enclosed you will find the statement of General Fund Balance for the year ended June 30, 2017. In addition, you will find a schedule of General Fund revenues and an analysis of the variances between the 2017 estimated and actual revenues prepared by the Bureau of Revenue Estimates.

The State closed the fiscal year ended June 30, 2017 with a fund balance of $258.5 million in the General Fund. Of this amount $2.2 million was assigned by the 2017 General Assembly for fiscal year 2018 operations leaving an unassigned fund balance of $256.3 million.

Please advise me if you have any questions or would like additional information.

Sincerely,

Sandra L. Zinck
Director, General Accounting Division

SZ:mh

Enclosures

cc: The Honorable David Brinkley
The Honorable Nancy Kopp
Mr. Warren Deschenaux
Mr. Len Foxwell
Ms. Sharonne Bonardi
Mr. Andrew Schaufele

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General Fund Balance
June 30, 2017

General Fund Balance, June 30, 2016		$ 384,503,037
Add:		
2017 Estimated Revenues (Board of Revenue Estimates March 2017)		16,586,016,737
Adjustments to Revenues (See detail)		22,388,000
Reimbursement from reserve for Tax Credits		29,475,000
Other adjustments to revenue - 2017 Session:		
Transfer from other funds (See detail)		32,500,000
Transfer from Revenue Stabilization Account		170,000,000
Deduct:		
2017 General Fund Appropriations		
Appropriated by 2016 General Assembly	$ 17,288,781,941	
Specific reversions (See detail)	(125,788,821)	
Estimated agency reversions	(30,000,000)	
Net appropriations		(17,132,993,120)
Estimated 2017 General Fund Balance		91,889,654
Add:		
Excess of Actual Revenues over estimates	90,302,674	
Excess of Actual Transfers over estimates	2,262,764	
		92,565,438
Add:		
Excess of Actual Reversions over estimates		74,094,863
Total General Fund Balance		258,549,955
Deduct:		
General Fund Balance Reserved for 2018 Operations	91,889,654	
Minus 2018 Estimated Surplus	(89,684,940)	
		2,204,714
2017 Unassigned General Fund Balance		$ 256,345,241

EXHIBIT A

GENERAL FUND BUDGET SUMMARY

Detail - Fiscal Year 2017

Adjustments to Revenues - Other	
Lottery Revenue - BPW Reduction	$ 982,000
Volkswagen Settlement Revenue	12,000,000
Maryland Environmental Service	2,000,000
Lottery Revenue - Reduce Chapter 727 of 2016 transfer	500,000
Veteran's Cemetery Funding	236,000
Moody's Settlement Revenue	6,000,000
Debt Settlement Services Complany Settlement	200,000
Questcor Pharmaceuticals Settlement	470,000
Total	$ 22,388,000
Transfers from Other Funds	
University System of Maryland - Fund Balance Transfer (2017 Session)	$ 30,000,000
Public Safety - Maryland Correctional Enterprises (2017 Session)	2,500,000
Total	$ 32,500,000
Specific Reversions	
Restricted Funding	
DGS - Critical Maintenance	$ (500,000)
DHMH - Behavioral Health Administration	(2,130,000)
DHMH - Supports Intensity Scale and Individual Indicator Rating	(214,000)
DHMH - Entry Points report	(100,000)
Children's Cabinet - Youth Services Bureaus and case management	(3,489,624)
MHEC - Various legislative initiatives	(1,100,000)
Commerce - Biotechnology Business Support	(400,000)
Reserve Fund - Restricted funds in the Revenue Stabilization Account	(79,959,234)
DHMH - DDA case load trends	(17,097,963)
Public Safety - Vacant position salary savings	(5,000,000)
MSDE - Non-public placements	(5,000,000)
MSDE - Out of County Placements	(200,000)
MDE PAYGO - Drinking Water Revolving Loan Fund	(3,003,000)
MDE PAYGO - Water Quality Revolving Loan Fund	(6,792,000)
MDE - Operations	(803,000)
Total	$ (125,788,821)

STATE OF MARYLAND
State Reserve Fund
June 30, 2017
(In Dollars)

	Revenue Stabilization Account (Rainy Day) A0101 (fund 0201)	Dedicated Purpose Account A0201 (fund 0202)	Economic Development Opportunity (Sunny Day) A0301 (fund 0203)	Catastrophic Event Account A0401 (fund 0204)	Total
Beginning Balance - July 1, 2016	$ 832,390,041	$ 2,500,000	$ 26,243,339	$ 10,172,937	$ 871,306,317
Investment Earnings	14,725,784				14,725,784
Replenishment	155,376,558		5,000,000		160,376,558
Distributions/Transfers	(170,000,000)	(2,499,500)	(9,509,725)	(2,943,526)	(184,952,751)
Ending Balance - June 30, 2017	$ 832,492,383	$ 500	$ 21,733,614	$ 7,229,411	$ 861,455,908

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Peter Franchot
Comptroller

Andrew Schaufele
Director
Bureau of Revenue Estimates

August 31, 2017

To: Honorable Peter Franchot
Honorable Nancy K. Kopp
Secretary David R. Brinkley

From: Andrew Schaufele
Director, Bureau of Revenue Estimates

Subject: Fiscal Year 2017 Revenues

General fund revenues in fiscal year 2017 were $16,698.7 million, an increase of 3.1% over fiscal year 2016, and 0.5% or $90.3 million above estimate. The ongoing growth rate for the general fund was also 3.1% – an improvement on fiscal year 2016, to be sure, but remains tepid and still yet may be explained by other factors, outlined below. As we have mentioned previously, this economic expansion continues to benefit some, but not all; households dependent upon wage income continue to experience only moderate wage growth and, for some, heightened economic insecurity, which in turn deters taxable spending, as illustrated by the sluggish 2.1% growth in sales and use taxes. Antiquated sales tax policy that has not adapted to the current retail environment serves to further restrain sales tax growth. On a more positive note, ongoing withholding growth seems to be settling in around 4.5%, having maintained that rate for approximately three years; while lower than in other expansionary periods, the consistency of the growth is a welcome signal of aggregate stability.

Income Tax

Driving the positive variance was the personal income tax, up 5.9% in fiscal year 2017. In a departure from recent years, non-wage income growth did not contribute to the variance in a significant manner; non-withholding revenue declined 9.6% and was under the estimate by 1.7% (see chart below for volatility and recent results). As non-withholding was just 8% of the income tax, this variance is fairly immaterial. Rather, it was withholding that was the source of growth, finishing the fiscal year up 6.2% and 1.1% above the estimate. While a 1.1% variance may seem relatively insignificant, withholding accounts for the other 92% of the income tax and 50% of total ongoing general fund revenues. This would appear to indicate that underlying wage growth has accelerated; however, in reality, wage growth has merely met expectations. An investigation into withholding payments revealed that pay period timing may explain the variance.

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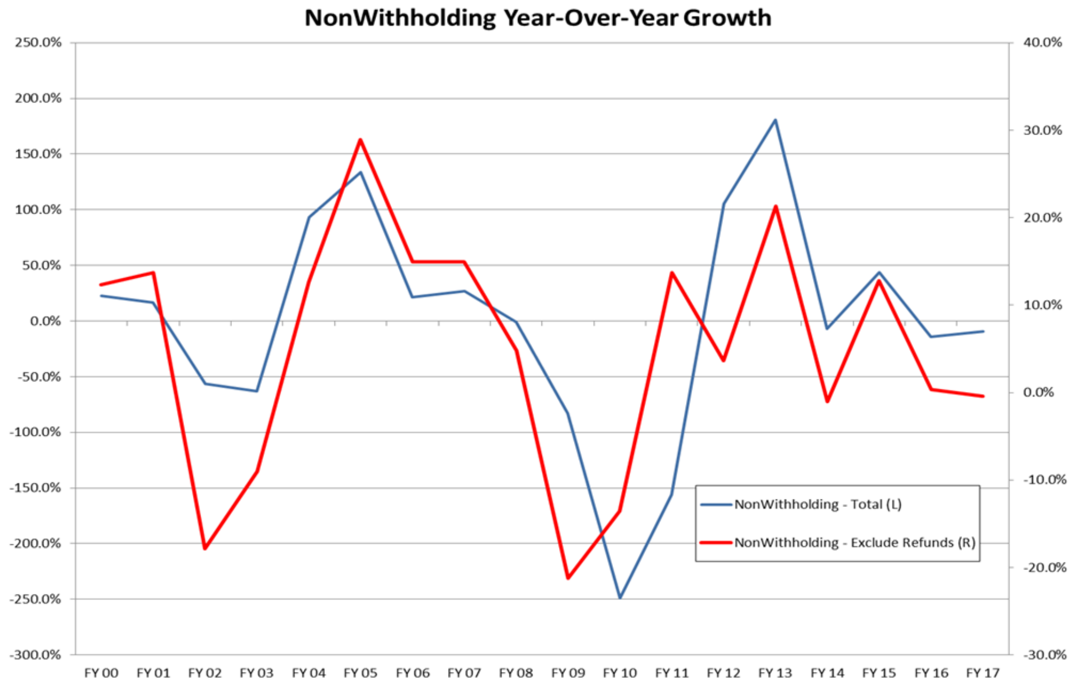
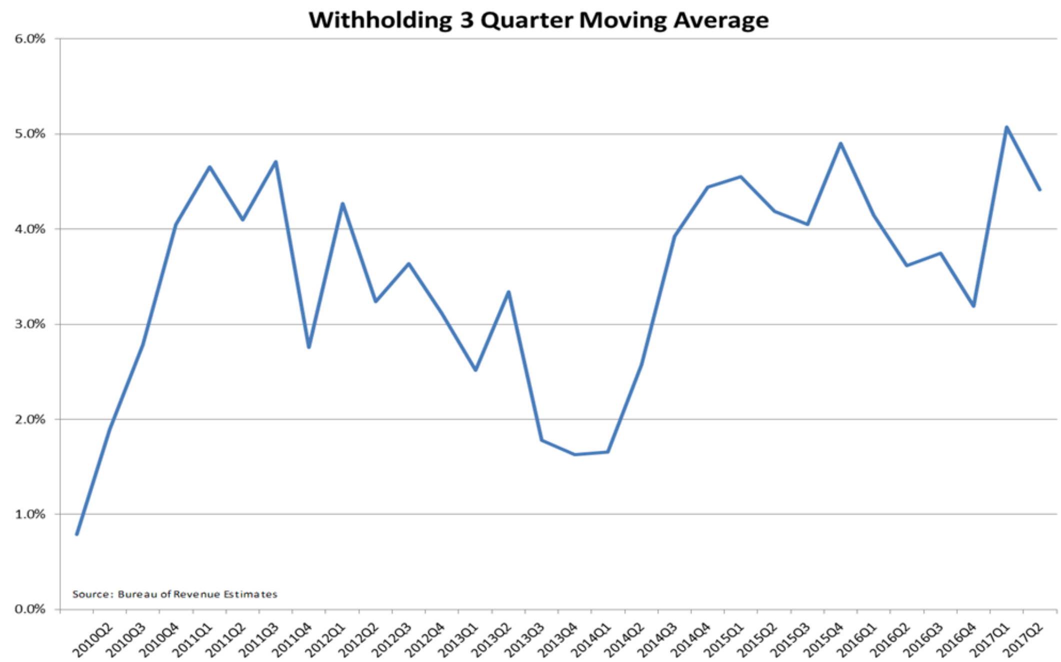


Joint research from the Revenue Accounting Section and Bureau of Revenue Estimates shows that employer pay periods can trigger significant shifts in withholding revenue from one year to another. We examined the top 60 withholding accounts which comprise approximately 35% of all withholding. Having extrapolated our findings both forward and backward in time, we found that, of these top 60, 46 accounts comprising 16% of all withholding had biweekly payrolls whose timing causes fluctuations in the number of payments made in a given year. Assuming the average 2017 payments from those 46 accounts remained consistent across years, fiscal year 2017 withholding would have increased 1.0% relative to fiscal year 2016 solely as a result of the additional pay periods. Furthermore, the accrual period for fiscal year 2016 was depressed due to similar yet unfavorable circumstances; as a result, cash which we had slated for fiscal year 2016 was pushed into fiscal year 2017.

This patterning of regular and accrual pay periods that converged in fiscal years 2016 and 2017 in a perfect storm produced the volatility we saw in withholding receipts. Underlying withholding growth is likely closer to our expected rate of 4.5% (see chart below; rate smoothed out with three quarter moving average to ameliorate pay period timing impacts). We are currently exploring what kind of an impact these timing circumstances will have in fiscal year 2018.

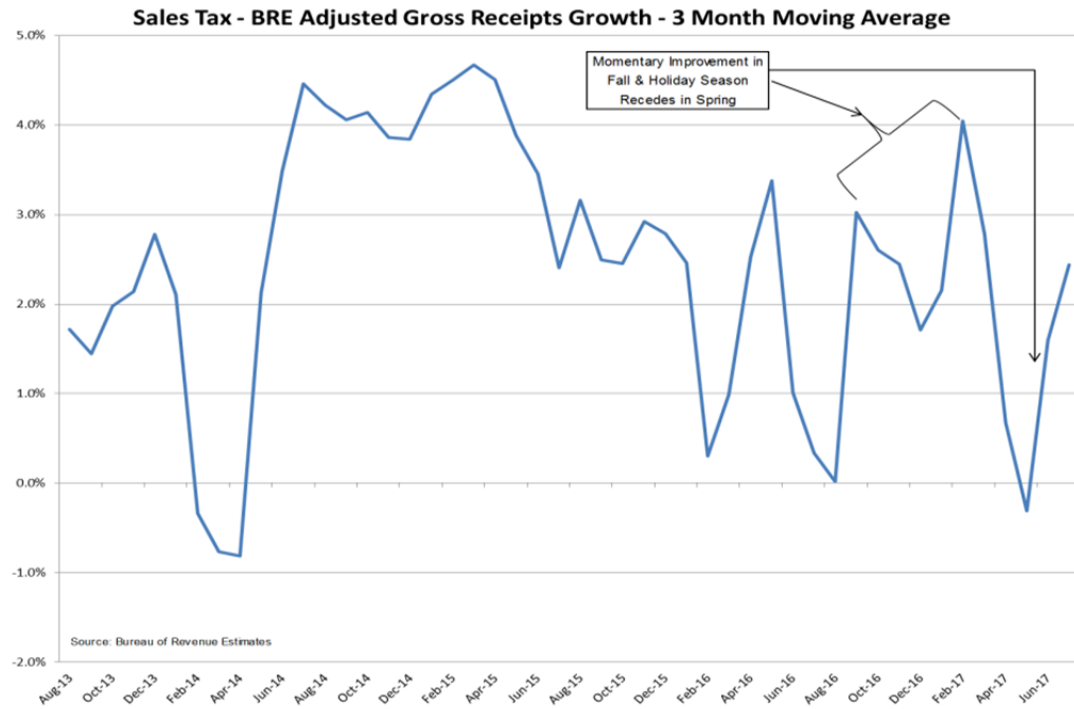


Finally, underlying employment and wage growth reveal a familiar picture. Employment growth for the fiscal year currently stands at 1.5%. Recent data suggests that the first quarter of 2017 as reported by BLS (1.8%) may have been lower, and a downward revision may be imminent. However, it is clear that, similar to other years, employment growth has been strong while wage growth remains muted relative to pre-Great Recession employment expansionary periods. The suspected causes remain the same as have been documented in the last several closeout documents:

1. Historically low inflation, particularly in 2015, has eliminated the need for employers to raise pay to maintain standards of living, and thus would have likely impacted fiscal year 2016 compensation;
2. Age demographics: as highly paid baby boomers retire, employees with less experience replace them at lower wages;
3. Job mix favoring lower wage jobs.

Sales Tax

In fiscal year 2017, sales tax revenues increased just 2.1%, a slight slowdown from fiscal year 2016, which saw growth of 2.2%. As noted, the historically low levels of inflation (near or sub 2%) experienced recently have more than likely stifled wages as well as nominal prices for taxable goods, creating significant impacts on consumption and sales tax revenues.



The last several years have seen periods of volatility for the sales tax as well as historically low rates of growth. Following the most recent holiday season, there was reason for optimism that the trend was turning more consistently above the 2.5% mark that has been difficult to crack in recent years. However, uncertainty at the federal level, a function of the Trump administration's prerogative to "drain the swamp" and dismantle several federal agencies, has amplified economic uncertainty around the Capital Region. As such, it comes as no surprise that federal non-defense employees would pull back on springtime spending and instead focus on essentials and perhaps savings. We find ourselves, yet again, in an environment that creates great uncertainty for a large swath of our taxpaying population.

Other factors have compounded these negative impacts on sales tax revenues. In addition to the economic challenges, depressed revenues reflect shifting consumer preferences toward non-taxables, both in terms of goods and services, as well as the mode of acquisition. Several of the factors follow:

1. The proliferation of spending on nontaxable digital goods, such as mobile applications, streaming music, digital media subscriptions, and digital downloads of historically taxable goods (books, music, software, etc.), has replaced that spending that would have traditionally gone towards tangible goods;
2. While fiscal year 2017 was the second full year of collections that include the largest internet retailer, Amazon, online sales that originate at an online retailer that lacks a physical presence within the State remain untaxable;

3. A manifestation of the era of internet and mobile application disruption, the sharing economy presents challenges to sales tax collections as more taxpayers transact used goods between one another through various online applications;
4. Spending on services as a share of GDP has increased almost 4.5% since 2000. While certain services are taxable in Maryland, the larger share of those represented in GDP figures are not;
5. Shifting age demographics alter a population's spending behavior. As Maryland's labor force continues to become concentrated in the young and old age cohorts, spending will reflect the needs of those populations. For example, older individuals consume more in out-of-pocket health expenditures (exempted from the sales tax) than the young, while the young tend to earn more than they consume.

Actual and Estimated General Fund Revenue
Fiscal Year 2017

	Fiscal Year 2017				Fiscal Year 2016		
			Difference from Estimate			Growth FY 16 - FY 17	
	Actual	Estimated [1]	$	%	Actual	$	%
INCOME TAXES							
Individual	9,019,277,722	8,942,373,718	76,904,004	0.9%	8,517,585,385	501,692,337	5.9%
Corporations	795,593,546	784,601,800	10,991,746	1.4%	874,464,801	(78,871,256)	-9.0%
Total	9,814,871,268	9,726,975,518	87,895,750	0.9%	9,392,050,186	422,821,081	4.5%
SALES AND USE TAXES	4,539,320,011	4,587,253,651	(47,933,639)	-1.0%	4,444,481,368	94,838,643	2.1%
STATE LOTTERY RECEIPTS	484,332,421	493,790,540	(9,458,119)	-1.9%	529,753,844	(45,421,423)	-8.6%
OTHER REVENUES							
Business Franchise Taxes	228,436,706	223,513,459	4,923,246	2.2%	221,966,885	6,469,820	2.9%
Tax on Insurance Companies	328,733,917	294,801,822	33,932,095	11.5%	287,406,711	41,327,206	14.4%
Estate and Inheritance Taxes	227,946,637	206,719,678	21,226,959	10.3%	261,932,260	(33,985,623)	-13.0%
Tobacco Tax	386,976,488	393,826,933	(6,850,445)	-1.7%	395,279,375	(8,302,887)	-2.1%
Alcoholic Beverages Excises	32,489,553	32,947,456	(457,903)	-1.4%	31,946,225	543,329	1.7%
Motor Vehicle Fuel Tax	-	-	-		4,624,687	(4,624,687)	-100.0%
District Courts	69,302,834	70,254,539	(951,705)	-1.4%	72,333,915	(3,031,080)	-4.2%
Clerks of Court	36,145,515	36,946,617	(801,102)	-2.2%	34,203,350	1,942,165	5.7%
Hospital Patient Recoveries	62,180,339	57,781,250	4,399,089	7.6%	57,498,710	4,681,630	8.1%
Interest on Investments	22,491,751	20,000,000	2,491,751	12.5%	15,007,511	7,484,240	49.9%
Miscellaneous	355,277,244	353,390,548	1,886,696	0.5%	334,144,612	21,132,632	6.3%
Total	1,749,980,985	1,690,182,303	59,798,683	3.5%	1,716,344,241	33,636,744	2.0%
TOTAL ONGOING REVENUES	16,588,504,685	16,498,202,011	90,302,674	0.5%	16,082,629,640	505,875,045	3.1%
Extraordinary Revenues [2]	47,431,726	47,431,726	-	0.0%	-	47,431,726	#N/A
Transfer Tax Revenues [3]	62,771,000	62,771,000	-	0.0%	115,366,700	(52,595,700)	-45.6%
GRAND TOTAL	16,698,707,411	16,608,404,737	90,302,674	0.5%	16,197,996,340	500,711,071	3.1%

[1] The 2017 Legislative Session resulted in an additional $22.4 million in estimated revenues beyond the March 2017 official estimate; this table has been adjusted accordingly

[2] The fiscal year 2016 GAAP audit of the Local Income Tax Reserve account found that the account was overfunded by $47.4 million

[3] The Tax Property Article §13-209 has been been altered across several legislative sessions so as to provide various distributions to the general fund

Bureau of Revenue Estimates, August 31, 2017