The Maryland Public Policy Institute

The Annapolis Report

A Review of the 2010 Legislative Session

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The Maryland Public Policy Institute

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THE ANNAPOLIS REPORT

A Review of the 2010 Legislative Session

BY GABRIEL J. MICHAEL

INTRODUCTION

WELCOME TO THE SECOND ANNUAL ANNAPOLIS REPORT, a review of Maryland's 2010 legislative session. The Annapolis Report is designed to be a concise, plain-language guide to many of the major topics addressed during the session: the state's budget, taxes, education, health insurance regulation, and more.

This year's session spanned the 90 days from January 13 to April 12. During that time, a total of 2,700 bills were introduced, and more than 700 were passed by the General Assembly and signed into law by the Governor. Even perusing the titles of new legislation can be a time-consuming task. Our goal in producing this report is to condense the highlights of the session into an accessible format: we discuss the best and worst the session had to offer, topics of general importance throughout the state, as well as issues that are likely to affect many readers personally.

The Annapolis Report differs from many other projects in that we do not assess the performance of individual legislators; rather, our focus is on the legislative session as a whole. While voting records are available online, they are significantly less instructive than might be assumed. This year also marks the first year that committee voting records have been made available online, a practice that the General Assembly should and intends to continue.[1] While committee votes present a more nuanced picture of voting in the General Assembly, they can understate the complexity of much of the legislation the General Assembly considers. For this reason, we focus on analyzing, interpreting, and condensing that legislation for our readers. While we do include a scoring system and report overall scores for the entire session, the primary goal is for the analyses to educate and inform.

The bills considered are divided into a number of subject areas: budgetary matters and fiscal policy; taxes; education; heathcare and health insurance; ethics and transparency; regulation; labor and collective bargaining; pensions and retirement; and miscellaneous. Immediately following this introduction is a presentation of aggregate scores and general commentary, and a brief discussion of the methodology used in the report; following that is the bulk of the report: the analyses. Towards

SCORES

TABLE 1 GRADES & PERCENTAGES

SUBJECT	GRADE	SUBJECT	GRADE
BUDGET & FISCAL	D (27.0%)	ETHICS & TRANSPARENCY	B (60.0%)
TAXES	D (22.4%)	REGULATION	C (57.8%)
EDUCATION	B (70.0%)	LABOR & COLLECTIVE BARGAINING	F (0.0%)
HEALTHCARE & HEALTH INSURANCE	D (39.3%)	PENSIONS & RETIREMENT	D (28.3%)
		OVERALL	**D (39.8%)**

THE ANNAPOLIS REPORT – SUBJECT EVALUATIONS

SUBJECT	COMMENTS
BUDGET & FISCAL	*Once again, the budget was balanced through a series of one-time transfers from various funds and dedicated-purpose sources. The state is facing ballooning pension and health insurance costs for its employees. Finally, a significant amount of capital funding scheduled to be paid from current revenues will now be provided by issuing public debt.*
TAXES	*The low score in the taxes category comes mainly from a host of poorly-conceived tax credits that will likely result in windfall gains for recipients, without any concomitant public gain. Several tax increases were proposed, along with a proposal to return the sales tax to 5 percent, but these made no progress.*
EDUCATION	*Once again, the report's highest score goes to the education category. Several bills dealt with changes designed to assist the state's application for federal Race to the Top dollars; indeed, it appears that these changes have paid off, as Maryland was recently awarded $250 million in Race to the Top funds. Stricter rules for teacher tenure along with several other innovative proposals helped boost the score as well.*
HEALTHCARE & HEALTH INSURANCE	*The legislature performed below average, primarily due to expansions of mandated benefits that drive up insurance premiums and reduce consumer choice. The General Assembly also missed an opportunity to study the feasibility of purchasing health insurance from out–of-state.*
ETHICS & TRANSPARENCY	*Like last year, the General Assembly scores well in ethics and transparency. While we would like to have seen the Maryland Open Government Act and the Legislative Voting Sunshine Act definitively passed, both the legislature and the administration have begun to implement the provisions of these bills without delay. Stricter local ethics rules were also passed.*
REGULATION	*Performance on regulatory matters was slightly above average. Electricity re-regulation was not a major focus during this year's legislative session; however, one major bill requires increases in the mandated amounts of electricity derived from solar sources, and increases fines for failing to meet these amounts. On the other hand, two positive bills deal with consumer protections for reverse mortgages and sensible regulatory policy for oil and gas well drilling.*
LABOR & COLLECTIVE BARGAINING	*This, the worst scoring category, was driven down by several significant expansions in collective bargaining and the associated cost increases that are expected. Most notable are the establishment of a Public School Labor Relations Board and an expansion of collective bargaining to certain child care workers accepting state subsidized wards.*
PENSIONS & RETIREMENT	*The relatively poor score in this category is due mainly to further delay in addressing the state's post-employment benefits liabilities, as well as a questionable proposal that would have implemented significant corporate tax changes for the sole purpose of shoring up state employees' pensions. By passing an emergency bill to ensure that pensioners did not lose even a single dollar in benefits, despite the original benefits formula calling for a slight decrease this year, the legislature also demonstrated the political difficulty of pension reform.*
OVERALL	*Accounting for all of the above categories, as well as several miscellaneous bills dealing with gambling, traffic safety, and other topics, the overall score comes to a high "D," at a slightly higher percentage (39.8 percent) than last year (36 percent).*

the end of the report is an appendix describing the scoring process in detail, as well as an index of bills and subjects.

METHODOLOGY

Selection. The sheer number of bills introduced in each legislative session precludes an exhaustive treatment of each one; nor would that necessarily be helpful, as many bills pertain to purely local issues, or are related to technical matters such as liquor licenses for special events. Thus, in constructing a legislative report card, we are necessarily faced with the difficult question of which bills to include.

Following the strategy developed in last year's report, we have eschewed examining a large, unwieldy number of bills, in the belief that focused analyses of the most important issues will ultimately prove more helpful to readers. On the other hand, only analyzing a handful of bills can result in a skewed perspective of what happened during the legislative session. This report seeks a middle way. Because the Maryland Public Policy Institute is not a single-issue advocacy organization, we have a broad flexibility to examine any bill we believe merits attention.

Selection of bills has a large effect on the overall scoring, but there is no entirely objective way to select bills for inclusion. Even a report that scored every single bill could not attain complete objectivity, since assessing the relative importance of bills always retains elements of subjectivity.

This report attempts to include most bills of moderate or high importance that passed in our subject areas of interest, along with a number of bills that did not pass, to give the reader a sense of other proposals made in the legislative session. A strict focus on only the legislation that passed is unhelpful, since this year's failed bill may become next year's law.[2]

This year's report includes about 89 pieces of legislation, many of which have both House and Senate versions. In some cases, there are several similar proposals, and we have chosen to group the legislation together. This leaves us with about 60 discrete legislative issues.

The report is organized by topic and subtopic, rather than by bill number; because so many bills are interconnected, we felt it made more sense to organize the report in this manner than as simply a list of bills. However, to facilitate quick reference to bills discussed in the report, an Index of Bills & Subjects is included at the end of the report.

For further information on all bills, including those not treated in this report, the reader is directed to the General Assembly's website at http://mlis.state.md.us/. The legislative history, text of the bill, results of roll call votes, proposed amendments, and fiscal and policy notes can all be found there.

This report relies heavily on the analyses performed and data collected by the Department of Legislative Services (DLS); the first place to seek a more detailed look at any given bill is its fiscal and policy note, if available. Written by non-partisan DLS staff, these notes provide a summary of the bill, estimated fiscal effects, a comparison of proposed and current law, and often comparisons with similar policies and legislation in other states.

Scoring. Last year's report used a relatively simple two-factor scoring system. The first factor, a coefficient (C), represented our judgment of the General Assembly's final action on a bill, and can either be positive or negative. For example, a good bill that was passed would have a positive coefficient (C = 1), whereas a bad bill that was passed would have a negative coefficient (C = -1).

The second factor, a multiplier (M), was a measure of how far a bill progressed during the legislative session. The larger the multiplier, the more progress the bill made, and the more weight its score carries (for better or worse). For example, all bills that are introduced receive a first reading, which corresponds to a multiplier of 1; a bill that receives a third reading and passes corresponds to a multiplier of 3. Table 2 (page 6) shows how a bill's status corresponds to a given multiplier.

This relatively simple two-factor scoring system nevertheless allow for some nuance. First, any bill that is to become law must be passed by both chambers of the General Assembly; such bills would receive a total score of 6, reflecting the much greater importance of legislation that actually becomes law. Second, using a coefficient allows us to properly account for situations in which good or bad bills are rejected. Because

TABLE 2	MULTIPLIER VALUES
BILL STATUS	**CORRESPONDING MULTIPLIER**
FIRST READING	1
REASSIGNED	1
REFERRED FOR INTERIM STUDY	1.5
UNFAVORABLE REPORT	2
SECOND READING	2
THIRD READING	3
PASSED	3

TABLE 3	GRADING
LETTER GRADE	**CORRESPONDING PERCENTAGE**
A	GREATER THAN OR EQUAL TO 80%, UP TO 100%
B	GREATER THAN OR EQUAL TO 60%, LESS THAN 80%
C	GREATER THAN OR EQUAL TO 40%, LESS THAN 60%
D	GREATER THAN OR EQUAL TO 20%, LESS THAN 40%
F	GREATER THAN OR EQUAL TO 0%, LESS THAN 20%

the coefficient depends on the General Assembly's final action on a bill, if a chamber rejects a good bill in a floor vote, or a committee gives a good bill an unfavorable report, the coefficient, which would normally be positive, instead becomes negative. This penalizes the legislature for rejecting good ideas; likewise, it also rewards the legislature for rejecting bad ideas.

For example, a good bill that passed would have a positive coefficient (C = 1) and a multiplier (M) of 3. The final score is thus simply C x M:

$$1 \times 3 = 3$$

A bad bill that received a second reading would have a negative coefficient (C = -1) and a multiplier (M) of 2 . Again, the final score is given by C x M:

$$-1 \times 2 = -2$$

Finally, consider a good bill (C = 1) that passed one chamber (M = 3), but only went as far as a first reading in the other chamber (m = 1). In this case, the total score is simply the sum of the scores in each chamber, or (C x M) + (C x m):

$$(1 \times 3) + (1 \times 1) = 4$$

Weighting. While this scoring system accounts for both the General Assembly's actions and the progress of legislation, it suffered from some flaws. The primary drawback was that it was incapable of differentiating between bills that made the same amount of progress during the session. For example, every bill that passed and became law was given the same weight as every other bill. Clearly some laws are more important than others, but “importance” is a slippery concept, and so last year, the decision was made to avoid arbitrarily weighting some bills more heavily than others in the interests of consistency.

This year's report attempts to address this drawback by incorporating an objective measure of relative importance into the scoring system. Specifically, it incorporates a new weighting variable derived from the estimated net fiscal effect of each bill. This weighting variable (W) is used to adjust the unweighted scores, giving more weight to bills with larger net fiscal effects than those with minor net fiscal effects. While fiscal effects are not the only way of assessing relative importance, they are objective and widely available.

Scores are calculated exactly as before, with the additional inclusion of the weighting variable (W). For example, a good bill (C = 1) that passes one chamber (M = 3) and has a weight of 3 (W = 3) would be scored as C x M x W:

$$1 \times 3 \times 3 = 9$$

For a detailed explanation of how the weighting variable is calculated, see Appendix A: Scoring and Grading Details.

Grading. For each category and for all bills, the individual raw scores are summed to form a total raw score. Then, this total raw score is converted to a percentage and assigned a letter grade. Unlike typical grade school report cards in which only the 65 percent to 100 percent range matters, our letter grades make use of the entire percentage scale. Thus, a score between 100 percent and 80 percent is an “A”; between 80 percent and 60 percent, a “B”; and so on.

For a detailed explanation of how raw scores are summed and converted to percentages, see Appendix A: Scoring and Grading Details, at the end of this report.

ANALYSIS

Budget & Fiscal

Operating Budget

(SB 140 / HB 150)

The FY 2011 operating budget totals just under $32 billion, and is about $300 million less than the FY 2010 budget.[3] The state is left with a balance of $274 million, though more recent estimates suggest the balance will be $204 million.[4] In order to eliminate a $2 billion funding gap, the Governor's proposed budget relied heavily on one-time transfers from various special funds to the general fund and curbing spending from the general fund, "mostly by assuming additional federal Medicaid aid at the higher match level, constraining employee compensation, Medicaid cost containment, and higher assumptions of video lottery terminal revenue."[5] Reductions in spending from the general fund are in large part covered by $1.3 billion in ARRA funds being used in their place; as such, these reductions are only temporary.[6] Simply put, "In the long term, some combination of revenue increases and spending reductions will be necessary to place the State back on the path of fiscal sustainability."[7]

Structural Deficit. Since 2007, the state has been facing a significant and growing structural deficit.[8] In FY 2011, the Governor's proposed budget had to close a $2 billion gap; however, the measures adopted to do so do not have a long-term effect, with the result that the state faces a projected $1.5 billion gap in FY 2012, and an over $2 billion gap in FY 2013.[9] Major factors contributing to the gap have been: the flatlining of tax revenues over the past several years; significantly increased costs for primary and secondary education, Medicaid, pensions, and health insurance, far outpacing growth in other forms of spending; and the future loss of $1.3 billion in federal stimulus funds.[10]

Federal Funds. As a result of the American Recovery and Reinvestment Act (ARRA), federal funds continue to play a larger than usual role in the budget. In FY 2011, they account for about 29 percent of revenues, compared with 25 percent in FY 2010, and 22 percent in FY 2009, the last budget before the ARRA became law.[11] Since many of the provisions of the ARRA are set to expire after 2011, most states will be facing a significant drop in federal funds when they begin assembling the FY 2012 budget. This will present a significant challenge, especially to Maryland, which even without the loss of stimulus dollars is facing a significant structural deficit. Some states have been thinking ahead about how to deal with the loss. Pennsylvania Governor Edward Rendell, for example, proposed the creation of a "stimulus transition reserve fund," funded by a number of tax reforms, in order to wean the state off of stimulus dollars.[12] By contrast, Maryland currently has no specific plan for dealing with the impending loss of these funds.

Medicaid Match. As we reported earlier this year, one of the most controversial and well-publicized features of this year's budget had been the assumption of an extra $389 million in federal funds which would be received if Congress decided to extend certain provisions of the ARRA for an additional six months.[13] Specifically, the question was whether the Federal Medical Assistance Percentages (FMAP) would continue at a higher than typical rate until the end of FY 2011, as opposed to reverting to the normal rate at the end of the 2010 calendar year. Congress had been debating the extension for several months, facing pressure from state governments who argued the federal aid was sorely needed in order to shore up precarious budgets, but also hearing calls to rein in spending, especially before this November's elections. The compromise proposal eventually adopted extends the enhanced match for six months, but at a diminishing rate.

According to a survey conducted by the National Conference of State Legislatures in April, around 30 states assumed an extension of the enhanced match in some form for their current budgets. Nine states, including Maryland, had a clearly defined contingency plan in case the extension was not granted.[14] Some contingency plans involved across the board budget cuts and provider rate cuts. Maryland's plan, however, involved using an existing $189 million balance in the general fund and transferring an additional

$200 million from the Local Income Tax Reserve Account (discussed below), which would be repaid over a number of years. While the match was partially extended, the practice of assuming significant amounts of additional federal funding before that funding is actually approved falls into the category of legislative tricks used to present a "balanced" budget that is anything but.

Local Income Tax Reserve Account (LITRA). For the second year, the state's budget borrows about $350 million from a little-known fund called the Local Income Tax Reserve Account (LITRA). The funds are scheduled to be paid back at a rate of $50 million annually for seven years. According to the DLS, the LITRA:

> *is used to manage the cash flow of personal income tax payments and distributions to local governments. It is also used to meet the State's liability for local income taxes according to generally accepted accounting principles. Each month a portion of personal income tax net receipts is put into the account representing an estimate of local income tax payments. In all but two months, a distribution of local income tax revenue is made from the account to local governments. The account balance fluctuates throughout the year but was $1.3 billion at the end of January 2010.*[15]

By borrowing from this account, the state is essentially relying on future tax revenues to pay current expenditures from the account. According to Warren Deschenaux, director of the Office of Policy Analysis in the DLS, "diversion of the funds is inconsistent with standard accounting practice by shift from accrual to cash accounting. The result will show as a $350 million liability on our books."[16]

Rainy Day Fund. The state's rainy day fund, an emergency fund that factors into the state's credit rating, remains at the recommended level of $633.5 million, or 5 percent of general fund revenues. The state did not tap into this fund to balance the budget. There is a possibility that drawing funds from the Rainy Day Fund could be negatively perceived by bond rating agencies, potentially leading to a credit downgrade for the state. Likewise, the political ramifications of tapping into the fund in an election year are significant. In any case, according to the DLS, the state's Spending Affordability Committee (SAC) has recommended using funds from the Rainy Day Fund "only as a last resort and in combination with a multi-year plan to achieve structural balance."[17]

Higher Education. This year marks the end of the tuition cap at the state's universities after four years of tuition freezes. Tuition increases at these universities are capped at 3 percent, a cap supplemented by the equivalent of an additional 2 percent tuition increase in state funding.[18]

Pension & Health Insurance Costs Increasing Significantly. Total state payments to localities for retirement benefits were $900.4 million, an increase of $96.8 million, or more than 12 percent, from 2010's amount. Retirement payments are the fastest growing portion of state assistance to local governments; overall growth in payments was only 3 percent. The increase in retirement payments rivals the increase in aid for primary and secondary education, which was $119.7 million, but only 2.5 percent over 2010. Other areas of state aid to localities, such as to libraries, community colleges, transportation, and public safety, actually declined.[19]

The state paid $897.5 million towards health insurance for its employees and retirees. The DLS notes that one-time payments offset an 8 percent increase in costs this year, but that both State and employee and retiree contributions will be increasing in future years.[20]

Human Resources. This year's budget included several furlough days as a cost-saving measure, along with no salary increases or merit pay. This year the state will also not fund a $600 match to a voluntary deferred compensation plan some employees participate in. Prior to legislative action, the Governor eliminated over 500 employee positions, though more than 40 percent of these positions were vacant to begin with.[21] The budget calls for an additional 500 positions to be eliminated by the end of FY 2011.[22]

To some extent, the large increase in the cost of providing pension and other retirement benefits is partially responsible for the budgetary problems that necessitate cutbacks in human resources spending. To the extent that pension

and other retirement benefits are considered incentives for attracting quality human resources, this should be balanced against the fact that furloughs and other salary reduction provisions are significant disincentives.

Budget Reconciliation and Financing Act (BRFA)
(SB 141 / HB 151)
In order to address the quickly growing costs of retirement benefits (discussed above), the BRFA creates a "Public Employees' and Retirees' Benefits Sustainability Commission" that is charged with giving recommendation to the General Assembly prior to and following the 2011 legislative session. According to the DLS, "The commission is charged with reviewing and evaluating the recruitment practices, retention incentives, actuarial liabilities, actuarial funding method, cost drivers, employee contribution rates, and the comparability and affordability of the benefit systems."[23] As this is an issue the Maryland Public Policy Institute has been examining for a number of years, we will be closely watching the recommendations produced by the committee to ensure that they are based on sound research and public policy.

Revenue Distribution Changes: Highway User Revenue (HUR). In a bid to shore up the state's general fund, the General Assembly approved a permanent change in the distribution of Highway User Revenue (HUR). From this year on, the portion of HUR that counties and Baltimore City receive will be significantly reduced; in the case of counties, this revenue will have been all but eliminated. According to the *Washington Post*, "For the next year, counties will have to contend with almost no "highway user" revenue, which is supposed to be a local share of the state's gas tax. And through 2015, they will have to make do with less than 10 percent of the hundreds of millions they have typically received each year over the past two decades."[24] Other commentators have described this change as a "monumental heist," and suggest that Maryland drivers, already driving on roads whose quality lags behind the national average, are paying hundreds of dollars extra in vehicle maintenance costs because of the lack of funding.[25]

The changes will represent a loss of nearly $400 million to the counties and Baltimore City in 2010 and 2011, and additional losses in future years.[26] While this is not the first time that Highway User Revenues have been reallocated away from localities to shore up the general fund (a total of $271.2 million was transferred between 2003 and 2005), this session's distribution changes go far beyond past transfers.

The BRFA contains numerous other fund transfers, totaling more than $1.04 billion in all; while some of the transfers are understandable in times of budgetary stress, others represent a misdirection of collected taxes towards purposes they were never intended for. For example, the BRFA transfers $200 million total in 2010 and 2011 from the state's Bay Restoration Fund to the general fund. The majority of this fund is derived from taxes paid by users of wastewater treatment plants, and the fund is intended to pay for upgrades to those plants. Thus, the transfer misdirects tax revenue. Furthermore, since the $200 million is replaced by an equivalent amount of bond funding, the state accumulates additional debt and the associated debt service costs.

The change in revenue distribution and fund transfer discussed above represent two of the largest provisions in the BRFA. It should be noted, however, that the General Assembly rejected several of the Governor's proposals for fund transfers. The Governor's original proposal suggested transferring $25 million from the Land Records Improvement Fund and $20 million from the Injured Workers Insurance Fund, both of which would have constituted misdirection of tax revenue collected for specific purposes.[27]

The Capital Budget
(SB 142 / HB 152)
The consolidated bond bill for the capital budget authorizes more than $1.03 billion in debt for various capital projects throughout the state.

Issuing Additional Debt in order to use General Fund Revenues for Other Expenses. This year's budget continues the troubling practice of issuing debt in the form of general obligation (GO) bonds to pay for capital projects originally slated to be paid for in the current year with general funds.[28] Several hundred million dollars worth of projects that would normally have been

funded with current year revenues are now to be funded by issuing debt. For example, a $157 million payment that was scheduled to be made for InterCounty Connector construction this year from the general fund has been reduced and will now be covered by GO bonds. Furthermore, instead of the full amount, the budget authorizes $89 million in debt for the payment; the remaining amount will be pushed into next year's budget, where it will also likely be funded by debt. This despite the fact that these payments were originally supposed to be made as recompense for a transfer of $315 million directly from the Transportation Trust Fund to the General Fund back in 2003.[29]

The capital budget as originally proposed requested more than $440 million slated to be paid from the general fund to be replaced by GO debt.[30] A total of $423.6 million in bonds to replace general fund revenues was eventually approved by the legislature.[31] While this practice is technically legitimate from a public finance perspective because the bonds are being used to purchase capital assets, Warren Deschenaux notes that this new debt is essentially being used as a method of refinancing current capital assets, instead of actually adding new capital assets.[32] Indeed, had it been foreseen that GO bonds would be necessary; the timing of the purchase of these assets may have been affected. To make an analogy, imagine that you decide to purchase a car, and you believe you have enough money in your bank account to pay for it without taking out a loan. Then, after agreeing to purchase the car, you find that you actually don't have the money, and that you'll need to take out a car loan. Had you known this in advance, you might have decided not to purchase the car in the first place.

Bond Bills. Every year the General Assembly is able to fund $15 million of individual projects submitted by various organizations and sponsored by individual delegates or senators. Most of these "bond bills" require the organization to have obtained funds matching the amount they request from the state; however, in many cases, the "match" may consist of funds that have already been spent, as well as donated services or materials. In some cases, no match is required at all, and the bond bill, if awarded, is simply a grant. Only a fraction of the bond bills that are approved have a state-wide effect; most are localized and special-interest oriented. From our point of view, the question isn't whether any individual project is a worthwhile endeavor; some undoubtedly are. The question is whether state dollars and associated debt service costs should be funding such projects when the state is facing serious fiscal challenges. A full list of all the bond bills submitted this session, along with their sponsors and any funding awarded, can be found at the following address:

http://mlis.state.md.us/2010RS/budget_docs/2010_bb_funding.pdf

Transportation-Related Legislation

HB 710 / SB 229 establish a Blue Ribbon Commission on Maryland Transportation Funding, charged with examining the status of the state's transportation funding, the Transportation Trust Fund (TTF), construction and maintenance funding needs, and long-term revenue issues related to transportation. The Commission's first report is due by January 1, 2011.

HB 383, a reintroduction of the Transportation Trust Fund Protection Act, would prohibit transfers from the Transportation Trust Fund, which supports the Maryland Department of Transportation's operating and capital expenditures, to the general fund, except under extraordinary circumstances, and then only if repaid within five years.

In recent years, the Transportation Trust Fund has been continually targeted as a piggy bank for balancing the state's budget. While in theory any money borrowed from the fund must be repaid, in practice, repayments are often delayed years beyond their original schedule. In the case of $315 million of borrowing in 2003-2004, the repayment was to consist of state funding for construction of the Inter-County Connector (ICC). Ideally, that repayment would have come from general funds and arrived on time; instead, it was funded primarily by issuing additional debt, and has been continually delayed.

With both the Administration and the General Assembly seeking to preserve the maximum budgetary flexibility, they will be unlikely to exercise the self-restraint necessary to pass this bill,

and we can expect future borrowing along with delayed, debt-ridden repayment of the TTF.

SB 466 / HB 445, in a bid to increase TTF revenue, requires that off-road vehicles, including ATVs, snowmobiles, and dirt bikes (but excluding farm vehicles, tractors, etc.) be titled, thereby requiring that purchasers pay title fees. While the title fees are unlikely to dissuade many purchasers, since off-road vehicles are driven on private property, it makes little sense to tax them as if they were driven primarily on public roads. Owners of such vehicles already pay sales taxes and motor fuel taxes; this bill is clearly a money grab, but an ineffective one at best. Compared with overall TTF revenues, and indeed, TTF titling revenues, the revenue generated by extending titling to these vehicles is negligible, and avoids the hard issues of dealing with chronic TTF raiding.

Other

HB 1034 / SB 633 change the way in which the rates paid to community developmental disabilities services and mental health services providers are calculated. Whereas in the past, a rate-setting commission within the Department of Health and Mental Hygiene would suggest the increases, with prior year increase ranging from no increase to 4 percent, this bill would directly link rate increases to increases in the agency budgets, but limited to a range between no increase and 4 percent. Because future year budgets for any given agency are difficult to predict, there is no precise estimate of the potential costs of this linkage; however, the bill's fiscal and policy note suggests that costs could be significant, and provides illustrative examples ranging from a $14.6 million increase to a $43.8 million increase.[33]

HB 73 expands the use of funds in the Water Quality Revolving Loan Fund, and by doing so, makes the state eligible for significant amounts of federal funds to aid public water capital projects. While the expansion requires a significant investment of state resources (over $9 million in 2012 and 2013), the five-to-one match by federal funds represents a huge net benefit to the state. To the extent that the state's 20 percent match is provided from this special fund, rather than the general fund, this constitutes an appropriate and prudent use of water fees.

Healthcare and Health Insurance

False Claims. The passing of **SB 279**, the Maryland False Health Claims Act, was one of the best outcomes of this year's legislative session. Similar legislation was introduced in both of the previous two sessions, and in both instances was narrowly defeated.

In general, false claims or qui tam legislation permits private individuals to sue for fraud committed against the government; in turn, they receive a portion of any award that comes as a result of the suit. The logic behind false claims acts is to encourage individuals with knowledge of fraudulent activity to become whistleblowers for the benefit of the government. At least 23 other states have false claims acts.[34]

This specific bill is limited to false claims made under a State health plan or program, or submitted to the Department of Health and Mental Hygiene (DHMH). Awards of proceeds to private individuals who file suit are limited, ranging from 10 percent to 25 percent, and safeguards are included to ensure that individuals filing suit were not involved in the violations at issue. According to the DHMH, hundreds of millions of dollars worth of fraudulent Medicaid claims are received each year.[35]

A portion of any money recovered in a suit is due to the federal government, since federal aid for Medicaid constitutes a major portion of state Medicaid spending. By enacting qualified legislation, Maryland could have been eligible for an increased share of any recoveries made, with more money being returned to the state rather than the federal government. Unfortunately, Maryland's act does not go far enough in order to qualify for the increased share. While the act is better than nothing, in the future, Maryland would be better served both by bringing this act into compliance with federal regulations, thereby qualifying the state for a greater share of proceeds, and by passing a broader general false claims act, such as this year's **SB 187.**

Competition

HB 1015 would have required the Maryland Insurance Administration to conduct a study on the possibility of permitting Maryland residents

to purchase health insurance from providers in other states. Costs for conducting the study would have been negligible, but the information provided would have been invaluable. Allowing residents to purchase policies from out-of-state companies that are subject to fewer coverage mandates could reduce the cost of insurance for Marylanders who want policies without such mandates. Unfortunately, while the bill passed the House, it was unanimously opposed by the Senate Finance Committee. Policymakers should encourage this type of study.

Coverage Mandates

SB 27 would have required health insurance providers to cover the costs of in vitro fertilization (IVF) in rare cases where both spouses suffered from specific fertility problems. The change would have applied to the individual market and group markets only, not the small group market. However, it would likely have also been adopted by the State insurance plan.

While the cost increases associated with this particular bill would have been small, it provides an opportunity to examine the issue of the large number of conditions which health insurance providers are required to cover by Maryland law. According to the Maryland Health Care Commission, Maryland's mandated benefits are responsible for more than 18 percent of the cost of individual premiums, more than 17 percent of the cost of small group premiums, and more than 15 percent of the costs of group health insurance premiums.[36] The cost of any one mandate may be relatively small, but taken together, they drive up the price of health insurance for all residents significantly.

HB 1017 / SB 700 is another example of expansion to mandated health insurance benefits that drive up the costs of premiums for Maryland residents. The legislation expands the services that health insurers must cover under child wellness services, which are benefits mandated by the state. Whether the individual services are worthwhile is not the issue; rather, the question is whether every person who wishes (or, after health insurance reform, is required) to purchase health insurance should be forced to purchase coverage for them.

HB 878 / SB 313, by mandating that a vision examination be included as part of an annual preventive care covered by insurance, also expands mandates and contributes to increased cost of premiums in the state.

Taxes and Fiscal Policy

Income Tax

HB 1177 would have repealed the expiration of the increased "millionaire's tax" that has generated so much controversy over the past two years. The tax, which created a new 6.25 percent income tax bracket for filers with more than $1 million in income, will expire this year, and these filers will once again pay a 5.5 percent rate. According to the bill's fiscal summary, the continuation of the tax increase could generate about $350 million over the next five years.

However, we should remember that when the tax was originally passed in 2008, projections indicated that it would generate over $100 million in tax years 2008 and 2009.[37] Instead, revenue from the bracket actually decreased by over $100 million in 2008, and figures for 2009 are still being tallied.[38] The number of tax returns reporting income in excess of $1 million dropped by nearly one-third. The exact cause of the decline is contested: some suggest that the decline can in large part be attributed to the generally poor state of the economy. People are simply not making as much money as they used to.[39] Others argue that taxpayers affected by the hike, who disproportionately live in Montgomery and Baltimore counties, could easily change residence to Virginia or Pennsylvania and benefit from those states' lower tax rates.[40]

In either case, we have good reason to view these revenue projections with some skepticism. Furthermore, though the full extent is difficult to determine, it is clear that the extension of the tax increase will affect at least some small businesses. In 2008, about 25 percent of tax filers with incomes exceeding $1 million reported the majority of that income coming from business activities, such as sole proprietorships, LLCs, or similar structures.[41] Small businesses affected by the tax may also be less able than high-income individuals to change residence to another state.

All of the above criticisms apply equally to SB 913, which is identical to the above bill, except that it would have extended the increased tax rate until 2014, rather than permanently.

HB 896 would have made all taxpayers eligible for the maximum standard deductions, which are $2,000 and $4,000 for single and joint/head of household filers respectively. Currently, single and joint/head of household filers making less than $13,333 and $26,667 respectively are eligible for slightly lower standard deductions ($1,500 and $3,000 at the lowest). As neither Maryland's standard deductions nor its income tax brackets are indexed to inflation, increasing the standard deduction provides lessens the burden of inflation for filers below the threshold amounts. However, a better approach might be to simply index both tax brackets and the standard deduction to a measure of inflation, as HB 238 proposed. At least 20 states index some portion of their income tax using a measure of inflation.[42]

Sales Tax

HB 1286 / SB 739 both proposed reducing the State sales tax from 6 percent back down to 5 percent. While the tax cut would likely increase sales for some businesses, the enormous tax revenue decreases associated with these bills made them both politically and fiscally infeasible for the time being.

SB 824 was an attempt to capture sales tax revenue on Internet sales. Under current law, many online sales made to Maryland residents are exempt from the sales tax because the seller has no physical presence in Maryland, nor any representatives or sales staff operating in Maryland. This bill would have applied the sales tax to online sales in which customers were referred to the seller by someone in Maryland. This is commonly known as an "affiliate program."

North Carolina recently established a similar law, after which online retail giant Amazon.com ended its affiliate program in the state. This bill's fiscal and policy note indicates that the effect of this law on business in the state is indeterminate: the termination of affiliate programs could hurt businesses, but the imposition of sales tax on some online purchases may make local, in-state businesses more attractive to customers. Estimated revenues are approximately $7 million annually.

The shift of a significant amount of retail sales away from brick-and-mortar stores, which are required to collect sales taxes, to online sellers who are exempt from sales taxes as long as they lack physical presence in the state, is a serious issue in fiscal policy nationwide. Technically, customers who purchase from online retailers who do not collect sales tax are then required to remit the appropriate "use tax" to the state themselves; however, enforcement of the use tax is practically impossible, and compliance is minimal.[43]

Other efforts at addressing the broader policy problem involve Congressional action to require online retailers to collect the sales tax, and projects such as the Streamlined Sales Tax Project, which involves harmonization and clarification of myriad sales tax rules across the country.[44] It is clear, however, that without cooperation between Maryland and other states, and possibly Congressional action, it will be nearly impossible to appropriately treat the tax implications of online sales.

Motor Fuel Taxes

Three different bills proposed increasing motor fuel taxes: HB 479, HB 969, and SB 827 would have increased the tax by 10 cents (phased in over five years), half a cent followed by indexing to inflation, and pure indexing, respectively. While these proposals would have generated significant tax revenues at the cost of higher gas, delivery, and product prices for all consumers, they also represent a cash grab by the state: since motor fuel taxes are credited to the Transportation Trust Fund, one would expect the revenues to go toward improving the state's transportation infrastructure, and also to benefit local governments through Highway User Revenue distributions. Yet as noted in the discussion of the budget bill above, changes made this year have altered the distribution of highway user revenues, so that more money goes directly to the state's general fund.

Tax Credits/Economic Stimulus Measures

HB 475 primarily extends the Heritage Structure Rehabilitation Tax Credit through 2014 and renames it the Sustainable Communities Tax Credit.

This tax credit allows claimants to be reimbursed a portion of building rehabilitation costs when other criteria are met. The tax credit is available for both commercial and residential structures, though commercial structures account for the vast majority of forgone tax revenue. According to the bill's fiscal and policy note, "The Heritage tax credit for commercial properties has evolved into one of the State's largest economic development programs… [and] is the largest business-related State income tax credit and one of the largest of all State income tax credits."

While the administration's public comments on the credit tout the general economic benefits of the tax credit, claiming "more than $8.50 in economic output [was returned] for every $1 invested by the State government," and that "The state's tax credit investment…has generated 1,850 more jobs than would have been created," the DLS provides a notably more even-tempered analysis, saying that while some economic impact studies have attributed large multiplier effects to the tax credit, in reality, the effect is likely much more moderate, on the order of $1.7 to $2.1 generated for every $1 in tax revenue forgone, without accounting for other tax incentives that may further lower this ratio.[45] Additionally, the DLS analysis of the distribution of credits awarded suggests that they are skewed towards higher-income areas and households with assessed values well above average.

Yet again, with **HB 1249**, the Maryland Economic Stimulus Act, the General Assembly passed over an opportunity to encourage small businesses in the state to purchase capital equipment in the current year, thereby stimulating the economy. This bill would have permitted business owners to deduct a larger portion of the cost of qualified property and equipment purchased in the current year from their taxes, rather than having to depreciate the purchases over a longer period of time. According to the Department of Legislative Services, small businesses in particular would have benefited. Meanwhile, the costs of the legislation are relatively limited: $3.4 million in forgone tax revenues for the current year.

Compare that with the cost of **SB 106**, the Job Creation and Recovery Tax Credit, at $20 million. This legislation provides a tax credit to employers who hired new employees during 2010. At first glance, this seems like a reasonable idea, an incentive for businesses to hire new employees during a time when the state and country are facing very high unemployment rates. However, this bill specifies that the tax credit applies to employees hired between January 1, 2010 and December 31, 2010. Yet the bill had not even passed both the House and Senate until late March. This means that even though the bill will provide a tax credit to businesses that hired employees in the early months of 2010, there is no way the tax credit could have acted as an incentive for those businesses to hire, because the tax credit did not yet exist. Furthermore, since the tax credit is provided on a first-come, first-serve basis, businesses that already hired employees in advance of the tax credit being established will be more likely to receive the credit.

SB 384 proposed the same tax credit, only with a higher cap of $30 million, and a higher cap on the total amount of credits permissible to be claimed by one employer.

More fundamentally, the problem with tax credit programs such as these is that it is always impossible to determine the counterfactual: i.e., to know how many employees would have been hired in the absence of the tax credit. Thus, it is impossible to determine how effective the tax credit will have been.[46] Or, as the bill's fiscal and policy note puts it, "A significant portion of credits claimed will provide money to businesses that would have otherwise hired individuals, representing a windfall gain to these businesses."[47]

HB 1520 proposed a tax credit for new or expanded business facilities that created at least 10 new qualified jobs. 10 percent of eligible costs for the facilities, up to $50,000, would have been available as a refundable tax credit. To the extent that this tax credit would have encouraged construction now rather than later, it is positive; also, though the structure of the credit is similar to existing programs, its eligibility thresholds are lower. However, it also suffers from the same problem of determining whether any additional construction or jobs would have taken place in the absence of the credit. The total amount of

the credit would have been capped at $10 million.

HB 1266 proposed a tax credit for "first-time" homebuyers, though "first-time" is defined as not having owned a home in the past three years, or not having purchased a home in the past five years. Though the bill includes limits on the total purchase price of homes, the $800,000 limit is high enough that the credit could simply end up subsidizing the purchase of luxury homes. There are a number of other state programs targeted at first-time homebuyers and others to assist in the purchase of homes, leading to the question: is another tax credit, and a very expensive one at that, justified? Estimates place the loss of tax revenue at $250 million over two years.

Once again, two Hollywood-friendly bills, **SB 98** and **SB 976,** were introduced with the intent of expanding a state subsidy to film production companies, and converting the subsidy program from a rebate subject to an annual appropriation to a tax credit without any cap. The bills would allow film production companies operating in the state to receive tax credits for 28 to 30 percent of their qualified costs. The cost to the state in lost revenue would be in the tens of millions each year, possibly approaching $100 million. The purported benefits of job creation may be only temporary, and local sales and contracts may simply represent a shift of economic activity from one state to another. Finally, revenue lost to this tax credit must come from somewhere, which likely means service cuts or increased fees or taxes in some other area.

SB 64 extended the Maryland Research and Development Tax Credit, which was due to expire in 2012, until 2021. The tax credit provides up to a total of $6 million to businesses engaging in qualified research and development activities. Since the credit's inception in 2000, every year the full $6 million has been claimed.

Continued growth in the number of applicants and number of credits applied, combined with the steady cap on total credits has meant that the value of the tax credit to applicants has diminished significantly. The Department of Legislative Services estimates that "the incentive provided by the basic credit…translates to a company receiving $1,938 for conducting an additional $1 million in qualified research and development activities."[48] The same analysis also notes that the benefit to small businesses is minimal, in large part likely due to the large amount of qualified costs required to receive even a minimal credit.

In 2009, the Government Accountability Office issued a report on similar types of federal tax credits, noting that "a substantial portion of credit dollars is a windfall for taxpayers, earned for spending they would have done anyway, instead of being used to support potentially beneficial new research."[49] Currently, over 30 states offer similar credits. While state tax credits can play a large role in determining the cost of conducting research and development in a given state, the fact that Maryland's credit is effectively tiny, combined with the potential for windfall gains as well as the costs of wasteful tax competition between states, suggests that the state should have discontinued this credit.[50] Instead, Maryland will now spend an additional $48 million through 2021 for only murky benefits.

Unemployment

HB 591 would have reduced the amount of unemployment insurance charged to employers in the state from its current maximum levels to a schedule with lesser rates. Every private employer in the state is required to contribute to unemployment insurance at a rate that varies both with the balance of the state's Unemployment Insurance Trust Fund, and the individual employer's historical experience with unemployment.

While reducing the contribution rates would have been beneficial for most businesses, particularly those forced to lay off workers due to economic conditions, the drop in contributions would have driven the Unemployment Insurance Trust Fund in negative territory. This would have necessitated loans from the federal government to the state in order to close the gap. While such loans are interest-free for a short period of time, Maryland would have had to begin paying interest in 2011. Over four years, interest payments would have amounted to over $75 million.[51] Even though this bill did not pass, Maryland had already received a loan from the federal government in February 2010, with an

outstanding balance of more than $133 million at the time of writing.[52]

SB 107 provided a much better approach to handling the enormous strain on the Unemployment Insurance Trust Fund. The legislation coupled a modest expansion of benefits with several stricter requirements of qualification in a cost-neutral fashion; additionally, in order to provide employers some relief, it reduced the penalty on late payments, and established payment plans that allow employers to spread their contributions over a longer period of time. These changes also qualified Maryland for over $126 million in federal stimulus funds to assist with paying unemployment benefits.

Combined Reporting

This year saw two bills dealing with combined reporting. Combined reporting is a method of calculating corporate income taxes that treats legally independent, yet practically connected, business units as one large unit for tax purposes. Rather than solely looking at the income reported in Maryland, combined reporting would tally up the nationwide income of a business, then calculate what fraction of that income should be allocated to Maryland based on a number of factors.

About half of the states that have a corporate income tax use the combined reporting method, as opposed to the "unitary business" method that Maryland uses.[53] Several of those states adopted combined reporting within the past decade in response to a number of high profile tax evasion cases. Supporters of combined reporting argue that it will be more effective in combating tax evasion than legislation targeting specific types of tax havens, and that it ensures multi-state businesses are paying a fair share of state taxes when compared to individuals or businesses operating only within the state. Opponents warn that the changes are unnecessary, will impose higher accounting costs on businesses, and simply shift taxes from one sector to another.

The Comptroller has so far provided two analyses of projected revenues in tax years 2006 and 2007, had combined reporting been adopted.[54] Estimates indicate that in 2006, combined reporting would have generated approximately $144-$197 million in additional tax revenue; in 2007, the increase would have been $92-$144 million. The analyses stress that these estimates are not generalizable to current or future years, as the economic climate has changed drastically in the intervening time, and in some cases the sectors responsible for the additional revenue were those most affected by the recession.

While significant contention over the merits of combined reporting remains, the dearth of empirical evidence regarding the effects of its adoption, along with the unclear effect on state revenues, indicate that further study is needed before a decision is made as to whether to adopt combined reporting, rather than proceeding forward with implementation, as **HB 584** advocates.

What lawmakers should not do is simply view combined reporting as a guaranteed revenue boost, a quick fix for more serious, long-term structural problems. Unfortunately, this is just the approach that **SB 354** takes. Instead of addressing the serious long-term burden of the state's growing pension costs, the bill seeks to push these costs onto some other revenue source, and singles out combined reporting as the solution to all the state's pension woes.

HB 395 / SB 336 moved the deadline for the final report of the Maryland Business Tax Reform Commission up by one year, to December 15, 2010. The commission is charged with evaluating a variety of business tax reform proposals, including combined reporting. The final report from the commission will likely play an important role in determining the reception of combined reporting in next year's legislative session.

Estate Tax

SB 591 would have increased the upper limit on exclusions from the state's estate tax from $1 million to $2 million. The appropriateness of the estate tax is a contentious issue; this legislation would have had a significant fiscal effect, resulting in revenue decreases from $22 million in 2011, up to $33 million in 2015. The fiscal and policy note suggest that some small businesses would benefit from the increased exclusion amount, though figures from the Congressional Budget Office indicate that the number of

small businesses and farmer filing estate taxes is relatively small (around 2 percent).[55]

See the "Education" section for an analysis of four other bills that involve tax credit legislation, but are categorized here as educational legislation: **HB 946 / SB 385, HB 952,** and **SB 203.**

Ethics & Transparency

SB 315 requires local ethics laws regarding conflicts of interest or financial disclosure to meet or exceed State requirements; while a similar requirement already existed, the state has adopted model regulations for local governments to follow, and because a significant number of local governments do not yet meet state standards, this bill will have a positive effect.[56]

HB 107, the Legislative Voting Sunshine Act, would have required the results of all roll call votes of standing committees to be made available on the General Assembly's website for easy public access. Currently, the results of such votes are recorded and are part of the public record, but until this year were not available online. Committees play a critical, powerful role in the actions of the General Assembly, and Maryland's citizens should enjoy convenient access to the results of committee votes in order to see how their elected representatives voted. The cost of making the information available online is minimal, but the public benefit large. While the bill did not pass, the Department of Legislative Services nevertheless did post committee votes online during this legislative session.[57] At a minimum, the General Assembly should ensure that this practice is continued in future years, if not expanded to all committee votes, as this bill proposes.

Another bill that would have had significant effects on open government in Maryland failed to pass. The Maryland Open Government Act, **HB 344 / SB 407,** would have required meetings of the Board of Public Works (BPW) and standing committee of the General Assembly to be streamed live over the Internet, allowed members of the public to sign up online to testify at a hearing on a bill, required the Board of Public Works to take public comment on its proposed budget actions in advance of meetings and archive the recordings of the meetings, and repealed an $800 annual fee charged to access real-time legislative information at the General Assembly's web site.

It also includes the provisions of the Legislative Voting Sunshine Act discussed above. Costs are partially offset by an increase in the registration fee for lobbyists. While the notice requirements for meetings of the Board of Public Works could potentially cause logistical problems, this bill would have done much to shed light on the critical apparatus of the state. In any case, despite the bill failing to pass, the current administration began the practice of streaming BPW meetings online, and the $800 fee for real-time information from the General Assembly website has been dropped. These practices should be continued in the future; passing legislation will ensure that a future administration or legislature cannot undo this progress.

HB 1570, the Open Government Modernization Fund Act, would have established a fund dedicated to improving transparency and public participation in the legislative process with the proceeds from a significant increase in the registration fee for lobbyists. However, the specific goals of the fund are not indicated; the assumption is that the fund will be used to purchase equipment for the live streaming and archival of legislative sessions and committee meetings and General Assembly website upgrades. While this bill has a noble goal, the Maryland Open Government Act, discussed above, makes clearer and more immediate steps towards transparency and public participation, albeit at higher cost.

Once again, **HB 1195,** which would have prohibited revolving-door style lobbying by former members of the executive branch for a period of one year, passed the House but made no progress in the Senate.

Pensions & Retirement

One of the most controversial proposals of the legislative session was **SB 959,** which would have begun the process of shifting the cost of teacher pensions away from the state and on to local county governments. Currently, the state pays the full cost of employer contributions for teachers' pensions, even though teachers are employed by local governments, and local governments set

the salaries and compensation upon which pension benefits are based. In order to take some of the pressure of growing pension costs off the state, this bill would have shifted increasing increments of the costs to the counties, with the ultimate goal of costs being shared equally between the counties and the state. Detailed information on the fiscal effects of shift was not made publicly available, but the Maryland Association of Counties has posted a scanned copy that was distributed during discussion of the bill; costs to counties quickly increase from $63.4 million in 2012 to $328 million in 2014 and $337 million in 2015.[58] A similar proposal is expected in next year's legislative session, and numerous observers are predicting a higher chance of success. While this bill does not directly address the factors contributing increased pension costs, by shifting costs onto the counties, it does give the counties an incentive to seek ways to reduce pension costs. As it stands now, counties have no incentive to keep teacher pension costs in check, since they do not have to foot the bill for them.

SB 141, the Budget Reconciliation and Financing Act, also establishes the Public Employees' and Retiree's Benefit Sustainability Commission which is "charged with reviewing and evaluating the recruitment practices, retention incentives, actuarial liabilities, actuarial funding method, cost drivers, employee contribution rates, and the comparability and affordability of the benefit systems."[59] While the state could have benefited from such a review several years ago, specific legislative recognition of the unsustainability of Maryland's public sector pensions is a positive change. The value of the commission, however, will only be proven by the recommendations it is due to make in advance of the next legislative session, as well as the extent to which the General Assembly acts on those recommendations.

With **HB 771 / SB 444**, the General Assembly delayed yet again the deadline for long-awaited final report from the Blue Ribbon Commission to Study Retiree Health Care Funding Options. An interim report was issued by the commission was in late 2008, and identified a potential $15 billion liability for unfunded retiree health care costs. The commission was slated to deliver a "comprehensive, multi-year plan to fully fund the State's OPEB obligation" by the following year.[60] However, the deadline for the report has been continually pushed back. Initially set for late 2008, it was extended to 2009, then mid-2010, and now another two years, until mid-2012. One reason for the delay is the current debate over healthcare reform at the federal level; some observers have suggested that a federal "bailout" plan of some sort could eventually address the problem of ballooning OPEB liabilities.

In the meantime however, the state lacks any consistent, sustainable plan to address its OPEB liabilities, which constitute a huge and growing portion of retirement costs. Part of the challenge is that faced with declining tax revenues, poor investment performance, and increasing health care costs, state legislators may simply not want to face the fact that any comprehensive plan addressing OPEB liabilities will either require significant benefit cuts or large tax increases.

As noted in the discussion of combined reporting, **SB 354** proposed using increased revenues from the corporate income tax to establish a fund devoted to shoring up the State's pension system. Yet the actual revenue increases due to combined reporting in the coming years are unclear, and without addressing ballooning pension costs, such a proposal is simply an irresponsible attempt to pass the buck.

HB 845, if passed, would have constituted inappropriate legislative interference with the pension system's stewardship of funds. The bill would have required the pension system to invest millions of dollars of its assets in certain high-tech business sectors based in Maryland. Rather than having the General Assembly pick investments for it, the pension fund management should retain complete flexibility to seek out the most promising and prudent investments, especially given the volatile market conditions of the past few years. Mandating investment in certain businesses by law is a bad idea: if the high-tech business sectors specified in this bill are truly good investments, then nothing will prevent the pension system from investing in them on its own initiative. **SB 793**, the Senate version of the bill, did pass, but instead of requiring a certain amount of investment, simply has the pension

system provide a list of businesses and amounts invested in such sectors.

HB 1543 would have required the preparation of a quarterly report containing information on the status of the state pension system's funds, as well as quarterly reports assessing the state's OPEB liabilities. Since most of the information on the system's fund balances and performance is already available, albeit not necessarily in a convenient format, a quarterly report would be both inexpensive and a public convenience. Quarterly actuarial valuations of the state's OPEB liabilities, however, would necessitate additional spending on an actuarial consulting firm. Since an annual valuation is already conducted, three additional valuations each year are likely unnecessary. A better option would have been to insist that the Blue Ribbon Commission on Retiree Health Care Benefits prepare its final report.

HB 775 / SB 317 were emergency bills passed in order to prevent retirees receiving benefits from the state from experiencing a slight decrease in benefits due to a negative cost-of-living adjustment (COLA) based on a drop in the consumer price index (CPI). Benefits are instead held constant, necessitating a slight increase in pension contributions paid by the state. Many of the state's pension plans include COLAs that are indexed to inflation; however, in 2009, the commonly used measure of inflation decreased slightly. For an average beneficiary, the decrease would have meant about $6 less in monthly benefits.[61]

While the increase in liabilities for the overall pension system due to this measure is relatively minor, the fact that legislators are going out of their way to avoid even the slightest reductions in benefits does not bode well for the future. With a massively underfunded pension system (the total funding status of all the state's pension systems combined stands at 64.36 percent) and growing retirement costs, the General Assembly is well aware that action is urgently needed in the near future.[62] But when the time comes, it's unclear if the political will for change will exist.

HB 1379 / SB 1061 were proposals to change the funding method for the state's pension system; in the short term, they would have required significant additional contributions by the state. The long-term intent of the bills is unclear, and may either revert to the original funding method, or continue the new method, resulting in some savings but continual underfunding of the pension system. Regardless, the proposed change in the funding method has almost no discernible effect on the overall funded ratios of the state's pension systems. This sort of proposal represents a stopgap measure that does nothing to address the fundamental issues facing the state's pension system.

Education

HB 350 / SB 758 express legislative support for the state's Department of Education to take the necessary steps to allow the state to compete for federal Early Learning Challenge Fund dollars. The federal fund will target educational environments for young children, and will be awarded to states through a competitive process.

HB 439 / SB 452 require the State Board of Education to study alternative schooling schedules, such as year-round schooling, specifically for low-performing schools. While the bill is targeted at low-performing schools, its fiscal and policy note suggests that all students could benefit from an alternative schooling schedule that avoid long gaps in instruction. Because this bill does not include any reporting requirements, however, it seems unlikely to engender serious consideration of alternative schooling schedules.

SB 275 creates a data collection and research system that will link student school data with data about the Maryland workforce, with the goal of generating information and improving research, and in turn informing policy and spending decision in the State. A revamping of the state's current data collection system is one component that likely helped Maryland win $250 million in federal Race to the Top funds, which were awarded on a competitive basis to states implementing a number of reforms. The data collection system will include privacy safeguards, complying with applicable federal privacy laws, such as ensuring that no individual student/worker data is made available.

Since one of Maryland's economic assets is a highly educated workforce, and education

spending constitutes a large portion of the state's budget, projects such as this data collection system, which will provide the raw information to help ensure that the state's education dollars are being spent effectively, are a worthwhile investment. The data collected by the system will also be available to outside researchers, allowing for independent analyses to be conducted.

SB 551 / HB 836 permits local governments to give preference in procurement bidding both to businesses located in the same county, and businesses located in the state, for certain public school construction projects. To the extent that procurement decisions are not based on standard criteria, such as the lowest qualified bidder winning, this may increase the cost of procurement. While such increased costs could in theory be offset by increased tax revenue and multiplier effects that come as a result of awarding contracts to local businesses, in general, the fiscally responsible approach avoids playing favorites with the procurement process. As the Board of Public Works is required to set regulations regarding such preferences, limitations on the extent of the preferences should be established; for example, if a local bid exceeds the lowest bid by a certain amount, then the preference should be for the lowest bid, rather than the local bid.

HB 1362 permits local school boards to establish "virtual schools," which will offer full, state-approved school curricula and classes conducted online. While the fiscal analysis of the bill notes that overall state expenditures could increase, if, e.g., virtual schools attract formerly home-schooled students, it also notes that in the long-term, virtual schools may reduce per-student costs for the state. Additionally, virtual schools could also attract current public school students in some cases, potentially decreasing costs. Before such schools are established, however, the state Department of Education will spend a year developing rules regarding how they are to function. The cost estimates in the bill only reflect the development of regulations, not the actual operation of virtual schools.

HB 1263 / SB 899 lengthens the time before which public school teachers may be granted tenure from two years to three years; the lengthening only applies to new employees. Maryland's previously shorter pre-tenure period may have contributed to its failure to receive a grant from the Bill and Melinda Gates Foundation; likewise, lengthening the period may have made the state's application for Race to the Top federal funds more competitive.

The bill also provides for an incentive program to support high quality teachers in low-performing schools; the program would offer stipends to teachers and principals deemed "highly effective" working in such schools. Federal funds could be used to provide these incentives, but do not necessarily have to be. Criteria for determining "highly effective" teachers have not yet been specified. While this program has the potential to be a form of merit pay, the state should ensure that the selected criteria actually identify quality teachers based on performance, rather than simply the fact that teachers are working in underperforming schools.

HB 470 / SB 283 establishes a college tuition stabilization fund that will be used to supplement expenditures from the general fund in order to prevent tuition at public universities and colleges from increasing too quickly. The fund is created within the Higher Education Investment Fund, which itself is funded from a portion of the corporate income tax. When the corporate income tax was increased in 2007, a partial distribution from the tax was temporarily authorized; this bill makes that distribution permanent, so that 6 percent of the corporate income tax goes to the HEIF and 9.15 percent to the general fund, rather than the entire amount to the general fund.

Because the tuition stabilization fund is used to supplement general funds that would be spent anyway, the net financial effect of the bill is small. Still, while the goal of the bill is to constrain tuition increases to a reasonable level (defined by linking them to a rolling average of state median family income), without a clearer picture of why tuition costs keep rising, far outpacing inflation, we are not treating the root of the problem.

Three related bills this session attempted to establish legislation codifying a financial literacy curriculum to be taught in public high schools across the state. **HB 764 / SB 264** and **HB 335 / SB**

1030 both would have required the state's Board of Education to develop such a curriculum and made it a requirement for graduation. **HB 853 / SB 1060** proposed reporting requirements for the curriculum.

The push to establish a financial literacy curriculum comes as a result of recommendations from a state task force established in 2008, itself a response to the housing and financial crises. Even though these bills did not pass, the state's Department of Education has been developing content standards, and with the approval of the Board of Education will implement it in the 2011-2012 school year. It will be up to local school systems to determine how best to teach the curriculum, and whether to make any specific courses a graduation requirement.[63] Fiscal analyses suggest that the total costs to local school systems will be about $17.4 million for both instructors and materials.

HB 1384, the Restore Respect at School Act, was introduced again this year. The bills attempts to create a financial incentive for parents to encourage their child's attendance and participation at school by prohibiting parents from receiving tax credits for their dependent child if the child failed to meet certain minimal standards for completing homework assignments, behavior, and attendance. The homework requirements are evaluated on the basis of effort, so that they do not penalize children who may have learning disabilities or difficulty with particular subjects.

Likewise, the attendance requirement is minimal, penalizing parents only if a child was absent and unexcused for more than 20 percent of the school year. The tax credit may be reinstated if a parent takes certain actions, such as meeting with school officials after a suspension. The bill also has income restrictions to ensure that the tax credit cannot be denied to needy families; however, these restrictions may prevent the legislation from achieving its full potential effect. In any case, the bill received an unfavorable report in its committee.

HB 946 / SB 385, Building Opportunities for All Students and Teachers (BOAST), would create an income tax credit for 75 percent of a business's contributions to non-profits that offer scholarships to private K-12 schools that offer grants to public schools that adopt innovative educational programs, or than support public school teachers in obtaining certification.

BOAST is a particularly good investment for all parties involved: students who receive scholarships through the program have the opportunity to attend high-performing private schools; as fewer students attend public schools, the state saves money; all the while, the state still captures 25 percent of the value of business contributions as tax revenue.

BOAST passed in the Senate this year, as well as in 2008. In both cases, however, it did not manage to pass the House. By passing BOAST, the General Assembly will take a step towards ensuring that high-performing private schools do not have to close. Rather than simply a subsidy to private schools, it is in the state's self-interest to ensure the continued operation of private schools: students who leave private schools for public ones require the state to absorb (and pay for) them at a cost of nearly $13,000 per student.[64]

So that the total amount of tax credits does not overwhelm the state budget, the bill requires a cap on the total amount of money available for credits each year. Similar programs exist in several other states; in Pennsylvania, for example, nearly $45 million worth of tax credits for scholarships to private K-12 schools were used this past year. A similar program in Arizona awarded about $11 million in tax credits for corporate contributions to scholarship organizations. Florida has also enacted a similar tax credit, awarding about $113 million in credits last year; in exchange, an average of about a $7,000 scholarship was donated to over 21,000 students to attend private schools. While Florida has a per-pupil spending amount below the national average, Maryland's amount is well above the average, so the potential returns to the program are even greater.

As last year, **HB 952,** a scaled-down version of the legislation which would have applied only to preschools was also introduced. The credit would have been available for contributions to scholarship organizations targeted low income families. The "Great Preschools Tax Credit Program," received only a first reading, however.

HB 1121, the "Great Preschools Scholarship Program" was introduced last year as the "Smart Start Scholarship Program." The bill proposes a voucher-like program that creates a scholarship for up to 100 percent of the amount of state and local money spent educating a child, permitting parents to use that scholarship to send their children to participating public or private prekindergarten programs.

While this would give parents more flexibility in choosing a pre-kindergarten program, and create further competition between both public and private pre-kindergarten programs, the bill as written could impose significant fiscal burden on localities that would not be offset by state aid. Furthermore, the bill could potentially end up providing a significant portion of scholarships to children already attending private preschools, subsidizing these current students rather than encouraging new ones to attend. The tax credit programs discussed above have the advantage of offsetting their cost by potentially reducing state expenditures in other areas, whereas this program would require local governments to increase spending without a corresponding reduction in costs elsewhere.

SB 203 would have conformed state income tax treatment of Coverdell Educational Savings Accounts to be more like the treatment of 529 plans. Coverdell ESAs differ from 529 plans primarily in that they may be used for educational expenses not only for college, but also primary and secondary schooling. This bill would have allowed up to $1,000 ($2,000 for those filing joint returns) of contributions to be deducted. The maximum contribution allowed in a given year for Coverdell ESAs is $2,000. To the extent that extending these tax benefits encouraged more Marylanders to save and invest in anticipation of their children's future educational expenses, the relatively minimal cost of the benefits would be worthwhile.

SB 674, the Robert Kittleman Scholarship Reform Act, would have eliminated senatorial and delegate scholarships. Each year, in a little-known program, every state senator is allotted $138,000 and every delegate $35,436 to distribute essentially as they see fit, with very few restrictions and almost no oversight. The scholarships have persisted for decades, are unique to Maryland, and have been a subject of criticism for decades.[65] Some have likened the scholarships to a vestige of patronage, and indeed, instances of senators or delegates awarding scholarships to friends and relatives are widely known.

Eliminating the scholarships completely would only save the state about $11.6 million annually; a better idea might be to transfer the funds to other scholarship programs, some of which were targeted for cuts this very year. For example, the governor's original budget proposal aimed to eliminate the Maryland Distinguished Scholar program, a merit-based award, a program that costs slightly over $1 million annually.[66]

HB 1036 / SB 866 would have altered the method by which the calculation of state aid to counties for education is computed. Currently, the full amount of enrolled students is used; this bill would shift to a method that recognizes that only 94.3 percent of students show up on an average day. This policy change has the potential to create incentives for local school systems to decrease absenteeism, since by doing so they will be eligible for more state aid.

The change has the potential to save the state a significant amount of money: over $100 million by 2012, and reaching a $180 million savings per year by 2015. The bulk of reductions in state aid will fall upon Baltimore City and Prince George's County (nearly a third and one-sixth, respectively). The fiscal and policy analysis notes that the reduction in aid could be partially offset by a reduction in the amount of education aid required to be contributed by the county or city—the "maintenance of effort" requirement.

Maintenance of Effort

HB 223 / SB 476 waives a penalty that would have been imposed on Montgomery County for failing to meet its required "maintenance of effort" levels of funding for county schools. Had the penalty been imposed, the county would have not received a $23 million increase in state funds for county schools.

Maintenance of effort (MOE) refers to a state law that requires county governments and Baltimore city to fund their school systems with at least as much money per student as provided in

the prior year. The impetus behind this requirement is to ensure that counties do not simply use state aid for education to replace local spending on education, but rather use the state aid as a supplement.[67] While the intent is reasonable, the implementation is less than perfect.

First, as numerous commentators have pointed out, it hardly makes sense to penalize the school system for the failure of the county to provide enough funding to that school system. Reform of MOE will have to include a more properly targeted application of any penalty. Instead of withholding funding increases from the school system, for example, the state could instead require the county to contribute the amount of the penalty in funding for teachers' retirement payments, which are normally paid by the state.

Second, the design of MOE creates a ratchet mechanism: while counties are only required to meet last year's per-student funding, if they exceed it, they thereby set a new, higher bar for next year. The effect is that while funding may be generous in good years, when a tough year comes around, the prior year's funding determines the minimum level of funding for the current year.[68] This is essentially what spurred the current failure of three counties to meet MOE requirements. A better alternative would be to constrain the growth of the baseline to which the current year's funding is compared, perhaps by linking the baseline to a measure of inflation. Finally, MOE effectively makes it impossible for a county to ever reduce per-student spending.[69]

Spending is not a proxy for the quality of education provided. There are legitimate reasons why per-student funding might decrease, either through increased administrative efficiency and cost-cutting programs, or in recent years, deflation, lack of salary increases, and declining enrollment. Yet, the only way for a county to propose a decrease in per-student funding is to request a waiver from the State Board of Education. Until this year, no waivers had ever been requested.

In this case, the General Assembly's decision to waive the MOE penalty for Montgomery County was sensible. Next year's legislative session will likely include a hard look at reforming MOE; in doing so, legislators should ensure that 1) in accordance with the original intent of MOE, state funds are not simply replacing local funds, thereby shortchanging state taxpayers; 2) MOE requirements do not penalize states for funding school systems beyond the minimum; and 3) the requirements do not discourage spending reduction when appropriate.

Regulation

HB 72 expands the regulatory capacity of the Maryland Department of the Environment in anticipation of a large increase in the number of natural gas drilling permits requested for the Marcellus shale formation, portions of which exist in several western Maryland counties. Other states have also expanded regulatory capacity in order to deal with side effects of drilling, such as concerns about overuse and quality of water supplies and other environmental issues.

The additional regulatory staff and operating expenses are funded by permit fees charged directly to the businesses involved in drilling, and estimates indicate that the regulatory program will be self-sustaining, needing no infusions of funds from general state coffers, although the bill does permit outside funding. Additionally, to ensure that the cost of regulatory permits is not excessive, the legislation requires fees and permits to be linked to the operating expenses of the program, and reduced if revenue exceeds those expenses.

HB 799 requires private lenders offering reverse mortgages to conform to the same standards as federally insured home equity conversion (HECM) mortgages. Federally insured mortgages comprise the vast majority of the reverse mortgage market, but because of consumer complaints and confusion and the complexity of some reverse mortgage offerings, there has been a push for enhanced regulation of these financial products.

SB 277 increases the required amount of solar power that electricity suppliers must obtain. Under current law, electricity suppliers are required to purchase an annually increasing amount of power from renewable energy sources. This bill accelerates the annual increase in the years 2011 to 2016, but maintains the final target percentages for 2022.

Electricity suppliers must either purchase solar power credits, whose price is determined by a market for trade in such credits, or pay an alternative fee should they fail to obtain such credits; this bill also increase the associated fee. The total amount of available credits is determined by the amount of solar power being generated in the state. Given that only a limited amount of solar power generation capacity exists in the state, electricity suppliers historically have been unable to meet the state's requirements through the purchase of credits alone; compliance is achieved by a mix of purchased credits and fees paid to the state, and this is likely to remain the case for the foreseeable future.

As a result, this renewable energy requirement has the effect of a tax on electricity suppliers. Estimates indicate that due to the increase in fees, state revenues will increase by $2 million in 2012, up to $25 million by 2015. These revenues accrue to the Maryland Strategic Energy Investment Fund, which in turn is used to subsidize the installation of solar power generating facilities.

This bill, and the policy of setting renewable energy requirements in general, are based on the premise that funds generated from fees will be used to incentivize enough investment in solar energy to offset the short-term costs of the requirements. However, 2022 is a long way off, and just as this bill has increased requirements today, it is entirely possible that a few years down the road, when the requirements begin to become more and more costly, that they will be capped or revoked. Thus the long-term outcomes of this policy are highly uncertain.

However, according to the bill's fiscal and policy note, "Regardless of the assumptions made, what can be predicted is…a near-term cost that must be absorbed by all electric customers in the State."[70] This includes the State government itself, whose annual expenditures on electricity exceed $220 million. Estimates indicate that the increased requirements will add an additional $0.77 per month for residential customers, and nearly $10 per month for commercial customers; these estimates account only for the increased requirements, and so do not fully convey the full cost of the policy. As the requirements continue to increase significantly until 2022, the cost per month to customers will also increase significantly.

SB 807 represents the perennial effort of some lawmakers to return to a regulated electricity market. In this case, the bill would have required the Public Service Commission to develop a plan for returning to a regulated market for residential and small commercial customers. As we noted last year, a study conducted by the Public Service Commission concluded that a return to a pre-deregulation state would be risky and potentially involve significant costs and uncertainty for Maryland ratepayers. Little has changed since last year's similar proposals, and this year's fiscal and policy note for the bill reflects this: "In the long run it is unclear whether electricity purchased by residential and small commercial customers under a regulated market will be less expensive than electricity purchased in a competitive market."[71]

Instead of pining for pre-deregulation days, lawmakers should be focused on new solutions, such as encouraging new generation capacity in Maryland, and potentially promoting longer-term contracts for electricity suppliers, thereby increasing price stability.

HB 744 would have required the Public Service Commission to conduct an advertising campaign designed to make electricity customers aware of potentially lower priced electricity suppliers available to them. The Commission originally hired a contractor to complete a multi-million dollar awareness campaign around the original time of deregulation, but the impact of the campaign may have been mitigated by the fact that at that time, other state energy policies severely limited the benefits of choosing alternative electricity suppliers.

In this case, the Commission would be authorized to essentially levy a small tax on electricity suppliers to pay for the campaign. From the perspective of alternative electricity suppliers, this campaign would be a form of free advertising. While alternative suppliers in many cases can offer more competitive pricing, it is hardly appropriate to tax one supplier in order to offer free advertising to another.

Labor & Collective Bargaining

HB 243 / SB 590 establish the Public School Labor Relations Board, essentially replacing the authority of the state's Board of Education (BOE)

to decide labor disputes involving public school employees. The bill also removes the authority of local boards of education to make final decisions on negotiable issues, a provision which has garnered criticism from the Maryland Association of Boards of Education. In the past, the State Board of Education's decisions on labor disputes between unions and local BOEs were not binding; the new PSLRB, however, will be able to make binding decisions. On the other hand, teachers' unions have supported the bill.

It is hard to predict the effect that the new PSLRB will have on collective bargaining specifically, and other general issues such as teacher salaries, educational policy, pensions, etc. To the extent that the PSLRB is more favorable to labor organizations, labor costs, and associated costs, such as retirement contribution rates, could increase.

HB 465 / SB 284 codifies the existing agreement the Administration has recognizing Service Employees International Union (SEIU) as the exclusive collective bargaining group for child care providers who participate in the state's child care subsidy program. The subsidy program provides payments to child care providers who care for children from families meeting certain requirements: e.g., the parent must be working or in school and fall within income thresholds.[72]

Separate from this bill, the union has negotiated a 3 percent rate increase for providers caring for children in the subsidy program. Funds for the child care subsidy program have exceeded $100 million since at least 2004, though the FY 2011 appropriates $93 million; the state portion is held constant at $33.6 million, with federal funds accounting for the other $60 million.[73] Federal funds used for this purpose have been declining in recent years; rate increases combined with declining funding may therefore represent a budgetary problem in future years.

While child care providers who receive subsidies are currently not required to join the union, they may be required to pay a service fee intended to represent the contribution of the union to the benefits accrued in a contract negotiated with the state. For this reason, providers are divided in opinion over whether union representation represents a positive thing.[74] Because this bill codifies current policy, cost estimates are not included; to the extent that union bargaining raises costs, the amount the state must devote to the subsidy program may increase significantly in the future.

SB 225 / HB 881 would have established collective bargaining with an exclusive union for certain library employees, excluding those in Montgomery and Prince George's counties, which already have a collective bargaining arrangement. According to the bill's fiscal and policy note, union dues in those counties are $10 per week.[75] The bill was contentious, with several counties requesting to be removed from consideration; library administrators suggested that union leadership, rather than actual library employees, were the driving force behind support for the legislation.[76]

Collective bargaining has the potential to increase costs for localities, both administratively for hiring outside mediators, and for increased salaries and benefits awarded in negotiations. State expenses could also increase, since the state contributes to both pension and non-pension retirement benefits for librarians that are based on salaries set at the local level. While retirement contributions for library employees represent only a fraction of those made for school system employees, this is yet another example of the disconnect between salary-setting at a local level, and retirement payments at the state level.

HB 815, strongly supported by the Fraternal Order of Police, grants collective bargaining rights to certain Maryland Transportation Authority (MDTA) police officers. As MDTA police are a relatively small state law enforcement agency with a budget sustained by toll revenue rather than general funds, the effect of collective bargaining negotiations on the rest of the state budget will be limited. Nevertheless, MDTA generally is facing a major budgetary imbalance that will likely necessitate future toll increases.

SB 887, the State Correctional Officers' Bill of Rights, establishes new procedures for correctional officers accused of misconduct. Supported by the AFSCME, the bill requires disciplinary cases to be reviewed internally with the potential for appeal. Prior to this bill, cases that resulted in suspension or termination would have included

30 days of paid leave; this bill allows the employee to remain on the payroll throughout any appeals process, and accounts for the significant fiscal effect of the bill, ranging from $2.6 million to $3.1 million annually over the next five years.

Miscellaneous

Car Insurance

HB 825 increases the minimum amounts required to be covered by car insurance policies sold in the state. Minimum covered amounts for injury or death increase from $20,000 to $30,000 (one person) and from $40,000 to $60,000 (multiple persons). While these amounts have not been adjusted since 1972, it remains unclear whether these adjustments, which will undoubtedly increase car insurance premiums in Maryland, are necessary.[77] The fiscal and policy note for this bill indicates that for 99 percent of claims handled by the Maryland Automobile Insurance Fund (the public insurer of last resort for Maryland), the current coverage amounts are sufficient; indeed, more than 98 percent of MAIF's covered clients choose the standard amounts.[78]

While the Department of Legislative Services rightly indicates that MAIF's experience with coverage choices cannot be considered representative of the entire market, it is not clear that MAIF's experience with claim amounts should not reflect the larger market. Finally, even if coverage amounts did eventually require adjustment, choosing to do so in the current economic climate is likely to adversely affect thousands of Marylanders, hitting them with car insurance increases just as they are likely to face higher health insurance premiums and flat earnings.

Voting & Elections

HB 1060 would have delayed the purchase of a new voting system several years. Although Maryland law requires the use of voting machines producing a paper record, the state's current system is incapable of doing so. The FY 2011 budget contains no appropriation for the purchase of a new system.

Maryland's experience with voting systems in recent years has been less than enviable. In 2001, the state purchased electronic machines from Diebold (now Premier Election Systems). Soon thereafter, numerous problems and flaws with the machines were discovered. In spite of this, and in large part because of budget constraints, the machines remain in use, even though they do not comply with current Maryland law. The state is still paying down the purchase price of the machines, with the last payment scheduled for 2014.

Although the fiscal and policy note for the bill suggests that small businesses could be adversely affected by the state's delay of purchasing equipment, given the very high concentration of vendors in the voting system market (so concentrated that the top vendor was recently scrutinized by the Justice Department's antitrust division), this appears very unlikely.[79] If and when the state does purchase a new system, it should ensure such a system is both secure and reliable.

Gambling/VLTs/Slot Machines

SB 882 / HB 1077 increases the operator's share of slot revenue in Allegany County, but only if the operator also purchases the troubled Rocky Gap Lodge and Golf Resort from the state. The resort has long been the subject of criticism for being a money drain, consistently failing to operate profitably, and accumulating millions of dollars in debt that are still being paid off.

This bill, by temporarily increasing the operator's share from 33 percent to 35.5 percent for five years, attempts to encourage a slot machine operator to also purchase the resort and golf course. It remains to be seen whether the 33 percent distribution alone is enough to induce qualified bids for the license in Allegany County; the one bid that was received was rejected. Obviously it is in the state's interest for the money-losing resort to be taken over by a private operator, and for that reason, this bill's logic is sound; if anything, an even greater incentive might have been appropriate.

HB 1288 proposed expanding the availability of slot machine licenses by allowing 5,000 new machines to be distributed across the state, with a maximum of four machines at any one location, and was contingent on a related proposed constitutional amendment, HB 1066. The revenue impact of additional machines is notoriously difficult to estimate; ever since Maryland voters approved slot machines in 2008, the awarding

of licenses and installation of the machines has been plagued with delays. The bill's fiscal and policy note gives a tentative suggestion of a $120 million annual increase in revenue, assuming that all 5,000 machines are distributed.

As many Marylanders recently discovered, the original legislation permitting slot machines in the state requires the state to either purchase or lease those machines, at a substantial up-front cost to taxpayers. The state's first contracts were concluded in June, and consisted of the purchase of nearly 800 machines, and the 5 year lease of another 260. The total cost of the contracts, concluded with six vendors, was over $49 million or an average cost of over $46,000 per machine. A significant portion of that cost covers installation and maintenance of the machines; nevertheless, the logic of this policy is questionable. Instead of purchasing the machines with taxpayer dollars, a significant acquisition of illiquid capital, it would make more sense for the state to allow private businesses and operators to purchase the machines themselves. This would shift the risk away from the state and onto the individual businesses that choose to operate slot machines. Otherwise, the state could be spending anywhere from $100 million to $250 million purchasing or leasing new machines.

Given this bill's proposal to permit the small number of four machines in a given location, requiring individual businesses to foot the bill for the machines they operate only makes more sense. There is no way the state can know whether each of the potentially 1250 locations will be a profitable endeavor; some will doubtless be losing propositions. Let individual businesses take the risk with their own funds, rather than using state-owned equipment.

While both the state and local revenue implications of expanding slot machine licenses are in theory positive, as long as the state is purchasing and maintaining the machines, the whole enterprise remains questionable.

HB 512 proposed allowing up to 2,500 slot machines to be installed at BWI airport, and having state revenues from these machines distributed primarily to the Transportation Trust Fund, rather than the Education Trust Fund, as is the case with other locations. Currently, only two other airports in the United States, both in Nevada, have slot machines. As with the bill discussed above, this would have been contingent upon a constitutional amendment proposed in **HB 513.**

From a policy standpoint, there are good reasons to place slot machines at an airport rather than some other facility, especially inside the security zone where only ticketed passengers are permitted. A large portion of patrons at the airport will be non-residents, and may only have the chance to patronize the machines at the airport. This represents a potential revenue gain for both operators and the state, without taking away business from other slot facilities in the state.

Nevertheless, as discussed above, since the state is required to purchase, lease, and maintain slot machines, adding additional machines represents a significant initial outlay for capital, potentially $50 million to $100 million. It would be better policy to permit a private business to assume the risk for a such a venture.

Second, this bill attempts to shore up the financial position of the Transportation Trust Fund; however, a better solution to this problem would be for the state to stop borrowing from that fund in order to balance the budget, as it has done in previous years, and as **HB 383**, the Transportation Trust Fund Protection Act, proposed. Estimates indicate that adding slots at BWI as this bill proposes could generate about $18 million in revenue for the Transportation Trust Fund annually, beginning in 2015.

This is less than one-half of one percent of the TTF's annual revenue. By comparison, since 2003, over $737 million has been borrowed from the TTF to balance the state's budget. While this borrowing comes with a promise of repayment, in some cases that repayment has come in the form of new debt issues, and so does not really represent true repayment.

HB 885 would have altered the distribution of revenues from slot machines. Instead of directing up to $100 million of revenue to the "Purse Dedication Account," which is a subsidy for the horse breeding and racing industries, the revenue would instead have been dedicated to public school construction and capital improvement. To the extent that this revenue could decrease the amount of debt the state would normally have to issue, this change would be welcome and a

significantly more prudent use of slot machine revenues.

However, the bill also contained a provision that would have allowed the state to borrow money for such construction and improvement in anticipation of slot machine revenue. Borrowing in anticipation of revenue that is already below estimates and behind schedule is a bad policy, to say nothing of potentially adding additional debt to the state's already large burden. According to this bill's fiscal and policy note, "Debt service costs are projected to exceed revenues beginning in fiscal 2012;" the costs are growing significantly faster than the revenue supporting them.[80]

Traffic Laws

HB 829 now requires that people receiving traffic tickets must request a court date if they intend to dispute the ticket and fine, instead of automatically being assigned a court date. Failure to pay the fine combined with failure to request a court date could lead to suspension of one's license. Because the police officer who issued the ticket is required to be present at the court when a ticket is disputed, court appearances can result in increased overtime payments for police officers, as well as scheduling problems, potentially decreasing the efficiency of police services. Importantly, in a large amount of court dates, the person issued the ticket fails to appear; estimates indicate that this may be as often as 50 percent of the time. By requiring persons who receive tickets to request court dates, they are more likely to show at the trial, and potentially fewer court dates will be requested than assigned. This will increase savings in various police departments (e.g., Montgomery County reports that $3.5 million in overtime pay are spent to have officers appear in court), and increase the efficiency of those departments and the traffic courts.

SB 321, the Delegate John Arnick Electronic Communications Traffic Safety Act of 2010, bans the use of cell phones for conversing without the concomitant use of a hands-free device, such as a headset. Under current law, composing or sending text messages is already illegal; however, in what some consider to be a loophole, reading such messages remains lawful: the General Assembly failed to agree on the specific language of a ban this session, despite HB 192 passing both houses.

While the text messaging ban is a "primary offense," meaning that one can be stopped for text messaging alone, the law banning phone conversations without hands-free devices while driving is a "secondary offense" only, meaning that one must be violating some other traffic law in order to be stopped. Penalties include fines that increase with the number of stops. While the link between phone use of any kind and the risk of traffic accidents is well-supported, it remains to be seen whether bans such as these have any effect in reducing accidents due to phone use. This may stem in part from the fact that distracted driving can often be attributed to phone conversation itself, irrespective of whether one is using a hand-free device or not; and that these bans are poorly enforced.

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1 See HB 107.
2 A prime example of this is the Maryland False Health Claims Act, introduced in prior years, but not passed until this year. Despite the bill not passing last year, we decided to include it in last year's report, as well as this year's (See SB 279).
3 "Operating budget" as distinguished from "capital budget."
4 "SB 140 Text, Chapter 482," April 10, 2010, p. 252; *The 90 Day Report–A Review of the 2010 Legislative Session*, Department of Legislative Services, April 16, 2010, p. A-1.
5 Ibid., p. A-13.
6 Ibid., p. A-24.
7 Ibid., p. A-1.
8 The term "structural deficit" refers to an imbalance between projected revenues and projected spending. When facing a structural deficit, balancing the budget each year requires a number of one-time measures designed to close this gap; however, without long-term reform, the gap will persist in future years.
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27 Ibid., p. A-20.
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30 "Capital Budget Fiscal Briefing," Department of Legislative Services, January 2010, p. 9, http://mlis.state.md.us/2010rs/budget_docs/all/Capital/Fiscal_Briefing.pdf.
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APPENDIX A – SCORING AND GRADING DETAILS

As discussed in the Methodology section, this year's report begins with the same two factor scoring system as last year's report. This produces unweighted raw scores, which, if converted to percentages, would duplicate the original scoring method.

Instead, this new scoring method includes a weighting variable designed to indicate the relative importance of bills. This variable is derived from the "Fiscal Summary" included in the fiscal and policy notes provided for many bills. The summaries are produced by the state's Department of Legislative Services, and calculate estimated revenues and expenses to general, special, and federal funds, as well as the net fiscal effect of most bills for the fiscal years from 2011 to 2015.

Our weighting variable uses the net fiscal effect as-is from fiscal year 2011; the figures from 2012 to 2015 are discounted at an annual rate of 3.95 percent. Discounting the estimates for future years is a standard practice reflecting the difference between the future value and present value of money. Since a sum of money invested today will generally be worth more in the future, the future value of both revenues and expenses equates to slightly lower present values. We do not differentiate between revenues and expenses for the purpose of weighting; i.e., a bill that involves $10 million in spending would receive the same weight as one involving $10 million in revenues. The chosen rate of return represents the average rate of return for the state's general fund during the five years from 2005 to 2009, as reported by the Treasurer's Office.

The present values for all five years are summed to obtain the total present value. Some bills lack a fiscal summary, either because it is too difficult to predict the fiscal effects or because the bill does not have a direct fiscal effect on government operations. To obtain weights for these bills, we assign them the median value of all the bills for which we have calculated the total present value. Because of the presence of many statistical outliers, it is more appropriate to use the median value than the mean value.

At this point we have weights for every selected bill. However, these weights cover an extremely large range and have a high variance. For example, without any further treatment, SB 141, the Budget & Reconciliation Finance Act, would be weighted nearly 4,400 times more heavily than the median bill. Untreated weights would allow the scoring to hang completely on the outcome of a few large-fiscal effect bills. In order to avoid this situation, we use a standard logarithmic transformation to reduce variance in the weights. The result is that large fiscal effect bills still command significantly more weight, but not so much that they overwhelm all other bills. For example, after the transformation, the BRFA is weighted only 2.95 times as heavily as the median bill, but five to ten times as heavily as some very small fiscal effect bills.

Now that the transformed weights have been obtained, we simply include them in the older scoring system: i.e., we multiply each bill's coefficient (C) by its multiplier (M), and then by its adjusted weight (W): C x M x W. If the bill was cross-listed or passed in both chambers, this is done for each chamber, and the two scores are summed. This gives us the transformed weighted raw score.

The range of raw scores for a given set of bills runs from the negative total raw score to the positive total raw score; i.e., we sum the multiplier (M) times the weight (W) for all selected bills. If the coefficient for every bill were negative, this would produce the maximum negative raw score; if every coefficient were positive, this would produce the maximum positive raw score. In mathematical notation, the range of raw scores (R) is simply:

$$[-R, R]$$

Where R is the sum of each bill's multiplier (M) times its weight (W), beginning with the first bill (b) and ending with the last bill in the set (B):

$$R = \sum_{b=1}^{B} M_b W_b$$

The actual score of a given set of bills will fall within this possible range, but where exactly depends on the coefficients (C). Thus, the actual score (S) is calculated by adding up the score of each bill (C x M x W) in the set:

$$S = \sum_{b=1}^{B} C_b M_b W_b$$

To convert the actual score (S) to a percentage (P), we use the following equation:

$$P = \frac{S + R}{2R}$$

Percentages are then assigned to letter grades according to Table 3 in the Methodology section.

For reference purposes only, Table 4 compares this year's weighted percentages with unweighted percentages obtained using the old scoring method.

For further information, contact the author.

TABLE 4 PERCENTAGES

CATEGORY	WEIGHTED PERCENTAGE	UNWEIGHTED PERCENTAGE
BUDGET & FISCAL	27.0%	31.1%
TAXES	22.4%	30.8%
EDUCATION	70.0%	72.1%
HEALTHCARE & HEALTH INSURANCE	39.3%	39.3%
ETHICS & TRANSPARENCY	71.1%	60.0%
REGULATION	57.8%	72.7%
UNIONS & COLLECTIVE BARGAINING	0.0%	0.0%
PENSIONS & RETIREMENT	28.3%	19.2%
OVERALL	39.8%	44.5%

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