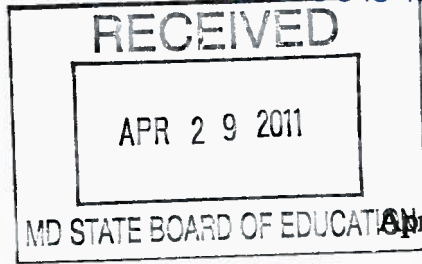


Wicomico County, Maryland

P.O. BOX 870
SALISBURY, MARYLAND 21803-0870
410-548-4801
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RICHARD M. POLLITT, JR.
COUNTY EXECUTIVE



THEODORE E. SHEA, II
DIRECTOR OF ADMINISTRATION

EDGAR A. BAKER, JR.
COUNTY ATTORNEY

JAMES V. FINERAN
PUBLIC INFORMATION OFFICER

Anthony South, Executive Director
Maryland State Board of Education
200 West Baltimore Street
Baltimore, Maryland 21201

Dear Mr. South:

Wicomico County is submitting a waiver request for FY 2012 as a reflection of the county's fiscal condition, which we believe significantly impedes the ability to meet the maintenance of effort funding level. We have elected to proceed with this waiver request, mindful of the uncertainty of such matter in recent years, yet acknowledging the input from our local Board of Education that suggests a loss of state funds may occur if the waiver is not granted.

My letter of intent to file a MOE waiver request dated March 31, 2011 provides the majority of our arguments in support of this waiver request, a copy is attached to be included as part of this waiver submission. The two required items not included in that document are detailed below.

Reserve Funds

The County's Reserve Funds are listed on pages 35 through 36 of the County's enclosed FY 2010 financial statements. Explanations for why they can or cannot be used for general fund expenses are included on page 34 of that document and are not duplicated here. But in summary, the County has \$10,615,258 in unassigned fund balance available for general fund use, or 9.5% of the proposed general fund budget. The County is proposing to use \$1,000,000 of these funds in FY2012, bringing its unassigned fund balance down to 8.6% of its operating budget. These funds are also used to cash flow County expenditures and cannot be completely depleted without impacting payroll, vendor payments, and debt service. Further, these funds must take us not only through FY 2012 but also through FY's 2013 and 2014, which we believe will also be difficult budget years. The County does not feel it would be fiscally prudent to deplete these funds further than the 8.6% that is currently projected for the FY 2012 budget.

Public Meetings

Although not required by law, and not specific to MOE, the County Executive held a public input session on the proposed FY 2012 budget at the County's Civic Center, which was well attended. The BOE also has held one public meeting, with another to be held in May, to discuss their proposed budget. In addition, the County Council will be holding a public hearing on May 3rd to get comments from our citizens.

We have met with our local Superintendent and members of our Board of Education to review our financial situation and the potential impact on our school system. None of us are pleased with the prospect of continued, long term reductions in funding to our school system, however, we both concur that an incremental reduction of \$4,529,799 million for this fiscal year can be managed with as little as possible direct impact on the classroom experience.

Funding Proposal

	FY 2010	FY 2011	FY 2012 Proposed
WCBOE Request (MOE Level)*	\$ 50,781,711	\$ 50,596,892	\$ 50,126,691
Actual/Proposed County Appropriation	\$ 50,781,711	\$ 43,196,892	\$ 38,196,892
Amount Requested to be Waived	\$ -	\$ 7,400,000	\$ 11,929,799
*MOE Level increase/(decrease)		\$ (184,819)	\$ (470,201)

The Tax Rate Challenge

I have submitted my FY 2012 budget proposal to the Wicomico County Council, a copy of which is included herein. They have until June 15th to act on my proposal. The proposal, as submitted, reflects the \$4.5M incremental reduction from the county's FY 2011 appropriation. This is the low end of the reduction amount described in our March 31st letter of intent. Holding to this level of funding is contingent upon the County Council's approval to increase the real property tax rate to the maximum amount allowable under Wicomico County's Revenue Cap: a 5-cent increase from \$0.759 to \$0.809 per \$100 in taxable assessed value.

The real estate assessment process whereby one-third of all property is reassessed each year has the effect of "smoothing" the market changes in property valuation and also delaying the time when those changes are fully reflected in tax collections. A second feature of the tax code, the Homestead Credit, further defers the effect of increasing values while offering no such benefit in a declining market: decreases are fully recognized in the assessment year.

The "housing bubble" burst in 2006, which triggered the sub-prime mortgage crisis and then the recession. According to the Maryland Association of Realtors, the average price of a home in Wicomico County in July 2006 was \$250,468. In July 2010 it was \$174,900, a 30% decline in value. The latest month available, March 2011, shows the average price at \$141,998, which is down 10% year-over-year from March of 2010. Assuming July 2011 will be the "bottom" of housing market in terms of price, there will be five continuous years of price declines that must work their way through the state assessment cycle. It is impossible to predict when property valuations will stabilize and then be fully reflected in the county's assessable tax base, but for

FY 2012 our taxable base is down by 5%¹. One can only hope that the declines in FY 2013 and FY 2014 will be a gradual tailing-off to a new stable housing base.

The new problem presented by a declining assessable base is the emotional citizen resistance to "tax increases" of any form. The algebra of property tax revenue is rudimentary, rate times base equals revenue. When the base goes down, the rate must go up to collect the same amount of revenue: it is not really a tax increase; in the aggregate the payment is the same². The Wicomico County Revenue Cap adds a twist to this by constraining revenue to that of the previous year plus the lesser of 2% or the consumer price index. This year the CPI constrains us to a growth of 1.5% which is the \$0.05 cent rate increase I have proposed in the budget. It is absolutely critical for our education, as well as public safety and recreation functions that our citizens support this minimal real increase in property tax revenue. Should this not be approved, the repercussions have a permanent effect on future budgets because the prior year revenue becomes the permanent base for the succeeding year cap computation; much like a payment made above MOE is added to the base in succeeding years, only in reverse.

Many citizens are going to have a difficult time understanding why we need them to write bigger checks to their government when the value of their property has declined, their income may have diminished and they know neighbors who are out of work. This is an unprecedented time when we must all work together to balance reductions in government expenditures with the need to provide critical services and protect our community's quality of life and economic viability. This second waiver request is a necessary step in achieving that balance. Your support is greatly appreciated.

Sincerely,



Richard M. Pollitt, Jr.
County Executive

Attachments: Wicomico County letter of intent dated March 31, 2011
FY10 Audited Financial Statements
Proposed FY 2012 budget document (includes the FY 2011 adopted budget)

¹ The dramatic losses in market value are buffered by the homestead credits accumulated during the 2003-2006 run-ups in home values, thus the taxable assessment base will not decline dramatically until all assessment credits have been depleted. These credits are expected to be non-existent by FY13.

² While the total revenue collected under a constant yield tax rate is the same as the prior year, individual homeowners write a check based on their current year's taxable base which varies depending on where they are in the assessment cycle and whether or not they have homestead credits. Some taxpayers will write a check for less, some for more and some for the same amount. It is an equitable system over the long term, but it is difficult to demonstrate on a customer by customer basis due to the complicating factor of the homestead credit.

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JAMES V. FINERAN
PUBLIC INFORMATION OFFICER

March 31, 2011

Anthony South, Executive Director
Maryland State Board of Education
200 West Baltimore Street
Baltimore, Maryland 21201

Dear Mr. South:

Wicomico County requests a waiver from the Maintenance of Effort requirements of the Education Article, Section 5-202 for fiscal year 2011-2012. Based on information in the Governor's budget, and pending any negative actions by the Legislature or County Council, the waiver would decrease the County's contribution to BOE Operating Expenses from the FY11 appropriation of \$43,196,892¹ to between \$36,196,892 to \$38,196,892. Because MOE looks back two years, this is a reduction from the MOE amount of \$50,126,691 of 24% to 28%, and a reduction from the FY2011 appropriation of 12% to 16%. Note that this is still substantially above our FY12 Local Share of Foundation Formula of \$28,202,108². Using information that is currently available to us, we believe that a county appropriation of \$38,196,892 will be an affordable and sustainable level of funding until the county economy and tax receipts improve substantially.

KEY FISCAL INDICATORS

Wicomico County's recurring annual revenue receipts have declined by \$16 million in the last five years; if one includes the State's elimination of Highway User Revenue distribution, the total budget challenge exceeds \$23M. The decline began with the collapse of the housing bubble in 2006 and accelerated during and beyond the national recession of December 2007 through June 2009. The underlying changes in economic conditions have been dramatic. The recovery rate has been slower than projected last year at this time³. The County is struggling mightily to reduce its expenses to the "new normal" level of revenue and economic growth. The majority of the revenue decline can be attributed to two sources, \$4.6M from recordation tax and \$10.5M from income tax.

¹ Wicomico County discussed its intention of likely seeking a waiver in FY2012 at its hearing last year due to the protracted economic downturn, which has resulted in a multi-year reduction of funding. The FY11 appropriation of \$43,196,892 includes the approved FY11 MOE waiver of \$7,400,000 from the original FY11 local BOE request: thus, \$50,596,892 less \$7,400,000 less \$5,000,000 equals Wicomico County's appropriation for FY12 of \$38,196,892.

² Under proposed legislation HB 44, the local share of the foundation program represents the floor for local appropriations to the boards of education.

³ Last year's revenue estimates for FY12 and beyond assumed some recovery in the housing market, faster job recovery and achieving maximum property tax revenue under the revenue cap. None of these assumptions have proved to be valid; thus the projected reduced funding to the LBOE of \$38M which is below last year's estimate of \$40M-42M.

Recordation tax receipts are directly related to the housing industry by both the volume of transactions and price of the property being recorded. The first graph on Tab (1) shows the number of taxable deed and mortgage transactions from the 1st quarter 1995 through the 4th quarter 2010. The second graph on Tab (1) shows the recordation tax collected from fiscal year 1990 through the current estimate for fiscal year 2011. The key points are these;

- the current transaction volume is 320 LESS than 15 years ago in 1995,
- the most recent 7 quarters do not indicate improvement or recovery
- tax revenues have plummeted \$4.6M since the peak in 2006 to levels last seen in 1997
- not only have the numbers of transactions decreased, the value of the properties being recorded has also decreased, further reducing recordation revenue
- we cannot expect a meaningful recovery in revenue from this source.

Income tax receipts are highly correlated to the total number of people in the county who are employed. Referring to Tab (2); the first graph shows the 12 month moving average of total employment from December 1999 through December 2010. The second graph depicts the relationship between income tax revenue and total employment. The chart then projects that relationship into the future based on a scenario of slow job recovery. The key points are these,

- total employment declined dramatically from the peak in June of 2007
- cumulative employment loss through December 2010 stands at 4,522
- the magnitude of job losses goes well beyond the loss of several major employers
- while the decline abated in September 2010, there is yet no indication of job growth
- income tax receipts are expected to decline \$10.5M (cumulatively) from FY08 through FY11
- there are no known economic factors that would indicate a “bounce back” to pre-recession levels; we must live within this funding level for a long time.

WHAT DIFFERENTIATES WICOMICO COUNTY FROM OTHERS?

Differentiation by Employment - Wicomico County’s economy felt the effects of the housing collapse sooner than many counties; the severity of the impact has been greater, and the recovery is lagging behind the metropolitan counties and State average. Tab (3) contains two charts that use a smoothed (12 month moving average) computation of changes in total employment to illustrate the relative and absolute effects of the housing bubble and the resulting recession⁴. The first graph shows the cumulative percentage change in total employment computed from pre-recession peak employment levels. This differentiates the counties by both the start of employment decline and relative severity of the decline. The key points are these,

- the Lower-Shore Counties began losing jobs 12 to 16 months sooner than the metropolitan counties and the State as a whole
- the relative severity of job losses is dramatically different. Wicomico lost 8.9% from its June 2007 peak while Montgomery County lost just 4.2% from its August 2008 peak
- while there is clearly job recovery in the metropolitan counties, Wicomico shows no signs of job growth

The second chart on Tab (3) shows the absolute change in jobs for the Lower-Shore Counties. While Worcester had the greatest percentage decline shown on the first chart, Wicomico County lost by far the most jobs in absolute terms; 4,500 fewer people working, collecting wages and paying income taxes to the county. There is no indication of employment improvement, which means income tax revenues are not going to improve either.

⁴ Data from State Department of Labor, Licensing and Regulation at www.dlir.state.md.us/lmi/laus

Differentiation by Sales Tax – Sales Tax receipts may be used as an indicator of economic activity⁵: while Wicomico County does not levy or collect a sales tax, the sales taxes collected in Wicomico County can be used as a relative measure to compare economic activity in Wicomico County to the State average and the adjacent counties of the Lower Shore.

The first chart on Tab 4 shows the 12 month moving average of sales tax collected state-wide. The sales tax rate increased from 5% to 6% in January of 2008. In order to show “equivalent” economic activity, the actual sales tax collections from January 2008 onward were restated to what they would have been at 5%, thus the line splits in January 2008. The line moving upward from that point shows the actual receipts at 6% while the line that goes downward reflects the restated receipts, and therefore the economic activity, at a constant 5% tax rate.

It is easy to see the correlation between the declining tax receipts and the period of recession from December 2007 to June 2009. After the recession, economic activity was positive through calendar year 2009. However, the trend for January through December 2010 (last data available) was down: hardly a reassuring direction. It is also significant that restated State tax receipts for December 2010 were the same as March 2005, thus economic activity, as measured by sales tax collections, has regressed to the levels of 2005.

How did Wicomico County fare compared to the State and other Lower Shore Counties? To answer this question the percentage change in the 12 month moving average of the restated (economic activity measure) sales tax receipts from peak pre-recession levels was computed and charted. Looking at the second chart on Tab 4, the point on the horizontal axis where the trace begins is the month in which tax receipts peaked before the recession. The trace then shows the percentage change in restated 12 month moving average of sales tax receipts through December 2010. With the exception of Somerset County⁶, sales tax receipts for the State and other lower shore counties began declining at the beginning of the recession. Sales Tax receipts declined across the board through the recession⁷. While Worcester County rebounded at the end of the recession with nearly constant improvement through December 2010, **Wicomico County declined faster and farther than the State and other Lower Shore Counties through the recession; and then, continued declining for a cumulative loss of 26%: 14% below the State average.**

EXTERNAL CONSIDERATIONS

Aggravating factors - Discrete actions taken at the State level are not making budget decisions at the county level any easier and cannot help but exacerbate the already negative effects on education funding. The withdrawal of over \$7 million dollars per year of Highway User Revenue is forcing Wicomico County to divert millions of dollars per year from the general fund to sustain minimum roads services. In addition, ongoing State fiscal year 2012 budget deliberations include proposals to

- transfer \$776,000 in operating costs for the local State Assessment Office operations
- withhold \$440,000 of the county’s income tax revenue
- reduce reimbursement to the county detention center for State prisoners, and
- shift part of the cost of teacher pensions to the local level.⁸

⁵ Raw sales tax receipt data provide by the State via the Business Economic and Community Outreach Network (BEACON) of Salisbury University

⁶ Somerset County had declining economic activity compared other counties as early as April 2006 which coincides with the end of the real estate market growth. This mirrors Somerset’s employment change as well. Oddly, this correlation between sales tax and employment pattern is not present for Dorchester County.

⁷ There may be data or reporting anomalies in April-June of 2009

⁸ Without a dramatic change in citizen sentiment towards tax increases, and a change to its revenue cap; the local Board of Education must be prepared to absorb the cost shift within appropriations as proposed by this waiver request.

Citizen sentiment - It seems illogical to assume that the citizens who are perceived to oppose revenue increases at the State level, the same people who live, work and vote in the counties, are somehow more willing to support county tax increases to pay for costs transferred from the State; or to replace the revenue lost from the sale of homes (recording tax) or loss of income tax caused by job losses. Our perception of voter sentiment is that government as a whole must reduce spending to balance its budget.

OTHER REVENUE LIMITATIONS

Property Tax Revenue – The FY12 Net Assessable Base declined by 5% over FY11⁹. With the exception of the Great Depression, this is an unprecedented event in our economic history. The county’s property tax rate will have to be increased by 5.1% just to reach the “constant yield” rate that will generate the same amount of tax revenue as last year. Given citizen sentiment and the perception that taxes are being raised¹⁰, when of course they are not, just maintaining revenue at last year’s levels will be challenging. So, while Wicomico County does have a property tax “revenue cap”, it is unlikely that the county will be able to increase its tax rate to enough to reach the cap level.¹¹

Other Revenue Enhancements – Returning to the income tax, the county could raise the income tax rate from 3.10% to 3.20%. Such an increase could bring in another \$1M, but citizen sentiment makes this action most unlikely. Increasing the recording tax rate or imposing a transfer tax would raise precious little revenue given the depressed state of the housing market and would be seen as an anti-business/anti-recovery tax.

MAINTENANCE OF EFFORT HISTORY

Maintenance of Effort – Ironically, the actual incremental change in MOE from FY11 to FY12 appropriation based on enrollment would be a decrease of \$400K; a number that seems inconsequential in comparison to the planned \$5M reduction. The following table shows the history of contributions that were in excess of MOE. We do not expect to see these levels of funding for many years.

Fiscal Year	Operating Appropriation	Maintenance of Effort	If we only funded MOE	Amount Funded Over Maintenance of Effort
Last Ten Years				
2001	\$ 42,843,788	\$ 143,746	\$ 38,287,534	\$ 4,556,254
2002	\$ 43,743,788	\$ (201,571)	\$ 42,642,217	\$ 1,101,571
2003	\$ 44,665,088	\$ (235,712)	\$ 43,508,076	\$ 1,157,012
2004	\$ 45,679,815	\$ 452,297	\$ 45,117,385	\$ 562,430
2005	\$ 46,131,073	\$ 451,258	\$ 46,131,073	-
2006	\$ 46,925,458	\$ 348,916	\$ 46,479,989	\$ 445,469
2007	\$ 48,329,815	\$ 764,985	\$ 47,690,443	\$ 639,372
2008	\$ 49,443,053	\$ 113,238	\$ 48,443,053	\$ 1,000,000
2009	\$ 50,204,655	\$ 61,602	\$ 49,504,655	\$ 700,000
2010	\$ 50,781,711	\$ 577,056	\$ 50,781,711	-
Last 10 Years Total Funding over MOE				\$ 10,162,108.00

⁹ Net assessable real property base for FY12 is \$6,578,257,054 per State 2011 Constant Yield Tax Rate Certificate. This is \$347.6M less than FY11.

¹⁰ Many taxpayers and those inclined to demagogue rather than educate will consider the *rate* increase the same as a *tax* increase even though total tax revenue remains the same – i.e., there is no *tax increase*. At the individual homeowner level, unfortunately in some cases, a rate increase will in fact translate into a larger tax bill.

¹¹ Under the Revenue Cap computation, the county could raise the tax rate 5.9% from the FY11 rate of \$0.759 to \$0.809. The incremental difference in real property tax receipts between the constant yield and revenue cap maximum is approximately \$765K.

LONG RANGE BUDGET OUTLOOK

Maintaining investment in the future – The County Executive and local Board of Education remain committed to the completion of the Bennett High School/Bennett Middle School phased replacement plan. The Bennett High School building was completed and opened for student use one year ahead of schedule. The completion of the high school complex is contingent upon completion of the equally important replacement of Bennett Middle School. We believe that this critical capital investment remains affordable with significant sacrifices to operating budgets; however, our citizens and County Council have raised serious concerns about affordability, and accordingly the County Council has postponed this construction project for one year.

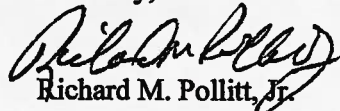
Charting a long term path -The long term economic viability of the county together with any hope of finishing the Bennett Middle School project requires approval of this MOE waiver together with additional operating budget reductions by the County. The first chart on Tab (5) shows the unsustainable relationship between expenses and revenue if a waiver is not granted, which will result in total depletion of the counties fund balance before the end of FY14.

The second chart depicts a path-to-survival where

- minimum fund balances are preserved,
- tough financial choices enable the County to retain acceptable bond ratings required to complete Bennett Middle School construction, and
- retain the kind of quality of life that will attract new business and residents.

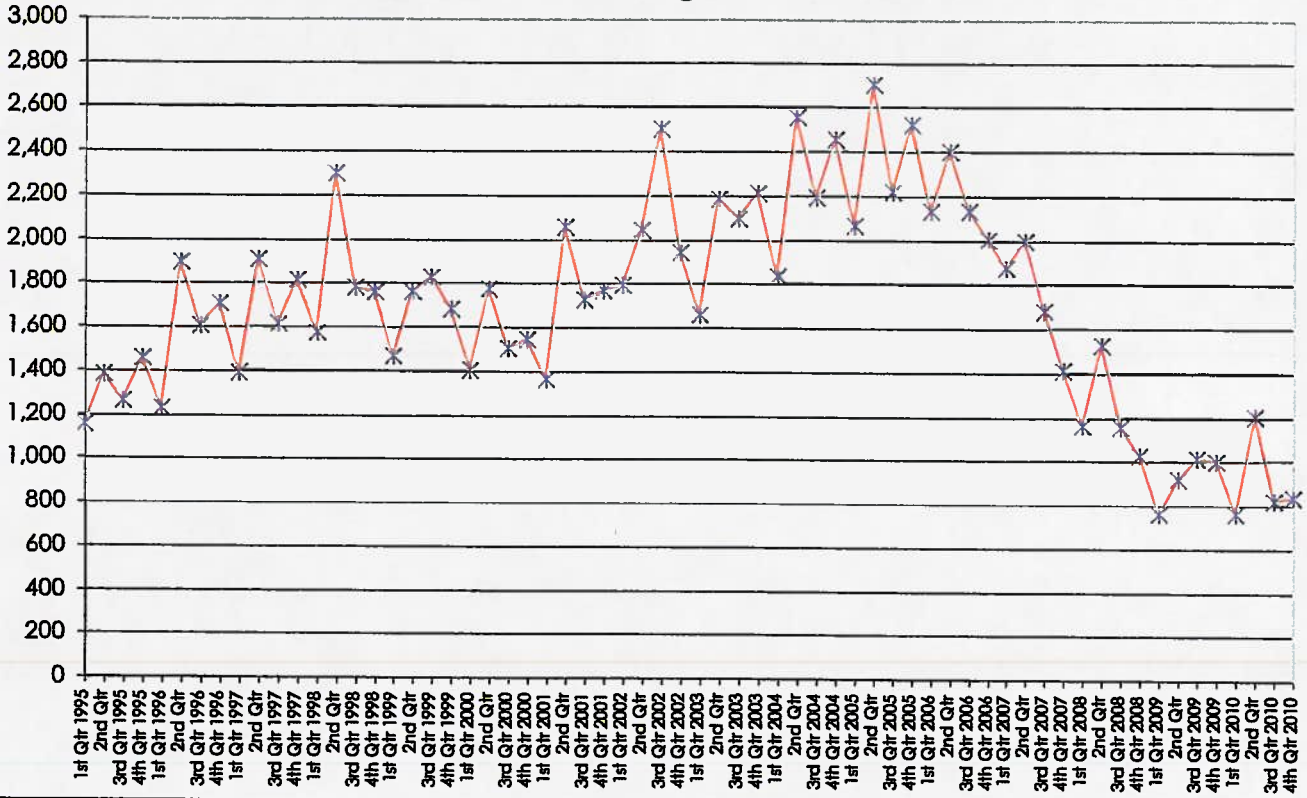
In conclusion, as I have stated on each of the other occasions of our seeking the waiver of the Maintenance of Effort standard, I take no pride or pleasure in making this request. It violates every facet of my own personal commitment to providing the highest possible level of support for public education. However, as I've also said, our self-imposed burden represented by our Revenue Cap, exacerbated by the continuing challenges of a severe recession, make this the only option available in hopes of protecting at least some measure of additional funding for our school system. I respectfully seek the indulgence, understanding and support of the State Board of Education.

Sincerely,

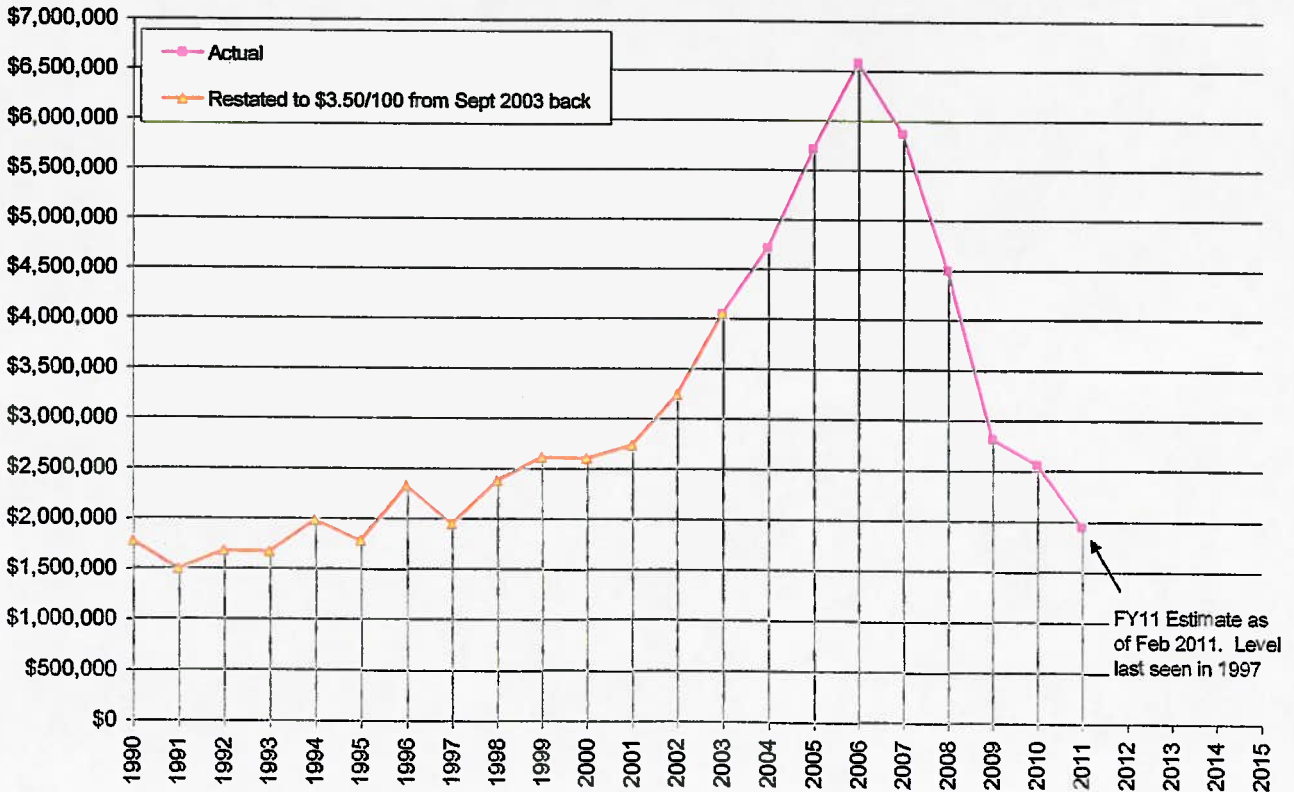

Richard M. Pollitt, Jr.
County Executive

Attachments: FY 2011 Budget
Wicomico County's Audit Financial Statements (last 3 years)

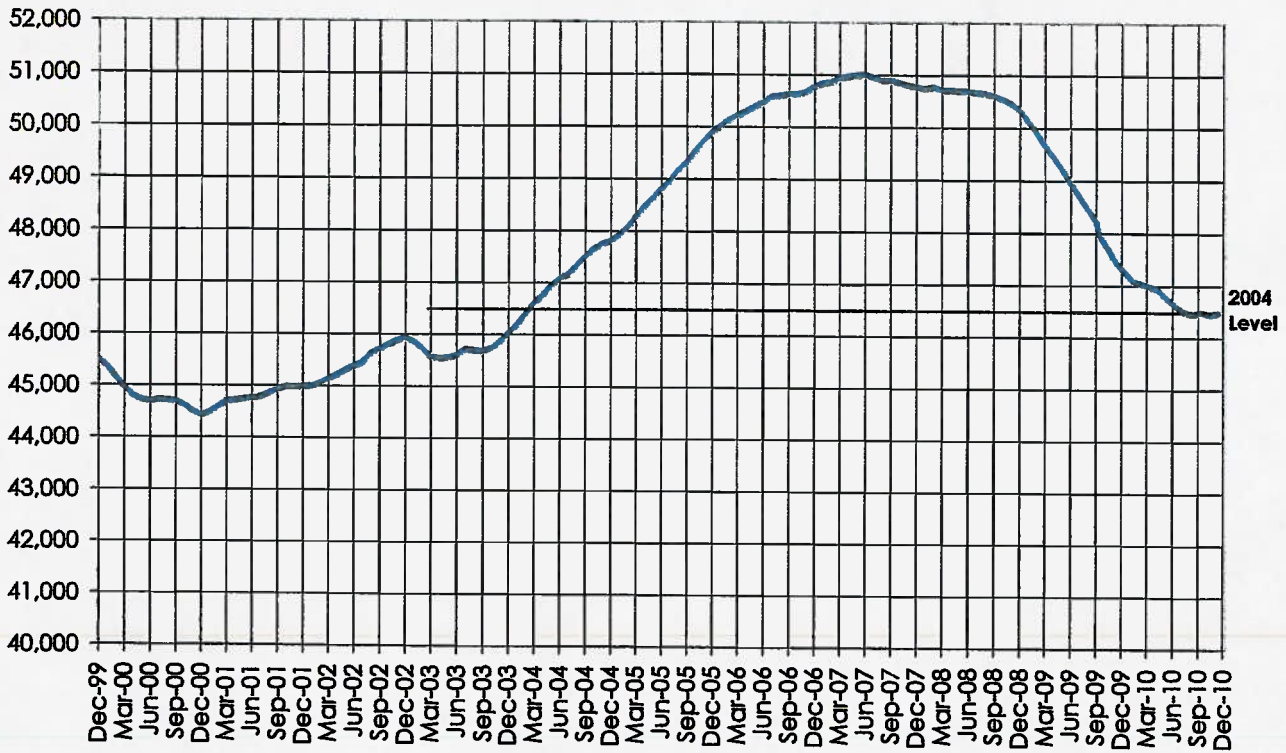
Number of Taxable Deed and Mortgage Transactions 1st Quarter 1995 through 4th Quarter 2010



Recordation Tax Receipts FY1990 through estimate for FY2011



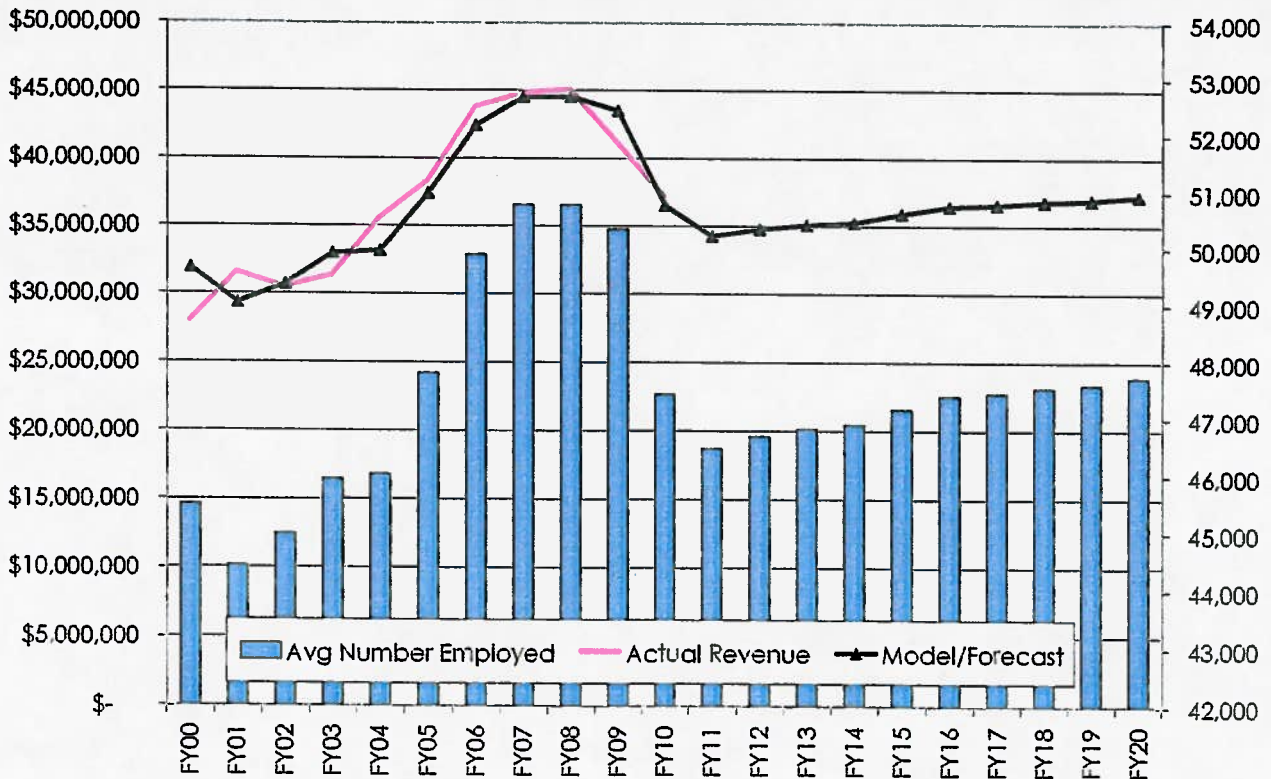
Wicomico County Total Employment 12 Month Moving Average

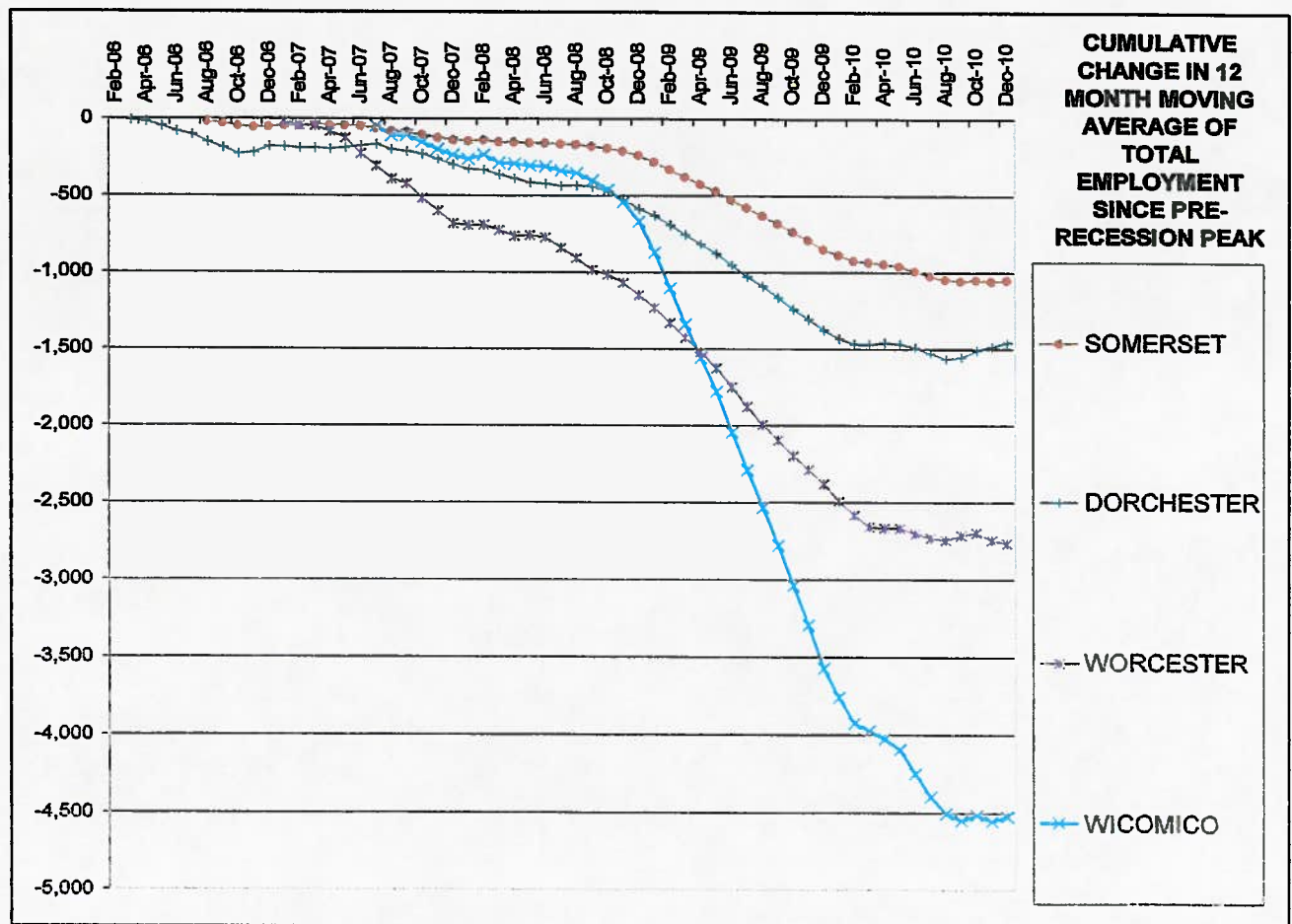
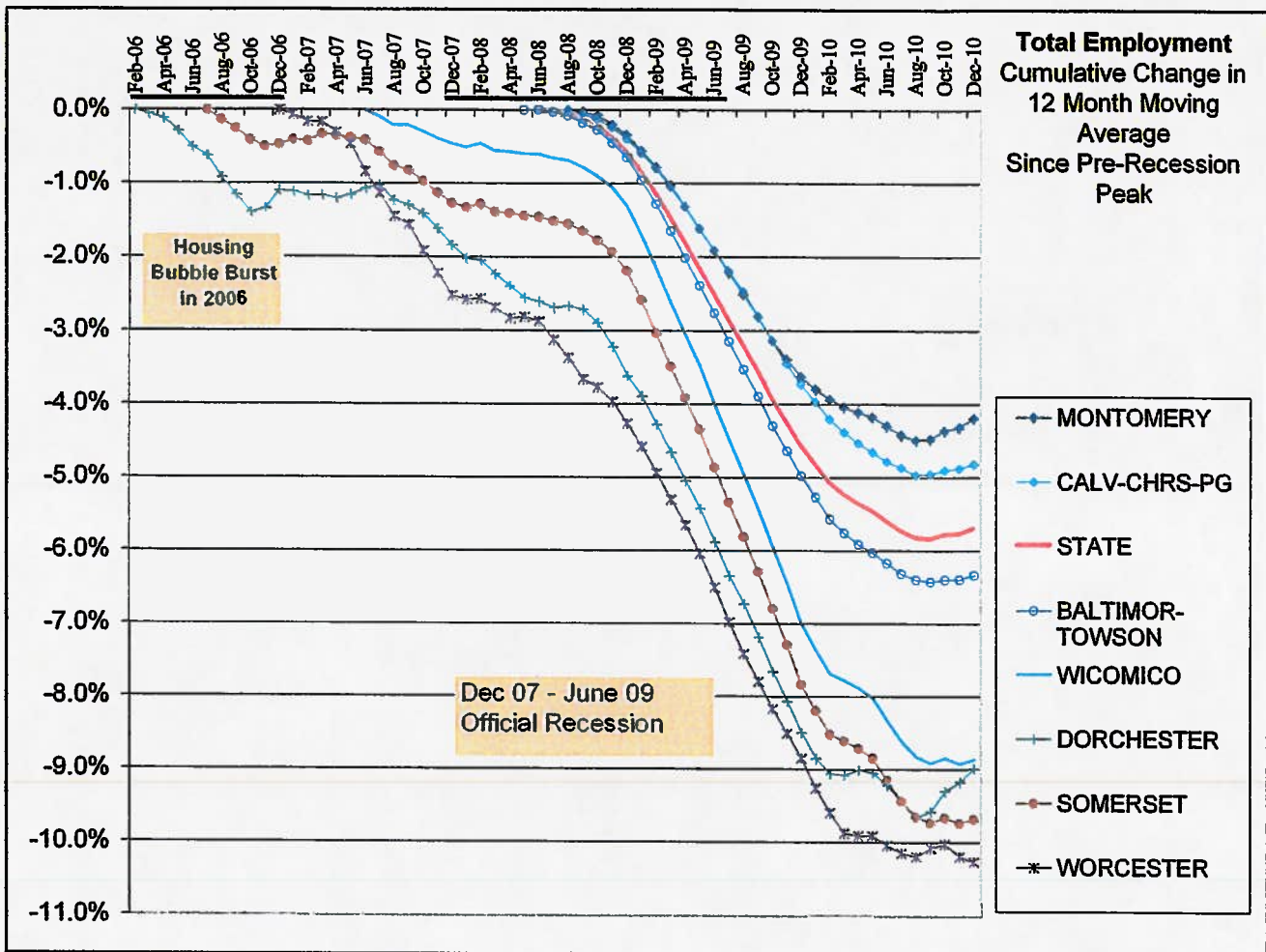


Employment Drives Income Tax Receipts

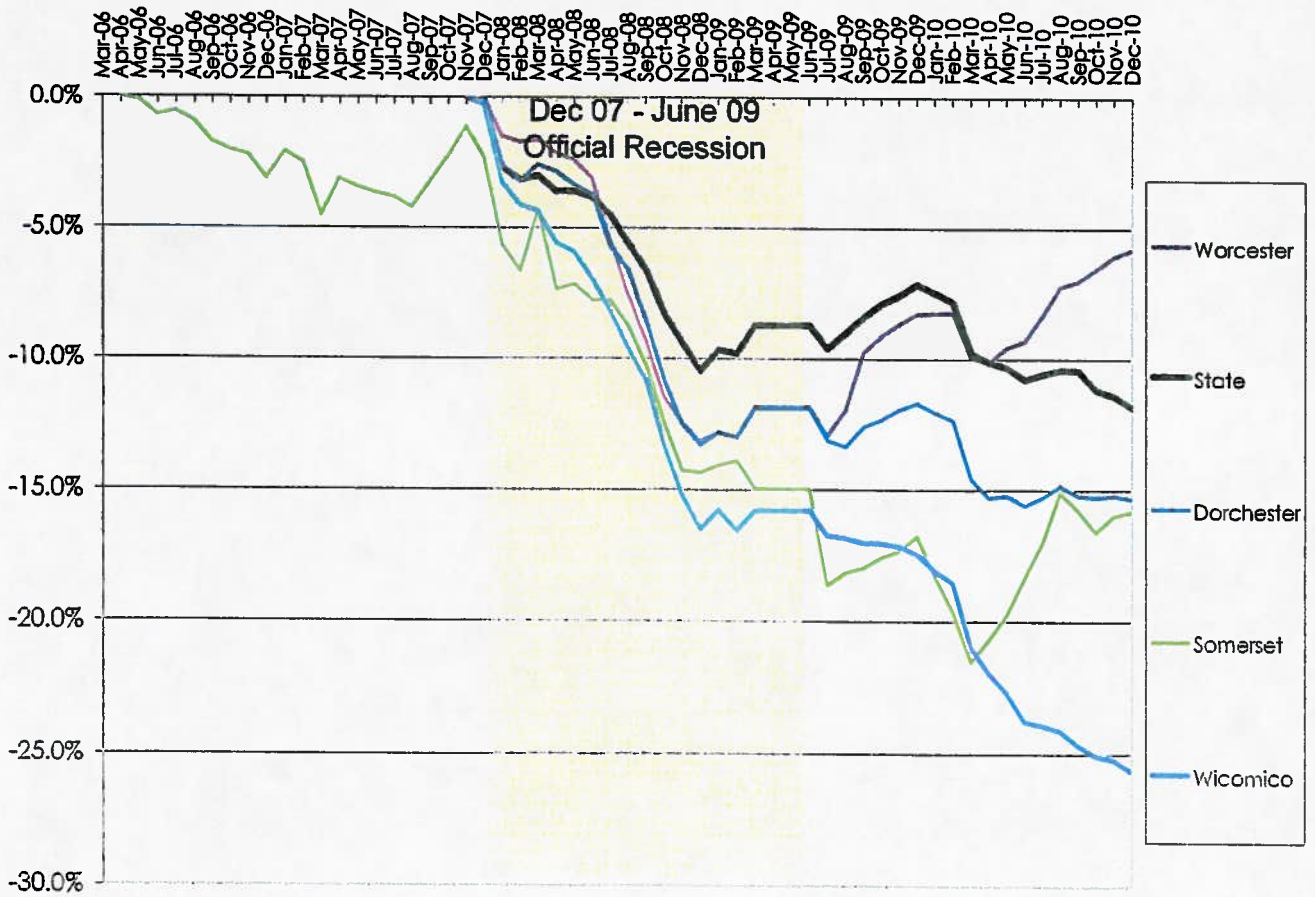
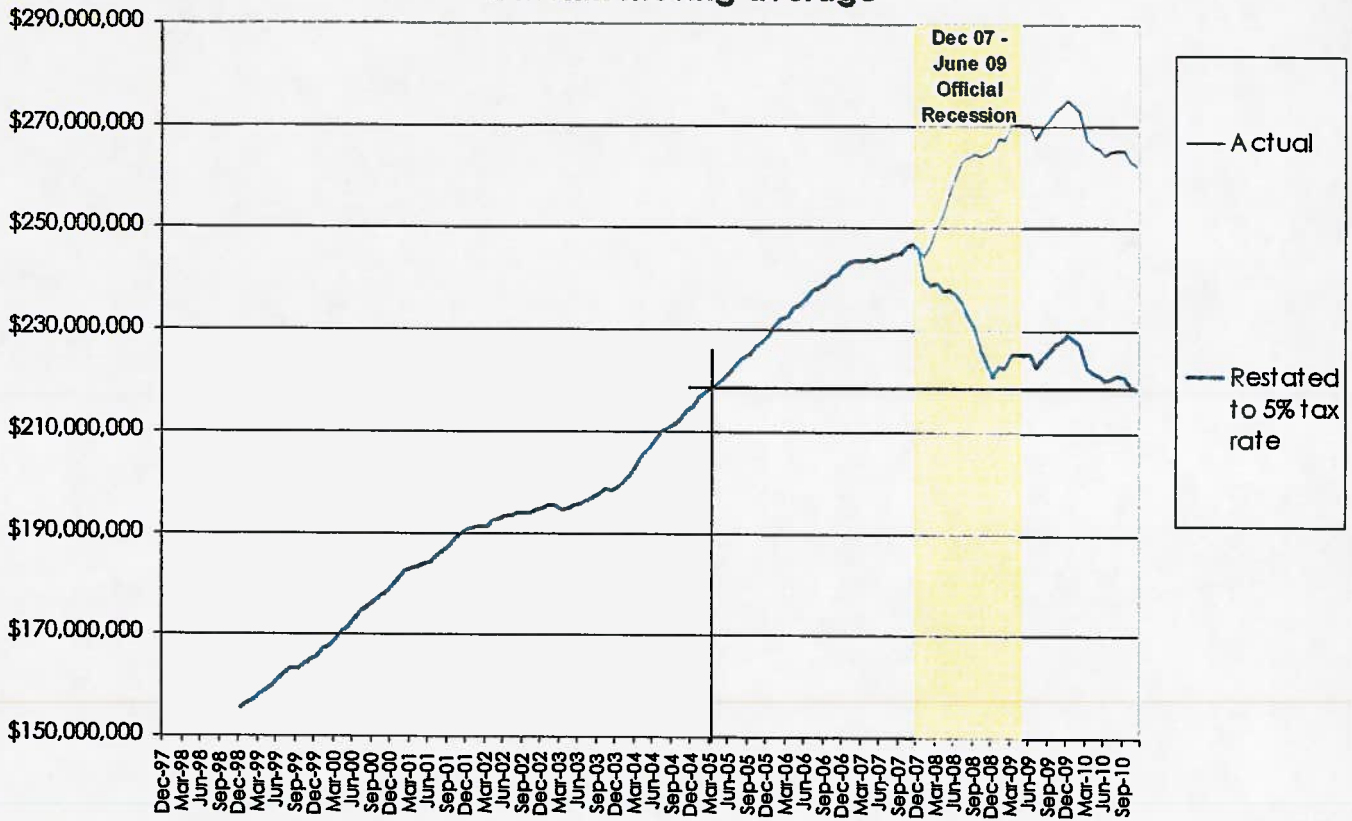
Income Tax Revenue

Annual Average
Number Employed

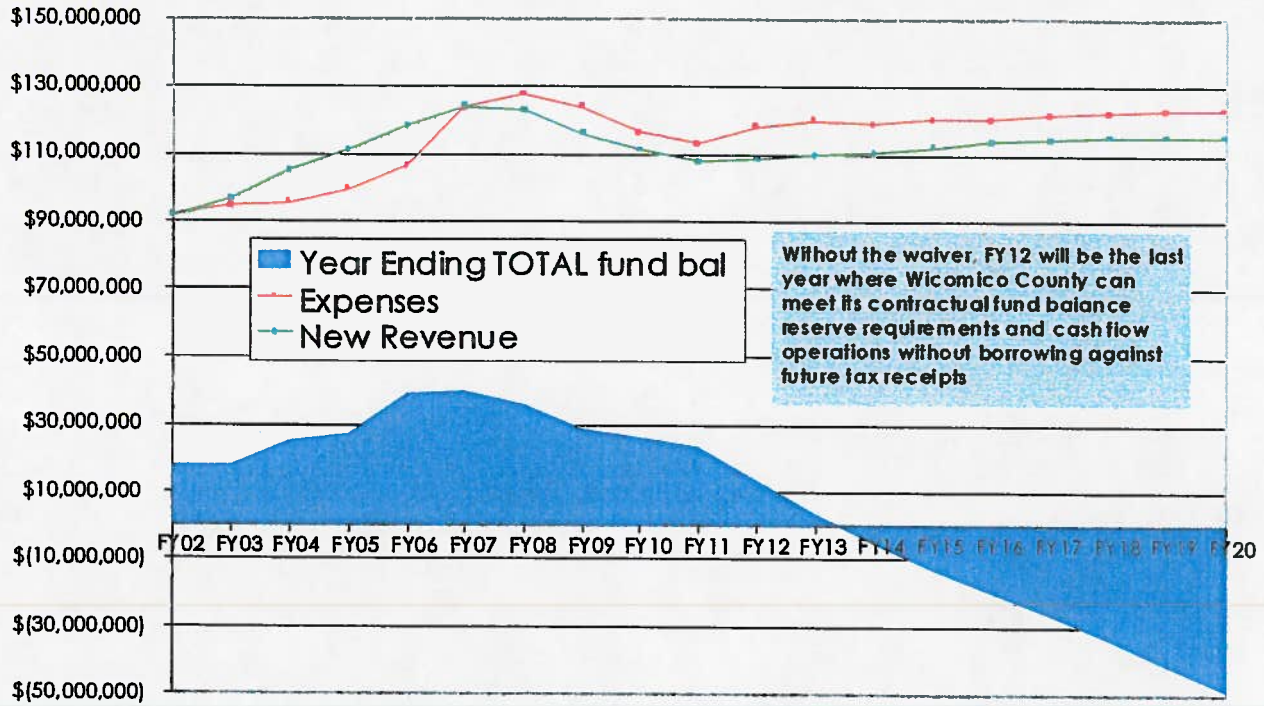




Maryland State Sales Tax Collections 12 month moving average



Wicomico County Future without MOE Waiver



A Sustainable Path for Wicomico County

