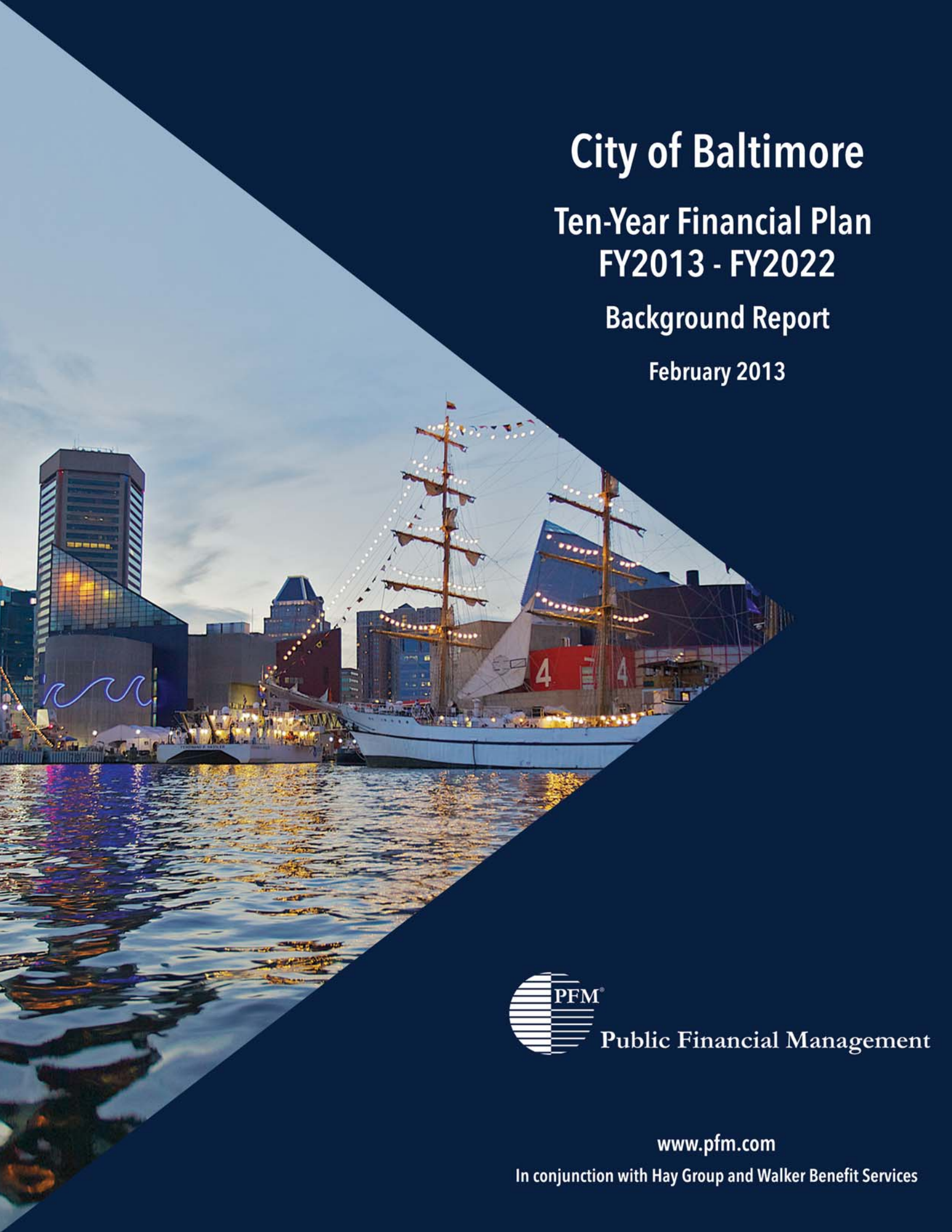


City of Baltimore

Ten-Year Financial Plan FY2013 - FY2022

Background Report

February 2013



Public Financial Management

www.pfm.com

In conjunction with Hay Group and Walker Benefit Services

**City of Baltimore Ten-Year Financial Plan
Background Report**

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Executive Summary



... this Ten-Year Financial Plan has been developed to help ensure that this is the time when Baltimore truly begins to move forward in a new direction.

- Facing the ten years ahead, the City of Baltimore is now at an **inflection point** — the juncture where a trend or curve changes direction.
- For more than half a century, Baltimore’s narrative has been a story of post-industrial decline. From 1950 to 2010, the City lost more than a third of its population, manufacturing jobs relocated, once-vital neighborhoods destabilized, and City government has been left with a legacy of high tax rates and growing liabilities — compounded in recent years by the worst recession in generations.
- Even with the economic downturn, however, a new Baltimore story has begun to emerge. The City’s education and health services sector has grown from 80,300 to 113,100 jobs since 1990, global linkages are strengthening through expansion of the Port of Baltimore, and the City ranks high among the nation’s top cities for technology jobs. Over the past half-decade, the City’s overall population has largely stabilized, with positive growth in an increasing number of neighborhoods.
- Having now reached this crossroads, this Ten-Year Financial Plan has been developed to help ensure that this is the time when Baltimore truly begins to move forward in a new direction, with recent progress becoming more than just a momentary pause in a longer-term story of decline.
- As a Financial Plan, this effort does not encompass every aspect of service delivery, urban planning, or economic development. At the same time, this long-range fiscal planning process is more than just a spreadsheet exercise.
- This Ten-Year Financial Plan begins with the premise that Baltimore’s new narrative must be grounded first in stable City finances. A structurally sound budget and improving balance sheet will provide a necessary foundation for municipal government to play an effective role in sustaining the growth and vitality of the broader community.
- In this **Ten-Year Financial Plan Background Report**, the consultant team engaged by the City to support this effort outlines key findings regarding Baltimore’s opportunities, challenges, and options going forward.
- This research and analysis is centered primarily around the City’s General Fund — the primary operating budget for tax-supported municipal services. Certain fee-supported “enterprise” activities, such as the City’s water and wastewater utility, are also important to Baltimore’s future, but are not the focus of this report.
- The Ten-Year Plan analysis begins with an overview of the economic forces that drive Baltimore’s finances, and then turns to a set of “baseline” General Fund budget projections based on mainstream economic assumptions and the carry-forward of existing municipal services without changes in current practices or law.
- While the City’s budget is balanced for Fiscal Year (FY) 2013 following another round in a series of recent cuts, recurring revenues in the years thereafter are not forecast to keep pace with projected, recurring expenditures. Without corrective action, this structural imbalance is projected to result in a fiscal gap of over \$30 million in FY2014 — growing to nearly \$125 million by FY2022 — for a cumulative shortfall of almost \$750 million across this plan period. Quite simply, a status quo approach is not financially sustainable, and will not support a new narrative for Baltimore’s future.
- In addition to this General Fund operating budget shortfall, Baltimore also faces significant infrastructure and retiree benefit liability challenges that are also important to address for the City’s long-term fiscal health. Based on a high-level capital needs analysis conducted for this report, the City would

need to spend a cumulative \$1.1 billion in local infrastructure investment through FY2022 above the levels included in the baseline forecast just to maintain the current state of repair for capital assets and to begin to make slow progress toward improvement. With regard to retiree benefits, the City's FY2011 actuarial valuations identified a \$3.2 billion unfunded liability across Baltimore's combined pension and retiree healthcare programs.

- To address these important concerns, this Ten-Year Financial Plan process has highlighted critical long-range challenges and potential strategies in each of four cornerstone areas:

- **Structural Budget Balance:** Bringing recurring spending in line with recurring resources by shaping a smaller, more productive government, and by restructuring fast-growing employee healthcare and retirement benefits while maintaining a competitive total compensation approach.

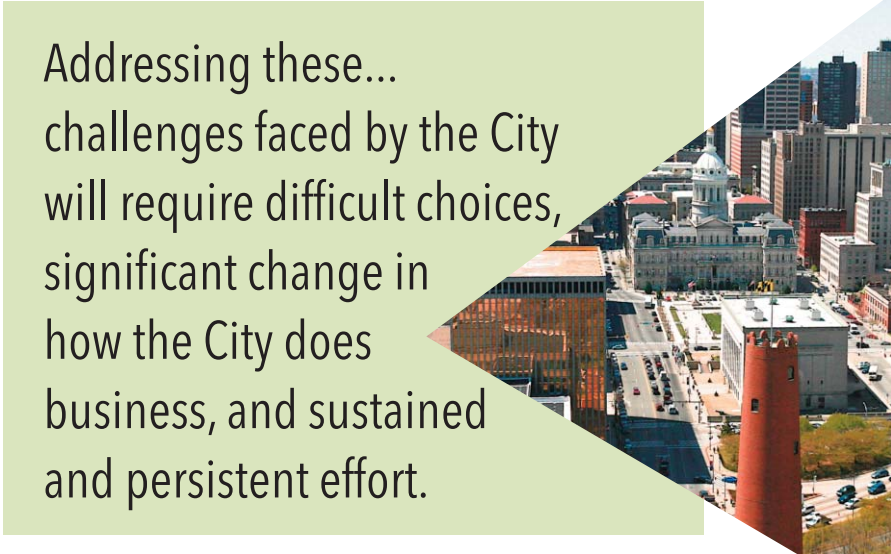
- **Tax Competitiveness:** Reducing the City property tax burden to improve Baltimore's position as a location of choice for residents and businesses, while seeking to diversify revenue streams creatively, maximize collection of existing taxes due, and rely more on user-based charges to sustain services that now draw on the general tax base.

- **Infrastructure Investment:** Reversing historical underinvestment to renew and rebuild the City's core assets, improve school facilities, enhance the tourism and hospitality sector, and eliminate the blight of vacant structures in Baltimore's neighborhoods.

- **Addressing Long-Term Liabilities:** Demonstrating long-term fiscal stewardship by reducing underfunding of the City's retirement benefits, maintaining debt at manageable levels, and strengthening budget stabilization reserves.

- Meeting these and other challenges faced by the City will require difficult choices, significant change in how the City does business, and sustained and persistent effort. It will require strategic collaboration and support, not further cutbacks, from the State and federal governments, and strengthened partnerships with Baltimore's business and nonprofit communities. To successfully chart an upward trajectory, all of the City's stakeholders must come together.

- With the findings detailed in this background report in hand, Mayor Stephanie Rawlings-Blake developed **Change to Grow: A Ten-Year Financial Plan for Baltimore**, a separate document available on the City's website at www.baltimorecity.gov.
- In *Change to Grow*, Mayor Rawlings-Blake charts a specific course of actions designed to not only strengthen the City's long-range financial position, but also to launch Baltimore forward as a **growing** City again.



Addressing these... challenges faced by the City will require difficult choices, significant change in how the City does business, and sustained and persistent effort.



Financial and Economic Analysis:
City Economic Position

For more than half a century beginning in the 1950's, Baltimore's economic story has paralleled that of many great cities built on manufacturing — marked by the decline of traditional industries and jobs, population loss to the suburbs, and increasing challenges of poverty and disinvestment.

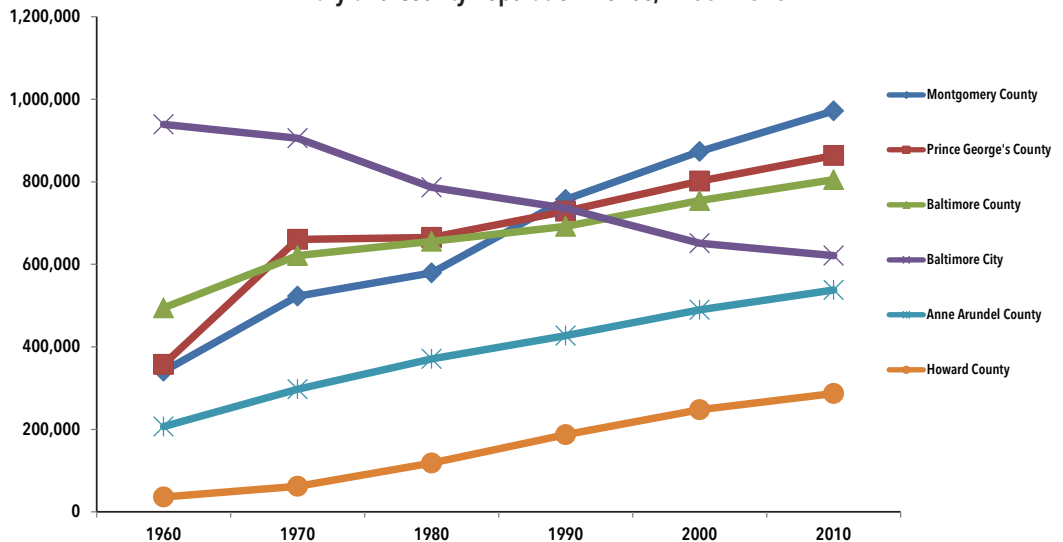
As the 21st century has begun, however, there are emerging indications that a new urban story is developing in Baltimore. In recent years, the City's population has stabilized, crime rates have declined, and exciting opportunities are now building around jobs in a knowledge-based, global economy.

As 2013 begins, this new narrative is yet to be fully written, and remains at serious risk if not reinforced by sound — and sometimes difficult — policy actions and change. With the right measures, and a little help from the broader economy and regional partners, Baltimore's next half-century holds renewed promise for transitioning from emergent stability to economic growth and revitalization.

Baltimore's Old Narrative (1950-2010)

Like many core urban communities, Baltimore's post-World War narrative was a story of post-industrial decline. The City's population fell from a peak of 949,708 in 1950 to 620,961 by

Maryland County Population Trends, 1960 - 2010



2010, while surrounding suburbs grew steadily. Even into the 1980's, Baltimore was still larger than any Maryland county, but was surpassed by Montgomery, Prince George's, and Baltimore County by the start of the new millennium. From 30% of the state's population as of 1960, Baltimore City has fallen to 11% as of the 2010 Census.

As the City lost population both in real terms and relative to the growing large Maryland counties, its relative wealth eroded as well. Following half a century of decline, Baltimore has been left with much weaker income levels, lower home values, and higher poverty rates than its suburban neighbors — contributing as well to lower governmental credit ratings.

In the City's labor market, over just the past two decades from 1990 to 2010, the City lost nearly 110,000 jobs (23.7%).

Approximately 70 percent of those losses came from the

manufacturing, transportation, trade, and utilities sectors, which collectively lost 76,400 jobs over the 20 year period. Those sectors represented 27.4% of total employment in 1990, and just 14.2% of total employment by 2010.

During the last 50 years of post-industrial decline, as a result of challenges not unique to Baltimore, the City has experienced a "vicious cycle" of disinvestment that has

	Per Capita Income 2011	Median Family Income 2011	Median Monthly Owner Housing Cost 2011	Median Home Value 2011	% of Individuals Below Poverty 2011	% of Children in Poverty 2011	Moody's Credit Rating 2013
Baltimore City	\$22,754	\$47,247	\$968	\$154,400	25.1%	37.4%	Aa2
Anne Arundel County	\$39,537	\$94,215	\$1,643	\$332,800	5.7%	7.0%	Aa1
Baltimore County	\$32,726	\$74,716	\$1,227	\$254,900	9.6%	11.8%	Aaa
Harford County	\$33,703	\$88,216	\$1,413	\$277,500	9.3%	17.1%	Aaa
Howard County	\$46,760	\$116,560	\$1,792	\$412,400	6.1%	8.8%	Aaa
Montgomery County	\$45,614	\$112,422	\$1,803	\$443,800	6.5%	8.0%	Aaa
Prince George's County	\$31,365	\$81,134	\$1,553	\$257,300	9.3%	11.2%	Aaa
Baltimore City Rank	7 of 7	7 of 7	7 of 7	7 of 7	7 of 7	7 of 7	7 of 7

Sources: US Census Bureau, American Community Survey, 2011 One-Year Estimates; Moody's Investors Service

Reason for leaving Baltimore	% of those indicating they were likely to leave within 3 years
Crime/Safety	31%
Taxes are too high	13%
Pursue another job	10%
Poor quality public schools	8%
Cost of living is too high	7%
Lack of opportunities	3%
Better housing	3%
City conditions	3%
Children's benefit	3%
Change	3%
Pursue an education	2%
Moving is involuntary	2%
All other	10%

Source: Baltimore City Citizen Survey, 2011 Report. Schaefer Center for Public Policy, University of Baltimore.

Baltimore's New Narrative (2010 - Forward)

Despite the City's legacy "old narrative" challenges, there is emerging evidence that Baltimore's post-industrial decline has begun to level out, and may even be positioned for reversal. While intercensal estimates indicated a loss of 29,702 residents between 2000 and 2005, that trend slowed to just 2,067 from 2005 to 2011.¹ During the same period since 2005, the City largely held its share of population within the Baltimore-Towson Metropolitan Area, losing less than one percent of its share of the area's population. The City's regional competitiveness appears to be stabilizing.

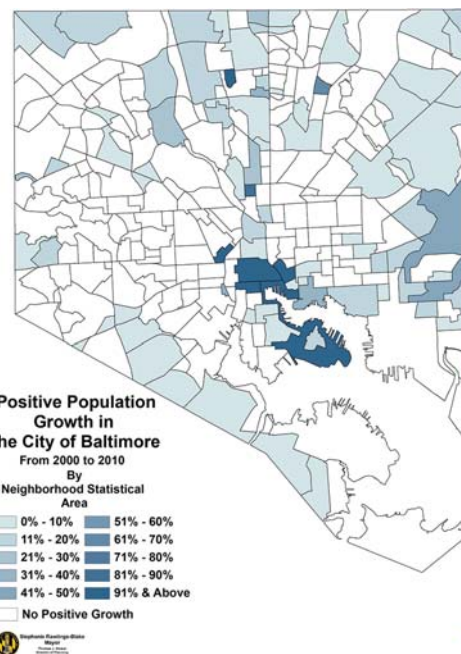
Further, within these overall trends of stabilization, an increasing number of City neighborhoods are already experiencing positive growth. From 2000 to 2010, 87 of Baltimore's 278 neighborhood areas remained stable or grew in population, up from 57 areas between 1990 and 2000 — and of the 87 growing City neighborhoods, 10 saw population gains of 50% or more.

Another positive trend is the growing number of young, working-age people living in Baltimore. While the City's population patterns among age cohorts from 2000 to 2010 generally mirror those seen across the State, two notable exceptions are the 20-24 and 25-34 age categories. The population of Baltimore residents in these cohorts grew by 17,489 from 2000 to 2010, increasing the City's share of the total population by 3.9%.

Across the state, this same cohort reduced its share of the total

eroded both community and fiscal stability. There are estimated to be over 16,000 vacant, abandoned structures in the City, representing a major impediment to public safety, community vitality, and property values. Although crime rates have improved in recent years, crime — and perceptions of crime — remains a major concern. City schools are also improving, but keeping young parents in the City is still a challenge. Compounding these factors, the City's legacy of non-competitive property tax rates and high overall tax burdens is a major impediment to growth and makes it that much more difficult to retain residents who can afford alternative locations.

These critical challenges — jobs, crime, schools, and taxes — are among the top reasons people choose to leave the City. In the 2011 Citizen Survey Report compiled by the University of Baltimore, 31% of respondents who indicated that they were likely to leave the City in the next three years cited "crime and safety" as their reason for leaving. Another 13% responded that taxes were too high, 10% anticipated leaving to pursue employment opportunity elsewhere, and 8% cited "poor quality public schools."



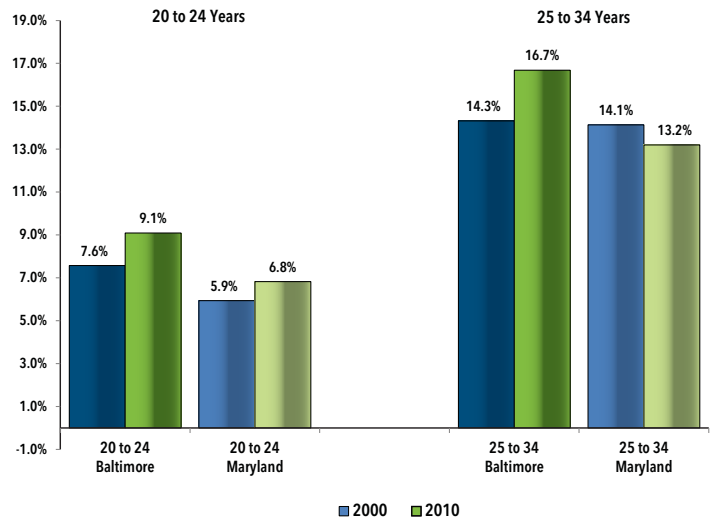
¹The City has challenged the 2011 Census estimates based on concerns regarding potential understatement. If revised upward, Baltimore's trajectory may be even more positive.

population. Maintaining this key demographic — especially as they begin to raise school-age children — is vital to the City’s growth strategy, and achievement of the Mayor’s goal of adding 10,000 new Baltimore families by 2020.

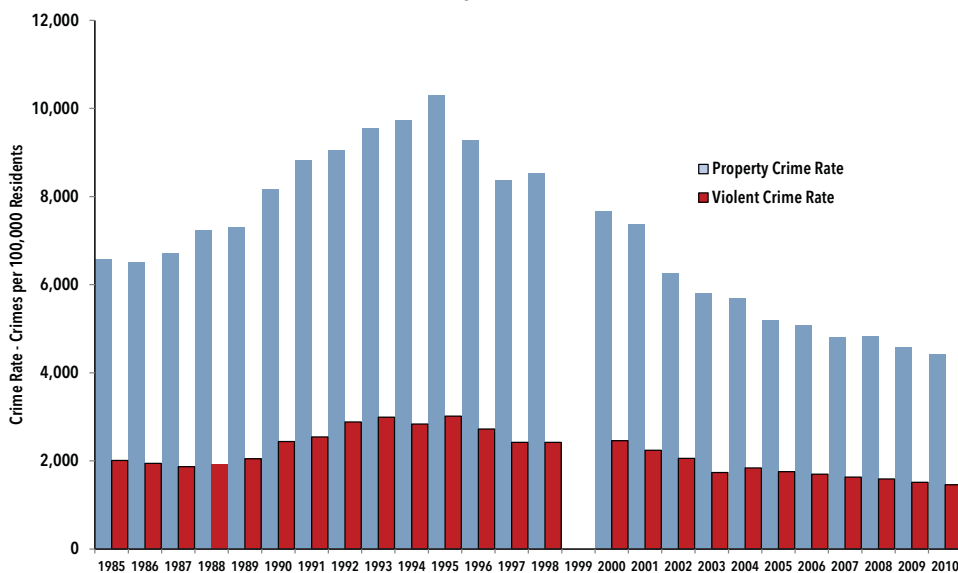
Crime rates have also seen steady improvements since their peak in 1995. As of 2010, both property and violent crime rates were half of what they were 15 years earlier.

Along with improving population and crime trends, Baltimore is also redefining itself as a growing City focused on a knowledge-based economy — with strengths in research and education, life sciences, hospitality, green industries, and global interconnectedness. The “old economy” manufacturing sector — while still important — now represents a much smaller share of the City’s jobs than the service industries, and the education and health services sectors in particular. From 1990 to 2011, while the City lost more than half of the remaining 126,400 jobs in the manufacturing, transportation, trade, and utilities sectors, employment in the educational services and healthcare and social assistance sectors grew from 81,700 to 113,100. In 1999, education and health sector employment was greater than manufacturing, transportation, trade, and utilities sector employment for the first time, and by 2009 the former was more than double that of the latter.

Percent of Total Population by Age
City of Baltimore and State of Maryland, 2000 to 2010

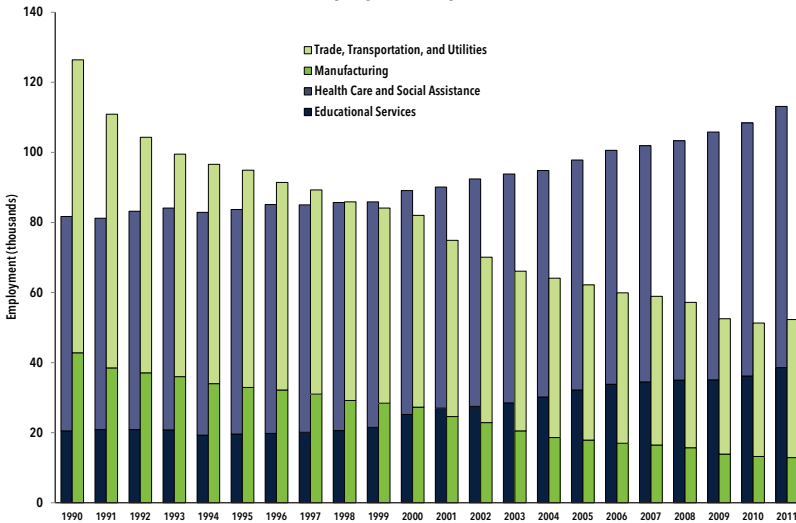


Baltimore City Crime Rates – 1985-2010



Source: FBI UCR Data
Note: 1999 data not available

Baltimore Employment by Sector, 1990-2011



price range may not exactly parallel the median), these statistics do reflect the general deflation of the past decade's housing bubble.

In turn, this decline in overall home value has had a significant impact on City Property Taxes — Baltimore's single largest revenue source representing nearly half of the FY2013 General Fund budget — and will continue to dampen these receipts going forward. With Property Taxes, there is a built-in lag between changes in the housing market and actual tax receipts. In Maryland, the State assesses real property on a triennial basis, such that valuation changes are phased-in over a multi-year period. In addition, the Homestead Tax Credit program caps annual increases at 4%, which can result in deferred recognition of value during periods of rapid market increases. In any subsequent period of market decline, this "pent up"

accumulated value can help to "buffer" Property Tax receipts, such that revenues will not fall as quickly or sharply as the market. Conversely, however, if the housing market does continue to rise, the City will not see revenues bounce back as quickly as the market recovery due to the same lag and buffer effects of the assessment cycle and the Homestead Tax Credit.

Employment levels in the City were similarly hit hard by the Great Recession. From the most recent peak in 2008 to a historic low in 2010, Baltimore lost approximately 19,000 City resident jobs (7.2%). Although the City has experienced positive job growth

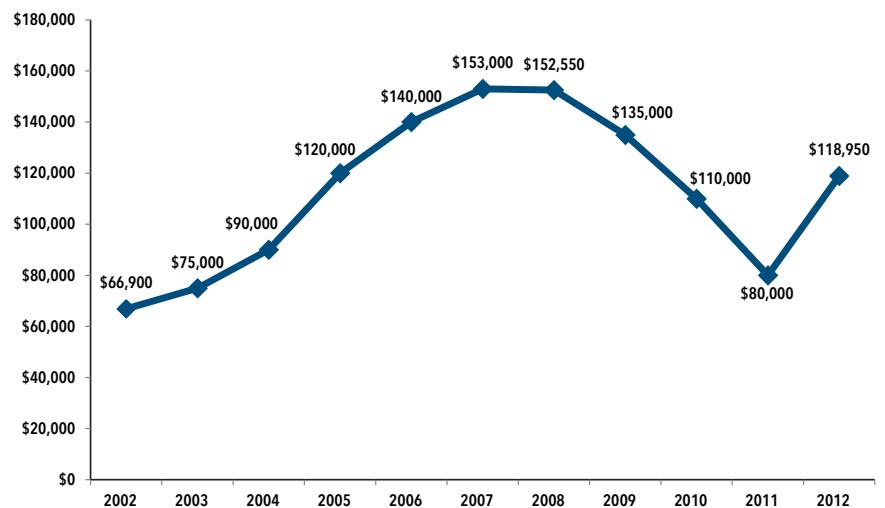
Impacts of the Great Recession

Many of the City's economic indicators have shown promise in recent years — overall population stabilization, growing competitiveness as a regional place of choice for young adults, declines in the crime rate, and health care and education job creation — even during the most severe economic downturn in generations. Nonetheless, the "Great Recession" did strike Baltimore's housing and jobs markets hard, with significant adverse impacts on the major revenue sources linked to these segments of the economy.

Between 2002 and 2007 — the years of the housing bubble — median home sale prices in the City of Baltimore grew rapidly, more than doubling overall. After plateauing in 2008, prices dropped precipitously through 2011, falling to the lowest levels seen since 2003. In 2012, prices turned upward markedly to approach the levels of 2005, indicating the potential for recovery in the City's housing market.

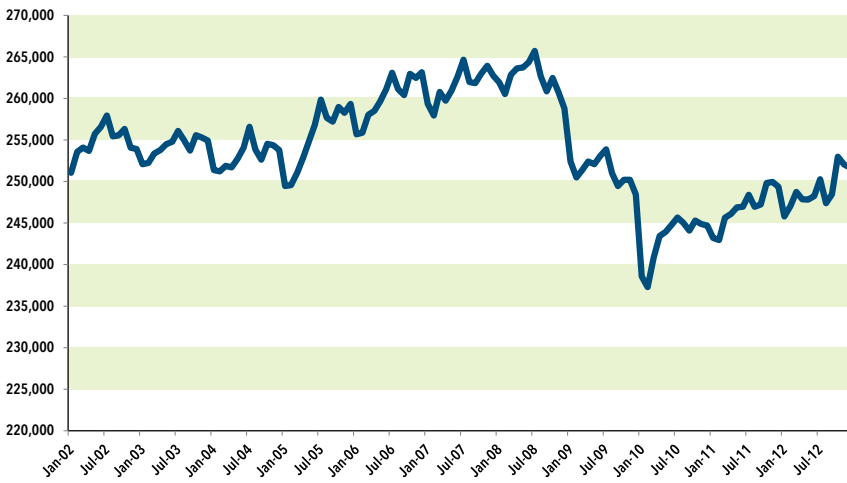
While median home sales prices do not correlate precisely to overall property values in the City (as different segments of the housing market may be more or less active during different periods, and as values at the higher and lower ends of the

Median Sale Prices – Owner-Occupied Residential Property FY2002-12



Source: MRIS Multiple Listing Service (MLS)

Baltimore Employment – City Residents
January 2002 to December 2012 (monthly, not seasonally adjusted)



Source: Bureau of Labor Statistics, Local Area Unemployment Statistics

over the last three years, employment levels of City residents in 2012 were still below those of the last decade, even in the earlier part of the decade during and following the 2001 recession. Effectively, City employment levels have “reset” after the downturn at a markedly lower ratchet.

As jobs were lost, unemployment rates also rose steeply. Unemployment levels for Baltimore residents that had dropped as low as 5.0% in late 2007 and that were consistently below 8.0% for most of the past decade, skyrocketed as high as 12.0% in 2010 and remained at double-digit levels for most months of 2012.

Employment of Baltimore City residents is a particularly relevant indicator of Income Tax receipts, the City’s second largest source of revenue at 16.2% of the FY2013 General Fund budget, because the City tax rate (“piggybacked” on the State Income Tax) is applied only to residents. The City does not receive revenue from taxed commuter income. Along with Income Tax receipts, City employment levels are also associated with other economically sensitive revenues such as the Parking Tax.

Going forward, as outlined in the Ten-Year Budget Projections section of this Background

Report, this Financial Plan assumes continued economic recovery, such that these recent trends turn back upward at a steady pace. Given the significant impact of the economic downturn, however, such growth is projected to take place from a new base now well below the levels that would have been reached had the recession not occurred, and to remain dampened by the City’s underlying economic challenges.

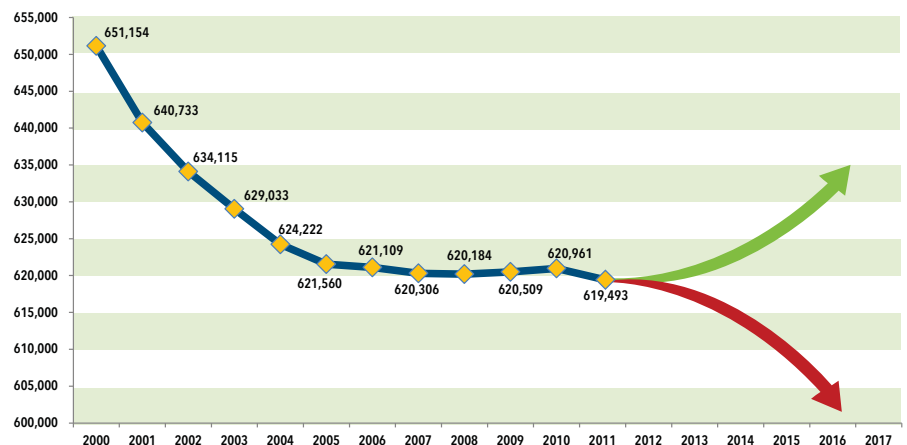
Further, these same factors that have weakened the City’s revenue growth — long-term population and economic decline, compounded by headwinds from the more recent recession — have also created pressures on the expenditure side of the budget. Vacant structures, concentrations of poverty requiring health and human services supports, and the limited job opportunities that contribute to crime and other social ills, are all, in large part, a reflection of Baltimore’s overall economic trajectory.

Inflection Point

Facing the ten years ahead, the City of Baltimore is now at an inflection point — the juncture where a trend or curve changes direction. With population stabilizing after more than half a century of post-industrial decline, and the broader economy now beginning to recover from the downturn:

- At the end of the decade now ahead, will Baltimore look back at this period of stabilization as having been no more than a

Baltimore City Population, 2000-2011 (Census Data)



Population Trends 1960 - 2010 with Percentage Change from Previous Decade

City	1960	1970	1980	1990	2000	2010
Atlanta, Georgia	487,455	496,973 2%	425,022 -14%	394,017 -7%	416,474 6%	420,003 1%
Austin, Texas	186,545	251,808 35%	345,496 37%	465,622 35%	656,562 41%	790,390 20%
Baltimore, Maryland	939,024	905,759 -4%	786,775 -13%	736,014 -6%	651,154 -12%	620,961 -5%
Boston, Massachusetts	697,197	641,071 -8%	562,994 -12%	574,283 2%	589,141 3%	617,594 5%
Charlotte, North Carolina	201,564	241,178 20%	314,447 30%	395,934 26%	540,828 37%	731,424 35%
Cleveland, Ohio	876,050	750,903 -14%	573,822 -24%	505,616 -12%	478,403 -5%	396,815 -17%
Dallas, Texas	679,684	844,401 24%	904,078 7%	1,006,877 11%	1,188,580 18%	1,197,816 1%
Denver, Colorado	493,887	514,678 4%	492,365 -4%	467,610 -5%	554,636 19%	600,158 8%
Indianapolis, Indiana	476,258	744,624 56%	700,807 -6%	731,327 4%	781,870 7%	820,445 5%
Minneapolis, Minnesota	482,872	434,400 -10%	370,951 -15%	368,383 -1%	382,618 4%	382,578 -0%
Philadelphia, Pennsylvania	2,002,512	1,948,609 -3%	1,688,210 -13%	1,585,577 -6%	1,517,550 -4%	1,526,006 1%
Pittsburgh, Pennsylvania	604,332	520,117 -14%	423,938 -18%	369,879 -13%	334,563 -10%	305,704 -9%
Portland, Oregon	372,676	382,619 3%	366,383 -4%	437,319 19%	529,121 21%	583,776 10%
Raleigh, North Carolina	93,931	122,830 31%	150,255 22%	207,951 38%	276,093 33%	403,892 46%
Richmond, Virginia	219,958	249,621 13%	219,214 -12%	203,056 -7%	197,790 -3%	204,214 3%
San Diego, California	573,224	696,769 22%	875,538 26%	1,110,549 27%	1,223,400 10%	1,307,402 7%
Seattle, Washington	557,087	530,831 -5%	493,846 -7%	516,259 5%	563,374 9%	608,660 8%
St. Louis, Missouri	750,026	622,236 -17%	453,085 -27%	396,685 -12%	348,189 -12%	319,294 -8%
Tampa, Florida	274,970	277,767 1%	271,523 -2%	280,015 3%	303,447 8%	335,709 11%
Washington D.C.	763,956	756,510 -1%	638,333 -16%	606,900 -5%	572,059 -6%	601,723 5%

momentary pause — a footnote — in the longer-term story of decline?

- Or will this have been the point where Baltimore began to turn the corner, and to write a new narrative that redefines “urban” as an exciting and energized place to visit, to work, and to live?

While global, national, and regional economic forces and policies will greatly affect Baltimore’s prospects in the decade ahead, local strategies, choices, and actions will also have a critical impact on this future direction.

- A new narrative will require difficult choices and significant change in how the City does business.
- It will require strategic collaboration and support, not further cutbacks, from the State and federal governments.
- It will require new partnerships from regional and civic stakeholders.
- It must be grounded in stable City finances, with a structurally sound budget and improving balance sheets.

Reversing the trend of population decline will not be easy, but other cities have managed to overcome decades of shrinking populations. For example, the 2010 Census shows that Philadelphia grew in population for the first time since 1950.

Boston has seen three consecutive decades of growth after losing nearly 30% of its population between 1950 and 1980. Other cities that have stemmed population decline and grown in recent decades include Atlanta, Denver, Minneapolis, Richmond, and Washington, D.C.

As part of this Ten-Year financial planning process, the project team has assessed the City’s strengths, weaknesses, opportunities, and threats (SWOT) to help evaluate the key factors and considerations now shaping Baltimore’s future economic and fiscal environment, and potential forces that may impact the City going forward. This SWOT analysis is summarized in the Appendices, and informs the sections of this report to follow regarding the City’s structural budget balance, tax competitiveness, infrastructure investment needs, and long-term liabilities.

Accordingly, within what is primarily a government financial planning framework, the following broader economic considerations remain important:

- The most impactful economic and neighborhood development strategy for any City government is to do the basics well: deliver quality municipal services at a competitive rate.

Accordingly, virtually every issue highlighted within this plan ties back to the economic growth and community vitality of the City — particularly, property tax rate reduction, ensuring safe and clean neighborhoods, helping to support better schools, and improving core public infrastructure.

- At the same time, certain focused initiatives hold the potential to reinforce and move beyond the basics through strategic investments in Baltimore’s new economy and strengthening neighborhoods.
- Some of Baltimore’s most transformative economic development opportunities are not directly sponsored by City government, but all will require strong coordination and championing to bring successfully into place:
 - The Baltimore Red Line will be a 14.1 mile, 19-station, \$2.2 billion light rail transit line providing improved connections to jobs and major attractions along the east-west corridor from Baltimore County, through Edmondson Village, West Baltimore, downtown Baltimore, Harbor East, Fell’s Point, and Canton to the Johns Hopkins Bayview Medical Center campus. With final State and federal funding, construction could start by 2015 with operations beginning within the Ten-Year Plan period in 2021.
 - Already experiencing record cargo levels, the Port of Baltimore recently opened a new 50-foot container berth at the nationally competitive Seagirt Marine Terminal, is bringing new super-cranes on line to further improve capacity, and is pursuing development of a new intermodal facility to enable more cost-effective double-stacking of containers for rail transport. With these investments, the Port of Baltimore is poised for even greater growth and connection to global markets when the Panama Canal expansion is completed in 2014 to allow more and larger cargo ships to transit.
 - Following the opening in 2012 of Johns Hopkins Medicine’s new \$1.1 billion patient towers, the City’s life sciences sector is experiencing growth at both the University of Maryland Baltimore’s BioPark and the Science + Technology Park Johns Hopkins.
 - Baltimore is also becoming increasingly central to a fast-growing regional IT sector, with the metropolitan area ranked in the top five “Best Cities for Tech Jobs” and “New Tech Hot Spots” by *Forbes* magazine within the past year. As IT and information security become increasingly larger parts of

the national economy, Baltimore is well-positioned to take advantage of continued growth.

- To modernize Baltimore’s entertainment and hospitality assets, development plans are being pursued for a potential new complex downtown just blocks from a revitalized Inner Harbor to include an arena and hotel connected to an expanded convention center. The City’s hospitality sector provides jobs and a good career path for many residents, and is now at risk of decline with the aging of the 1st Mariner Arena (over 25% smaller and more than three decades older than the average across the same 35 metro areas) and Convention Center (now with less than half the exhibit space of the average among competing facilities in the nation’s 35 largest metro areas).
- Beyond such major projects, Baltimore’s new economy also includes opportunities created by the growth of a regional information technology sector, dynamic hometown firms like Under Armour, and a broad range of entrepreneurial small businesses. Along with ongoing City partnership and support, Baltimore’s business community as a whole requires a municipal government that is business-friendly and customer-focused.
- To support neighborhood development across Baltimore, three key Citywide issues and initiatives will be critical over the decade ahead, and are further addressed within this Plan:
 - To create a better learning environment for Baltimore’s children, the City launched a major school construction and renovation initiative earlier in FY2013 — The Better Schools Initiative.
 - Launched in November of 2010, Mayor Rawlings-Blake’s Vacants to Value initiative encourages reinvestment in neighborhoods impacted by blight by strengthening code enforcement, promoting rehabilitation; streamlining the sale of vacant city property, and providing new, targeted incentives for homebuyers and developers who invest in vacant homes.
 - To address federal environmental mandates to improve the health of the Chesapeake Bay, the City is launching a wave of stormwater management investments to promote a “greener” urban environment.
- Beyond such citywide neighborhood investments, a series of specific community development initiatives are also underway.

These real estate development activities are generally at a scale large enough to transform the broader communities in which they are based, ultimately improving the attractiveness and marketability of entire Baltimore neighborhoods.

- For example, ongoing redevelopment at the 60-acre Uplands site will impact the market and improve property values in a number of surrounding communities.
- Investments by the City and Housing Authority in Barclay have already begun to positively impact the entire neighborhood, with newly constructed homes selling above originally expected levels.
- East Baltimore Development, Inc. (EBDI), one of the largest redevelopment efforts on the east coast, is well underway and moving forward.
- Other areas that have recently experienced large-scale redevelopment or that will soon be receiving such investment include: O'Donnell Heights, where the first 75 of an anticipated 900 new homes are under construction; Orchard Ridge, where the latest phase of housing should begin this year; Poppleton; Johnston Square; and Park Heights, still in the beginning stages of a well-planned turnaround.
- Also ongoing, fully private sector real estate investment is actively adding to Baltimore's residential base and options, such as Harbor Point on the City's east side waterfront.
- Bridging these economic and community development approaches, the City now offers a range of tax abatements and incentives. By reevaluating these tools to maximize their impact, Baltimore may be able to identify refined approaches to further improve its competitiveness for

attracting private investment. For example, to meet growing demand for residential options, a new apartment development incentive program as proposed by Mayor Stephanie Rawlings-Blake could help to spark significant new investment that could create more of a 24/7 environment in both downtown and neighborhood commercial districts.

- This construction and development activity to advance all of the major public and private investments planned for the years just ahead also creates a once-in-a-generation opportunity for local economic stimulus. To fully capture this potential, however, it will be critical to link these projects to workforce development for City residents. While these are major opportunities for the region no matter who works on the projects, Baltimore will receive no income tax from those construction workers on these projects who live outside the City, no sales tax from dollars spent at the project sites, and no direct property tax gains from projects to be owned by governmental and nonprofit institutions. Alternatively, to the extent this decade of new investment can be leveraged to create more jobs for City residents, then Baltimore will receive stronger tax receipts in the near-term, while building a more skilled workforce for the long-term.

All of these economic opportunities, however, depend on a financially stable and sustainable City government that can provide reliable municipal services at an increasingly competitive rate — and establishing this sound foundation will require strong actions beyond the status quo.

Accordingly, the next section of this foundational analysis turns to a detailed assessment of where the City is headed financially if change does not occur.

Major Baltimore Investments Potentially Coming On Line Within the Next Ten Years	
Red Line light rail construction	School facility investment
Port of Baltimore growth	Stormwater management "greening"
BioScience parks expand	Vacants to Value demolition accelerated
New apartment development	Neighborhood redevelopment across the City
New Arena and Convention Center expansion	Expanded community capital investment (e.g., Recreation Center upgrades)



Financial and Economic Analysis:
Ten-Year Budget Projections

In developing the City's FY2013 Budget, Baltimore had to close a \$48 million shortfall in the projected funding levels required to "carry forward" prior year service levels, even after a series of sharp cuts and revenue increases had already been adopted over the preceding four years.

Fundamentally, Baltimore now faces a structural imbalance between the rates of growth in the City's recurring revenues and its faster-growing expenditures, such that new shortfalls will continue to open up in each new fiscal year despite past corrective actions. Until the City is able to "bend the curve" on these growth rates, Baltimore will face continued budget pressure for many years to come.

This structural budget challenge is not purely a result of the recent economic downturn, nor is it unique to the City of Baltimore. An April 2012 study¹ by the U.S. Governmental Accountability Office (GAO) projected receipts and spending for the national, state, and local sector as a whole, and forecast a steady decline in fiscal position across the sector for the next half century. According to the GAO, the actions necessary to close this gap would equate to a 12.7% reduction in current expenditures nationally.

In this GAO analysis, the primary driver of long-term state and local government fiscal challenges is projected growth in health-related costs — which impact active and retiree benefits for local governments, and Medicaid costs at the state level. Such health-related costs are forecast to continue to outpace overall economic growth and the public sector revenues closely linked to overall economic performance. In addition, the GAO cites pension funding requirements as a further pressure on state and local finances.

For older cities such as Baltimore, these general structural forces are often compounded by economic and revenue trends that lag faster-growing communities, as well as concentrations of poverty, maintenance demands for aging infrastructure, the challenges of vacant and abandoned properties, and other legacy costs associated with historical population decline. For example, older cities will tend to have proportionately more retired municipal workers already drawing down pension benefits relative to the number of active employees still paying into the retirement system when compared to less mature, high-growth cities that served much smaller populations with much smaller workforces

only a few decades ago. Further, as state governments face pressures of their own, cuts in state funded grants and local assistance will often flow downward to create added budget difficulty at the local level — with a greater impact on communities more reliant on state-supported programs and investments.

For the City of Baltimore, PFM worked closely with the City Finance Department to develop a baseline forecast that takes into account Baltimore's particular fiscal factors. For this analysis, PFM developed a detailed, multi-year budget model that applies assumptions about future growth to thousands of individual revenue and expenditure lines, and that can evaluate alternative economic scenarios. Building on three-year projections regularly produced by the Finance Department, the analysis updates and extends such forecast assumptions through the end of the Ten-Year Plan period. As detailed below, these projections also rely on input from Hay Group and the actuarial firms for the City's two major retirement systems, on debt analysis developed in conjunction with the Finance Department's Bureau of Treasury Management, and on input from various operating departments.

Conceptually, the Ten-Year Plan baseline forecast is intended to represent a "carry forward" or "current services" set of projections — such that no reduction or enhancements in services, headcount, or tax rates are generally assumed, except where already adopted into current law or consistent with existing policy.

Base Case Ten-Year Plan Projections

The primary baseline projections highlighted within this Ten-Year Plan are intended to reflect anticipated General Fund budget results on a carry-forward basis under economic conditions consistent with mainstream forecasts and expectations:

- Steady, but modestly paced economic recovery.
- Employment levels gradually improving.
- City population levels stabilizing, with modest expansion of development/redevelopment.
- City housing market also stabilizing with moderate growth in out-years, supported by a continued low-interest rate environment.

¹United States Government Accountability Office, *State and Local Governments' Fiscal Outlook, April 2012 Update*

- Moderate growth in Baltimore’s income tax and economically sensitive revenues, commensurate with assumed population stabilization, job gains, and some wage gains under an improving overall economy.
- Ongoing, incremental gains in Baltimore City Public Schools (BCPS) student enrollment, consistent with recent trends.
- Pension costs meeting current actuarial assumptions.
- Moderate health care inflation relative to recent, prior years — approximately 6% in FY2013 with a slight downward trend.

Under the above set of economic conditions — while the City budget is, again, now balanced for the current Fiscal Year 2013 — future revenues are not forecast to grow at levels needed to sustain projected expenditures for current services. Without corrective action, this structural deficit is projected to result in a fiscal gap of approximately \$30 million in FY2014, growing to more than \$124 million by FY2022 — for a cumulative shortfall of nearly \$745 million.

The following sections highlight major revenue and expenditure assumptions, with detailed growth factors included in Appendix C.

Major Revenue Assumptions

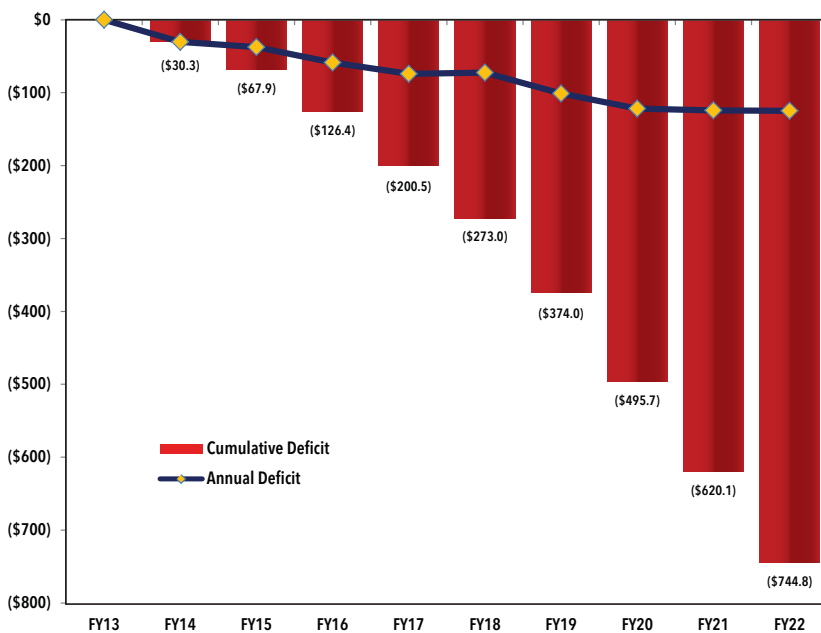
In the aggregate, baseline revenues are forecast to grow by a compound annual average of 1.9% over the ten-year forecast period. In FY2014, aggregate growth is forecast to be just 0.9%

as property tax revenues from prior triennial assessments lag the recovering housing market and weak economic conditions persist. While Property Tax revenue growth is assumed to gradually increase throughout the forecast period, other factors including the increasing Targeted Homeowners Tax Credit hold growth at an average of approximately 1.8% in the middle years of the plan before total revenue growth begins to rebound in FY2020 (2.1%) through FY2022 (2.9%).

Significant revenue growth assumptions include the following:

- **Property Tax** (\$768.3 million in FY2013) — Assumes slow growth in the housing market, with lagging receipts due to the triennial assessment process; prior losses offset somewhat by the recognition of value previously not taxed due to the Homestead Credit. The Property Tax rate is assumed to be flat; however the Mayor’s Targeted Homeowner’s Tax Credit is included in the baseline forecast.
- **Transfer and Recordation Taxes** (\$42.2 million in FY2013) — Assumes gradual recovery in property sales, with low near-term levels of sales offset somewhat by mortgage refinancings (Recordation Tax).
- **Income Tax** (\$256.1 million in FY2013) — Assumes continued recovery in FY2014, with growth rates gradually reducing in the out years, consistent with assumed Gross Domestic Product (GDP) growth.
- **Hotel Tax** (net) (\$22.0 million in FY2013) — Hotel tax revenue reflects the net transfer from the Convention Center Bond Fund, after payment of debt service associated with the Convention Center (scheduled to end during the plan period in FY2022, absent additional capital investment). Assumes moderate expansion in hotel rooms, rates consistent with inflation, and some improvement in occupancy rates.
- **Energy Tax** (\$38.8 million in FY2013) — Assumes growth generally consistent with inflation, offset somewhat initially by moderate activity decline during the first three years of the Plan.
- **Telecommunications Tax** (\$34.3 million in FY2013) — Increased demand for wireless phones is assumed to be somewhat offset by negative land line growth. Overall, the forecast assumes the net number of phone lines will parallel City population trends.

General Fund Baseline Projected Fiscal Gap



Summary of Major Revenues - FY2013-22

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Property Tax	\$768.3	\$759.4	\$767.8	\$784.1	\$803.8	\$828.9	\$842.8	\$870.0	\$901.7	\$934.8
Transfer and Recordation Tax	\$42.2	\$44.4	\$47.4	\$50.8	\$55.2	\$60.5	\$66.6	\$73.6	\$81.5	\$90.8
Income Tax	\$256.1	\$267.5	\$273.1	\$278.6	\$283.9	\$289.0	\$292.2	\$295.4	\$298.6	\$301.9
Hotel Tax (net)	\$22.0	\$24.0	\$24.9	\$25.4	\$25.9	\$26.5	\$27.2	\$27.9	\$28.6	\$34.2
Energy Tax	\$38.8	\$39.5	\$40.2	\$41.0	\$41.9	\$42.8	\$43.8	\$44.8	\$45.8	\$46.9
Telecommunications Tax	\$34.3	\$34.3	\$34.3	\$34.3	\$34.3	\$34.3	\$34.3	\$34.4	\$34.5	\$34.6
Highway User Revenue	\$132.0	\$134.4	\$142.6	\$145.9	\$145.9	\$145.9	\$145.9	\$145.9	\$145.9	\$145.9
State Aid	\$100.5	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0
All Other	\$176.8	\$180.5	\$180.4	\$186.4	\$184.5	\$181.9	\$177.6	\$175.1	\$176.1	\$177.1
Total	\$1,571.1	\$1,585.9	\$1,612.7	\$1,648.6	\$1,677.4	\$1,711.9	\$1,732.4	\$1,769.1	\$1,814.8	\$1,868.2

average rate of 5.7% from FY2015-22, however, and pension cost growth is forecast to grow by an average annual rate of 5.3% through FY2017 before decreasing gradually to 1.0% by FY2022 (excluding the newly mandated teacher pension costs).

■ Highway User Revenue (\$132.0 million in FY2013) — Increases

to this major state revenue stream are based primarily on the estimated budget appropriations established by the State Budget Reconciliation and Financing Act. Due to uncertainty around state funding generally, growth is assumed to be flat beyond the years of those estimates (FY2017-22).

■ State Aid (\$100.5 million in the FY2013 General Fund) — The

baseline scenario assumes flat growth in other state aid due to state budget uncertainty and consistent with recent history. Of the \$100.5 million estimated for FY2013, approximately \$77.5 million comes from the Income Tax Disparity Grant, a program designed to aid counties with low wealth relative to the state average. The State Budget Reconciliation and Financing Act of 2012, which shifted teacher pension costs to the counties and Baltimore City, added an additional \$7.0 million in state aid designed to partially offset those new costs. Another \$6.7 million derives from state grants for local health operations and \$6.5 million is from state grants for library services.

■ Wages (\$579.5 million in the FY2013 General Fund) — The

baseline assumes cost of living increases of 2% annually, generally paralleling forecast consumer price growth. In addition, the baseline assumes further 0.5% annual wage growth due to the net impact of step and longevity increases, turnover, hiring delays, and separation payments, consistent with historical experience. Stable overall headcount is assumed in this baseline scenario.

■ Health Insurance (Active Employees) (\$95.1 million in the

FY2013 General Fund) — In FY2014, annualized savings from recently implemented health plan changes results in a reduction of approximately 4% over FY2013 budgeted health insurance costs (including medical, prescription drug, dental and optical). The baseline assumes continuing growth of 5.9% and 5.8% for active employees' health insurance in FY2015 and FY2016, respectively. This growth is assumed to be moderated somewhat to 5.7% by FY2017 and 5.6% in FY2022.

■ Pensions (\$149.4 million in the FY2013 General Fund) —

Growth is consistent with actuarial assumptions, with ERS and FERS contributions growing at an average of 5.3% in the first four years of the plan and gradually reducing to a blended rate of approximately 1.0% by FY2022.

■ Retiree Healthcare (\$55.5 million net of transfers in the

FY2013 General Fund and excluding payments for school retirees, which are included in the BCPS contributions) —

Major Expenditure Assumptions

Baseline expenditures are forecast to grow faster than revenues in all years except FY2018, FY2021, and FY2022. Over the ten-year forecast period, expenditures are forecast to grow at a compound annual average rate of 2.7%. Aggregate expenditure growth is forecast to be 2.9% in FY2014, increasing to a top growth rate of 3.4% in FY2016 when debt service and pension cost growth peaks, before moderating to an annual average of 2.6% in FY2017-22.

Many of the City's

expenditures are assumed to trend with Consumer Price Index (CPI) assumptions (approximately 2% annually).

The cost of health benefits for active employees is assumed to grow by an

Summary of Major Expenditures - FY2013-22

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Wages	\$579.5	\$600.2	\$615.1	\$630.3	\$646.3	\$662.3	\$678.9	\$695.7	\$713.4	\$731.0
Health Insurance (Actives)	\$95.1	\$91.4	\$96.8	\$102.4	\$108.2	\$114.4	\$120.9	\$127.8	\$135.1	\$142.6
Pensions (ERS/FPERS/EOS)	\$149.4	\$162.6	\$166.6	\$177.7	\$183.7	\$188.1	\$191.6	\$194.5	\$196.8	\$198.8
Retiree Healthcare	\$55.5	\$53.2	\$54.9	\$56.2	\$57.7	\$59.3	\$61.1	\$62.7	\$64.4	\$66.1
BCPS Contributions	\$253.5	\$256.7	\$262.2	\$268.2	\$276.3	\$281.6	\$290.1	\$298.6	\$307.5	\$316.6
Services/Materials/Utilities	\$244.6	\$247.0	\$252.9	\$260.5	\$268.7	\$277.3	\$285.9	\$295.2	\$305.5	\$314.5
Debt Service	\$142.3	\$144.0	\$143.3	\$155.9	\$156.9	\$150.4	\$156.3	\$164.9	\$162.6	\$166.5
All Other	\$51.4	\$61.2	\$58.6	\$56.0	\$53.5	\$51.1	\$48.7	\$51.3	\$53.9	\$56.7
Total	\$1,571.1	\$1,616.2	\$1,650.3	\$1,707.1	\$1,751.4	\$1,784.5	\$1,833.4	\$1,890.7	\$1,939.2	\$1,992.9

The cost of retiree healthcare is assumed to grow at a slower pace than that of active employee healthcare, with blended growth for retiree medical premiums and prescription drug coverage of approximately 2% annually. This lower growth rate is primarily due to analysis of the size of the current and projected cohort of retirees not yet eligible for federally subsidized Medicare during the Ten-Year Financial Plan period.

■ **BCPS Contributions** (\$253.3 million in the FY2013 General Fund) — Contributions to Baltimore City Schools include the City’s local share of education costs under State Maintenance of Effort (MOE) requirements, the cost of BCPS retirees’ health benefits, and other City payments toward costs associated with the BCPS transition from past City control. Beginning in FY2013, as newly mandated by the State, direct support for BCPS also includes the cost of contributions for BCPS employee pensions (to be partially offset by new revenue streams authorized by the state, with a growing shortfall anticipated over time). Recent state legislation further increased local education funding requirements by introducing an automatic escalator to the MOE. Beginning in FY2015, if a county or the City is below the statewide five-year moving average education effort level it must increase its per pupil MOE. The required annual increase will be the lesser of the annual increase in local wealth, the increase in statewide average wealth, or 2.5%. To reflect this change, the baseline forecast assumes that the City’s local share of education will increase by an average of 2.9% from FY2015-22, higher than the projected annual increase in student enrollment. In FY2017, the City’s \$2.8 million termination pay costs are assumed to be eliminated after per the City’s agreement with the BCPS. Overall, direct contributions for BCPS are assumed to grow by an average of 2.5% annually over the Ten-Year Plan period.

■ **Contracted Services, Materials/Supplies, and Utilities** (\$244.6 million in the FY2013 General Fund) — Costs for contracted services and materials and supplies are generally assumed to maintain pace with inflation, growing by approximately 2% annually. Utility costs (\$25.8 million in the FY2013 General Fund) are assumed to grow at 4.4% annually.

■ **Debt Service** (\$142.3 million in the FY2013 General Fund) — In addition to debt service costs for existing City debt, the baseline scenario assumes issuance of

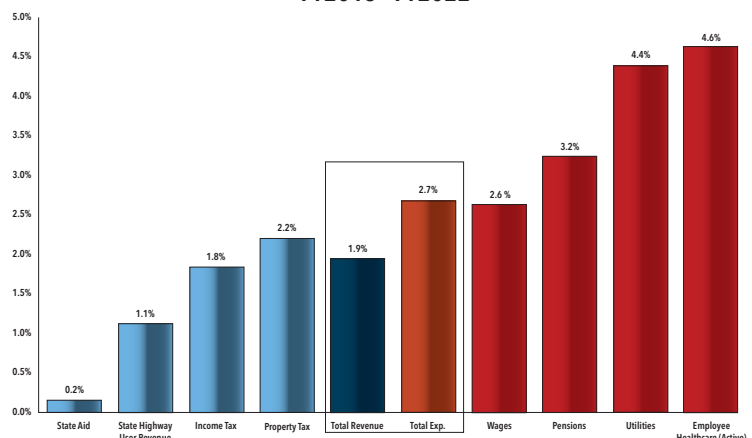
\$65 million in new debt in FY2014 and FY2015, and \$50 million annually thereafter. Debt service costs also include principal and interest payments on certain loans and leases, including \$30 million in financed vehicle purchases each year.

Major Deficit Drivers

For the Ten-Year Plan period from FY2013 to FY2022, the forecast 2.7% compound annual growth rate (CAGR) for all General Fund expenditures is projected to outpace revenue growth of 1.9% per year. This structural imbalance between recurring revenues and recurring expenditures drives the identified budget shortfalls.

Within these projected totals, weakness in several major revenue sources significantly constrains overall growth in available resources. As the City continues to phase-in the effects of the collapse in the housing market, total Property Tax receipts are projected to grow an average of just 1.5% annually for the first five years of the Plan period. Even with a modest rebound forecast for the second five years of the plan, this limited production from Baltimore’s largest revenue source drives much of the overall deficit projection. Further, the City’s second largest revenue source, the local income tax, is also forecast to grow slowly with a CAGR of just 1.8%, and State of Maryland Highway User Revenues (1.1%) and other State assistance (0.2%) also fail to keep pace with rising cost pressures.

Major Budget Drivers - Compound Annual Growth Rate (CAGR)
FY2013 - FY2022



	State Aid	State Highway User Revenue	Income Tax	Property Tax	Total Revenue	Total Exp.	Wages	Pensions	Utilities	Empl. Hthcare (Active)
FY13	\$100.5	\$132.0	\$256.1	\$768.3	\$1,571.1	\$1,571.1	\$579.5	\$149.4	\$25.8	\$95.1
FY22	\$102.0	\$145.9	\$301.9	\$934.8	\$1,868.2	\$1,992.9	\$731.0	\$198.8	\$38.0	\$142.6
\$ Change	\$1.5	\$13.9	\$45.9	\$166.5	\$297.1	\$421.8	\$151.5	\$49.5	\$12.2	\$47.5
CAGR	0.2%	1.1%	1.8%	2.2%	1.9%	2.7%	2.6%	3.2%	4.4%	4.6%

On the expenditure side of the budget, wages are assumed to grow with a CAGR of 2.6%, and rising benefit costs are projected to drive overall personnel costs upward at a rate well above forecast revenue growth. Over the full Plan period, aggregate employer pension contributions are projected to increase by a compound annual growth rate of 3.2%, and health benefits for active employees by 4.6% per year. While less significant in total dollars, rising energy costs and water/sewer rate increases resulting from federal environmental mandates are projected to drive total utility costs upward by 4.4% per year.

Risks

It is also important to note that the baseline forecast is calibrated to reflect a “reasonable” set of assumptions. While not intended to reflect a rosy scenario, it is also far from a pessimistic scenario — let alone “worst case.” The following are among the major areas of identified budget risk still present in the baseline:

■ Economically sensitive revenues

- Global market concerns may slow U.S. economic growth, or even drive the U.S. economy into another recession, reducing revenue growth relative to the baseline scenario.
- The housing market may not recover as quickly as assumed in the baseline scenario, and may decline again within the ten-year forecast period.
- Employment challenges may impact the City’s local economy more severely than anticipated, weakening Income Tax and other economically sensitive revenues.

■ Intergovernmental funding

- Potential State budget reductions below assumed funding levels for Highway User Revenues and the Disparity Grant program would further increase the projected fiscal gap.
- Additional State cost shifts and mandates, as occurred in FY2013 with teacher pension costs, could increase City expenditures.
- Reductions in federal and state grant revenue outside of the City’s operating budget — including federal cutbacks to address national deficit reduction goals — could create increased pressure for the City to provide additional local funding. The FY2013 Budget includes \$273.1 million in Federal and State Grant Fund revenue for a variety of

services and programs, including public safety services, housing for the homeless, workforce assistance, health, and Head Start and other education programs. The Capital Budget includes a combined \$57.7 million in federal and state grants for transportation, housing and community development, waste water, and recreation projects. Cuts to these federal and state grants may require additional support from the General Fund or other local funding sources in order to preserve core services.

■ Workforce

- The single largest, most immediate threat to the City’s fiscal stability is ongoing litigation related to reforms of the Fire and Police Employees Fire and Police Employees’ Retirement System (FPERS) adopted by the Mayor and City in June 2010. To date, the City has received favorable rulings regarding some, but not all, of the adopted reforms — and certain issues of major fiscal importance remain under active litigation. If the City’s approach is not fully upheld (and/or if equivalent reforms are not developed), the City’s recent fiscal progress would be set back dramatically to the severe detriment of the public interest and welfare, and the health and sustainability of the FPERS retirement system would also be eroded.
 - Any negotiated wage increases above assumed COLAs and level/longevity increases would further have a significant impact on the cost of services, if not funded by offsetting contract savings. Each 1% increase in wages would result in additional General Fund costs of approximately \$6-\$7 million.
 - Health care inflation may surpass projected levels of cost growth, as the Ten-Year Financial Plan forecasts assume some moderation from recent rates of increase.
 - Actual pension investment returns, overall plan experience, and the impact of new and anticipated accounting changes could require contributions higher than those assumed in the baseline forecast.
- ### ■ Other expenditures
- New service demands and costs could be generated by infrastructure failure and/or other unforeseen factors.
 - The City may have some potential exposure to the performance of existing economic development projects.

- Unfavorable litigation against the City could result in legal costs and/or settlements/penalties higher than those assumed in the forecast.

Alternative Economic Scenarios

While the “baseline” scenario seeks to present a reasonable forecast of future conditions aligned with current mainstream economic expectations, actual results will be different as “real world” events unfold. Actual results will almost certainly vary from the baseline forecast, based on an evolving economy, intergovernmental policies, and other factors.

To develop a working range of possible outcomes in support of planning, the following analysis presents two additional

scenarios under alternative economic conditions: “Pessimistic” and “Optimistic.”

- The “Pessimistic” scenario generally assumes economic conditions will worsen in the near-term, and recovery will be delayed. It is important to note, however, that the “Pessimistic” scenario is not intended to reflect the worst possible economic conditions. While it assumes a delayed recovery and a relatively shallow near-term recession, it does not assume another decline as sharp and protracted as the most recent downturn, nor any further recessionary periods in the latter years of the Plan period.
- Similarly, the “Optimistic” scenario does not assume the best possible set of economic conditions, and does not reflect any additional corrective action beyond the baseline scenario.

Pessimistic	Baseline	Optimistic
<p><i>The pessimistic scenario would assume another near-term recession, with GDP contraction and delayed recovery:</i></p> <ul style="list-style-type: none"> • Lower inflation relative to the baseline scenario • Economic contraction in the near-term and delayed recovery, with national GDP negative in FY2014, bouncing back in FY2015-2016, and stabilizing at 2.5% by FY2019 • Interest rates lower than baseline assumptions • Slower recovery in the housing market with low sales activity • Continued City population decline • Flattening, then declining BCPS enrollment • Higher levels of health care cost inflation • Pension funds failing to meet actuarial assumptions as investments underperform, yielding higher required contributions (1% below actuarial assumptions) 	<p><i>The primary baseline projections assumes a steady, but modestly paced recovery, including:</i></p> <ul style="list-style-type: none"> • Employment levels gradually improving • City population stabilizing, with modest expansion of development/redevelopment • City housing market growing slowly in initial years, returning to moderate growth in out-years, supported by continued low-interest rate environment • Moderate growth in Baltimore’s income tax and economically sensitive revenues, commensurate with assumed population stabilization, job gains, and some wage gains under an improving overall economy • Ongoing, incremental gains in Baltimore City Public Schools (BCPS) student enrollment, consistent with recent trends • Pension costs meeting current actuarial assumptions • Moderate health care inflation relative to recent, prior years – in FY2013 with a slight downward trend 	<p><i>The optimistic scenario assumes more rapid recovery relative to the baseline:</i></p> <ul style="list-style-type: none"> • General inflation increasing higher than the baseline scenario as the economy improves • Strong recovery, with national GDP at 4.0% in the near-term, stabilizing at 2.7% in FY2020 • Interest rates also increasing with economic growth • Accelerated recovery in the housing market, with increased sales activity • City population beginning to climb • BCPS enrollment increases somewhat greater than projected • Moderate abatement of health care cost inflation • Pension funds exceeding actuarial assumptions, reducing funding pressure

Rather, it is based on the assumption of a somewhat stronger and more accelerated near-term recovery, with more favorable long-term economic assumptions, but not a “boom” economy. Under each of these alternative scenarios — baseline, pessimistic, and optimistic — the City still faces projected budget shortfalls if no corrective action is taken. Reflecting the sensitivity of Baltimore’s budget to such economic conditions over time, the gap among the three alternatives widens in each year of the forecast as the scenarios are assumed to compound. As shown in the chart and table below, by FY2022, the pessimistic scenario results in an annual deficit that is approximately \$147 million larger than the baseline scenario and \$250 million greater than the optimistic scenario. On a cumulative basis, the optimistic scenario results in a shortfall of more than \$325 million over the next nine years – and under the pessimistic scenario, deficits would grow even deeper year-by-year, resulting in a cumulative shortfall of nearly \$1.3 billion.

In considering the potential impact of such alternative scenarios on the long-range financial planning process, it may be noted that a Ten-Year Financial Plan calibrated to resolve the baseline scenario would yield different outcomes under different scenarios. To the extent that fiscal and economic challenges over time are more consistent with the “Pessimistic” scenario (or worse), the City will likely face additional shortfalls – but will nonetheless be in a better position to weather weak economic

conditions than if plans had not been developed and pursued to close the base case fiscal gap. Similarly, if the future economy is more consistent with the “Optimistic” scenario and the City plans for the baseline forecast, some additional resources may then become available to invest in ways aligned with the long-range plan strategies for reducing unfunded liabilities, lowering tax rates, strengthening the balance sheet, and/or growing the City.

Liabilities Beyond the Primary Baseline

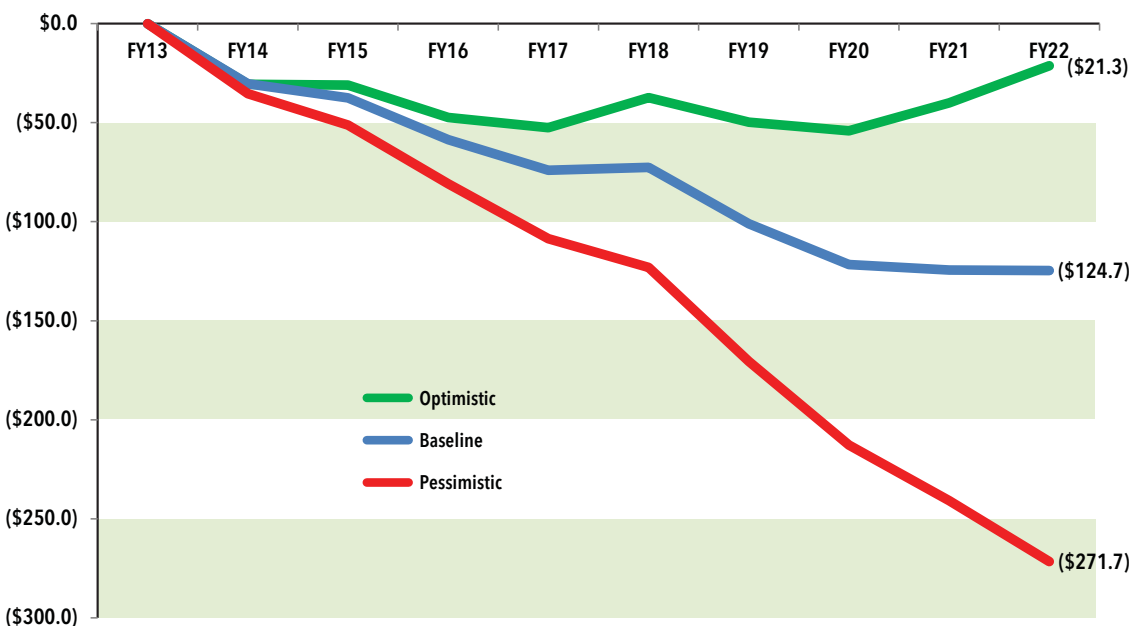
As previously outlined, the primary baseline scenario used for this Ten-Year Financial Plan process is generally reflective of a “carry forward” approach to current services and programs. To the extent that some current activities are underfunded, however, this approach will actually understate the City’s “true” budget needs.

Among such concerns, appropriate funding for long-term retiree medical obligations (Other Post-Employment Benefits – “OPEB”) and for capital investment to renew and replace basic infrastructure have both been identified as areas of concern:

- Like many governments nationally, the City of Baltimore has historically funded its post-employment healthcare obligations to retirees primarily on a “pay as you go” basis – covering only the costs of benefits for those who have already retired and are receiving post-employment benefits. In recent years, the Governmental Accounting Standards Board (GASB) has

required that the cost of such benefits be accounted for on an actuarial basis – reflecting how much should be set aside to prepare for long-range funding sustainability, much as public employers have long done for pension obligations. While GASB has not required that governments fully fund up to these actuarially

Economic Scenarios - Projected Deficits



determined levels, continued “pay as you go” funding generally falls short of these actuarially determined costs – creating a growing liability to be addressed in future years.

To help address this liability, the City has created an OPEB Trust, and has made some contributions above “pay as you go levels” – a positive financial management practice assumed to continue in the Ten-Year Plan baseline. In the FY2013 Budget, this supplemental payment totals \$8.5 million in the General Fund (\$9.5 million All Funds). According to the City’s most recent FY2011 OPEB valuation, however, to fully fund the cost of future retiree medical liabilities at actuarially determined levels, the City would need to contribute an additional \$31.6 million above PAYGO funding on an All Funds basis.

- Of even greater fiscal significance, “carry forward” capital investment in renewal and replacement of basic City infrastructure – roads, bridges, and facilities – now falls far short of the levels required just to maintain the current state of repair. Simply to maintain current, suboptimal asset conditions and begin to make, slow incremental progress towards bringing conditions to adequate levels, however, City departments estimate that capital funding would need to be increased by \$115 million in FY2014, rising to more than \$130 million annually by FY2016. On cumulative basis, the estimated shortfall in local capital funding relative to “reasonable” levels exceeds \$1.1 billion through FY2022.

This underfunding represents a major, long-range challenge for the City, further detailed in the “Infrastructure Investment” section of this volume.

In the projected baseline shortfall of \$745 million from FY2014-FY2022, again, neither of these long-range concerns is fully addressed, consistent with current funding approaches in Baltimore (and many other cities) that fall short. If the estimated annual funding requirements for these liabilities were added to the Ten-Year Financial Plan baseline projections, the City’s cumulative shortfall would increase by more than \$1.2 billion through FY2022. Combined with the cumulative deficit in the primary baseline forecast, this would result in a total ten-year shortfall of over \$2.0 billion.

Under each of these alternative scenarios — baseline, pessimistic, and even optimistic – the City still faces projected budget shortfalls if no corrective action is taken. As shown in the chart below, even the optimistic scenario results in deficits in every year — with a cumulative shortfall of more than \$325 million over the next nine years. Under the pessimistic scenario, deficits would grow even deeper year-by-year, resulting in a cumulative shortfall of nearly \$1.3 billion.



Key Challenges:
Structural Budget Balance

Findings and Options

- Achieving structural budget stability requires realigning recurring revenues and expenditures into sustainable balance. As outlined in the preceding Ten-Year Budget Projections section of this Plan, this is a difficult challenge for any government, due to current revenue structures that struggle to keep pace with overall economic growth, and a mix of expenditures in most public sector organizations that tends to be heavily weighted toward benefit costs growing at a much faster rate.
- For the City of Baltimore, these general challenges are made even more difficult by the imperative to address Tax Competitiveness, as outlined in the subsequent section of this Plan. If the City is to grow its economy and tax base, Baltimore must develop a more competitive revenue approach, and has almost no flexibility to simply increase existing tax rates.
- Given these factors, to close the City's projected, recurring budget shortfalls, a key focus for this Plan is to identify viable strategies for bending cost curves downward. While a series of recent actions have already closed nearly \$300 million in projected gaps over just the past three years, primarily through spending reductions, further initiatives are needed to maintain and improve Baltimore's fiscal position.
- The first set of strategies for reducing the City's cost structure involves a range of **Innovative Government** initiatives. Already, Baltimore is at the forefront of performance management with the nationally recognized CitiStat program, and has established an Innovation Fund and Budgeting for Outcomes approach that have led to smart investments and retooled service delivery.
- Looking ahead for the next few years, the City has further launched a new wave of innovative government initiatives — from fleet management efficiencies to energy efficiency investments — that can continue to reduce overall expenditures without reducing service levels. Building on these efforts, this Plan identifies additional opportunities going forward to capture the potential of emerging developments in technology and management practices.
- At the same time, the labor-intensive character of municipal government requires that workforce costs be thoughtfully managed. Employee wages and benefits are the single largest component of total City spending — representing more than 60% of total General Fund spending in the FY2013 Budget.
- With improved technology and equipment, business practices, and productivity, the City should focus over the decade ahead on gradually reducing the total number of municipal employees. Importantly, this recommended goal is not intended to be critical of Baltimore's current workers. An effective City government requires people to respond to emergencies, maintain clean and safe streets, and deliver other core municipal services. Baltimore relies on a quality public workforce. Nonetheless, when the cost structure for existing workforce levels becomes unsustainable within available resources — and when technologies and business processes emerge that can improve efficiency — change becomes necessary.
- Within the context of a long-term financial plan, strategies can be adopted to work toward a smaller, more efficient and productive, and better compensated workforce through attrition — using approaches such as business process redesign and managed competition. In contrast, if a budget is allowed to reach a crisis point before change begins, headcount reduction can be devastating for public employees facing layoffs, destructive for the delivery of basic services, and corrosive for an organization that may lose an entire generation of recent hires.
- In addition to managing headcount, Baltimore's approach to compensation for its workforce is also a critical factor in determining overall budget costs and pressures — and is central to the successful recruitment, retention, development, and motivation of City employees.
- Recent benchmarking indicates that current City of Baltimore salaries range from low to moderate in comparison to equivalent private sector positions, and rank at or near the bottom among larger public employers across the region. In evaluating such differences in pay, it is important to note that many of these other large public employers are located in the higher-wage Washington, DC labor market, and all have stronger tax bases rooted in more affluent communities. Further, for many positions, the City's competition for a quality workforce takes place primarily within the overall, localized

labor market — inclusive of private employers — and not against more distant suburban governments.

- Nonetheless, from a recruitment and retention perspective for most people in the workforce, wages and salaries are the most important and visible component of a total compensation package — and, again, the City typically pays toward the lower end of the regional mainstream for many positions.
 - Recent benchmarking also indicates, however, that City employee healthcare, retirement, and paid leave benefits are generous relative to private sector norms — and multiple elements of Baltimore’s benefits package also exceed typical public sector levels in the region. Further, because healthcare inflation and pension funding requirements have significantly outpaced City revenues — and are projected to continue to do so without corrective action — addressing benefit cost growth is imperative for financial sustainability.
 - Given these current dynamics, over the course of the decade ahead, PFM recommends that the City work to **“rebalance its total compensation portfolio”** by focusing personnel cost containment efforts primarily on non-cash benefits and paid leave, while prioritizing the investment of available compensation dollars into improved wages and salaries. Over time, this rebalancing approach will best maintain the City’s competitiveness for talent, generate increased capacity to improve pay competitiveness, continue to provide for a quality package of non-cash benefits, and improve the affordability and sustainability of Baltimore’s total compensation package.
 - By strategically addressing both the average costs per employee and the total number of municipal workers, Baltimore can build a more affordable, sustainable, and competitive workforce over the decade ahead.
- The City imposed unpaid furloughs in FY2010-2012, froze and contained wages, restructured its health benefits program for both active employees and retirees, and adopted significant reforms of its Fire and Police Employees’ Retirement System (FPERS).
 - Capital program investments were severely curtailed, with reduced debt financing and lower “pay-as-you-go” (PAYGO) funding, resulting in widespread deferrals of needed renewal and replacement.
 - The Baltimore Fire Department implemented rotating company closures from FY2010 to FY2012, permanently closed a company in FY2010, and made two of its rotating closures permanent in FY2013.
 - The City shifted to once-weekly trash and recycling pick-up, several recreation centers were closed, and the City reduced tree maintenance, street lighting, building upkeep, prisoner re-entry and mentoring programs, Arts and Culture funding, library hours and book purchases, and multiple other services.
 - The City increased its income tax rate from 3.05 to 3.20 percent (the maximum allowed under State law), established a new beverage container tax, reached a new voluntary contribution agreement with the City’s largest nonprofit institutions, and raised parking, hotel, and energy tax rates.

Overall, Baltimore eliminated nearly \$300 million in projected shortfalls over the past three years, primarily through spending reductions and restructuring. While such adjustments in the aftermath of the Great Recession have not been unique to Baltimore, this recent history now means that the remaining options for the City’s fiscal realignment will be that much more limited and difficult going forward.

Recent Budget Context

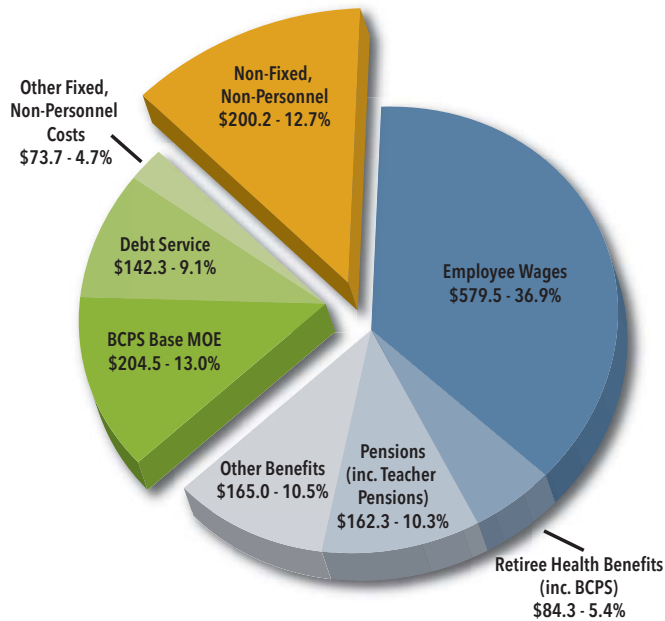
Compounding Baltimore’s prospective fiscal challenges, the City’s projected future shortfalls follow several years of severe budget strain in the wake of the recession, such that many difficult choices have already been made:

- A sustained hiring freeze was initiated in FY2008 and continued through FY2012, and layoffs were imposed in FY2010 and FY2011, resulting in sharp overall headcount reductions.

Innovative Government

More than 60% of the City’s costs are associated with employee wages and benefits, and much of the balance involves commitments to core responsibilities that are difficult to reduce — such as Baltimore’s state-mandated Maintenance of Effort (MOE) payment to the Baltimore City Public Schools (BCPS) and debt service for the City’s past investment in capital infrastructure. Of the City’s FY2013 Budget, only 12.7% was neither employee-related nor substantially “fixed” in structure.

Majority of City Costs are Personnel and/or Fixed FY2013 Budget (\$ millions)



Note: "Other Fixed" includes utility costs, tipping fees, and state-mandated contributions to Baltimore City Community College.

Because so many of the City's non-workforce expenditures cannot be avoided, it is difficult to make a major impact on Baltimore's cost curves without addressing spending on personnel. At the same time, however, several key areas associated primarily with non-workforce costs also present meaningful opportunities for savings and increased efficiency.

Management and Efficiency Initiatives

The City of Baltimore is a nationally recognized leader in municipal government performance management with a focus on results and innovation through its CitiStat program, Outcome Budgeting process, and Innovation Fund.

For more than a decade, CitiStat has evaluated the operational performance and efficiency of major departments for the delivery of citizen services. Staff analysts examine data and perform investigations in order to identify areas in need of improvement, and large agencies regularly present to the Mayor and her senior advisors at a bi-monthly CitiStat session.

Since FY2011, the City has also deployed an Outcome Budgeting process to better align resource allocation with priority results.

Instead of just starting from the prior year's budget and adjusting allocations up or down, the Outcome Budgeting approach begins from identified priorities — informed, in part, by a comprehensive citizen survey. Next, interdisciplinary Results Teams made up of representatives from City agencies, community organizations, and citizens evaluate budget proposals from agencies to focus resources on the achievement of priority goals.

Building on the Outcome Budgeting process, the City established an Innovation Fund in Fiscal 2012 to provide seed money for one-time investments that will lead to improved results, increased revenue, and/or reduced ongoing operating costs. So that the Innovation Fund will be self-sustaining, savings achieved from successful projects are reinvested on a revolving loan basis. Each year, funds are awarded through a competitive process among City agencies, and initial awards have helped to advance automated business processes and the installation of new fiber optic technology as part of an inter-county broadband network.

Within this established framework, the following set of opportunities highlights the next wave of initiatives already under development by the Rawlings-Blake Administration as identified through this Ten-Year planning process, but not yet reflected in the baseline forecast. In some cases, these ideas have not yet been fully developed, and others may be modified or replaced as they begin to move forward. In the aggregate, however, these potential initiatives reflect the City's ongoing drive for greater efficiency and cost-effectiveness.

■ **Fleet modernization.** The City currently maintains a fleet of approximately 4,265 vehicles — ranging from police cars, to public works trucks, to fire engines. Inclusive of repair parts and service, fuel costs, and vehicle replacement, total City fleet expenditures are approximately \$58 million per year.

In 2011, the City launched a comprehensive study to assess opportunities for both modernizing and reducing the cost of its fleet. Based on this analysis, the City determined that the average age of Baltimore's municipal vehicles is approximately eight years, with an average replacement cycle of 16 years — double the recommended cycle length. Such an aging fleet requires much higher maintenance and repair costs, and is also associated with higher fuel costs due to older, less fuel-efficient and "green" vehicles. In addition, an aging fleet will

have substantially higher down-time, which can affect service delivery and require a large reserve fleet for core operations. In order to break away from this counterproductive condition, the City has developed the following planned approach:

- Adopt a lease financing strategy. Currently, Baltimore funds vehicle purchases through an Internal Service Fund. Rental charges to City agencies are used for maintenance, repair, and new vehicle purchases. Purchases are acquired on a pay-as-you-go basis, using dollars from these charges to agencies that have accumulated in a mobile equipment reserve. With lease financing, the City would be able to significantly accelerate vehicle replacement, modernize the fleet to include more fuel-efficient and reliable vehicles, and place the City on a more sound replacement schedule going forward.
- “Right-size” and reduce the City fleet. At the same time, the City has also been evaluating vehicle usage and reserve needs to determine the optimal size of the fleet. Based on this review, as well as the planned fleet modernization, the City anticipates a reduction of at least 5% of the fleet.

Without a change in the City’s approach, the estimated average vehicle age would continue to rise to 9.2 years over the next ten years. Under the proposed fleet modernization, the average vehicle age could be reduced to 4.2 years. As a result, the City’s fleet evaluation team estimates that the combination of reduced fuel, maintenance, and repair costs and the up-front vehicle acquisition savings generated by using lease-purchase financing will generate net savings.

Much of the estimated savings will be derived from reduced costs for fuel, parts, staff overtime, and contracted maintenance. In addition, some long-term reduction may occur in the City’s workforce for vehicle maintenance, however, it is projected that the phased approach of the program would enable this to take place through natural attrition.

In addition, this shift in Baltimore’s approach to fleet financing will also allow for release of the City’s reserves for vehicle acquisition, totaling \$43.5 million as of July 2012. Because this is a non-recurring release of resources, it would not be an appropriate funding source for ongoing City expenses, however, it could provide a meaningful one-time boost for needed capital investments in areas such as transportation infrastructure, blight elimination, and/or aging facilities.

- **Police technology.** The Baltimore Police Department is now exploring the opportunity to improve patrol efficiency by investing in field-based reporting technology. Currently, officers must hand-write crime reports and carry the physical documents to data-entry operators. These operators then manually enter the reports into the system. In contrast, field-based reporting technology would allow patrol officers to create and enter reports electronically right from their patrol cars. This would save paper, reduce the opportunity for data entry errors, save officer time, reduce the need for data entry operators, and lower vehicle fuel and maintenance cost pressures by eliminating the need for four trips daily now required to deliver hand-written reports. Along with improved report accuracy and patrol availability, the Department estimates potential savings of nearly \$500,000 per year. To finance the upfront cost of implementation, the Department is pursuing a combination of grant and asset forfeiture funds.
- **On-street parking technology.** EZ Park and multi-space “smart meters” communicate electronically with a central system, and are just one example of the application of technology to parking management and enforcement. The use of these smart meters reduces operating costs by allowing for more efficient collection, and can allow for payment with credit card, rather than just coins. Currently the City has 745 smart meters and between 5,000 and 6,000 original single space meters. With positive experience to date, the Baltimore City Parking Authority is moving forward to replace a growing number of single space meters with smart meters. Along with new technology, the Parking Authority is also pursuing a broad range of other opportunities for net revenue gain — from improved administration of parking programs for the disabled so that all parkers pay on an equitable basis, to enhanced surface lot management.
- **Facility cost accountability.** In recent years, the City’s Department of General Services (DGS) has advanced a set of initiatives to reduce the costs associated with City facilities — including energy conservation programs and space consolidation. Going forward, DGS is now phasing-in the implementation of an Internal Service Fund for facilities, intended to promote greater agency accountability. In addition to energy costs, rental rates will include: utilities; custodial services; maintenance and repair (e.g., extinguisher inspection, elevator maintenance, pest control, and building systems);

security; and debt service associated with energy conservation investments. Given limited capital dollars available for City facilities, as further detailed in the Infrastructure Investment section of this Plan, generating such savings will provide a critical resource for reinvestment into much-needed maintenance and capital improvements.

- **Telephone cost savings.** The City's FY2013 budgeted General Fund payments to the Municipal Telephone Exchange total \$8.1 million. To reduce this cost, the City Comptroller's Department of Communications and the Mayor's Office of Information Technology have explored options for new technology to lower the cost per line. In addition, telephone usage and billing audits may further eliminate the total number of lines and ensure appropriate billing.
- **Board of Election cost reduction.** In 2012, the State of Maryland authorized a change in the City's election cycle to align with the presidential cycle beginning in 2016. This shift is expected to improve voter turnout, and also to save the several million dollar cost of holding a separate City election every four years. To further capture efficiencies while still promoting high voter access, the City's Bureau of the Budget and Management Research has developed a proposal to co-locate selected precincts, consolidate entry lines, and reduce the number of Election Day poll workers. *[Note: it is anticipated that the State will require the City to contribute toward the cost of planned, new Optical Scan voting systems, beginning in FY2015, an added cost already assumed in the Plan baseline that will offset against potential savings].*
- **Semi-Automated Trash Collection.** Under this approach, consistent with best practices nationally, City trash trucks for appropriate routes would be retrofitted with collection arms to help lift containers provided by the City, and equipped with radio-frequency identification (RFID) chips. This technology is safer for employees, typically resulting in fewer injuries and reduced workers' compensation costs. In addition, the improved efficiency of operations can translate to smaller crew sizes and/or route redesign to reduce overtime pressures and long-term staffing needs (by attrition). With standardized, rugged trash containers, such programs can also help to improve neighborhood cleanliness, and better control rodent problems. While upfront investment for retrofits and containers can be significant, the long-term returns are generally far greater. To help launch this program, the City could consider

the use of funding from the Mobile Equipment Reserve and/or an enterprise funding approach (see the Tax Competitiveness section of this Plan for more details regarding a solid waste enterprise).

- **Market-based credit system for storm water management.** Currently, the City Department for Public Works (DPW) covers lot maintenance costs for vacant sites retained under public ownership following demolition. Under a National Fish and Wildlife Foundation grant, the City is now exploring development of a program to establish a "credit" mechanism for developers to meet their storm water management obligations at sites without sufficient, cost-effective on-site options by paying into a fund for the ongoing maintenance of cleared lots used for storm water management. In addition to offsetting operating budget costs associated with blight elimination, such a program would improve the viability and cost-effectiveness of development within the City more generally.
- **Alternative uses for non-core facilities.** In 2012, the City Planning Department launched an analysis of alternative uses, potentially encompassing sale or lease, for multiple historic City-owned facilities, such as the War Memorial and Shot Tower. While not anticipated to generate significant fiscal impact, this represents a positive approach to identify self-sustaining funding approaches for important civic assets not associated with core City functions.
- **Reevaluation of service delivery models.** For example, the City currently operates 13 "walk-to" neighborhood pools, six wading pools, and three "splash pad" facilities, and is evaluating the possibility of converting selected neighborhood pools to splash pads. While there is an initial upfront cost of pool conversion, splash pads have proven popular among residents, and require comparatively lower operating and long-term capital costs. No staff is required except for periodic maintenance/testing, and safety risks are considerably reduced.

Looking longer-term, the following are additional strategic approaches that can be pursued to reduce expenditure growth trends in the out-years of the Plan:

- **Strategic sourcing and purchasing reforms.** In the FY2013 Budget, the City is slated to spend \$42.3 million within the General Fund on materials, supplies, and equipment alone,

with tens of millions more expended on other contracts and services. The City Finance Department has identified purchasing strategies as an area of prospective opportunity for improvement, with the potential for significant savings. At the federal level, for example, the U.S. General Services Administration reports savings of over 13% in office supplies for FY2012 among federal agencies pursuing “strategic sourcing” — a comprehensive approach to evaluating supply options and developing optimized contract terms. Major state and local governments that have adopted strategic sourcing also report comparable results. The State of Iowa, for example, lowered the cost of procuring office supplies by 15% and the cost of office equipment by 20%. Related opportunities include enhanced change order controls after contracts are initiated.

■ **Enhanced technology.** The City of Baltimore’s information systems are still heavily reliant on outdated mainframe technology, and many business processes across the government remain manual and paper-intensive. General strategies include migration to cloud-based solutions, and increased standardization and centralization of information technology applications and approaches. Specific project opportunities already identified include improved computer aided dispatch (CAD) to comply with smart 911 systems, enhanced permitting and billing systems, tax system upgrades, and criminal justice and civil summons applications. To help move such initiatives forward, Baltimore’s Innovation Fund is a positive tool, however, supplemental, one-time funding could help to accelerate the return on investment.

■ **Expanded community partnerships.** In recent years, the City has forged multiple, creative community partnerships to help ensure high quality, locally grounded services, for example:

- In 2010, the City created a Recreation Center Task Force of community leaders that developed a plan for both increased public investment in a core set of facilities, and a call for community partners to take over operation of some of Baltimore’s most vulnerable centers. To date, such community partnerships have been established for multiple recreation centers — including the Brooklyn O’Malley Recreation Center in South Baltimore, to be operated with improved services by the Boys & Girls Clubs of

Metropolitan Baltimore, and the Easterwood Center in West Baltimore, transitioned to the Omega Baltimore Foundation, Inc. after more than three years without programs.

- In May 2012, the City teamed with the Bryn Mawr School and Gilman School under a formal Memorandum of Understanding to have these independent educational institutions contribute toward the cost of major streetscape improvements and continued landscape maintenance along areas of Northern Parkway and Roland Avenue.
- Earlier in 2012, the City also entered into an agreement with the Mount Vernon Place Conservancy to restore the City-owned Washington Monument and surrounding park squares. The Conservancy is a nonprofit organization with the mission of improving this public space, and the partnership is helping to leverage a \$1 million City capital investment by raising an additional \$11 million in private and non-City capital funds. Additional private funds are also being raised to provide special activities and enhance day-to-day park maintenance.

Where neighborhood institutions and organizations have the resources and commitment to share in the upkeep and delivery of quality of life public services, the City should continue to embrace and encourage such partnerships.

■ **Managed competition,** promoting competition between the public sector and private firms to deliver municipal services, can be another effective strategy and for reducing costs and improving service delivery. For example, the City of Phoenix, AZ successfully implemented managed competition for solid waste collection by allowing both private companies and City departments to bid on sections of the City. After the Phoenix Public Works Department at first lost several bids, the public sector agency adopted new technology and approaches learned from the private firms selected, and eventually won back the contracts. In another example of managed competition, the City of Indianapolis achieved savings both from contracting out some services such as wastewater treatment, and by reforming some services retained under municipal operation after a competitive process, such as fleet management and street repair. Through similar competition, Baltimore might also encourage new efficiencies and strategies to reduce costs — as the City has already achieved with

selected initiatives such as contracted mowing of street medians and the use of shared savings contracts for implementing energy efficient facility improvements. Looking forward for additional opportunities, managed competition tends to work most effectively with service areas where there are competitive, existing private marketplaces — for example, security services, facilities and grounds maintenance, golf course management, fleet maintenance and repair, and print shop operation.

- **Ongoing program review**, to reduce investment in non-core and low priority functions. Already, the City's Budgeting for Outcomes approach has identified multiple, well-intentioned programs in areas such as neighborhood development, mentoring, and arts promotion that did not achieve the level of impact desired. By eliminating or cutting back on spending in these areas, the City has been able to reallocate resources toward services with stronger evidence of results. Going forward, the City Bureau of the Budget and Management Research is also pursuing the application of "lean" principles of efficient business processes to municipal service delivery, and has started a new project to conduct detailed management research reports for selected functions.

Workforce Size

The Ten-Year Plan baseline assumes that headcount will remain constant for the decade ahead, consistent with a "carry-forward" set of status quo budget assumptions. To the extent, however, that the City can identify productivity gains and policy initiatives to reduce its workforce size, significant savings can be generated to help sustain priority, core services.

For FY2013, the City has 10,559 budgeted full-time positions in its General Fund and related Internal Service Funds. If the City were able to reduce this total headcount by 10% over ten years, the impact would be dramatic. Based on average civilian new hire wages and benefits as of FY2013 (assuming most savings would come from not making new hires as on-board personnel separate from service), the gross impact would reach nearly \$50 million.

Of course, some offsetting investment in equipment, technology, compensation, and/or contracts may be required to achieve staffing change without eroding services — such that the net savings potential would not be as great. Nonetheless, as wage and benefit costs continue to escalate, and as the new hires

avoided through increased efficiency would have gained step and longevity increments, the gross impact against which net savings could be achieved would only continue to grow.

Further, while recent hiring freezes have indeed strained capacity in some areas of Baltimore's municipal operations, multiple options have been identified that can maintain — and, in some cases, even improve — service levels with a lower personnel complement. Such targeted approaches may include:

- **Schedule and work rule changes**, such as a new Fire Suppression shift structure, further outlined below.
- **Managed competition**, as outlined previously, to seek the most efficient service delivery approach by benchmarking in-house operations against contractor options where strong competitive markets exist (e.g., printing, facilities maintenance).
- **Technology improvements** — such as the Police Department field-based reporting also described previously, that can reduce the need for paper-intensive, manual activity.
- **Business process change**, for example, applying the lean principles used to streamline contemporary manufacturing to municipal work flows (i.e., identify and eliminate non-value-added tasks in delivering services, cut cycle times from receiving a work request to completing the job, eliminate conflicts between multiple departments or divisions that need to work effectively together, and align daily work assignments with the organization's short- and long-term goals).
- **Expanded partnerships** to leverage intergovernmental and community resources for service delivery.
- **Staffing and span-of-control analysis** to identify opportunities for business process redesign to create more efficient and streamlined management and operational structures.

In support of such a strategy, a general approach might feature:

- Development of multi-year and annual targets for a smaller, more productive City government.
- Strengthened position control.
- Enhanced review and pre-approval for filling vacancies.

In addition to the potential effect on service levels, the impact of workforce reduction on dedicated, career employees can also be

of concern. In a budget crisis, employers must often resort to layoffs and/or retirement incentives that can be disruptive operationally, and — in the case of layoffs — create hardships for individual workers and their families. With a long-range, multi-year approach, however, workforce reduction can be achieved primarily by attrition — providing greater stability for operations and employees alike, and potentially creating opportunities to reinvest a share of the savings generated in better compensation levels than the City might otherwise be able to sustain.

Again, many of the strategies noted above would bring new costs that would offset gross headcount savings — for example, to invest in new technology, or to share savings in the form of improved compensation. Even if half of the gross savings potential requires such investments to be achieved, however, a sharpened focus on streamlining City government would generate tremendous returns for Baltimore’s next decade.

Fire Suppression Schedule

Along with technology and program-related ideas for achieving a smaller, more productive City workforce, other opportunities may be developed through the collective bargaining process — by engaging employees and their representatives in developing better approaches for work redesign.

As an example of such possibilities, the City might explore the negotiation of a new shift structure for Fire Suppression, which could achieve a dramatic reduction in firefighter staffing requirements while fully maintaining current service levels. In Baltimore, City firefighters now work a four platoon system with two 10-hour day tours and two 14-hour night tours averaging 42 hours per week per firefighter. Both nationally and regionally, however, many departments use a schedule based on 24-hour tours that results in much longer average work weeks — and, therefore, much lower staffing requirements.

Under the Fair Labor Standards Act, reflecting the special characteristics of the job, firefighters can generally be scheduled for up to 212 hours in a 28 day period (essentially, a 53 hour week) without incurring overtime. Accordingly, many departments will use schedules based around 24 hours on duty, followed by 48 hours off duty — resulting in a 56 hour average week. In some cases, departments just pay the several hours of scheduled overtime that results from such a schedule; in other cases, departments design a schedule with extra days off (“Kelly Days”) that bring the average work week down to a level without automatic overtime rates.

- Among the 25 largest U.S. cities, 19 of the other 24 departments have work weeks exceeding Baltimore’s current 42 hour shift system, and the median firefighter work week is 52 hours.
- Within the region, both Howard and Montgomery Counties use a 24/48 shift schedule (less Kelly days) for an average weekly work schedule of 48 hours. Several jurisdictions in Northern Virginia, including Fairfax County, Arlington County, and Alexandria City, have a 56 hour work week for firefighters.

25 Largest U.S. Cities

Firefighter Schedule (Hours Per Week)	
New York City	40
Los Angeles	56
Chicago	45
Houston	47
Philadelphia	42
Phoenix	56
San Antonio	56
San Diego	56
Dallas	54
San Jose	56
Jacksonville	56
Indianapolis	48
San Francisco	48
Austin	53
Columbus	48
Fort Worth	56
Charlotte	52
Detroit	48
Portland	52
El Paso	56
Memphis	56
Baltimore	42
Boston	42
Seattle	42
Washington	42
MEDIAN	52

Movement to the 3-shift model would require nearly 25% fewer fire suppression personnel, a net reduction of over 300 positions, to staff the same number of companies. In turn, significant savings would be generated — with projected impacts varying based on such factors as the specific shift structure adopted (e.g., use of Kelly Days), the level of savings shared with employees, and the timing of retirements and other separations to enable transition by attrition.

For individual firefighters, this approach would, of course, have an impact on employee lifestyles. Nationally, however, many departments report that the 24 hour schedule is popular among employees once adopted, as it requires an average of only 121 appearances annually before paid leave (albeit for longer tours), relative to the City’s current 10-14 schedule that requires 183 appearances before paid leave. Further, if a portion of the savings generated were reinvested in improving Fire Department compensation, this could help to significantly improve Baltimore’s overall competitive pay position.

Compensation Costs and Competitiveness

In developing a long-range, strategic approach to workforce costs, short-term affordability and long-term sustainability are paramount concerns. At the same time, it is also important to maintain compensation that is competitive for the recruitment, retention, and motivation of a quality workforce, and sufficient to ensure the opportunity for career employees to provide for a dignified retirement.

Affordability and Sustainability

In simplest terms, the City's workforce costs are a function of the total number of municipal employees multiplied by the average cost per employee. In recent years, Baltimore has acted to address both of these major drivers of workforce costs:

- A sustained hiring freeze and the resulting effects of attrition have resulted in overall headcount reductions.
- The City has frozen wages, imposed furloughs, restructured some aspects of its health benefits program for both actives and retirees (with additional cost containment in the FY2013 Budget based on concepts developed through this Ten-Year Financial Plan process, as further detailed below), and has also

adopted significant reforms of its Fire and Police Employees' Retirement System (FPERS).

Nonetheless, over the five years from FY2007 to FY2012 (budgeted), total workforce costs increased 19.6% — even with a declining headcount — while revenues rose only 3.0%. Within these totals, the key cost drivers have been healthcare benefits for active employees (38.7%) and employer pension contributions (89.3%).

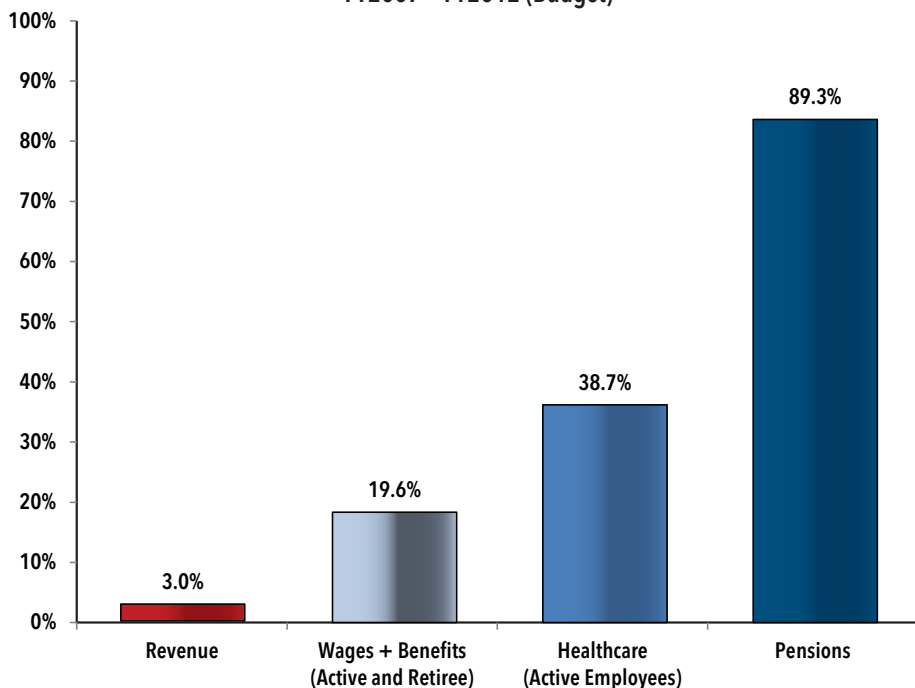
As a result of these trends, benefits grew to represent a larger share of total compensation expenditures, growing from 33.6% of total personnel costs in FY2007 to 40.7% in the FY2012 Budget — creating downward pressure on the City's capacity for wage and salary gains.

In turn, such benefit cost growth has driven overall personnel costs to consume a larger, overall share of the City's resources — rising from 53.9% of total expenditures in FY2007 to more than 60% in the FY2012 Budget.

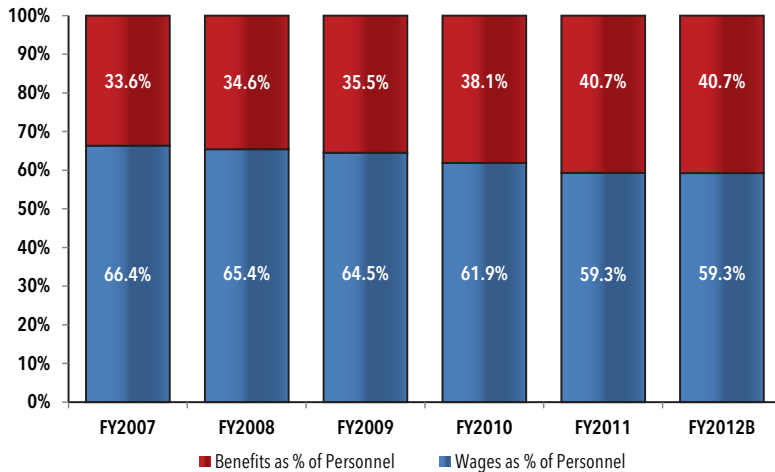
In the FY2013 Budget, continued headcount reduction, salary cost containment, and a set of health benefit reforms is projected to moderate these trends for the current fiscal year. Looking forward in the longer-range baseline forecasts, however, without corrective action (and assuming steady headcount):

- Active employee healthcare costs are projected to revert to grow at approximately 5% per year — roughly double the rate of general consumer price inflation, and even farther above forecast revenues.
- The City will continue to fall short of full actuarial funding for retiree medical benefits, resulting in a growing liability for such Other Post-Employment Benefits (OPEB) — adding to underfunding already in excess of \$2 billion as of the FY2011 valuation.

**Growth in Revenues vs. Workforce Expenditures
FY2007 – FY2012 (Budget)**



**Wages and Benefits - % of Total Personnel Expenditures
FY2007 to FY2012 (budget)**



- Ongoing pension funding challenges will be brought into sharper focus by forthcoming changes in pension accounting rules recently adopted by the Governmental Accounting Standards Board (GASB), as well as evolving credit rating agency criteria for evaluating such liabilities. In addition, City funding requirements may increase if the FPERs Board and City Council adopt adjustments to current actuarial methodologies recommended by the system’s actuary to ensure more sustainable funding — and the City’s Employees’ Retirement System (ERS) has already adopted lower, more conservative investment return assumptions (to 7.75% for actives and 6.55% for retired members, from a prior assumption of 8.0%).

If such cost pressures and growing liabilities are not strategically and decisively addressed, the resulting budget shortfalls will continue to erode the quality of City services and lead to further job and compensation cuts among the municipal workers who remain.

Competitiveness

From a total compensation perspective, the City of Baltimore currently offers health, paid leave, and retirement benefits that are substantially more generous than private sector norms — and often more generous than found among other large Maryland counties and other public employers. The City’s cash compensation, on the other hand, is relatively less generous.

This imbalance, in many respects, represents “the worst of both worlds” — as many workers will focus most closely on salaries and wages when choosing among job opportunities, while the City’s compensation dollars are flowing disproportionately to benefit programs that feature high cost growth rates that are increasingly difficult to sustain. At the same time, however, this dynamic presents an opportunity for the City to identify benefits savings for potential reinvestment in both pay improvements and greater benefit sustainability while still providing high quality and competitive health, paid, leave, and retirement benefits for career employees.

Health Benefits

Regional benchmarking has found the City’s health benefits program to be generous among regional public employers, and even more so in comparison to the overall labor market.

The City’s comparative employee contribution requirements toward healthcare premiums are summarized in the table below, and more detailed comparisons may be found in the Hay benchmarking report included in the Appendices.

For 2013, based on recommendations developed through the work of the Health Benefits project team for this Ten-Year Financial Plan, Baltimore has already negotiated and adopted plan design changes to achieve over \$20 million in annual savings, while retaining a highly competitive program:

- The 2013 program preserves the City’s existing premium cost-sharing structure for a competitive Preferred Provider Organization (PPO) “standard plan,” but realigns other out-of-pocket costs (deductibles and co-pays) more closely with current market practices to achieve cost savings. While this standard plan does require greater out-of-pocket costs from employees, it also provides protection against catastrophic claims with the use of annual out-of-pocket maximums.

Health Care Premium Cost-Sharing Percentages (2012)

City of Baltimore		Regional Public Sector Median*	Maryland Private Sector
HMO: Individual: 10% Family: 10%	PPN: Individual: 20% Family: 20%	Individual: 20% Family: 22%	Individual: 22.5% Family: 26.7%

*Based on the highest enrollment plan for civilians in Anne Arundel County, Baltimore County, Howard County, Montgomery County, Prince George’s County, and the State of Maryland.

- Under this new approach, employees may alternatively still choose to be covered under a “high plan” offering the prior, more generous structure of co-pays, deductibles, and co-insurance, but will be required to make higher premium contributions if they select this more costly option.
- In addition, the City has also established 20% employee contributions for prescription drug coverage premiums for 2013, which will not only share total pharmacy costs under a structure more consistent with most regional employers, but it will also encourage greater use of more affordable, generic drugs where appropriate.
- Overall, these reforms are estimated to achieve annualized General Fund savings of more than \$20 million for the health plan enrollment year 2013 (which bridges FY2013 and FY2014), and to provide a more sustainable cost structure going forward.

To analyze overall benefit competitiveness from this new base following the 2013 changes, Hay Group has developed a method for comparison based on the standardized cost of the benefits provided under each employer's healthcare program, including medical, pharmacy, dental and vision benefits. Actual costs for each employer will vary from these standardized costs, because individual employers may use different benefit funding approaches, have different bargaining power and vendor management approaches, and will also have different demographic mixes of employees with regard to relevant factors such as age and family size. In the table that follows, costs are estimated independent of such factors so as to illustrate the standardized value of the benefits offered.

Employer	Healthcare Benefit Value
Anne Arundel County	\$17,726
State of Maryland	\$16,514
Baltimore City (2012)	\$15,732
Howard County	\$15,622
Baltimore City (2013)	\$14,222
Prince George's County	\$14,103
Federal	\$13,876
Harford County	\$13,445
Montgomery County	\$13,390
Baltimore County	\$12,697

Based on Hay Group's analysis, the value of Baltimore's overall healthcare program, again following those changes already adopted for FY2013, remains fully competitive with the regional public sector — above the midpoint relative to the six largest Maryland counties (Anne Arundel, Baltimore County, Harford County, Howard County, Montgomery County, Prince George's County), and ahead of the plan available for federal employees.

Given high rates of underlying health care inflation, other regional public employers have also pursued cost containment approaches in recent years, and may continue to do so going forward. In FY2012, for example, Montgomery County, MD increased employee health care contributions from 20% to 25% of premium for their CareFirst POS Plan (Standard and High Option), and also increased employee contributions for the Standard Rx Drug Plan from 20% to 25% of total premium.

Retirement Benefits

Baltimore also provides municipal employees highly competitive retirement benefits relative to general labor market norms, including a traditional defined benefit pension (DB) and post-employment medical coverage. While such provisions are generally within the mainstream for regional public employers, the City's retiree benefit design features several characteristics that exceed the norms even among regional governments:

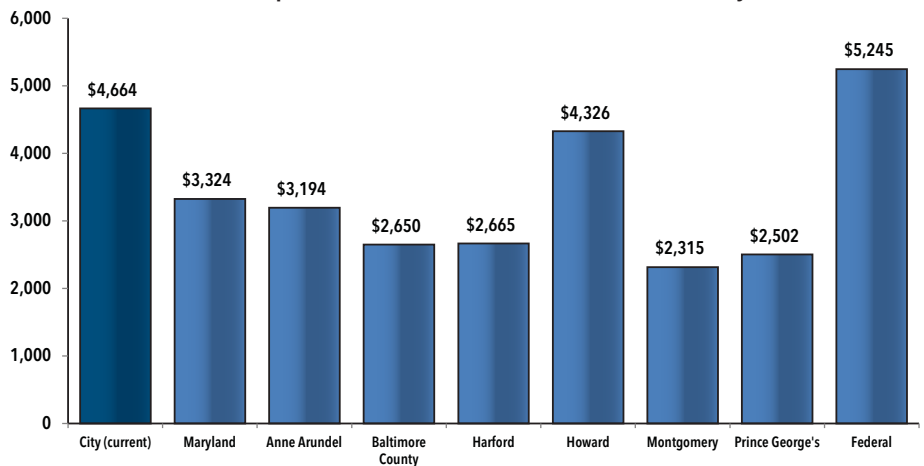
- The U.S. Bureau of Labor Statistics reports that, as of 2012, only 28% of U.S. private industry workers in medium and large establishments still participate in a defined benefit retirement plan, with a majority now participating in defined contribution (DC) retirement plans.
- While defined benefit plans remain prevalent in the public sector, as of August 2012, the National Conference of State Legislatures (NCSL) reports that 18 states now offer either a defined contribution, hybrid, and/or cash balance plan as a primary retirement benefit — and 9 of these states require (or have adopted legislation that will soon require) that newer hires enter into one of these non-DB programs.
- Regionally, most large public employers also continue to provide DB plans, however, both the District of Columbia and Montgomery County, MD have provided civilian employees with defined contribution retirement programs since the 1990s, with Montgomery County adding a cash balance option in recent years.

- Among the larger Maryland counties with traditional DB plans, Baltimore's Employees' Retirement System (ERS) for civilian workers is the only plan that does not require an employee contribution for comparable employees.
- Baltimore also provides City workers and their dependents with post-employment medical and prescription drug coverage, with a 50% premium cost share for retirees who had 15 or more years of City service and a 20% cost-share for prescription drugs.
- According to the 2012 Employer Health Benefits Annual Survey of the Kaiser Family Foundation and Health Research & Educational Trust, just 25% of large firms nationally that offer health benefits (private and public sectors combined) provide any form of post-retirement medical coverage.

More detailed Hay Group benchmarking findings regarding contribution requirements and plan designs may be found in the Appendices.

For the ERS plan, along with detailed benchmarking of major plan features, Hay Group also developed a comparison of retirement values assuming a \$40,000 salary. Similar to the healthcare benefit value analysis shown previously, these comparisons are standardized to incorporate the typical effects of benefit formulas, cost-of-living adjustments, early retirement

Comparison of Retirement Values at \$40,000 Salary



provisions, and employee contribution requirements. Actual costs to the employer and benefits received by individuals would vary. Based on Hay Group's analysis, the current ERS benefit structure was found to have the highest value among civilian plans of large, non-federal public employers in the region.

Facing growing retiree benefit affordability and sustainability challenges, public employers across the nation have taken action to control the growth in pension benefit costs. At the state level, for example, according to the National Conference of State Legislatures (NCSL), 45 states enacted significant pension reforms to help address both the short and long-term funding crisis from 2009-2012 alone — and similar actions have been taken at the local level. Examples of changes regionally include the following (examples cited reference benefit levels in non-public safety plans, but changes have been adopted across all types of employee groups):

- In 2011 the State of Maryland adopted comprehensive pension reform, including increased employee contributions (from 5% to 7%) and a lower COLA cap for current members of the Employees' Pension System. For future hires, a new tier also features a reduced benefit multiplier (from 1.8% to 1.5% of average final salary), an increased vesting period (from 5 to 10 years of service), full service retirement at age 65 with 10 years of service or a "Rule of 90", and an increased final salary calculation to the average of the highest 5 consecutive years of service (up from the highest 3 years).
- In recent rounds of bargaining, Baltimore County has adopted a series of pension adjustments since establishing a new tier in FY2008. Changes for hires since 2007 now include: increased

Employee Pension Contribution (Primary Civilian Group)	
Baltimore City	0%
Anne Arundel County	4%
Baltimore County	7%
Howard County	3%
State of Maryland	7%
Montgomery County (Retirement Savings Plan & Guaranteed Retirement Income Plan)	4% of regular earnings up to the Social Security Wage Base (SSWB), plus 8% of earnings above the wage base
Prince George's County	Civilian Supplemental Pension: Ranges from 1.6% to 4.3% Non-Contributory MD State Plan: 0% (5% on earnings above SSWB)

employee contributions to 7% (previously was based on age at time of hire); increased normal retirement age from age 60 with 5 years of service or 20 years of service (any age) to age 67 with 10 years of service or 25 years of service (any age); increased average final compensation calculation; and eliminated retiree COLA for employees hired after 7/1/2007 with less than 25 years of service.

- Effective July 1, 2012, the Virginia Retirement System (VRS) implemented significant reforms to its pension program, requiring all state and local government members to contribute 5% of salary. Participating local governments have the option to phase in the employee contributions for on-board employees, and are generally aligning the new contribution requirement with pay adjustments. As part of the VRS reforms, all state workers hired on or after January 1, 2014 will be required to participate in a mandatory hybrid plan, consisting of both a defined benefit with a lower multiplier (1.0% v. 1.7%) and a defined contribution component.

Looking forward, another important set of issues related to pension benefits involves new Governmental Accounting Standards Board (GASB) accounting standards regarding the actuarial approach required for assessing retiree benefit liabilities for governmental financial statements, more conservative methodologies being used by the credit rating agencies to evaluate pension liabilities, and a parallel trend among many public employers to adopt more conservative actuarial assumptions for pension funding. These considerations — which may impact the annual contribution levels determined to be prudent for sustaining the City’s retirement systems — are outlined in the “Addressing Long-Term Liabilities” section of this Volume.

Paid Leave and Injury Benefits

Like many public sector employers, Baltimore City’s paid leave program is more generous than private sector labor market norms. The following examples represent the benefit levels for civilian employees represented by the City Union of Baltimore, Local 800 (specifics vary somewhat by bargaining unit):

- 11 paid holidays annually, compared to a median of 8 among large private sector establishments (100+ workers).

- 12-24 days of vacation per year, depending on years of service, compared to private sector medians of 10-20 days for large establishments.
- 3 paid personal days per year (only 49% of private industry workers in large establishments have access to any paid personal leave).
- 12 days of paid sick leave annually, in comparison to a median of 6 days among large private sector establishments.

At the same time, in comparison to regional public employers and cities nationally, these City of Baltimore levels of annual paid leave accruals are within the mainstream for governments.

Nonetheless, Baltimore is an outlier — even among public employers — with regard to the level of paid leave available for City employees to cash out at the time of retirement. In FY2011, such payouts for vacation, personal, compensatory, and sick leave totaled approximately \$9 million. In Baltimore’s Comprehensive Annual Financial Report (CAFR), the City’s compensated absences liability of \$112 million for FY 2009 was equivalent to 8.6% of General Fund revenues). In contrast, the compensated absence liabilities reported by neighboring Anne Arundel County, Baltimore County, and Howard County ranged between just 2% and 4% of revenues.

Several factors contribute to the City’s high payouts, liabilities, and related costs:

- A much higher allowable maximum number of days of vacation that may be cashed out at separation (see table below).

Vacation Leave - Cash Out Provisions	
Baltimore City	CUB: 60 to 120 days (5 years at current vacation accrual rate) MAPS: 96 to 192 days (8 years at current vacation accrual rate) IAFF: 48 to 96 days (4 years at current vacation accrual rate) FOP: 192 days
Anne Arundel County	Up to 30 days of vacation leave paid at termination
Baltimore County	Up to 50 days of vacation leave paid at termination
Howard County	Up to 45 days (360 hours) of vacation leave paid at termination
Montgomery County	Up to 30 days (240 hours) of vacation leave paid at termination
Prince George’s County	Up to 45 days (360 hours) of vacation leave paid at termination
State of Maryland	Up to 50 days of vacation leave paid at termination

²BLS National Compensation Survey: Employee Benefits in the United States, March 2012

- Flexibility to carry over unused personal days from year to year, compared to a more common “use it or lose it” restriction on annual carryover among other regional employers.
- The provision of 90 days of additional paid leave just prior to retirement for sworn Fire Department employees.
- The option for civilian employees to convert 1 day of unused sick leave into an annual cash payment for each 4 sick days accrued during the year, again, a highly unusual benefit within the region.
- The provision of compensatory leave (“comp time”) to senior level, salaried managers, professionals, and executives for hours worked in excess of their normal work schedule. Under this practice, such employees may accrue and use compensatory leave time in lieu of vacation and/or personal leave, resulting in larger separation payments for senior employees.

In addition to generous paid leave, the City also offers injury benefits in excess of statutorily required Workers’ Compensation. For example, Baltimore provides civilian workers with 195 days of job-related injury pay at 100% of pre-injury salary, plus an additional 20 half-days, in comparison to 66.7% wage replacement under standard Workers’ Compensation requirements. Public safety employees receive 100% of pay for an even greater period of time. In FY2013, the City has budgeted \$38.2 million for Workers’ Compensation claims.

In Maryland, as in most states across the nation, Workers’ Compensation benefits are set statutorily at less than 100% of pre-injury pay for multiple reasons:

- Wage replacement for work-related injuries is generally exempt from federal income taxes.
- Employees at home with injuries will not have commuting costs.
- Such adjustments provide an incentive for employees to strive for timely return to work.

While many Maryland counties also provide some level of income replacement level exceeding the minimum benefits required under Workers’ Compensation, the State of Maryland provides 66.7% to state workers — consistent with the statute.

Cash Compensation

While Baltimore’s benefits are competitive with — and, in some areas, above regional norms — the City’s cash compensation is not as strong on a comparative basis:

- Compared to private sector workers for selected blue collar and clerical positions in the Baltimore-Towson Metropolitan Statistical Area, the City’s wage levels are generally within the mainstream, but not high.
- Compared to other large Maryland public employers (Anne Arundel, Baltimore County, Howard, Montgomery, Prince George’s, State of Maryland), the City’s wages rank below the median for many positions.
- Similarly, the City’s public safety workers tend to be paid toward the lower end of the regional public sector mainstream, with Firefighters ranking 5th of 6 among large Maryland counties at entry and maximum base, and 6th of 6 at maximum base plus longevity (the State of Maryland does not have a comparable position). For Police Officers, the City ranks 5th of 7 at entry (including State of Maryland Troopers), 6th of 7 at maximum base, and 7th of 7 at maximum base plus longevity.
- With regard to managerial and professional employees, a 2008 compensation study by Fox Lawson & Associates identified an average shortfall in Baltimore salaries of 5.9% relative to an identified “market” median across 59 surveyed positions. While some positions within the overall group were found to be competitive, other key titles evidenced even greater deficiencies. Salaries for Baltimore’s Engineer I professionals, for example, were found to be more than 25% below the median. While this survey has not been updated since 2008, wages in Baltimore and across the market have been relatively flat during the subsequent weak economic period, and such findings very likely remain relevant for comparative purposes.
- Further, because the City’s unionized employees have tended to receive higher wage increases than their managers over the years, the pay gap has narrowed between many Baltimore managers and the employees they supervise. For example, according to data provided by the City Department of Human Resources, the maximum of the pay range for an Engineer I

Regional Cost Containment – Civilian, Union-Represented Workers (FY2011-FY2013)

	FY2011	FY2012	FY2013
Baltimore City	0% + Step Furloughs	2% + Step Furloughs (reduced from FY2011)	0% + Step No Furloughs
Anne Arundel County	0% + No Step -5% wage reduction through increased pension contributions, reduced pay premiums, and furlough days	0% + No Step -5% wage reduction through increased pension contributions, reduced pay premiums, and furlough days	0% + No Step Restoration of pay premiums, no furloughs, continued increased pension contributions
Baltimore County	0% + Step	0% + Step	No new agreement
Howard County	0% + Step	1% + Step	0% + Step
Montgomery County	0% + No Step 3 to 8 furlough days	0% + No Step Increased employee health care and pension contribution	0% + No Step + \$2,000 Increased employee pension contributions
Prince George's County	0% + No Step	0% + No Step + \$1,000 bonus	0% + No Step + \$1,250 bonus
State of Maryland	0% + No Step Temporary Salary Reduction (TSR)	0% + No Step + \$750 bonus Wages restored to pre-TSR levels and pension reform	2% (1/1/2013) + No Step

service demands of an urban hub. Baltimore's significantly lower income levels, home values, growth trends, and credit ratings are noted in the City Economic Position section of this report.

So long as Baltimore remains sufficiently competitive within its overall labor market to continue to recruit and retain a quality workforce, however, it is not necessary — nor realistic — for the City to expect to match suburban counties

(BA required) in FY2002 was \$6,962 (16.2%) above that for an Engineering Associate II (High School + 2 years of experience). By FY2012, after a decade of pay scale compression — with no wage increases at all for managers since July 2008 — this difference had narrowed to just \$193 (0.3%).

Looking forward, there is not yet much indication that regional public sector wages will return to pre-recession rates of growth, although some modest improvements are beginning to be granted relative to the widespread freezes and cuts in the immediate aftermath of the recession. Further, some regional public employers continue to freeze base wages going forward (e.g., Prince George's County, which is also providing lump sum payments instead of base wage increases for both FY2012 and FY2013).

To the extent that such trends continue, even modest increases to Baltimore's cash compensation would be expected to maintain — and, potentially, improve — the City's regional competitiveness.

Options for Change

In developing a longer-term workforce compensation strategy, it will be important for Baltimore to avoid the trap of trying to “keep up with the Joneses” relative to Maryland counties with much stronger economic and revenue bases, and without the

dollar for dollar. Further, many of these same suburban Maryland counties have recently found their current compensation structures to be difficult to sustain, and have been negotiating wage freezes and benefits reform of their own.

At the same time, both general labor market benchmarks and regional public sector comparisons suggest that the City should seek to “rebalance its portfolio” of wages and benefits provided to municipal employees — directing available future compensation dollars proportionately more toward wages while focusing cost containment and reform efforts primarily on City benefits programs:

- From a recruitment and (perhaps to a somewhat lesser degree) retention perspective, many employees focus most intently on cash compensation, rather than benefits. Accordingly, improving the City's relative salary levels will likely have the greatest positive impact on workforce quality and stability. Further, because current benefit programs are particularly generous, the City has room to adopt some reforms and restructuring while still continuing to provide benefits that are fully competitive and address employee needs
- From a fiscal perspective, the high underlying growth rates for benefit costs are a major “budget buster” — and focus on

achieving more sustainable benefits programs will have the greatest long-range impact on Baltimore's fiscal position.

Pension Reform

Employees' Retirement System (ERS)

To ensure greater affordability and sustainability, the following adjustments might be considered for ERS:

■ **Establish a contributory structure**, ensuring a greater stake for civilian employees in the funding of their benefits, while achieving improved equity across Baltimore's employee groups participating in different retirement systems. Because such contributory structures are common among other regional public employers, this change is not expected to adversely impact competitiveness — and the reduced funding pressures on the City will provide greater capacity for wage increases to better balance the total compensation portfolio.

If employee contributions were targeted at 5% for all current and future ERS active members, phased in by 1% per year from FY2014 to FY2018, the City would ultimately increase budget capacity by more than \$10 million annually on a recurring basis, while still maintaining a competitive pension contribution structure relative to other large Maryland governments — with employee contributions remaining below those already required by the State of Maryland and Baltimore County.

■ **Eliminate the variable supplemental benefit**. Under the current ERS plan design, members receive percentage-based post-retirement cost-of-living adjustments (COLAs), plus may receive supplemental increases if the investment earnings of the plan assets exceed certain thresholds. This is an unusual benefit structure that siphons away resources generated in good years that would have otherwise been used to sustain and improve plan funding levels, and that provides an unpredictable benefit for plan participants. If eliminated for all ERS members, both active and retired, the City's General Fund contribution requirements would be projected to decrease by \$3.5 million in FY2014, with savings rising to \$7.5 million by FY2022. At the same time, plan beneficiaries would continue to receive consistent and reliable 1.5% COLA increases.

■ For future civilian hires, the City could **establish a defined contribution (DC) retirement savings plan**, consistent with the 401(k) model prevalent in the general labor market and the program in place for the District of Columbia government

since the mid-1990s. This approach would establish a predictable obligation for the City, without the budgetary risk and volatility of a defined benefit program.

- Because this new program would only be provided for future hires, with all incumbent workers remaining in the current DB plan, savings would be modest initially — but would increase steadily over time. At a City contribution rate of 5% of salary, the General Fund savings would be estimated at \$1.0 million in FY2014, growing steadily to \$7.8 million by FY2022.
- If the City's contribution were structured as a 3% City match on a mandatory 3% contribution by employees, plus a 50% City match on the next 4% contributed by employees, this approach would generate potential combined annual retirement savings contributions equivalent to 12% of salary.
- This DC structure would still provide an opportunity for significant, City-funded retirement savings above and beyond the Social Security benefits to which the City already contributes 6.2% of payroll on behalf of civilian employees. Based on analysis by Hay, a full career employee hired at age 25 at a \$25,000 salary, retiring at age 65 with contributions earning interest returns of 5.25%, could anticipate income replacement at retirement of 89.0% of pre-retirement earnings, inclusive of Social Security benefits. For the same employee at a \$45,000 salary, the structure would replace 82.8% of pre-retirement earnings. Based on standard industry analyses of sufficient "replacement ratios" for retirement (which take into account that retirees no longer pay into the Social Security system, are no longer saving for retirement, and have no commuting costs, etc.), this proposed benefit structure would be consistent with the level required to maintain a dignified post-employment standard of living.

Fire and Police Employees' Retirement System (FPERS)

In June 2010, the City adopted a series of reforms to improve FPERS sustainability. Building on a set of recommendations developed by the Greater Baltimore Committee, these adjustments included replacement of a volatile post-retirement benefit adjustment formula with a more predictable cost-of-living adjustment (COLA), increased employee contributions to further share funding responsibilities for pension benefits, and extended eligibility requirements for normal retirement age. In addition, the

City established a 36 month period for calculating the “average final compensation” used as the basis for pension calculation, and modified eligibility and guaranteed interest rates under the Deferred Retirement Option Plan (DROP) that permits late-career employees to build a lump sum payment from the City in lieu of additional pension service credit. Along with such benefit adjustments, the City also reduced its long-range actuarial investment return assumption from 8.25% to 8.0%, taking on higher contribution requirements in a more prudent approach toward addressing the FPERs unfunded liability.

As noted in the Ten-Year Budget Projections section of the report, these FPERs reforms are currently the subject of ongoing litigation. To date, the City has received favorable rulings regarding some, but not all, of the adopted reforms — and certain issues of major fiscal importance remain under active litigation. If the City’s approach is not fully upheld (and/or if equivalent reforms are not developed), the City’s recent fiscal progress would be set back dramatically to the severe detriment of the public interest and welfare, and the health and sustainability of the FPERs retirement system would also be eroded.

To build on these critical 2010 reforms, Baltimore City Council also called by ordinance for a comprehensive study to evaluate and develop options for modifications to the FPERs plan for future hires — prospective changes which would not be anticipated to be challenged in court. In 2011, the Segal Group

was engaged to conduct this “new hires” analysis, which encompassed regional and national benchmarking, stakeholder interviews, and the development of projections for the impact on sustainability and income replacement.

Through this evaluation, Segal identified a range of potential areas for further adjustment. As summarized in the chart below, their recommendations would tighten up general FPERs eligibility and vesting criteria. In addition, given Segal’s findings that Baltimore’s Deferred Retirement Option Plan (DROP) is unusually rich and that the City continues to provide relatively high Final Average Earnings replacement, the recommendations include a “Hybrid” Defined Benefit/Defined Contribution (DB/DC) approach as an alternative for employees to build individually controlled retirement savings.

Based on Segal’s analysis, these reforms would continue to deliver a competitive retirement benefit, while also providing public safety employees with income replacement after a full career with the City sufficient for a secure retirement. At the same time, such adjustments would help to further stabilize FPERs funding, reduce long-term unfunded liabilities, and improve plan affordability and sustainability.

In the near term, any budget impact would be relatively modest, because most funding requirements for FPERs are associated with employees already on board. Over time, however, the proposed changes would provide some relief for the City’s funding pressures. Under current FPERs actuarial practices, and

assuming all other factors (such as investment returns) are consistent with actuarial assumptions, Segal projects that these changes would generate several million dollars in annual savings within 3-4 years, rising to more than \$10 million annually by the end of the decade ahead.

At the same time, the FPERs actuarial firm, Cheiron, has recently proposed consideration of a set of changes to the

Benefit	Current (hired on or after 7/1/2010)*	Segal Co. Proposed Modifications
Normal Retirement Age	Earlier of 25 years of service or age 55 with at least 15 years of service as a Plan member	Age 55 with 25 years of service or age 60 with 10 years
Early Retirement	Age 50 with 10 years of service or any age with 20 years of service. Reduced 6.5% for first 5 years, 4.5% per year for next 5 years, 3.0% per year for next 5 years, and 2.0% per year thereafter to Normal Retirement Age	No more than 5 years prior to Normal Retirement Age, reduced 6.0% per year
Vesting	Any age with 15 years of service. Termination Retirement Allowance payable immediately or refund of employee contributions	Any age with 10 years of service. Normal Retirement Benefit accrual deferred to Normal Retirement Age
DB Normal Retirement Benefit	2.5% per year for years 1-20 2.0% per year for years thereafter No maximum	1.0% per year for years 1-10 1.67% per year for years 11-20 1.33% per year for years 21-30 Maximum of 40% of AFC
DC Plan	N/A	4.0% employee contribution matched by a 4.0% City contribution. No DROP option

system's actuarial methodologies, with a goal of improving long-term plan funding and sustainability. Among these changes, the FPERs Board has recommended reducing the system's investment return assumption from 8.0% to 7.75%, consistent with a national trend based on the experience of recent years and projections of the future, long-term economic environment. As detailed in the subsequent section of this report on Addressing Long-Term Liabilities, this change has been incorporated within the baseline assumptions for this Ten-Year Financial Plan, with an increase to the City's employer contributions of approximately \$4 million in the first two years, projected to decrease over time. This investment in improved benefit funding and sustainability may require use of a substantial share of the potential savings from restructuring benefits for future hires.

Elected Officials Retirement System (EOS)

Along with the City's major retirement systems, ERS and FPERs, Baltimore also maintains the separate EOS for elected officials. Because the EOS plan is comparatively small, its structure has a minimal fiscal impact — with FY2013 General Fund expenditures budgeted at just \$0.4 million. Further, as of the EOS plan's 2012 actuarial valuation for FY2014, the plan has a sound funding level of 109.2%.

While not a major budget driver, as part of a comprehensive approach to retiree benefits, the City could consider modifications to the EOS plan consistent with ERS and FPERs reforms and/or explore alternative benefit structures. Currently, the EOS is a contributory plan, with Elected Officials contributing 5% of their pay toward retirement (contribution ends at age 60 or after 35 years of service). Elected officials may retire with full benefits after 16 years of service or age 50 with 12 years of service, and receive 2.5% of their average final compensation for each year of credited service.

Health Benefits (active employees)

To manage within the budgetary parameters identified by the Ten-Year Financial Plan, it will be critical to develop a healthcare program that is more affordable for the City, with more sustainable rates of cost growth, building on the 2013 reforms already identified through the Ten-Year Financial Plan process and adopted at the start of the year. At the same time, however, it is also important to maintain a competitive, quality set of benefits. To reach these goals, it will be important to focus on three key areas of Baltimore's healthcare program:

- **Plan management:** The City currently offers six (6) plan options, however, these different plans have very similar designs — such that meaningful choice is limited beyond selection of an HMO or a PPO, and fragmentation of providers complicates coordination around opportunities such as health management. In upcoming rebidding, the City has the opportunity to rationalize plan offerings — using fewer carriers prospectively to maximize purchasing power, simplify the program to enhance and streamline employee communications, and establish a better platform for coordinating health management initiatives.

In addition, the City's Department of Human Resources is launching a dependent eligibility audit for Plan Year 2013 (January-December) to ensure that the City is not paying for benefits for ineligible recipients. While savings from this initiative are not included in the FY2013 Budget or Ten-Year Plan baseline, other large employers have experienced savings approaching 3% of plan spending.

- **Health management:** There is a growing national trend toward the development of strong health management programs to support employee wellness and reduce claims experience, such as recently announced by the State of Maryland — and already successfully in place with governments such as King County, WA. Preliminary analysis of Baltimore claims experience relative to the average experience for the City's carriers suggests significant opportunity for improvement with strengthened wellness and disease management programs and an accompanying set of incentives for employee participation. For example, 2010 plan analysis found significantly higher rates of diabetes and hypertension among City of Baltimore employees than seen in comparable regional plans.

While no effort can eradicate illness and disease altogether, many of today's most prevalent chronic conditions can be avoided or better managed through changes in patients' behaviors and habits. A robust wellness program can include a wide variety of tools, including health risk assessments (HRAs), classes and seminars, exercise programs, and a comprehensive marketing and communication plan to ensure employees are aware of and participate in the programs.

In 2009, the City engaged Walker Benefit Services (WBS) to conduct a wellness research project. As part of the PFM team for this Ten-Year Financial Plan project, WBS has revisited some of their earlier findings, and the Hay Group has reviewed that research and report and concurs with its recommendations, including the following considerations for developing a wellness program and disease management strategy:

- Wellness needs to become part of the Baltimore City culture.
- Employees need to better understand: the impact of unhealthy habits on their health, specifically how and what they eat; the need for regular screenings and the benefits of early detection; and why exercise is so important. There is now an overall lack of awareness as it relates to health and wellness.
- Any efforts to promote participation in Health Risk Assessments should be thoroughly marketed and communicated to be successful. There is much skepticism to be overcome as it relates to this tool, and confidentiality must be assured.
- There is little to no awareness of the disease management programs currently available, and also a lack of awareness and/or a fear factor that needs to be overcome as it relates to health screenings. Education and outreach will be critical to success.
- Programs should be marketed in multiple ways to reach everyone. Online outreach is positive, but does not reach everyone. Print materials are preferred if they are visually and graphically appealing. Group meetings are very popular but they must be brought to the work sites, as it is not always convenient to attend at a centralized location.
- Having a wellness contact person or “champion” in each Department would also help to promote available wellness activities and ensure the program’s success.
- Many employees are still more inclined to use their telephone, instead of the internet, when they have questions; they want to speak to a live person in the Employee Benefits Division rather than look for the answer themselves online.
- Incentives, such as gift cards, discounts, and vendor giveaways, can be effective incentives to encourage participation in wellness programs, and competition within and between Departments is also a popular motivator.

- **Plan design:** As the changes adopted in FY2013 take root over the next several years, future health care market changes under the Affordable Care Act — particularly the development of health care exchanges — are expected to create new opportunities for overall employee coverage. Such options are expected to include the addition of a lower cost (“value plan”) option set at the design level required to avoid “Cadillac Plan Tax” penalties, and modified employee contribution rates for dependent coverage, given the anticipated availability of coverage via the exchanges, and consistent with the practices of many other employers.

Health Benefits (retirees)

Much as with active employee healthcare, the benefit reforms adopted by the City in FY2013 have provided a more sustainable foundation for coverage going forward. At the same time, changing workforce demographics and ongoing healthcare inflation pressures continue to require thoughtful management of retiree medical plans.

Many of the general reforms outlined above for active employee healthcare could also help to achieve savings in Baltimore’s retiree healthcare program. In addition, the City could consider the following targeted options to address OPEB liabilities:

- **Improve Coordination of Benefits with Medicare:** The current Medicare Coordination of Benefits (COB) strategy used by the City allows retirees to use medical services with no out-of-pocket costs. As an alternative approach, the City could consider implementing COB in a way that requires Medicare-eligible retirees to share in the same out-of-pocket costs as non-Medicare retirees, creating reasonable incentives to prevent overutilization.
- **Implement Medicare Advantage Programs for all retirees:** Currently, retirees who elect the Kaiser Permanente plan option are participating in a Medicare Advantage plan. Medicare Advantage plans are private health plans that contract with Medicare to provide Part A and Part B benefits, and can be a cost-effective way to deliver quality coverage. If all Medicare-eligible retirees were enrolled in a Medicare Advantage plan, the City could potentially provide comparable coverage to the current plan at much lower costs.

- **Sunset the Rx subsidy for Medicare-eligible retirees in 2020, as equivalent federally subsidized coverage becomes available.** Under the terms of the Affordable Care Act, by 2020 a standard Medicare Part D Plan will feature a 75% federal subsidy after a deductible, with catastrophic protection for retirees with large drug expenses. As a result, supplemental City coverage to fill the Medicare “donut hole” will no longer be needed, providing an opportunity for significant savings. Further, if the above approach is adopted now, much as the State of Maryland has already done for state employees, the City will be able to recognize the impact of this plan change in its actuarial liability calculations well before the 2020 date is reached.

Along with such benefit reforms for municipal employees, the City might also consider the development of a new approach to financing BCPS retiree medical coverage for school employees hired since the BCPS became independent in 1997 (now funded by the City), as outlined in the Addressing Long-Term Liabilities section of this background report.

Paid Leave and Injury Benefit Reforms

Paid Leave

Substantial savings could be achieved in the City’s \$9 million separation payments by reducing carryover paid sick, personal, and vacation leave balances and cash-out formulas to better align with the mainstream offered across the surveyed jurisdictions. For example, the City could pursue options such as the following:

- **Reducing annual vacation carry-over and cash-out upon separation to a maximum of 30-50 days** for all employees, consistent with other regional public employers — paring back current levels that typically reach more than twice as high.
- **Eliminating carry-over and accrual of personal leave days**, also consistent with the prevalent regional approach.
- **Adopting other innovative means of payout rather than lump sum cash.** The City could potentially develop health savings accounts or other tax-qualified plans into which leave payouts could be deposited with tax benefits for both the employee and the City.
- **Eliminating compensatory leave accruals for certain management and executive level employees.** The City currently allows senior level employees to earn compensatory leave time for hours worked in excess of their normal work schedule. This practice allows employees to use compensatory

leave time in lieu of vacation and/or personal leave, resulting in even larger separation payments for senior employees. Savings might be reinvested in the improvement of management and professional pay competitiveness, to better attract and retain quality public sector leadership.

The adoption of such changes, many of which would require negotiation for union-represented employees, could generate meaningful savings in separation payouts. While some additional leave usage may result during active years of service, this can generally be managed without significant overtime or service impacts. In turn, the savings generated could help to create sufficient budgetary capacity for maintaining needed positions and/or improving salary competitiveness.

Other opportunities identified to improve productivity through paid leave reforms, include the following:

- **Replace “Injury and/or Sick Leave (Non-Line of Duty)” for International Association of Fire Fighters (IAFF) bargaining unit members.** The City currently provides Fire Fighters with up to 6 months (180 days) of sick leave provided that they receive approval from a department approved physician. A more traditional sick leave program of annual sick leave accrual would be more consistent with the benefits offered to other City employees and comparable public safety employees in the region.
- **Eliminate the outlier IAFF paid leave benefit, which provides for 90 days of additional leave just prior to retirement.** No other City union receives an equivalent benefit, which adds significantly to City costs (over and above separation pay and DROP benefits) with no return in productivity.
- **Restructure the annual conversion and cash-out of sick leave** (one day for every four unused), rarely found among other public employers. As an alternative, the City could explore establishment of a new incentive to promote health management program participation and outcome improvements, or potentially substituting a linkage between earning of personal leave and good attendance (e.g., 1 extra personal day if 5 or fewer sick days used, 2 extra personal days if no sick leave used).

For some potential changes, a phased-in approach may be beneficial to mitigate unintended consequences from an abrupt rules change, such as excessive use of paid leave no longer available for cash out.

Workers' Compensation

The City's Risk Management division is developing strategies for enhanced safety programs, based on analysis of injury and claims data, to better target resources to prevent employee injuries. As an additional option for reducing injury benefits costs and liabilities, Baltimore could also seek to negotiate reduced Accident-Time payouts (A-Time) that exceed the minimum benefit payable under Maryland's workers' compensation laws. As outlined above, the City's current policy is to provide 100% income replacement for on-the-job injuries, rather than the 66.7% received by State employees consistent with Maryland's Workers' Compensation statute.

Aligning A-time with statutory Workers' Compensation would not only generate direct savings in City payouts; it would also provide a better incentive to support return-to-work programs for employees injured on the job. At the same time, this restructured benefit would be consistent with coverage in the general labor market, as well as for State employees, thereby maintaining compensation competitiveness.

Cash Compensation

The Ten-Year Plan baseline assumes 2.0% annual wage increases across-the-board for City employees, plus additional pay gains for individuals based on step increments and longevity payments.

This level of wage growth would represent an improvement over the cost containment required in the wake of the economic downturn, would parallel projected increases in local consumer prices, and would likely maintain Baltimore's current position in the regional labor market. Because of fiscal pressures facing public employers across the region, wage and step freezes have been widespread, and pay moderation is continuing — even among jurisdictions with substantially stronger tax bases than the City.

These 2.0% baseline increases would not, however, be projected to significantly improve Baltimore's market position as the City competes to recruit, retain, and motivate a quality workforce. Accordingly, while some savings from employee benefit reforms are needed simply to bring the City's budget back into structural balance (again, the baseline scenario projects significant annual shortfalls), Baltimore might also consider the following strategies

for reinvesting in improved cash compensation to help rebalance the total compensation portfolio:

- A new Fire Department shift structure could provide sufficient savings to meaningfully improve annual compensation for fire suppression personnel.
- Police leave and benefit reforms could help to fund retention incentives for City patrol officers, targeting available dollars at key career junctures to law enforcement professionals who commit to long-term service to Baltimore.
- Paid leave reforms and overall productivity gains could also generate savings that could be reinvested to help fund pay improvements above baseline levels.

For management and professional employees, for example, an investment of \$2-3 million in base payroll growth beginning in FY2015 — some of which could be funded from paid leave reforms — could help to transition to new executive and managerial pay scales that would improve competitiveness for talent, start to address pay compression, and potentially include performance-based incentives and rewards.

To the extent that economic conditions and budget constraints require some continued cost containment, the City could also consider elongating the pay schedules by adding a new top step to the salary schedules, *in lieu of* an across-the-board increase. This approach would target compensation dollars toward improving the City's competitiveness at the top rate, while still providing annual pay gains for all workers as less tenured workers would receive adjustments via step increments

- 74.2% of Baltimore City civilian workers have 5 or more years of service (75.1% including police and fire employees), reflecting the approximate number of workers who would be at the top step of their respective salary grade.
- For civilians below the maximum of their pay range, annual step increases start at 1.5% and can be much higher, depending on employee group and tenure.

For the FOP, the City could explore the option of adding a new non-competitive, non-supervisory rank to the regular progression for police officers based on years of service *in lieu of* a cost-of-

living adjustment. In addition to tenure, the City could link the promotional advancement to satisfactory performance appraisals, proficiency testing requirements, and other measures as deemed appropriate by the department. Across the region, most jurisdictions have one or more non-competitive promotional police ranks, using variations of the approach outlined above, for example:

- Anne Arundel County: Police Officers receive an automatic promotion to Police Officer First Class with a 4% pay increase after two years of service and satisfactory performance evaluation; automatic promotion to Corporal with 4% pay increase after two years of service as a Police Officer First Class, satisfactory performance evaluation, and passage of a proficiency examination.
- Howard County: Police Officers may promote to Police Officer First Class with a 7% pay increase after three years of service.
- Montgomery County: A Police Officer I may promote to Police Officer II after two years of service with a 5% pay increase; a Police Officer II may promote to a Police Officer III after two years of service as a Police Officer II with a 5% pay increase.



Key Challenges:
Tax Competitiveness

Findings and Options

- Baltimore's existing, high tax burdens and regional tax competitiveness concerns — particularly with regard to the property tax rate for residents — are a critical factor in individual decisions to locate outside of the City.
- This is a real and critical challenge that erodes the City's tax base and economy, and that severely constrains the City's ability to increase revenues. Further, this reality is compounded by perception problems when comparisons are made to "headline" property tax rates among Maryland counties that do not always include additional municipal taxes and/or trash collection fees.
- The Mayor's "20 Cents by 2020" plan to reduce the tax burden on homeowners through the Targeted Homeowners' Tax Credit is a positive step and sends a strong signal to current and potential homeowners that the City is committed to reducing effective property tax rates over the long term.
- While tax cuts must be realistic — avoiding the erosion of core public services that are also critical to locational decisions and the quality of urban life — the City should seek to extend the Mayor's commitment to property tax reduction beyond 2020, and seek to broaden relief over time to businesses as well as homeowners.
- To more dramatically accelerate property tax relief, the City could also consider the establishment of self-supporting enterprise funds for stormwater and solid waste management — improving financial accountability and sustainability for these important environmental services, improving comparability of revenue structures with surrounding counties, and generating substantial General Fund savings for property tax relief.
- Other prospective options should aim to diversify Baltimore's revenue base, and to reduce the degree to which residents and City-based businesses shoulder the primary tax burden. Commuters, visitors, and tax-exempt organization for example, also benefit from City services, yet carry a disproportionately small burden for the cost of those services under the taxation framework established by State law.
- Going forward, the City should also reevaluate its mix of tax incentives to ensure alignment with the current vision for growth. Tax abatements and credits can be useful tools for sparking private investment and promoting policy goals. At the

same time, Baltimore's mix of such "tax expenditures" has developed through accretion over many years. By taking a fresh, comprehensive, and balanced look at the overall mix, the City may be able to better target such incentives to meet contemporary goals and needs, while also ensuring a positive return on these tax subsidy investments.

- Along with tax policy changes, the City should also continue to focus on strong tax collection and enforcement. In recent years, Baltimore's new Billing Integrity Unit has generated significant returns, and further opportunities remain to build on these initiatives.

Major Challenges

As currently projected without corrective action, the City's annual, structural deficit will grow to nearly \$125 million within the decade ahead. Over the Ten-Year Financial Plan forecast period, compound annual revenue growth is projected to be just 1.9%, well below the compound annual expenditure growth forecast to maintain the current level of services. While the City will continue to seek opportunities to reduce operating costs and their growth, it is also critical for revenues to be sufficient to pay for City services in the short term, with revenue growth that maintains pace with the cost of City services in the long term.

While much of this weakness in the City's projected revenues results from the lingering effects of the most severe economic downturn in generations, future growth forecasts are also dampened by the impact of high tax burdens on residents and businesses that impair the City's position as a location of choice. To shift Baltimore back onto a growth trajectory, the City must improve its tax competitiveness — while at the same time, ensuring a sufficient ongoing flow of revenue to fund the core services and strategic investments that are also essential to growth.

Existing, High Tax Burden

According to analysis by the State of Maryland Department of Legislative Services (DLS), Baltimore's combined per-capita yield of income and property taxes adjusted for differences in tax rates — the City's **tax capacity** — would be just 48.9% of the average of all Maryland counties.¹ Along with concentrations of poverty and below average per capita wealth levels within the City's tax base, this is also a function of Baltimore's high percentage of tax-

¹Maryland Department of Legislative Services, Office of Policy Analysis, "Tax Capacity and Effort of Local Governments in Maryland," March 2012 (2010 data).

	Income Tax	Recordation	Transfer	Hotel/Motel	Admissions & Amusement	Property Tax (County Level)	Total Property Tax- Largest municipality	Trash Fees
Baltimore City	3.20	\$5.00	1.5%	9.5%	10.0%	2.268	2.268	–
Anne Arundel County	2.49	\$3.50	1.0%	7.0%	10.0%	0.910	1.103 <i>Annapolis</i>	\$298
Baltimore County	2.83	\$2.50	1.5%	8.0%	10.0%	1.100	1.100	–
Harford County	3.06	\$3.30	1.0%	0.0%	5.0%	1.042	1.576 <i>Aberdeen</i>	<i>Citizens contract with private haulers</i>
Howard County	3.20	\$2.50	1.0%	7.0%	7.5%	1.150	1.150	\$210-\$225
Montgomery County	3.20	\$3.45	1.0%	7.0%	7.0%	0.959	1.165 <i>Rockville</i>	\$213.76 \$368.67 <i>(for applicable districts, varies by service level)</i>
Prince George's County	3.20	\$2.50	1.4%	5.0%	10.0%	1.319	1.513	\$234.33- \$326.01

Source: Tax data from the State of Maryland Department of Legislative Services, 2012 Overview of Maryland Local Governments; County rate shown includes special rates for services not funded from the general county property tax rate where applicable (Howard, Montgomery, Prince George's)

This is a real and critical challenge, compounded by perception problems when comparisons are made to Maryland County tax rates without considering additional municipal taxes and/or trash collection fees

While many private investment decisions are regional, national data also indicates that Baltimore's current, overall tax burdens are high relative to other major U.S. cities. Each year, the District of Columbia government develops a comparison of combined state and local tax burdens at varying income levels for a hypothetical family of three in each state's largest city, as well

exempt property. As of the 2010 Census, Baltimore's residents represented just 10.8% of the State of Maryland's population overall — but the City was home to 28.7% of State-owned tax-exempt property value, 30.4% of educational tax-exempt property value, and 31.4% of charitable property value within all of Maryland.²

Under the State's taxation framework, local governments rely heavily on property and income taxes that fall on local residents and businesses, without access to non-resident wage taxes or local sales taxes that would share funding burdens across commuters and visitors who also benefit from local services. As a result, in order to generate enough revenue to pay for services, the City must tax its base more heavily than the surrounding counties.

Accordingly, the City's **tax effort** — the degree to which it taxes its base to generate actual property and income tax revenue yields — is the highest in the State, 64% above the average county level. Further, under Maryland's local government tax structure, which relies heavily on the property tax and resident-only income taxes, Baltimore's high overall tax burden falls disproportionately on residents and businesses that have chosen to locate in the City, further impeding the City's ability to compete for growth.

as Washington, DC. Based on the most recent such analysis, Baltimore's overall tax burdens and residential property taxes both ranked in the highest quartile at every income level evaluated.³

Sound Tax Policy

There are multiple dimensions to sound tax policy. Ideally, a government's revenue structure should be reliable and not unduly vulnerable to disruptive swings in the economy. At the same time, a revenue structure should be equitable and not unfairly burden some taxpayers relative to others. The fiscal health of a city is closely linked to its ability to fashion a revenue structure that manages to balance such tenets of good tax policy — including adequacy, sustainability, equity (vertical and horizontal), neutrality, and sensitivity.

While these principles are generally used to evaluate individual taxes and fees, the table that follows analyzes key aspects of Baltimore's current, overall tax structure relative to these considerations, and outlines potential long-range goals and strategies (within the constraints of the existing State taxation framework):

²Maryland Department of Assessments and Taxation Sixty-Seventh Report (January 2011).

³Government of the District of Columbia, Tax Rates and Tax Burdens 2011 (issued September 2012).

Tenet	Characteristics	Baltimore Analysis	Goals/Strategies
Neutrality	Does current tax policy distort the market or heavily influence economic decisions?	<p>The City's current, overall tax burden is the highest within the metro region, and is consistently cited by stakeholders as a major impediment to economic competitiveness – with a particular focus by most on the property tax.</p> <p>The City has used a range of tax incentives to improve its ability to attract investment.</p>	<p>Begin to reduce the overall City tax burden, and particularly to incrementally bring down Baltimore's property tax rates – improving the City's attractiveness for locational decisions, strengthening the tax base, and growing Baltimore.</p> <p>Leverage private investment and job creation through tax incentives that are continuously evaluated to maximize impact on the long-term vitality of the City, and to ensure a positive return.</p>
Adequacy	In the short term, do the City's revenue streams generate enough resources to fund services currently demanded by citizens?	Baltimore's structural budget shortfalls and unmet investment needs indicate that current revenue sources are challenged, with insufficient growth to self-correct for the City's underlying, structural budget gap absent other changes.	While tax rate reduction is critical for improving Baltimore's competitiveness and growing the underlying tax base, the City must continue to ensure that sufficient revenue flow is maintained to support the core services that are also critical to Baltimore's fiscal health.
Sustainability	Over the long term, is the municipality's revenue stream able to support projected expenditure needs?	The City's largest revenue source, property taxes, is relatively stable – but is not projected to keep pace with the cost of future investment needs and certain fast-rising expenditure categories – such as environmental mandates and employee benefits.	<p>Restructure "budget buster" expenditure categories.</p> <p>Develop user-linked, self-sustaining revenue sources for key budget areas, such as storm water management "greening" and solid waste management.</p>
Horizontal Equity	Does the revenue structure provide fair treatment of similarly situated individuals and/or business taxpayers who benefit from public services?	<p>As a regional hub, Baltimore hosts a diverse mix of residents, commuters, visitors, for-profit businesses, and nonprofit institutions, all of whom benefit from and consume public services. With no commuter or sales taxes, however, the City's tax burden falls most heavily on residents and Baltimore-based for-profits. According to 2010 Census ACS data, less than half (43.6%) of the City's workers reside in Baltimore, and – even including City residents who commute out – Baltimore has a daytime population with nearly 100,000 more total workers than resident workers.</p> <p>The City's homestead tax cap can result in significantly different tax bills for residents with similar properties, based on length of residence.</p>	<p>The City's flexibility to tax commuters and visitors is significantly constrained by State law.</p> <p>Where possible within these constraints, the City should seek to diversify its revenue mix to more equitably balance funding burdens across service recipients.</p> <p>Reduce the overall property tax rate, such that the differential impact of the homestead cap is less severe.</p>
Vertical Equity	Does the revenue structure provide fair distribution of the tax burden across individuals or businesses at differing income levels that benefit from public services?	Some vertical equity is achieved through the City's income tax, which "piggy backs" on the Maryland definitions of taxable income, inclusive of available credits for lower income taxpayers. The City's largest revenue source of property taxes, however, is generally considered somewhat regressive – as lower income individuals tend to spend a higher percentage of their income paying these taxes than higher income individuals.	Reduce the overall property tax burden.

Tenet	Characteristics	Baltimore Analysis	Goals/Strategies
Stability	Is a high concentration of tax revenue subject to volatility from economic conditions?	<p>No government is immune from economic volatility, however, the City's property tax has historically been relatively stable – particularly as buffered by the effects of the homestead tax exemption, which can result in “pent up” value that may continue to be recognized even during a housing market decline. Certain other City taxes, notably real estate transfer and recordation, have been much more volatile – as is the piggyback income tax to a lesser degree.</p> <p>In addition, State revenues – particularly for core transportation services – have recently seen sharp downturns resulting from state-level economic pressures.</p>	<p>Create self-sustaining revenue sources for certain core services, and consider policies regarding the expenditure of highly volatile revenues that may moderate the pressure on core operations during a downturn.</p> <p>Seek dedicated and consistent State funding policies.</p>

Opportunities

Options to generate adequate, sustainable, and equitable revenue should focus on:

- Reducing the property tax burden for those residents and businesses that have decided to locate in Baltimore.
- More equitably sharing the burden of funding City services among all users.
- Maximizing collections for existing revenue sources.

Property Tax Relief

In the stakeholder interviews conducted for this Ten-Year Financial Plan, the City's high property tax rates were cited again and again as one of the most significant impediments to economic and neighborhood growth. Consistent with these views, academic research has strongly indicated that tax increases in communities with comparatively high tax rates will not only reduce the number of local jobs and erode the tax base, but also that some cities can reach the peak of their “revenue hills” such that any further rate increases will generate little or even no incremental revenues.⁴

While the revenue potential for any local government is bounded by the mobility of residents and firms, Baltimore's extraordinarily low tax capacity and high tax effort within its region makes such locational effects of taxation particularly powerful concerns.

To address the central goal of achieving a more competitive tax structure within the Plan period, a range of options has been identified to reduce Baltimore's property tax burden:

- **Targeted Homeowners Tax Credit.** The baseline forecast includes the Mayor's Targeted Homeowner's Tax Credit, which will reduce the effective tax rate by 20 cents by 2020 for owner-occupied residential properties. While the Credit and its cost are built into the baseline forecast and will be funded to some degree by anticipated gaming revenue, the commitment to increase the value of the credit each year will have a significant fiscal impact.
- **Continued Tax Reduction Beyond 2020.** The Ten-Year Plan extends beyond 2020, and one option is to continue incremental tax relief. Continuing this positive direction on an ongoing basis would send an important signal to current and potential residents that the City is moving in the right direction, and that investment in Baltimore will generate a good return. Beginning in FY2021, each further one cent reduction in the tax rate (all taxpayers, extending beyond a Targeted Homeowners Tax Credit) would reduce projected revenues in the short-run by an estimated \$3.9 million per year.
- **Establishment of Enterprise Funds.** Shifting services from the tax-supported General Fund to fee-supported enterprise funds can ensure sustainable funding for important services, improve

“20 Cents By 2020” Impact on Homeowner Property Tax Rate

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Homeowner Rate Impact (cumulative)		0.098	0.107	0.115	0.128	0.151	0.181	0.200	0.200	0.200
Effective Homeowner Rate	2.268	2.170	2.161	2.153	2.140	2.117	2.087	2.068	2.068	2.068

⁴See, for example, Andrew Haughwot, Robert Inman, Steven Craig, and Thomas Luce, “Local Revenue Hills: Evidence from Four U.S. Cities”, Penn Institute for Economic Research Working paper 03-012, Department of Economics, University of Pennsylvania (March 2003).

transparency and accountability regarding the use of the revenues collected from the public, and allocate funding burdens more equitably across those who use particular services. At the same time, such an approach can allow for reductions in the property tax rate as the General Fund is relieved of key cost centers, creating a more comparable mix of taxes and charges relative to Maryland suburbs that already rely more heavily than the City on enterprise funding structures.

○ **Stormwater:** State legislation enacted in April 2012 (HB987), mandates that the City and other large Maryland localities establish a watershed protection and restoration program by July 1, 2013. The legislation requires that such programs include a stormwater remediation fee and a local watershed protection and restoration fee. The City plans to establish a stormwater enterprise, which will remove the cost of stormwater remediation from the General Fund budget. In addition to providing a more sustainable funding source for important “greening” goals and environmental mandates, this approach could provide sufficient General Fund budget relief to allow for new, partially offsetting reductions in the City’s current property tax rates.

○ **Solid Waste:** In addition, Baltimore could also establish a solid waste enterprise, to provide a stable base of funding for sanitation, trash disposal, and future landfill needs. This approach would help to support investment in service improvements, such as new containers for semi-automated trash collection that would help to control litter and rodent control problems, while improving service efficiency. Already, four of the six largest Maryland counties charge a fee for solid waste collection (Anne Arundel, Howard, Montgomery, Prince George’s), and a fifth (Harford) county requires residents to contract on their own for trash collection. Nationally, major cities such as Cleveland, OH; San Jose, CA; and Austin, TX also use fee-based approaches to solid waste management — often including higher charges for setting out more trash (“pay-as-you-throw”) to promote recycling.

- In these other communities, the “headline” Property Tax rate is substantially lower than it would be if sanitation services were fully paid through General Fund revenues. Because Baltimore covers this cost with its General Fund taxes, this aspect of the City’s revenue structure

compounds the perception of high local property tax rates. Shifting costs to an enterprise fund and reducing the property rate on a dollar-for-dollar basis would allow more meaningful comparisons of tax rates to the other counties.

- Based on preliminary funding estimates by the City’s solid waste management consultants, adopting an enterprise model with charges comparable to those in other Maryland counties could enable a reduction of approximately 15 cents in Baltimore’s tax rate, a 31 cent reduction if targeted to homeowners only, or potentially a “hybrid” level of savings if used to fund a mix of general reductions and increases to the Targeted Homeowners Tax Credit.

■ **Tax Incentive Review.** In the FY2013 Budget, the City estimates the value of existing tax credits and abatements to equate to \$127.4 million. Of this total, the majority (\$97.8 million) is associated with the homestead tax credit that caps annual residential property tax increases at a maximum of 4% per year, and \$3.8 million represents the new Targeted Homeowners Tax Credit as outlined above to provide broad-based residential property tax relief. Beyond these major homeowner tax credits, the total value of existing property tax incentives exceeds \$25 million in the aggregate:

<i>Enterprise Zone Tax Credit:</i>	\$11,823,000
<i>Historic Restoration and Rehabilitation Credit:</i>	\$8,506,000
<i>Newly Constructed Dwelling Tax Credit</i>	\$3,800,000
<i>Brownfields Property Tax Credit</i>	\$1,334,000
<i>Home Improvement Property Tax Credit</i>	\$50,000
<i>Other Local Option Property Tax Credits</i>	\$53,000

These incentives are designed to encourage and leverage private investment, and, in the case of the Enterprise Zone Credits, also leverage State investment.

Over the years, the City has also negotiated multiple Payment in Lieu of Taxes (PILOT) agreements with developers, businesses, and landowners that substitute the annual real estate taxes due on a property for an established time period with a negotiated payment, with a goal of sparking economic development that would not have occurred “but for” the incentive.

The City has funded public infrastructure and site preparation using Tax Increment Financing (TIF) districts to attract private investment. A TIF functions by pledging property tax increments gained as a result of the new development (over

and above the existing revenues prior to the project) toward the issuance of TIF Bonds, which are in turn used to help finance capital improvements.

Going forward, Baltimore has an opportunity to review and align various tax incentives with the City's current vision for growth and priority outcomes. For example, while some existing incentives might be found through further analysis to have the potential for restructuring to become more effective and efficient, other new incentives — such as a credit to encourage development of new apartments to help grow the City's residential base — could help accelerate revitalization.

In pursuing a review of tax expenditures, it will be important to balance both fiscal targets and job creation and redevelopment goals — targeting tax incentive dollars to maximize economic impact, ensuring a positive return on the City's tax subsidy investments, and simultaneously continuing to focus on more broadly-based tax relief.

Maximizing Collections

As part of a stable, overall revenue program, the City is also investing in strengthening revenue collection coordination, systems, and processing, with better data analysis capabilities. For example, the City implemented a Billing Integrity Program in 2011, responsible for auditing and correcting assessment data received from the State Department of Assessments and Taxation. Since 2011, the program has identified approximately \$4 million in additional tax revenue by correcting errors in tax credits and exemptions given by the State.

In FY2013, the City Budget includes increased funding for the program to add staff for tax credit audits. Through such initiatives, inclusive of tax policy changes to promote improved tax compliance (e.g., tiered rates for the recordation tax based on the timeliness of filing), Baltimore's Finance Department projects the potential, at a minimum, to double the level of improved collection results achieved to date by the Billing Integrity Program within the Ten-Year Plan period.

Revenue Diversification

Through property and income taxes, Baltimore City residents and taxable businesses currently carry the primary burden of funding municipal services. While the City does levy smaller parking and hotel taxes, and non-residents do pay some fees and fines, the City does not have a "commuter tax" or any other large source of revenue from non-residents who work in the City. Wages earned by non-residents are not taxed by the City, and the City does not directly receive revenue from sales taxes levied on goods purchased in Baltimore.

According to Census data Baltimore's daytime population is nearly 100,000 people greater than the City's residential population — fueled by approximately 200,000 workers who commute into the City each day (while approximately 100,000 City residents commute out, reflecting the strong interconnectedness of the region).

Given Baltimore's current tax policy structure — to the extent that the City may require additional revenues to support new investments and/or to help sustain core services as property taxes are reduced — Baltimore should prioritize options that diversify the City's revenue streams to share the burden of funding services as equitably as possible. Of course, any additional taxes are undesirable, given the City's already high overall burden. At the same time, however, some, modest opportunities may be viable for the City to help meet dedicated needs.

Within this context, the following table lists a range of potential revenue diversification options for the City.

Revenue Option	Structure/Notes	Potential Use(s)
Maintain the Parking Tax at 20% beyond FY2013	<ul style="list-style-type: none"> ■ Beginning in FY2014, the Parking Garages and Lots Tax rate is scheduled to decline from 20% to 19% – resulting in a net General Fund revenue loss of over \$1.3 million annually. ■ The parking tax is one of relatively few current Baltimore revenue streams supported by a significant number of commuters and visitors, given the absence of a City commuter income tax or local sales tax. ■ While not low, Baltimore's current 20% parking tax rate is consistent with current rates in multiple other large eastern cities: Pittsburgh (37.5%); Philadelphia (20%); Washington, DC (18%); New York – Manhattan (18.375%). 	<p>Past increases in the parking tax have been associated with funding for the Charm City Circulator, for which funding pressures are ongoing.</p>
Taxi Cab Excise Tax	<ul style="list-style-type: none"> ■ An excise tax on taxi trips would allow the City to capture some additional revenue from visitors to the City. ■ New York City charges \$0.50 per trip within the City and to/from surrounding suburbs to help fund the MTA (transit). At \$0.25 per trip, a Baltimore tax could generate just over \$1 million annually. ■ In lists of fare levels by major U.S. city, Baltimore typically ranks below other major east coast cities such as Boston, New York, Philadelphia, and Washington, DC. 	<p>Taxi usage is associated with transportation infrastructure needs, as well as tourism and hospitality programs.</p>
Billboard Tax	<ul style="list-style-type: none"> ■ Consistent with recently proposed City Council legislation, an excise tax on outdoor advertising could provide an additional source of revenue for the City derived from activity that is generally not a public benefit (and often considered a public nuisance). ■ Philadelphia has a tax of 7% on billboard revenues, and the State of New Jersey has a 6% billboard tax. In Canada, Toronto recently adopted a billboard excise tax structure (varying by size and type of outdoor advertising) projected to generate \$10 million per year for the arts, and cities including Montreal and Winnipeg have similar excise taxes. 	<p>Could potentially be linked to other policy goals such as arts and culture funding.</p>
Restaurant Meal Tax	<ul style="list-style-type: none"> ■ A restaurant meal (sales) tax, which is a common revenue source in other major cities, could be considered as an option to meet any local funding requirements for an expanded Convention Center and Arena project. ■ According to a March 2012 study by the Tax Foundation, Baltimore ranks tied for 46th among the 50 largest U.S. cities in terms of combined sales and supplemental taxes on restaurant meals – with just the 6.0% state sales tax applied. Every other major east coast city has a substantially higher sales tax on restaurant meals than the 6.0% State rate in Baltimore, inclusive of any supplemental tax rate where applicable: Boston (7.0%); Miami (9.0%); Philadelphia (8.0% plus a supplemental "liquor by the drink" tax of 10% on every retail sale of liquor or malt and brewed beverage dedicated to the City school system); New York City (8.875%); Washington, DC (10%). ■ State authorization would be required for such a tax. While the State of Maryland has historically reserved sales tax receipts for state use, a 0.5% Worcester County food and beverage tax is authorized for the resort area of Ocean City to pay off the bonds issued to finance the Ocean City Convention Center. ■ Based on a high-level review of restaurant tax receipts in comparable cities, this revenue source would preliminarily be estimated to generate a minimum level of approximately \$5 million annually in Baltimore. 	<p>Financing for hospitality sector assets and programs.</p>

Revenue Option	Structure/Notes	Potential Use(s)
Market-Based Revenue Opportunities	<ul style="list-style-type: none"> Market-based revenue opportunities are agreements between cities and private companies that provide payments for ancillary use of City property and assets. This concept may encompass advertising and corporate sponsorships, exclusivity arrangements, and rental agreements to use municipal real estate for cell phone towers or other purposes. Cities that have successfully implemented market-based revenue programs include San Diego, CA; Boston, MA; and Seattle, WA. 	<p>May generate general revenue and/or defray the cost of particular facilities used for such programs (e.g., as bus shelter advertising revenues are used for transit).</p>
Nonprofit Contribution Program	<ul style="list-style-type: none"> The presence of strong nonprofits is one of Baltimore's greatest strengths. At the same time, the City's revenues resulting from tax-exempt institutions are much more limited than in cities with commuter income and/or local sales taxes. Only the income taxes paid by those nonprofit workers resident in Baltimore derive to the City, and other directly attributable tax receipts – such as parking, energy (at a reduced rate for nonprofits), and telecommunications are modest. Baltimore has an existing nonprofit contribution agreement with 15 major health care and higher education institutions, but it is slated to phase out after FY2016. Now at \$3.4 million for FY2013 (down from \$5.4 million in FY2011 and FY2012), the contributions will decline to \$1.4 million in the final year of FY2016. As the current agreement expires, the City could explore opportunities for renewed collaboration. 	<p>In addition to enhancing general revenue, some contributions could also continue to be linked to the neighborhoods immediately surrounding nonprofit institutions.</p>
Inter-County Broadband Network	<ul style="list-style-type: none"> For FY2013, the City awarded \$2 million from the Innovation Fund for an inter-county broadband network initiative, led by the Mayor's Office for Information Technology. The project will replace old 800 MHz lines with a fiber-optic network to increase connectivity between City agencies and schools. The Office plans to seek revenue opportunities by leasing network access to local businesses and internet service providers. 	<p>General revenue.</p>
Conduit Fund Return on Investment	<ul style="list-style-type: none"> The City of Baltimore maintains and operates an underground conduit used by private companies for fiber-optic lines and other utilities. Currently, user charges support the cost of this service, with all revenues limited to spending on the conduit. While this is a positive asset for local commerce, a modest return on investment to the General Fund could help to diversify revenues. 	<p>General revenue.</p>
Regional Funding for Regional Assets and Challenges	<ul style="list-style-type: none"> The City and other local governments in Maryland have historically received state funding for transportation through Highway User Revenue. The local share of this revenue was sharply reduced in 2009 and 2010 to help balance the State budget, and while it has increased slightly since, this revenue source is still far below what was historically available for local transportation needs. The Infrastructure Investment section of this report outlines options for restoring a commitment to these needs, including a dedicated regional sales tax and new sources of statewide funding to restore Highway User Revenue to pre-downturn levels. Other cities nationally, including St. Louis, MO, Minneapolis, MN, and Pittsburgh, PA, also have regional funding sources for other types of regional assets – such as arts and cultural institutions, sports facilities, and parks and recreation. 	<p>Regional assets, such as transportation infrastructure, and arts, cultural, and recreational institutions and services.</p>



Key Challenges:
Infrastructure Investment

Findings and Options

- As in many older cities, Baltimore's aging infrastructure and new capital investment needs require funding beyond available existing resources.
- For example, the physical condition of Baltimore's schools has emerged as a major concern in recent years. While identified school needs still outstrip the local dollars available, the City has responded with the Mayor's Better Schools Initiative to more than double the City's annual commitment to school facility needs — from \$17 million to \$40 million per year. This initiative is launching significant progress toward school renewal and reconstruction, relying on dedicated new revenues (beverage container charge and a share of gaming revenues) to augment traditional City funding.
- Looming not far below the surface, Baltimore faces many other infrastructure needs — from road and bridge repair, to aging recreation and public safety facilities, to stormwater management and landfill expansion. Overall, just to meet the capital needs identified by City departments to keep basic assets operational while beginning to move toward a state of good repair, Baltimore would need to identify over \$100 million more per year for its General Fund capital program — and a cumulative total of \$1.1 billion across the full Ten-Year Financial Plan period.
- Along with general infrastructure needs, Baltimore has approximately 16,000 vacant and abandoned structures, a large majority of which are in distressed communities with limited market potential for reinvestment. While repair, rehabilitation, and attraction of private investment are important strategies for reclaiming vacant structures in neighborhoods of strength, the Planning Department estimates that more than 10,000 properties are located in challenged areas generally best-suited for clearance, greening initiatives, and other non-housing reuse.
- Further, growing Baltimore's economy will require some new capital investments — such as potential development of a new Arena and modernization of the Convention Center.
- In addressing this challenge, the City is constrained by its structural budget shortfall, as detailed in the Ten-Year projections within this Plan. During the economic downturn, City pay-as-you-go (PAYGO) capital funding from the operating budget was already sharply curtailed, and annual capital borrowing is bounded by the need to maintain responsible levels of debt and debt service.
- Compounding these difficulties, federal infrastructure funding since the stimulus program ended is generally in decline, and key State capital programs have been cut severely. Of particular note, Maryland's Highway User Revenues (HUR) for Baltimore and other localities statewide are down dramatically. For the City, total State transportation funding as of FY2013 is nearly \$100 million below peak levels, and PAYGO capital dollars from this source have dropped from \$73.4 million in FY2007 to just \$5 million in FY2013.
- To make progress against these challenges over the decade ahead, a set of recommended strategies and options has been identified:
 - As structural budget challenges are addressed, expand City PAYGO capital funding and debt-financed investment, while remaining focused on maintaining a balanced overall budget and affordable levels of debt.
 - Launch an expanded Blight Elimination initiative to significantly accelerate demolition of long-abandoned structures, to reinforce the strategies of the Mayor's Vacants to Value program.
 - Continue to build on the Better Schools Initiative, seeking State partnership in facility renewal.
 - Establish self-supporting enterprise funding for key environmental and greening goals, including stormwater and solid waste management.
 - Challenge City agencies to consolidate and reduce City-owned space to improve operating efficiency and reduce capital costs.
 - Forge private partnerships for economic development investments, with creation of new revenue sources that do not add to Baltimore's residential tax burdens, if additional revenues are needed to advance critical projects.
- While increased capital investment at the local level will have a meaningful impact, fully addressing needs — particularly for regional assets such as transportation infrastructure — will require partnerships at the regional, state, and federal levels.

■ As capital investment does increase, such construction projects (along with non-City initiatives such as Red Line construction) will create a once-in-a-generation opportunity for local economic stimulus. To fully capture this potential, it will be critical to coordinate on a collaborative, multi-stakeholder basis to link these projects to workforce development for City residents — generating stronger tax receipts in the near-term, while building a more skilled workforce for the long-term.

City Capital Needs

In recent years, capital spending levels for most of Baltimore's basic infrastructure has been driven not by an assessment of underlying needs, but primarily by a determination of the level of debt that can be afforded. In turn, once the level of available resources to be generated from debt financing has been identified, projects have then been prioritized within such parameters to the best extent possible — whether or not such funds are truly sufficient to renew and replace core assets.

Across City government, many Departments are now engaged in more formalized capital needs assessments, however, such analysis is generally a work in progress. At the same time, from the perspective of long-range financial planning, the City Ten-Year Financial Plan team feels strongly that it is critical to seek to gain some sense of the magnitude of such infrastructure challenges — even if only preliminary and inherently “rough.”

Accordingly, to gain a high level sense of the City of Baltimore's underlying capital investment needs, the Ten-Year Financial Plan project team surveyed the City's major departments about their capital needs. Departments were asked to provide their best estimates as to funding levels required to meet “minimum,” “reasonable,” and “optimal” funding levels, as defined below:

■ **Minimum** — Lowest level of funding that would meet critical needs in order to continue operational use of the asset category over the next 10 years. In addition to basic maintenance, this would include any critical major projects already identified as a high priority.

■ **Reasonable** — In addition to addressing critical needs, this level of funding would include the estimated funding required (a) to maintain the current, overall asset condition plus (b) if the current condition is below generally accepted standards for a “state of good repair,” to begin to work incrementally toward attaining adequate condition over time.

■ **Optimal** — The level of capital expenditure required to bring the asset category to a desired level operating condition, to maintain this condition level, and also to meet City's future capacity needs.

For certain smaller agencies not surveyed (City Planning, Pratt Library, and Mayoralty Related), the project team assumed an annual carry forward of FY2014 funding levels from the City's current 6-year Capital Improvement Program (CIP) after FY2013. In addition, funding for the significant facility needs of the Baltimore City Public Schools (BCPS) was treated as a challenge separate from this analysis, and only the historic City BCPS capital funding of \$17 million is included in this analysis — with any school needs beyond this level, as well as the Mayor's Better Schools Initiative to address these concerns, evaluated separately.

Given this methodology, the data received relies substantially on the best estimates and responses of capital program staff, and should be considered indicative rather than precise. Even with this caveat, however, there is little question that the magnitude of Baltimore's infrastructure underfunding is very large, and of major concern. Based on the high-level estimates received from City departments, capital funding included in the Ten-Year Financial Plan “status quo” baseline scenario would fall short of reasonable levels by over \$115 million in FY2014, rising above \$130 million by FY2016.

Shortfall in Baseline Capital Funding Relative to Estimated "Reasonable" Needs

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
Baseline Capital Funding										
General Obligation Bonds	\$50.0	\$50.0	\$50.0	\$50.0	\$50.0	\$50.0	\$50.0	\$50.0	\$50.0	\$50.0
County Transportation Bonds	\$0.0	\$15.0	\$15.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
PAYGO	\$9.7	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0
Total	\$59.7	\$73.0	\$73.0	\$58.0	\$58.0	\$58.0	\$58.0	\$58.0	\$58.0	\$58.0
Schools (excluding Better Schools Initiative)										
	\$16.7	\$17.0	\$17.0	\$17.0	\$17.0	\$17.0	\$17.0	\$17.0	\$17.0	\$17.0
Contributions to Civic Assets and Other Miscellaneous Projects										
City Planning	\$0.2	\$0.2	\$0.2	\$0.2	\$0.2	\$0.2	\$0.2	\$0.2	\$0.2	\$0.2
Library	\$2.0	\$1.5	\$1.5	\$1.5	\$1.5	\$1.5	\$1.5	\$1.5	\$1.5	\$1.5
Mayoralty Related	\$2.9	\$2.0	\$2.0	\$2.0	\$2.0	\$2.0	\$2.0	\$2.0	\$2.0	\$2.0
Subtotal: Schools, Civic Assets and Other Misc	\$21.9	\$20.7	\$20.7	\$20.7	\$20.7	\$20.7	\$20.7	\$20.7	\$20.7	\$20.7
Departmental "Reasonable" Funding Estimates										
Transportation										
Alleys and Footways	\$2.0	\$3.5	\$3.5	\$3.5	\$3.5	\$3.5	\$3.5	\$3.5	\$3.5	\$3.5
Bridges	\$2.8	\$15.5	\$15.5	\$15.5	\$15.5	\$15.5	\$15.5	\$15.5	\$15.5	\$15.5
Streets and Highways	\$6.1	\$32.0	\$32.0	\$32.0	\$32.0	\$32.0	\$32.0	\$32.0	\$32.0	\$32.0
Traffic Engineering	\$2.0	\$6.0	\$6.0	\$6.0	\$6.0	\$6.0	\$6.0	\$6.0	\$6.0	\$6.0
Street Lighting	\$1.6	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0
Development Agencies Program	-\$6.4	\$5.0	\$5.0	\$5.0	\$5.0	\$5.0	\$5.0	\$5.0	\$5.0	\$5.0
Subtotal: Transportation	\$8.1	\$65.0	\$65.0	\$65.0	\$65.0	\$65.0	\$65.0	\$65.0	\$65.0	\$65.0
Housing and Development										
Housing and Community Development	\$6.7	\$20.3	\$20.3	\$20.3	\$20.3	\$20.3	\$20.3	\$20.3	\$20.3	\$20.3
Demolition (Citywide)	\$2.3	\$18.0	\$18.0	\$19.5	\$19.6	\$19.6	\$19.6	\$19.6	\$19.6	\$19.6
Baltimore Development Corporation	\$4.7	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5
Downtown Partnership	\$0.4	\$3.0	\$3.0	\$3.0	\$2.0	\$2.0	\$1.0	\$0.5	\$0.3	\$0.3
Subtotal: Housing and Development	\$14.1	\$49.8	\$49.8	\$51.3	\$50.4	\$50.4	\$49.4	\$48.9	\$48.6	\$48.6
General City Infrastructure										
Solid Waste - General (including Landfill expansion)	\$1.7	\$5.5	\$5.9	\$5.2	\$4.9	\$5.1	\$6.1	\$3.2	\$3.2	\$3.2
Stormwater/Pollution Erosion Control	\$2.7	<i>Existing CIP assumes establishment of enterprise after FY2013</i>								
General Services	\$7.4	\$36.0	\$36.0	\$36.0	\$36.0	\$36.0	\$36.0	\$36.0	\$36.0	\$36.0
Recreation and Parks	\$3.8	\$13.0	\$13.0	\$13.0	\$13.0	\$13.0	\$13.0	\$13.0	\$13.0	\$13.0
Subtotal: General City Infrastructure	\$15.6	\$54.5	\$54.9	\$54.2	\$53.9	\$54.1	\$55.1	\$52.2	\$52.2	\$52.2
Total: General-Fund Supported "Reasonable"	\$59.7	\$189.9	\$190.3	\$191.2	\$189.9	\$190.1	\$190.1	\$186.7	\$186.5	\$186.5
Difference	\$0.0	-\$116.9	-\$117.3	-\$133.2	-\$131.9	-\$132.1	-\$132.1	-\$128.7	-\$128.5	-\$128.5

Of note, these estimates reflect annual funding needs over a Ten-Year period from General Fund supported dollars only. In many cases, additional intergovernmental funding is assumed to meet the overall costs of core capital investment.

Examples of capital needs include the following:

- Of Baltimore's more than 300 bridges managed by the Department of Transportation (DOT), 21 have been rated below a level of 50 on the bridge sufficiency rating index used by the Federal Highway Administration to evaluate condition. This reflects a state of repair that renders those bridges eligible for replacement, and indicates a serious need for reconstruction. Looking forward over the decade ahead, DOT estimates that another 35-40 bridges will likely require major rehabilitation, reconstruction, or replacement. Estimated costs to replace or reconstruct those bridges already programmed for near-term replacement typically range from \$10-30 million per bridge.
- DOT also maintains approximately 5,000 lane miles of roadways across the City. As of a major survey in 2008, 43% of the City's roads were rated to be in a "poor" state of repair based on pavement condition index standards, and funding for repaving and resurfacing has only been further reduced since that review. Currently, DOT has funding sufficient to repave only 200 lane miles or less per year out of the total 5,000, resulting in roadways falling further into disrepair. Not only does this result in poor street conditions, but it will also drive up long-term, life cycle costs, as roadways reach the point where resurfacing is no longer an option and full-depth pavement reconstruction (at several times the cost) becomes necessary.
- Within the next decade, in order to manage Baltimore's solid waste disposal needs, the City is projected to need to begin a major expansion the Quarantine Road landfill. Preliminary cost estimates are in the range of \$40 million, which would add another quarter century to the landfill's life span.
- City facilities are also aging, with many in disrepair. Overall capital needs for Baltimore's fire stations and related infrastructure alone, for example, are estimated to exceed \$20 million. This includes needed electrical system upgrades and fixed generator installations, deteriorated concrete within station bays and outside aprons and sidewalks, and basic working condition concerns at active stations. Overall, the

City's fire stations average over 60 years old, and the older half average more than 100 years old. In addition to significant deferred maintenance needs at these fire houses, given population shifts within Baltimore over the decades, some fire companies might be better sited in other locations that would provide for enhanced response times.

- To improve the City's Recreation and Community Centers, many of which are also in very poor, unsafe condition, a Mayoral Task Force developed a comprehensive plan in 2011 to provide a smaller number of upgraded facilities focused on Baltimore's youth — with other facilities beyond the City's capacity to adequately sustain being transferred to nonprofit and community partners. In turn, this transformational approach requires significant new capital investment — estimated by the Parks and Recreation Department to cost approximately \$40-50 million over the decade ahead — to fully develop this new, core network of ten model community recreation centers to serve as anchors for Baltimore neighborhoods.

Beyond the examples highlighted above, Baltimore faces major needs and opportunities regarding many other asset categories — from inner harbor infrastructure to neighborhood sidewalks and alleys. Where such capital needs are financed under an Enterprise Fund (most notably, for the City's water and wastewater system, and, going forward, stormwater management and related "greening" programs), they are not addressed directly in this Ten-Year Financial Plan process, which has focused on the larger, tax-supported General Fund. Nonetheless, these parallel Enterprise Fund issues are also critical, and merit independent attention.

In addition, several other priority areas — school facilities, blight elimination, and economic development investments in the City's hospitality sector — are separately outlined in more detail to follow.

One further capital program issue of note is that some City departments now use capital dollars for maintenance and other ongoing expenses that would ideally be funded from the operating budget. While generally capital-related, and supportable from PAYGO capital funds, it would provide greater overall transparency to shift these costs to the operating funds, as has recently occurred in some areas of Baltimore's budget.

Options

To begin to address such needs and Baltimore's overall infrastructure funding shortfalls, the City could consider drawing from the following mix of local approaches:

- **Expanded City PAYGO capital funding**, providing additional resources while maintaining some flexibility relative to fixed debt in the event of future budget strain.

- **Increased debt-financed investment**, while remaining focused on maintaining a balanced overall budget and affordable levels of debt, such that debt service costs fall within a parameter of approximately 10% or less of operating revenues, as further detailed in the "Addressing City Liabilities" section of this report.

- **Establishing self-supporting enterprise funding for key environmental and greening goals**, including stormwater and solid waste management:

- In the Operating Budget, this will create the opportunity for property tax relief.
- In the Capital Budget, this will free up resources currently planned for landfill and other solid waste capital needs, while ensuring that such environmental investments are properly funded.
- Already, the City's adopted FY2013-2018 six-year capital program assumes that stormwater costs will be enterprise-funded in the years ahead.

- **Deploying one-time resources from release of reserves toward accelerating key investments**. Under budget options outlined elsewhere within this Ten-Year Financial Plan:

- In FY2014, approximately \$43.5 million of non-recurring resources for PAYGO will become available from release of the Mobile Equipment Reserve (funding as of 7/2012) as the City shifts to lease financing for vehicles.
- Further, as early as FY2015, approximately \$13.5 million could be released from the Landfill Development Reserve if the City shifts the full funding for future landfill expansion to a newly established enterprise fund.

- **Challenging City agencies to consolidate and reduce facility costs** to improve operating efficiency and reduce capital costs:

- A key example of this approach involves the work of the City's Recreation Center Task Force, recommending

increased focus and investment to upgrade and maintain a manageable number of recreation facilities, while seeking outside partners such as the Boys and Girls Clubs of Metropolitan Baltimore to take over those centers challenging for the City to serve effectively.

- More generally, consolidating and optimizing the City's use of real estate for offices and general use is an important area of focus, particularly as the size of the municipal workforce decreases. Similarly, the City could reinvest some or all of the savings from other facility-related initiatives, such as energy conservation. Further, to better encourage such approaches, the City could expand a chargeback system for municipal facility costs to increase accountability and competitiveness, a concept already under development by the Department of General Services and Finance Department.

In the aggregate, such strategies hold the potential to achieve a significant increase in the City's basic infrastructure investment — particularly for core neighborhood facilities such as recreation centers and fire stations.

At the same time, Baltimore should also continue to actively pursue opportunities to build on such local investment through expanded collaboration:

- **Building stronger intergovernmental funding partnerships at the state, federal, and regional levels**, particularly for regional assets such as transportation infrastructure.

- **Forging private partnerships for economic development investments**, with creation of new revenue sources that do not add to Baltimore's residential tax burdens, if revenues are needed to advance critical projects.

- **Exploration of Public-Private Partnerships (P3)**, to the extent further analysis identifies worthwhile opportunities.

In the remainder of this "Infrastructure Investment" section, specific needs and strategies are outlined for four key areas of concern beyond general municipal facilities:

- Better Schools.
- Blight Elimination.
- Competitive Hospitality Sector.
- Transportation Infrastructure.

Better Schools

While the Baltimore City Public Schools (BCPS) are operationally independent of the City government, the City's General Fund nonetheless supports the BCPS and its students through multiple operating budget commitments totaling over \$280 million per year — from direct “maintenance of effort” payments, to school health services, to retiree benefits for school employees, to debt service on past capital projects, to a share of school crossing guard costs. These investments are all assumed to continue at current program levels in the Ten-Year Plan baseline, including teacher pension costs newly shifted from the State to the City in FY2013. In addition, the City has contributed approximately \$17 million per year to the BCPS capital budget to renew and replace school facilities.

A 2012 BCPS school facility study supports what Baltimore parents, teachers, and students have long known — too many of the City's aging schools are now in substandard condition. To address the identified deficiencies in general condition and educational adequacy, the preliminary capital investment needs are estimated at more than \$1.4 billion. When further Ten-Year Life Cycle costs are added, the total estimated need rises to nearly \$2.5 billion.

At the level of capital investment made in recent years, sufficient progress would not be made toward addressing these severe condition deficiencies. In turn, school facilities in poor condition can contribute to lower student achievement, higher absenteeism, and increased dropout rates — and can potentially pose threats to the health and safety of staff and students. School facilities can also impact the ability to attract and retain high quality teachers.

In contrast, high quality school facilities can have a positive impact on rates of student learning, attendance, and graduation — and are important for keeping young families in the Baltimore as their children reach school age, and in attracting new families to the City. With test scores rising in the BCPS, this is an important juncture for building on the District's momentum.

Accordingly, to jumpstart investment in rebuilding the City's schools, the Mayor and City Council committed to a “Better Schools Initiative” in 2012, projected to more than double annual capital funds from the City to over \$40 million, potentially leveraging over \$300 million in bonding capacity. Funding sources include:

- 5 cent beverage container fee, projected to generate more than \$10 million annually.
- 10% of the City's Video Lottery Terminal (VLT) revenues, expected to increase with the recent authorization of table games.
- Supplemental resources based on the City's contribution for school retiree benefit costs.
- Continuation of the base City capital contribution at approximately \$17 million.

Because key components of the Mayor's Better Schools Initiative were adopted in the FY2013 Budget, the impact of this major increase in investment is already included within the Ten-Year Plan baseline.

With this major new local funding commitment now established, the BCPS has worked from the findings of its 2012 school facility study to create its own Ten-Year Long Range Facilities Master Plan — involving a comprehensive mix of approaches including renovation of 136 existing school buildings, some new construction, and closure of 26 underused school buildings as improved facilities come on line.

To build on this expanded City investment, additional partnerships will be needed to further address the BCPS Long Range Facilities Master Plan, once developed. Options include pursuit of additional State school construction funding, development of a BCPS foundation and private sector capital campaign, and increased financing flexibility to make the best use of those resources that are identified.

Expanded Blight Elimination

Launched in November of 2010, the Vacants to Value (V2V) initiative encourages reinvestment in neighborhoods impacted by blighted properties by strengthening code enforcement, promoting rehabilitation, undertaking demolition, and streamlining the sale of vacant city property.

Through early February 2013, the V2V initiative has made an impact: the sale of city owned vacant properties increased more than fivefold between FY2010 and FY2012 (from 100 to over 500 sales); more than 1000 citations have been issued to owners of vacant buildings and over 900 court receiverships have been filed or are in progress, prompting in excess of \$48 million in private investment; construction is underway or completed on over 900 previously vacant structures; 123 home buyer incentive grants at

\$10,000 each have been awarded and 700 vacant lots have been assigned to non profits and neighborhood groups for greening activities. In addition, 575 vacant and blighted properties have been demolished by the City while partners including EBDI and Telesis have demolished another 250.

This new V2V momentum holds tremendous potential for the City. In stakeholder interviews conducted for this Ten-Year Financial Plan, the blight of vacant and abandoned properties was cited as a major impediment to the City's progress by community leaders, economic development professionals, Police and Fire department leaders, and public health and environmental officials:

- Eroding the value of neighboring properties, and sapping the vitality of surrounding communities.
- Creating public safety hazards.
- Contributing to unhealthy environmental conditions from debris and the higher surface temperatures ("heat islands") associated with a lack of green space.

While too uncertain to be specifically quantified for the Ten-Year Financial Plan, reduced blight would also be projected to generate some positive, long-term fiscal impacts. Indirectly, such neighborhood improvement would help to stabilize and strengthen property values and the tax base in surrounding areas. In addition, less blight could also help to reduce the incidence of public safety calls, with some potential savings in terms of fuel usage and workplace injuries (although staffing levels would likely remain unchanged).

As of Q1 2012, the Planning Department estimates that Baltimore has approximately 16,000 vacant structures, a large majority of which are in highly distressed communities with limited market potential for reinvestment. While V2V initiatives to promote repair, rehabilitation, and attraction of private investment are important strategies for reclaiming vacant structures in neighborhoods of strength, there are an estimated 10,000 or more properties in challenged areas that are best-suited for clearance, greening initiatives, and other non-housing reuse.

Accelerating the demolition and re-use of these properties will not only realize available direct benefits of clearing current vacant and abandoned properties more quickly, it is also expected to help stem the pace of other neighboring properties becoming blighted in future years.

Accordingly, starting in January 2013, the City has committed to undertake a substantial ratchet upward in investment over the past two years to eliminate at least 3,000 vacant properties over the next three years — half by demolition, and half through expanded rehabilitation.

Fulfilling this commitment — and then building on it — will require a major new level of investment. In the FY2013 Capital Budget, there is just \$250,000 in general funds for emergency demolition, \$2,050,000 in debt financing and \$685,000 in Community Development Block Grant (CDBG) spending for planned demolition citywide, and some additional funds for demolition associated with various larger-scale redevelopment projects.

In contrast, Baltimore Housing and the City Planning Department estimate that it would cost approximately \$165 million to clear just the most cost-efficient subset of the City's vacant structures — representing only about one-third of the total number — while noting that marginal costs beyond this level would ratchet up substantially due to factors such as more complex acquisition and relocation needs. These priority "demolition clusters" were identified as part of a preliminary opportunity assessment, using GIS analysis to determine groups of structures that could be more cost-effectively cleared based on a set of factors including condition, density, contiguity, the rate of home ownership in the surrounding areas, crime and fire response rates, surface temperatures, proximity to redevelopment areas and anchor institutions, and distance from green space and the storm water system.

To ratchet up from a FY2013 investment level of just a few million dollars in demolition funding to quickly generate a meaningful surge of neighborhood improvement, the City could consider establishing a coordinated V2V Blight Elimination Fund to be used for demolition of vacant and abandoned properties, and associated costs such as acquisition, relocation, and conversion to reuse. Potential funding sources (inclusive of prior-year carryover for ongoing major development projects) include:

- A majority of the City's \$10 million allocation from the Maryland Attorney General's Office Mortgage Servicing Settlement, announced in 2012.
- State Capital Funds.
- Funding from certain CDBG-eligible projects.

- Housing Choice voucher program funding for relocation.
- Video Lottery Terminal (VLT) proceeds, much of which is restricted to the Park Heights Master Plan Area.
- Continuation and expansion of General Fund capital improvement program demolition funding, including expanded PAYGO funding and the potential release of certain reserves.
- Proceeds from the sale of vacant City-owned properties.
- Increased federal, state, and foundation partnerships beyond the State Capital Fund and CDBG resources already dedicated. For example, the proposed Project Rebuild Act at the federal level would authorize \$15 billion nationwide to replace the prior Neighborhood Stabilization Program, with demolition as an eligible use.
- Dedicated new revenue sources, such as increased vacant property and related code enforcement charges and penalties, and potential improvements to the tax lien sale process.

By launching a major acceleration of the demolition component of the V2V program, the City could make a significant impact on the level of overall blight in highly distressed communities, and help to curtail its spread into neighborhoods where property renovation remains viable — while working more cost-effectively by capturing the economies that would come from scaling the initiative.

Beyond capital costs, it is also important to note from a fiscal perspective that lot maintenance costs for the Department of Public Works in the City's operating budget could also increase following expanded demolition, to the extent that more vacant lots are created and retained under public ownership. To some extent, such incremental costs might be offset by sale of properties, and — over time — reduced demand for emergency demolition and cleaning and boarding expenditures. In addition, under a National Fish and Wildlife Foundation grant, the City is now exploring development of a program to establish a "credit" mechanism for developers to meet their storm water management obligations at sites without sufficient, cost-effective on-site options by paying into a fund for the ongoing maintenance of cleared lots used for storm water management. Along with supporting blight elimination, such a program would improve the viability and cost-effectiveness of development within the City more generally.

Competitive Hospitality Sector

Baltimore's hospitality and tourism sector is a major driver of the City's economy, creating jobs and career paths for workers of varying skill levels, and contributing to Baltimore's overall competitiveness and quality of life. Within this sector, key existing assets — most notably, the First Mariner Arena and Baltimore Convention Center — have been productive for many years, but are now aging and decreasing in competitiveness.

Accordingly, looking forward, the State and City are exploring opportunities to develop the next generation of hospitality sector assets under a public-private partnership — potentially resulting in a more contemporary Arena, expanded Convention Center, and new hotel. While some public investment is anticipated, such projects would also be expected to leverage significant private funds. Building on this opportunity, the Greater Baltimore Committee has further proposed redevelopment of Rash Field at the inner harbor into an urban park with a pedestrian bridge connecting the harbor's south shore to the north shore.

To assess such opportunities, at the request of the State and the City, the Maryland Stadium Authority engaged a preliminary market and economic analysis of Baltimore Convention Center Expansion by an industry consultancy, published in February 2012. Key findings from this assessment included:

- Due to the age of Baltimore's facilities and competitive market pressures, event activity is projected to decline over time if nothing is done.
- Significant job creation would result from the proposed investments, preliminarily estimated at 2,100-2,800 incremental, new jobs in Maryland, of which 1,900-2,500 would be in the City of Baltimore.

Incremental tax revenues gains were also projected, with the largest benefit for the State — which captures all of the sales tax benefit from these facilities and a majority of the income tax. On a gross basis, revenue gains in a stabilized year were projected to reach \$11.7-\$15.5 million for the State, and over \$5 million annually for the City, with partially offsetting increases to the public subsidies for the facility, ranging from \$487,000-\$695,000 for the City and \$975,000-\$1,392,000 for the State.

Based on this analysis, further pursuit of a new Arena and related hospitality investments is important for the Baltimore region not only to help support growth and a stronger tourism sector,

but also to preserve this core industry from possible erosion and decline.

At the same time, given the overall fiscal pressures outlined throughout this Ten-Year Plan, it will also be important to advance these City tourism and hospitality projects without further burdening the City's general tax base. To achieve these twin goals, the following options are recommended:

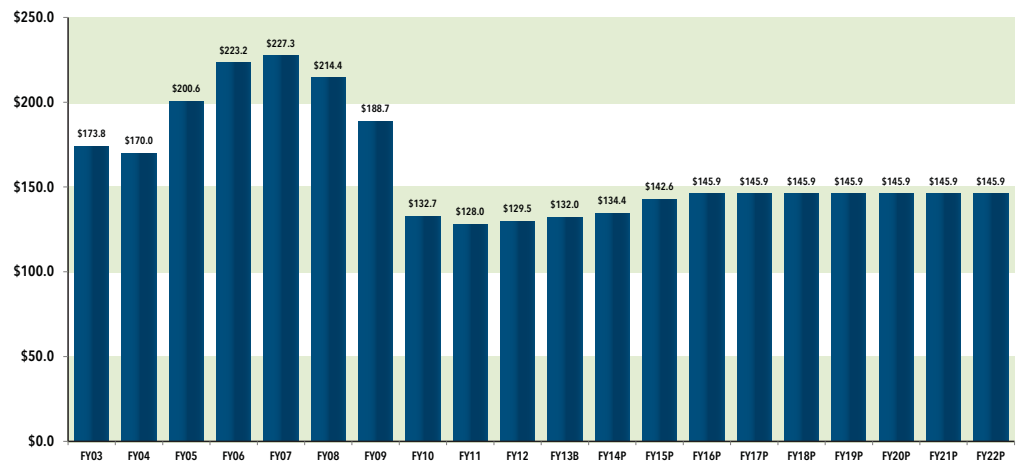
- Secure maximized private funding for Arena and hotel development before moving forward.
- Pursue significant State of Maryland funding partnership, particularly in light of the higher proportionate revenue return on investment for the State.
- Establish a new, sector-based revenue stream for any City funding required to make these projects happen, rather than relying solely on inherently uncertain projections of incremental receipts from existing taxes. As outlined in the "Tax Competitiveness" section of this report, options might include a restaurant meals tax (as has helped to finance convention facilities in Ocean City, MD) and/or a billboard tax, which might also be used to support other arts and cultural activities.

State and Regional Partnerships for Transportation Services and Infrastructure

As outlined earlier in this section, regional transportation needs — for bridge safety, roadway conditions, and related systems — are among the most critical infrastructure challenges facing Greater Baltimore, with among the largest funding shortfalls.

Historically, the City and other local governments in Maryland have received substantial State funding for transportation infrastructure and programs through Highway User Revenue (HUR) supported primarily by gas tax and vehicle-related fees. In recent years, however, the local share of this revenue was sharply reduced to help balance the State budget, and remains far below past levels. Further, because some of this funding is used to support transportation-related costs in the City's

Highway User Revenue (City of Baltimore) - FY2003-FY2022 (projected)



operating budget, these reductions have had the greatest impact on PAYGO capital resources for transportation infrastructure:

- The City's FY2013 budgeted Highway User Revenues (\$132.0 million) are nearly \$100 million below the FY2007 peak (\$227.3 million).
- PAYGO capital dollars from Highway User Revenues declined from over \$70 million in FY2007, to zero for FY2010 and FY2011, and remain at only \$5 million in the FY2013 Budget.

In November 2011, a State Blue Ribbon Commission on Transportation Funding issued a report recommending \$870 million in net new additional revenues for transportation across Maryland, over and above current annual revenues of \$3.5 billion. Further, the report recommended incremental restoration of statewide HUR to prior levels. In evaluating this report, however, the Department of Legislative Services calculated that even the Commission's recommended increase would fall short of the funding needs for all identified expenditure program goals. [While the Governor also proposed an alternative approach to fund local transportation projects via extension of the sales tax to gas, no legislative action was taken — and this plan would also have fallen well short of prior funding levels even if it had been approved

Given this lack of statewide progress to date, the Ten-Year Financial Plan baseline projects only modest growth in HUR funding for the City

Fundamentally, this transportation funding shortfall is simply beyond the City's capacity to make up using local resources alone. Baltimore's tax burdens are already too high to be

competitive, and the service demands on the limited resources available too great. At the same time, these transportation networks are vital for commerce and daily life within the City, the region, and Maryland as a whole. To address this critical challenge, State and/or regional partnership will be essential:

- At a State level, greater transportation funding must be a high priority — not only for the City's infrastructure networks, but also for Maryland's counties, and major highway and transit projects across the State. Within the first few years of the Ten-Year Plan period, Statewide resolution to this funding challenge is of critical importance.
- On a regional basis, an alternative approach used commonly nationally is a dedicated sales tax for transportation. In Austin and Dallas, TX, for example, local transit agencies are among multiple Texas systems with a regional sales tax (each at 1%). In 2011, Durham County, NC joined the Charlotte area as the second North Carolina region to approve a 0.5% local option sales tax for transit (and also approved a 0.25% tax for school improvements). In 2004, Denver, CO voters approved a 0.4% increase to a regional sales tax for public transit expansion (a further increase to 0.8% has been considered, but not yet advanced to the ballot). Further, San Diego County, CA has a half-cent tax for local transportation projects that was first approved by voters in 1988, and then extended in 2004 for another 40 years.

As a supplemental, one-time resource, the City could also explore potential Public Private Partnerships (P3) involving the sale or leasing arrangements for City-owned assets. For example, transfer of a subset of the City's off-street parking garages (excluding those in key locations for future economic development, or with other complications), could potentially generate a very significant, one-time cash infusion, remove the City from a portion of a business with an active, private market, and enable the Baltimore Parking Authority to better focus on other initiatives such as on-street parking programs and technology implementation.

Before proceeding with such an initiative, a detailed feasibility study would be required to fully assess such considerations as bond covenants and private-use limitations

for facilities constructed with tax-exempt financing (and any associated debt defeasance requirements), facility condition and anticipated capital requirements, air rights, local market dynamics, and other characteristics that could enhance value. Although short-term proceeds may be attractive, such benefits must be carefully weighed against the loss of recurring revenue streams and the impact on the continued quality of parking options within the City.

Baltimore Jobs

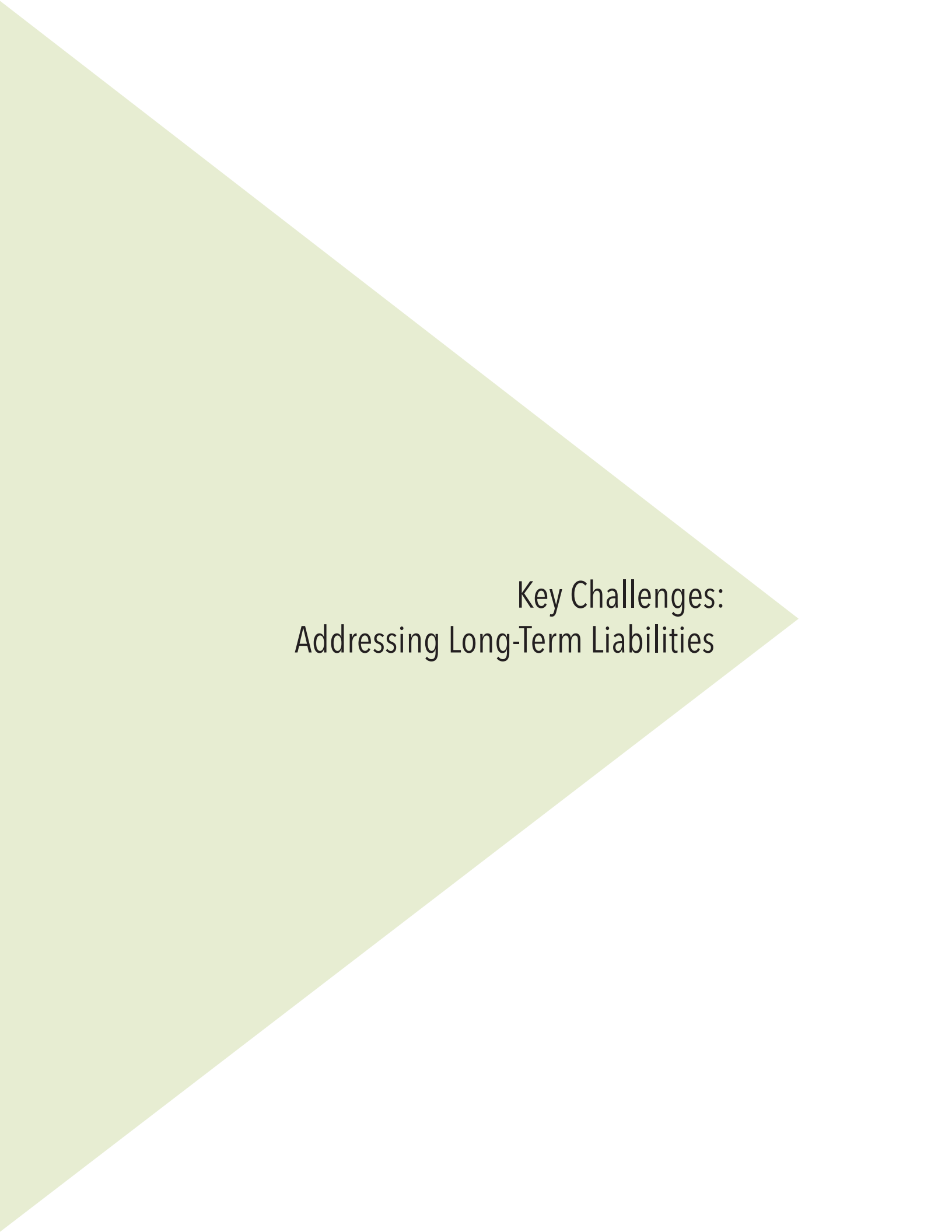
As the City and its partners increase investment to rebuild schools, renew basic infrastructure, develop new "green" stormwater systems, advance community redevelopment, enhance hospitality assets, and accelerate blight elimination, such projects (along with non-City initiatives such as Red Line construction) will create a once-in-a-generation opportunity for local economic stimulus.

While these are major opportunities for the region regardless of who works on the projects, and are also anticipated to create a significant number of job opportunities for City residents:

- Baltimore will receive no income tax from those construction workers who live outside the City.
- Baltimore will receive no sales tax from dollars spent at the project sites.
- Baltimore will receive no direct property tax gains from projects to be owned by governmental and nonprofit institutions.

Alternatively, if this decade of new investment can be leveraged to create an even greater number of jobs for City residents, then Baltimore will receive stronger tax receipts in the near-term, while building a more skilled workforce for the long-term

To fully capture the potential that such a wave of new project would create, it will be critical to coordinate on a collaborative, multi-stakeholder basis to link these projects to workforce development for City residents.



Key Challenges:
Addressing Long-Term Liabilities

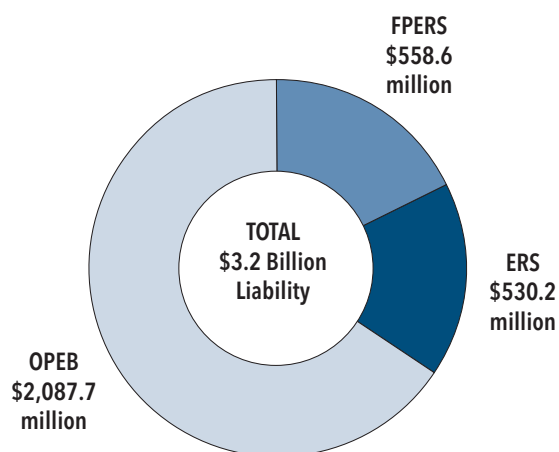
Findings and Options

- The City of Baltimore has long been recognized for good fiscal stewardship. As the rating agency Moody's Investors Service noted in its most recent (January 2013) credit report on the City, Baltimore's "sound financial position is supported by an established record of operating stability, proactive management, and recently-enhanced fiscal policies."
- Consistent with this financially responsible approach, it will be important for the City to make progress over the decade ahead with reducing its long-term liabilities and leaving behind a stronger "balance sheet" that does not overburden future generations nor inhibit opportunities for growth.
- As outlined in the "Infrastructure Investment" section of this report, one major, long-term stewardship concern is the need to address historic underfunding of the renewal and replacement needs associated with the City's capital assets. At the same time, while some additional borrowing may be needed to fund this infrastructure investment, it is also important that overall debt burdens and liabilities be limited to manageable levels within a framework of fiscal responsibility. Baltimore's conservative financial approach has long been a credit strength for the City — and is critical to maintaining market access at affordable rates.
- In addition to moderate debt burdens, Baltimore's reserve levels and policies are consistently cited as a positive and very significant ratings factor. As part of improving the City's long-term financial position, it will be important to further build the Budget Stabilization Reserve (BSR) toward the City's target level of 8.0% within the Ten-Year Plan period.
- As with many governments nationally, retiree benefit liabilities are also an important area of concern. As of the City's FY2011 actuarial valuations, Baltimore had an aggregate unfunded retiree liability of more than \$3 billion — including actuarial shortfalls in the City's Fire and Police Employees' Retirement System (FPERS - \$558.6 million), Employees' Retirement System (ERS - \$530.2 million), and non-pension Other Post-Employment Benefits, primarily retiree medical coverage (OPEB - \$2.1 billion).
- New Governmental Accounting Standards Board (GASB) accounting rules will further highlight these retiree benefit sustainability challenges, as more conservative approaches are coming into place for recognizing these liabilities in public

sector financial statements. Similarly, the major credit rating agencies now also have a growing focus on retiree benefit funding and other liabilities beyond just debt service.

- As outlined in the "Structural Budget Balance" section of this report, pension and retiree healthcare benefit reforms will not only help to reduce the immediate affordability challenges of rising City contribution requirements, but such modifications can also improve the security of these benefits for the long-term.
- At the same time, Baltimore can also consider funding improvements to further strengthen its retiree benefit program sustainability. Options include: basing contributions to the City's pension plans on more conservative actuarial assumptions; increasing pre-funding levels in the City's dedicated OPEB Trust; and, exploring with the Baltimore City Public Schools (BCPS) opportunities to reduce the City's liability for retiree healthcare associated with school employees hired since the BCPS became independent in 1997.

**Unfunded Pension and OPEB Liabilities
(FY2011 Valuations)**



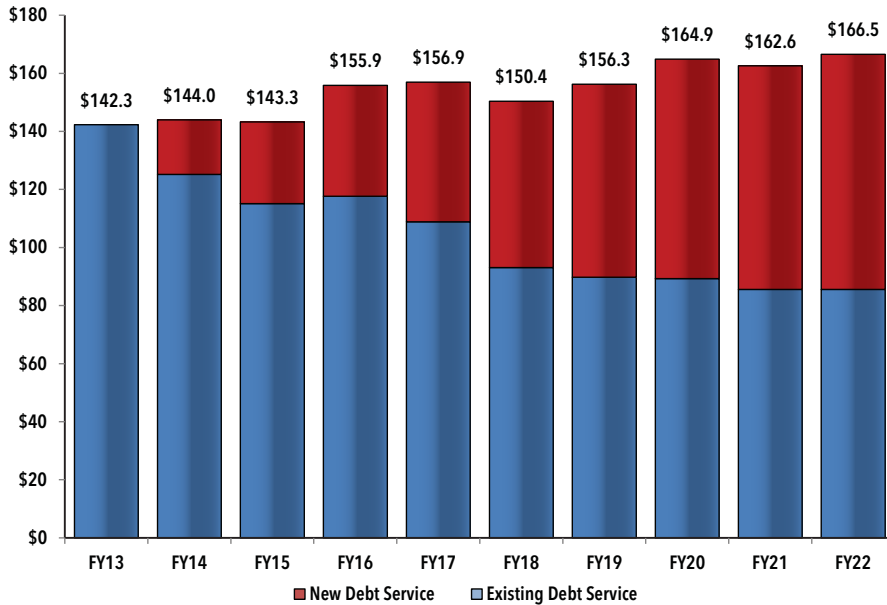
Note: The small Elected Officials' Retirement System, not shown, was above 100% funded as of FY2012 by \$1.6 million.

Major Challenges and Opportunities

Manageable Debt

Existing General Fund debt service as of FY2013 is budgeted at 9.1% of revenues. As a general parameter, the City seeks to maintain debt service below approximately 10% of revenues,

**Existing and Projected Baseline Debt Service
FY2013 (budget) to FY2022 (projected)**



New debt service shown reflects baseline scenario G.O. bonds, County Transportation Bonds, and Conditional Purchase Agreements. Existing debt service also includes all TIF debt service, MILA Loans, Bond Anticipation Notes, and costs of issuance.

consistent with good practice nationally. At current levels, the City is somewhat below this target upper bound, and debt service is scheduled to remain moderate over the next few years at baseline levels of issuance, as shown in the chart above. Further, much of the increase that is projected is driven by vehicle lease costs associated with the City's new fleet replacement program (see the "Structural Budget Balance" section of this report for more details) anticipated to be substantially offset by fuel and maintenance savings in the operating budget.

All other factors being equal, Baltimore's moderate debt levels and conservative repayment structure create some capacity for additional financing above these baseline levels to help address infrastructure investment goals. At the same time, however, given weaker economic factors than most other cities with similar credit ratings, it is important for Baltimore to maintain overall debt levels within the moderate range with a conservative structure.

To further minimize Baltimore's debt-related exposure, the City's Finance Department has developed a budget-neutral plan to take advantage of the current, low interest rate environment by refinancing certain existing variable rate debt and derivatives with more predictable fixed rate bonds. Identified as an initiative during the period of the Ten-Year Financial Plan's development,

this credit-positive debt restructuring was successfully executed early in 2013, and will further stabilize the City's already sound debt profile.

Healthy Reserves

One of the most important "best practices" in financial management is the maintenance of healthy reserve levels as a contingency against unforeseen events and to provide liquidity for stable cash flows. As the Government Finance Officers Association recommends: "It is essential that governments maintain adequate levels of fund balance to mitigate current and future risks (e.g., revenue shortfalls and unanticipated expenditures) and to ensure stable tax rates. Fund balance levels are a crucial consideration, too, in long-term financial planning." Such budget risks can include severe economic downturns, extreme weather events and natural disasters, and other emergency conditions.

In 1993, the City of Baltimore established a Budget Stabilization Reserve (BSR) consistent with such national best practices, and met the initial BSR target funding level of 5% of annual revenues three years earlier than originally anticipated. In 2008, the City's Board of Estimates strengthened the BSR policy by increasing the target reserve level to a minimum 8% of the subsequent year's operating budgets — with the use of such funds limited to addressing unanticipated and uncorrectable mid-year operating deficits, and featuring a further requirement to adopt a restoration plan should the BSR be drawn upon.

As of the City's audited FY2011 financial statements, the BSR totaled \$87.9 million, equivalent to 5.7% of operating revenues, and unaudited preliminary results indicate modest further growth as of the end of FY2012. For FY2013, the City has budgeted a further \$2 million contribution to this reserve, working incrementally toward the 8% policy target. As Moody's Investors Service noted in its 2013 Baltimore ratings report, the "enhanced policy affirms the city's long-term focus on operating stability and financial flexibility."

Going forward, it will be important to continue to maintain such stability and flexibility — and to work to reach the 8% BSR funding target within the Ten-Year Plan period.

Pension Funding

As of the FY2011 actuarial valuations, as shown in the table below, the City's two major pension plans are both underfunded — with an aggregate unfunded liability of nearly \$1.1 billion.

	Fire and Police Employees' Retirement System (FPERS)	Employees' Retirement System (ERS)
Valuation Date	June 30, 2011	June 30, 2011
Total Actuarial Accrued Liability	\$3,104,805,314	\$1,940,447,224
Unfunded Actuarial Liability	\$558,568,855	\$530,236,165
Funded Ratio	82.0%	72.7%

Long-term pension funding challenges are a growing concern nationally, with new Governmental Accounting Standards Board (GASB) accounting standards and evolving rating agency evaluation methodologies expected to further highlight actuarial risks.

In June 2012, the Governmental Accounting Standards Board (GASB) adopted two statements, GASB 67 and 68, to improve the accounting and financial reporting of state and local government pension plans.¹ Under these new guidelines, governmental employers that sponsor a pension plan or participate in a multi-employer plan will be required to report pension obligations and costs beginning in FY2015. According to GASB, these new standards were designed to improve and increase the transparency and comparability of pension reporting data across jurisdictions, resulting in a more complete representation of the full impact of unfunded pension liabilities.

Highlights of the new GASB Statement 67 (financial reporting) and GASB Statement 68 (pension accounting) include:

- Requiring governments to report their unfunded pension liabilities² on their balance sheets, rather than as notes to their balance sheets. Some underfunded plans will produce large balance sheet liabilities, even though the plan sponsor has been contributing the full Annual Required Contribution (ARC).
- Eliminating or reducing the amortization periods over which certain changes in Net Pension Liability can be spread, which will significantly increase annual pension expense volatility.

- Possibly reducing the actuarial discount rate currently used by plans, if the plan is failing to systematically collect enough contributions to avoid running out of money over time. As long as projected assets including future contributions exceed the projected benefit payments, the employer can continue to use its long-term expected rate of return. Once that threshold is crossed, however, the employer will be required to discount the projected benefit payments using a (typically much lower) municipal bond index rate. The use of lower discount rates could substantially increase the Unfunded Pension Liabilities.
- Requiring use of the Entry Age Normal actuarial method, the most common of several accepted actuarial approaches, to determine the total pension liability for accounting purposes. For Baltimore (and many other governments) that now use alternative actuarial methods to determine contribution rates for some of their retirement systems, this will result in different liabilities being reported for funding and accounting purposes.

While many government employers have traditionally used the ARC as the basis for contributions to their plans under the current rules, these new GASB requirements will not automatically affect the funding policy of a plan, which actuarially determines an employer's contribution. In fact, with many systems, it is anticipated that separate funding and accounting calculations will be used, as the new accounting rules could otherwise lead to much higher costs and more volatile funding amounts.

Even if not directly impacting funding, however, the new accounting changes will completely alter the balance sheet measure of a plan's unfunded liability. Further, for most governmental plans, the other changes included in the new GASB standards will mean that the volatility of the plan's unfunded liability — and, in many cases, the unfunded liability and the annual pension expense reported — will also increase sharply.

In parallel with the GASB changes, the major credit rating agencies are also taking steps to enhance their evaluation of pension liabilities across jurisdictions. Of particular note, in July 2012, Moody's proposed a new methodology for public comment to be used in their credit rating assessments.³ While not yet formally adopted, this proposal reflects a much greater focus on retiree benefit liabilities. In some areas, Moody's proposed changes match the new accounting standards set forth in GASB

¹ GASB 67 & 68, "Financial Reporting for Pension Plans" and "Accounting and Financial Reporting for Pensions", June 2012.

² Unfunded Pension Liability is determined as the difference between the total pension liability and the pension assets.

³ Moody's Investor Service, "Adjustments to US State and Local Government Reported Pension Data," July 2, 2012.

68. In other areas, however, Moody's approach would adopt an even more conservative perspective on these liabilities — most notably, adjusting accrued actuarial liabilities for comparative purposes based on a high-grade long-term corporate bond index discount rate (5.5% for 2010 and 2011) that will typically result in much higher estimated liabilities than those calculated based on long-range investment return assumptions.

As previously outlined in the "Structural Budget Balance" section of this report, a series of potential benefit reforms identified through this Ten-Year Plan development process and independent analysis conducted by the Segal Company could serve to strengthen the health of Baltimore's retirement systems through measures including establishment of a contributory structure for the ERS plan and greater risk-sharing in the benefit design for new hires.

In addition, the Ten-Year Plan baseline includes an assumed reduction in the investment return assumption for FPERs from 8.0% to 7.75%, consistent with the Board's recommendation and national trends. This adjustment, which follows a parallel change in the ERS plan in 2011, will lead to larger City contributions to improve plan sustainability.

OPEB Funding

As of FY2011, the City of Baltimore had an estimated OPEB liability of more than \$2.2 billion — of which nearly \$2.1 billion was unfunded. Over just the past two years, however, the City has taken multiple actions that have significantly reduced this underfunding that captures increased federal subsidies.

- Redesign of the City's medical plans and increased cost-sharing for prescription drug coverage.
- Improved management of the prescription drug benefit, including prior authorization, quantity controls, and step therapy.
- Establishment by the City's Human Resources Department of a cost-effective Employee Group Waiver Plan structure for Medicare drug coverage that captures increased Federal subsidies.
- Adoption of new retirement eligibility requirements under the Fire and Police Employees' Retirement system.
- Continued contributions to the City's OPEB Trust above the levels required to pay benefits for current retirees.

As a result, significant reductions are anticipated in the City's OPEB liability when the FY2012 valuation is completed early in calendar 2013.

Nonetheless, Baltimore's OPEB Trust is still severely underfunded, and the remaining long-term liability continues to pose a major long-range challenge for the City's financial health. Further, much as has just occurred with pension accounting, it is likely that GASB will propose new OPEB accounting standards within the next several years requiring more conservative recognition and reporting of OPEB liabilities in governmental financial statements.

To help address this challenge, several options are available — both to further reduce the City's OPEB liability for its own employees, and also to lower the portion of the liability associated with BCPS retirees.

Direct City OPEB Liability Reduction

Because the City provides subsidized pharmacy coverage to Medicare eligible retirees, it is important that the City develop a strategy to coordinate its pharmacy coverage with the evolving Medicare Part D retiree drug program. To date, the City has effectively captured available savings through strategies such as application for available federal retiree drug subsidies and establishment of an Employer Group Waiver Plan that improves coordination with Medicare pharmacy coverage.

Looking forward, following enactment of the federal Patient Protection and Affordable Care Act (PPACA), the Medicare Part D program is now being expanded with additional coverage that provides an opportunity for further, significant savings. Under the original Medicare Part D benefit design, there was a coverage gap commonly known as the "donut hole," such that beneficiaries would pay 100% of costs between the initial coverage limit and the maximum out of pocket threshold.

With the passage of the PPACA, however, cost sharing in the "donut hole" will be gradually reduced from 100% to 25% of costs over the years between 2011 and 2020, as shown in the table that follows. In addition, pharmaceutical manufacturers will be providing a 50% discount on the ingredient cost for "applicable" drugs (i.e. brand drugs for the group of Pharma companies in the program) in the donut hole.

Maximum Member Coinsurance for Non-Applicable and Applicable Drugs		
Year	Non-Applicable	Applicable
2011	93%	50%
2012	86%	50%
2013	79%	47.5%
2014	72%	47.5%
2015	65%	45%
2016	58%	45%
2017	51%	40%
2018	44%	35%
2019	37%	30%
2020 & later	25%	25%

As the coverage gap closes under national health care reform, federally subsidized coverage will become available that is equivalent to that now funded by the City. By 2020, Medicare Part D enrollees will have a 25% coinsurance on all costs above the deductible — and an out-of-pocket limit of about \$3,000 (after which Federal catastrophic reinsurance becomes available). As a result, the City could then phase out its post-employment prescription drug coverage, as retirees will be able to purchase their own plan for about the same cost as their current 20% premium share.

Further, if this change is announced now, the City will be able to adjust its OPEB actuarial valuation accordingly and substantially reduce its reported liability — much as the State of Maryland has already recently done. In turn, the City would be projected to be able to meet its OPEB actuarially required contribution (ARC) under current accounting standards in FY2014 and begin to make meaningful progress toward funding this liability with supplemental contributions above the costs for retirees already receiving benefits. Further, if OPEB funding levels are continued at a consistent level after the City's gross costs ratchet down in 2020, this will result in significant progress toward reducing the long-range OPEB liability.

In addition to improved Medicare Part D coordination, the City might also explore the opportunity to move post-65 retirees to the new Standard plan while changing the Medicare coordination method to “carve-out.” Under the current (high) plan, cost-sharing is very limited, and the City's healthcare provider uses the coordination of benefits approach, which results in the plan and Medicare paying 100% of medical claims. If the City were instead

to move to the Standard plan with a “carve out” approach, retirees would have the same deductible and coinsurance payments in the Standard plan both before and after enrolling in Medicare. As a result, the value of the deductibles would be preserved, and the cost of the plan would be lowered. In turn, the lower plan cost results in reduced premium costs for retirees, as well as lower costs to the City.

Baltimore City Public Schools (BCPS) OPEB Liability

In 1997, the BCPS separated from Baltimore City government. Since the separation, the City has continued to bear the cost and liability of health insurance benefits for BCPS retirees, budgeting \$28 million for the current medical and prescription drug costs of former school employees in FY2013. Of the approximately 21,000 participants in the City's retiree health benefit program, about 7,000 are former BCPS employees.

Until recently, all of the BCPS retirees receiving City-funded retiree medical coverage were individuals hired before the 1997 separation, when BCPS was a department of City government. Increasingly, however, prospective BCPS retirees will have been hired since the schools became an otherwise independent entity. Accordingly, if the City and the BCPS were able to negotiate reasonable terms for the transfer of this responsibility for post-1997 hires, the City's long-term risk exposure would be reduced — and responsibility for funding the benefit better aligned with the organization that now manages these employees. Under this approach, the City would still continue to provide coverage for those hired prior to 1997.

Of the City's overall actuarial OPEB liability, more than a third is attributable to BCPS employees and retirees. For those BCPS retirees hired since 1997, the full OPEB actuarial liability under the current plan structure is estimated by Hay Group at \$91.9 million.

Much as the City is pursuing cost containment initiatives to manage its liability associated with retiree healthcare downward, BCPS OPEB costs can potentially be lowered while still providing competitive benefits.

Because relatively few of these post-1997 BCPS employees have yet retired, the Ten-Year cash flow savings to the City from fully transferring this liability to the Schools would be modest — estimated at \$1.0 million in FY2014, growing steadily to \$5.2 million by FY2022. Nonetheless, from a longer-range perspective,

benefit funding responsibilities would be better aligned with the organization managing these workers, and growing City financial exposure to a liability it does not control would be eliminated.

At the same time, if this option is pursued, it will be important to avoid imposing any undue burden on the BCPS so that the financial capacity of the schools to educate Baltimore's children is not weakened. In this regard, the City could potentially transfer a portion of the accumulated assets in its existing OPEB Trust to the BCPS to help fund these benefits. If this transfer were made in an amount equivalent to the City's current level of prefunding, approximately \$12.1 million would be shifted.

Given that this prefunding level falls below the desired actuarial levels (as is the case for most OPEB prefunding among public employers nationally), a somewhat larger transfer could be considered to provide additional assistance to the BCPS with long-range funding.

Along with the transfer of prefunded OPEB reserves from the City, as well as the opportunities to contain these benefit costs through plan redesign, another significant new resource is anticipated to be available to help the BCPS absorb these expenditures without impacting spending on students. Under a new State of Maryland Maintenance of Effort (MOE) law passed in 2012, the City's MOE costs are expected to escalate by up to 2.5% a year starting in Fiscal 2015 — adding nearly \$60 million to the MOE during the ten-year plan period above the levels projected before this law was adopted. In turn, the City's higher MOE payments will trigger increased State aid for BCPS under the Guaranteed Tax Base (GTB) allocation formula. This additional aid — net of an amount already dedicated to capital spending — is projected to grow from \$4.3 million in Fiscal 2013 to \$8.5 million in Fiscal 2022, totaling \$75 million for the ten year plan period. Further, this amount could potentially be increased by \$1 million annually if the City folds its transition services payments, yearly funding transfers required under the separation agreement to cover school administrative functions formerly provided by the City, into the MOE.

Based on preliminary estimates, this GTB revenue alone is projected to eventually cover not only the current costs of benefit payments for retired school employees hired since 1997, but also much of the Actuarial Required Contribution (ARC) determined to be prudent for prefunding future obligations. Looking longer-term, this transfer would likely create some offsetting loss in GTB assistance, as the City's current OPEB payments are included in the base for this formula. Because the City would still be making substantial payments to the BCPS for pre-1997 retirees, however, any near-to-intermediate term impacts would be modest.

In sum, under the right structure, the combination of such increased GTB revenue, potential health benefit cost savings, and transfer of a reasonable level of City OPEB Trust assets, would be projected to enable the BCPS to fully absorb this new cost without affecting classroom spending. At the same time, the City would save approximately \$25 million over the Ten-Year Plan period, while significantly reducing a major balance sheet liability.



Next Steps

In working to achieve stable City finances while also supporting broader goals for a growing Baltimore, this Ten-Year Financial Plan process has highlighted critical long-range challenges and strategies in each of four cornerstone areas:

- **Structural Budget Balance**, to provide a stable financial framework for City programs and services.
- **Tax Competitiveness**, to become a more attractive place of locational choice for both residents and businesses.
- **Infrastructure Investment**, to rebuild and renew the City's assets.
- **Addressing Long-Term Liabilities**, to provide responsible stewardship for generations to come.

For the many civic leaders and Baltimore residents long committed to the City and its future, these issues are not new — and, in many cases efforts are underway toward meeting these goals.

The City's Outcome Budgeting process, for example, already directs investment toward achieving results with closely aligned priorities:

- Better Schools
- Safer Streets
- Stronger Neighborhoods
- A Growing Economy
- Innovative Government
- A Cleaner and Healthier City

Consistent with these goals, major policy initiatives have already been launched by Mayor Stephanie Rawlings-Blake to reduce homeowner property tax burdens, reconstruct school facilities, and bring back value where vacant and abandoned structures now blight Baltimore neighborhoods.

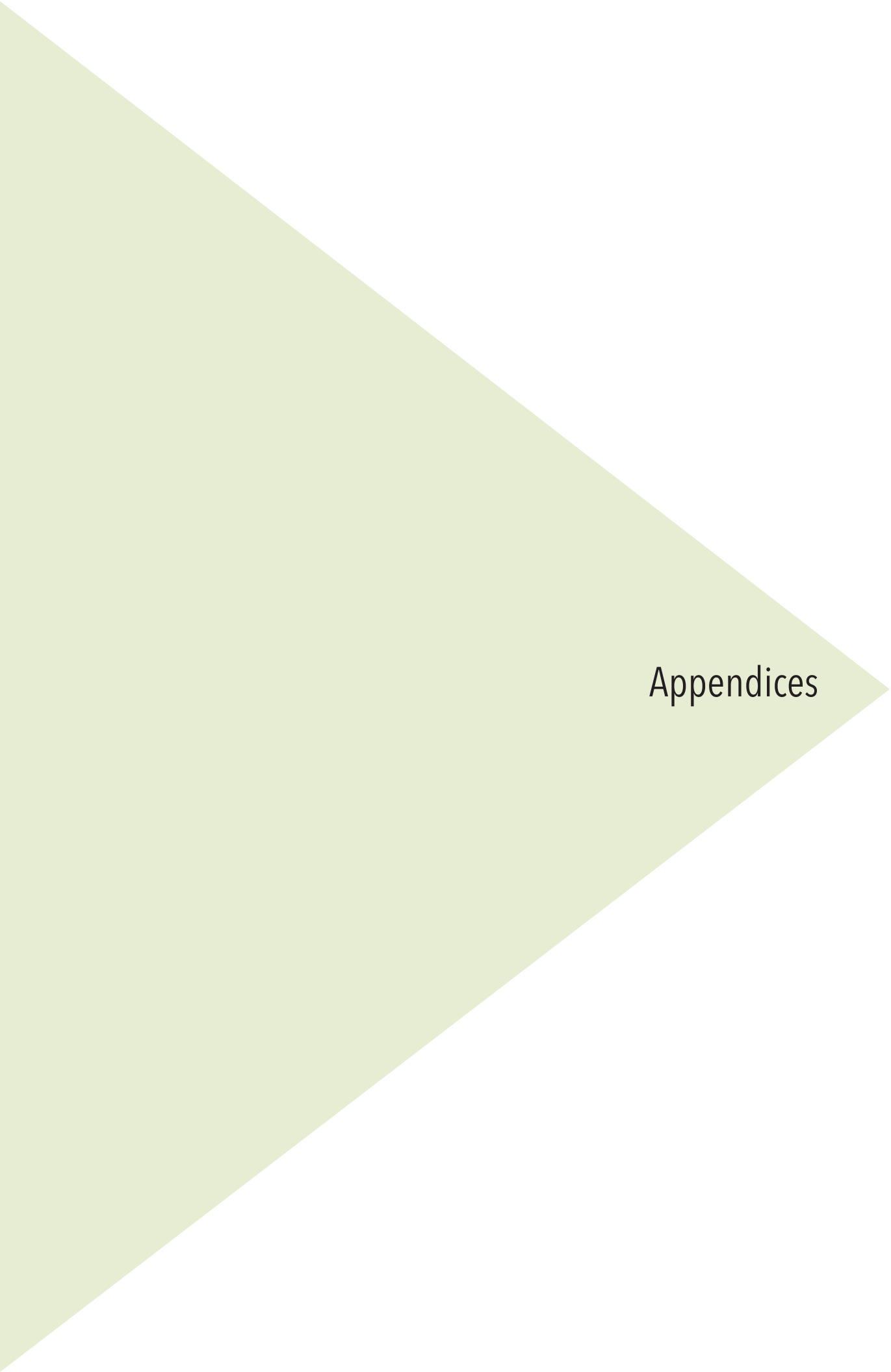
Further, these ongoing efforts are beginning to make a difference, and the City's finances and population have stabilized.

Looking forward, the City now holds the opportunity to build on this more stable platform to become a **growing city** again and meet the goal set by Mayor Rawlings-Blake of adding 10,000 new Baltimore families by 2020.

Achieving this goal is now within reach, but it is far from preordained. Such progress will require difficult choices, significant change, continued hard work, and new levels of collaboration across the public servants and private citizens throughout the Baltimore region who care about the City and its future.

The consultant team on this project sincerely appreciates this opportunity to have worked with the City to provide our perspective on these exciting opportunities, the challenges still to be overcome, and potential options for this new direction.

In an accompanying document building on this research and analysis, ***Change to Grow: A Ten-Year Financial Plan for Baltimore***, Mayor Stephanie Rawlings-Blake charts a specific course of actions to now move Baltimore forward.



Appendices

The City of Baltimore, Maryland, with nearly 620,000 residents, is the hub of the 20th largest metropolitan area in the nation. The City has tremendous civic assets — including world-class healthcare and higher education institutions, active trade and finance sectors, vibrant arts and culture, and many strong and diverse neighborhoods.

In recent years, however, like many governments nationally, Baltimore has seen its revenues eroded by the most severe economic downturn in generations, while key expenditure drivers such as employee healthcare and retirement costs have been growing at unsustainable rates. As in other mature cities transitioning from an industrial base to a new economy, these challenges have been compounded by a longer-term legacy of aging infrastructure, high taxes, and sections of the City blighted by crime and vacant properties.

To address these structural challenges, Mayor Stephanie Rawlings-Blake determined in 2011 to launch development of a Ten-Year Financial Plan. This proactive process builds on Baltimore's longstanding commitment to fiscal stewardship by working to establish a balanced framework for financial sustainability. This Plan seeks to set forth a set of actions designed to bring the City's recurring revenues and expenditures into alignment, while also prioritizing new investments to strengthen the Baltimore's fiscal foundation and promote economic and community stability and growth.

Long-range financial planning is considered a public sector best practice by the National Advisory Council on State and Local Budgeting (NACSLB), Government Finance Officers Association (GFOA), and major credit rating agencies. As the GFOA notes in its recommended Best Practice:

"Financial planning uses forecasts to provide insight into future financial capacity so that strategies can be developed to achieve long-term sustainability in light of the government's service objectives and financial challenges."

In support of this process, the City engaged a national consulting firm experienced in public sector long-range financial plans, Public Financial Management, Inc. (PFM). PFM led a team including Hay Group, a leading international human resources and actuarial benefits consulting firm, and two Baltimore area consultancies with strong experience regionally, Walker Benefit Services, and Advanced Benefit Solutions.

From the outset, this has been a collaborative process between the consultants and the City's leadership and staff. The team has met with the Mayor and members of her Senior Staff, as well as the President of City Council and staff, multiple City Council members, the City Comptroller, and dozens of City department and division managers and professionals. The City's Finance Department and its Bureau of the Budget and Management Research have provided extensive technical input and review, and key policy direction has been provided by three City Guidance Committees focused on health benefits, pensions, and the Ten-Year Plan as a whole:

- **Overall Ten-Year Financial Plan:** Councilman William Cole; Finance Director Harry Black; Director of Policy and Communications, Ryan O'Doherty; City Planning Director, Tom Stosur; Budget Director, Andrew Kleine; Director of Revenue and Tax Analysis, William Voorhees; and President and CEO of the Greater Baltimore Committee, Donald Fry.
- **Health Benefits:** Councilman Brandon Scott, Finance Director Harry Black; Director of Policy and Communications, Ryan O'Doherty; Health Commissioner, Oxiris Barbot; Deputy Director of Human Resources, Yvonne Moore; Benefits Director, Regina Sorrell; Budget Analyst, Lindsay Wines; Director of Revenue and Tax Analysis, William Voorhees; and Daryl Gaskin of the Johns Hopkins School of Public Health.
- **Employees Retirement System (ERS) Plan:** Councilman Edward Reisinger, Finance Director Harry Black; Director of Policy and Communications, Ryan O'Doherty; ERS Executive Director, Roselyn H. Spencer; Deputy Budget Director, Robert Cename; and Director of Revenue and Tax Analysis, William Voorhees.

In addition to City officials and staff, the project team met with a broad range of Baltimore stakeholders — including community and nonprofit leaders, regional and city business community representatives, City employee union leadership, and neighborhood participants in a community budget workshop.

Through this collaborative process, the project team has:

- Established a baseline budget forecast for the next ten years (FY2013-22).
- Highlighted key budget drivers, liabilities, and trends.
- Identified strengths, weaknesses, opportunities and threats facing the City.

Appendix A: Project Background and Approach

- Developed a series of options for addressing the affordability, sustainability, and competitiveness of employee and retiree health benefits, and the Employees' Retirement System (ERS).
- Conducted extensive benchmarking and best practice research regarding key budget drivers and strategies.
- With City staff, identified and analyzed scores of initiatives designed to reduce expenditures, generate additional revenue, and support the City's growth agenda.
- Provided technical support for the Mayor and her Senior Staff to help evaluate and prioritize alternatives for advancement in a plan of action for the City.

The result of this project is two companion documents:

- This **Ten-Year Financial Plan Background Report** — which includes the consultant team's diagnosis of the identified challenges facing the City over the decade ahead, a baseline financial forecast, and a range of potential financial and programmatic strategies.
- **Change to Grow: A Ten-Year Financial Plan for Baltimore** — the Mayor's blueprint for action, reflecting priorities and policy direction to close the City's structural budget gap, address long-term fiscal liabilities responsibly, and invest in growing the City.

In total, this effort builds on the project team's interviews, data review, benchmarking, budget projections, and supplemental research — providing a broad range of inputs for the long-term financial planning process. Through further collaboration drawing on the national experience of the project team and the local and regional insights of City staff, this report has been structured with a goal of highlighting major budget trends and issues to provide a better framework for decision-making.

As the National Advisory Council on State and Local Budgeting has noted as part of its Recommended Practice to Conduct Long-Range Financial Planning:

"A financial plan is not a forecast of what is certain to happen but rather a device to highlight significant issues or problems that must be addressed if goals are to be achieved."

In the months and years ahead, new challenges and opportunities will undoubtedly emerge that move Baltimore's future in directions this Ten-Year Financial Plan has not contemplated. As a result of this planning process, however, the project team believes the City will be better positioned to weather future storms, capture new opportunities, and begin to grow again as one of the nation's great cities.

Key consultant team members included: Michael Nadol, David Hoskins, Jelani Newton, Marissa Litman, Adam Benson, Trina Smith, Kate Flaming, Katherine Clupper, Tim Carden, Aliraza Hassan, David Eichenthal, Christopher Arlene, Sandra Sosinski, Gail McKelvie, and Larry Miracola of PFM; Adam Reese, Yuri Nisenzon, Jared Grove, and Sanjit Puri of Hay Group; Carl Walker and Courtney Walker of Walker Benefit Services; Suzanne Thompson of Advanced Benefits Solutions; and Milou Carolan.

Strengths

- For attracting and retaining residents:
 - Appeal of the urban environment to Gen Y, Empty Nesters
 - Growing economic competitiveness of cities as energy prices rise and suburban infrastructure ages
 - Arts, culture, history, architecture, entertainment, amenities, events
 - Accommodating to diversity (although immigration rates are comparatively low)
 - Multiple growing neighborhoods — including, but not at all limited to, increasingly residential downtown/ waterfront areas
 - Potential future-growth neighborhoods (e.g. Middle Branch)
 - Regional economic stability and locational advantages
- For attracting and retaining jobs:
 - Strong higher education and healthcare sectors, with established incubators (e.g., Emerging Technology Centers) and potential research spinoffs (e.g., Bioscience Initiative)
 - Federal government presence, with potential for increased transportation access to DC regional jobs
 - Hospitality and tourism sector, including opportunities for lower-skilled workers
 - Well-defined central business district, with waterfront proximity and improving retail and amenities such as the Charm City Circulator
 - Port of Baltimore resurgence, with related opportunities for distribution, fulfillment, and possibly new manufacturing
 - Overall transportation networks (highways, freight and passenger rail, BWI proximity, port)
 - Industrially-zoned land
- As a local government:
 - History of prudent and proactive financial management, and commitment to a Budget Stabilization Reserve
 - City enterprises (water as a regional asset, parking, conduit)
 - Focus on performance metrics and results (CitiStat, Citizens Survey, Budgeting for Outcomes, Innovation Fund)

Weaknesses

- For attracting and retaining residents:
 - Crime rates have improved, but perceptions have lagged, and both the reality and impressions of public safety and security remain core issues
 - City schools are perceived to be improving, and charters are viewed as an attractive alternative by some, but keeping Gen Y from moving out when becoming parents is a looming challenge
 - High tax effort and burden, borne substantially by City residents, eroding competitiveness and overall affordability
 - Vacant properties and blight
- For attracting and retaining jobs:
 - Regionally low educational attainment levels and gaps in workforce skills
 - Limited supply of apartments and residential environments to attract knowledge workers
 - Incomplete transportation networks, pending Red Line light rail development
 - High cost of doing business, including taxes and regulatory requirements
 - "Brand" challenges to define Baltimore's sectors of strength and to overcome image of post-industrial decline
 - High office and retail vacancy rate, with an underdeveloped downtown environment (e.g., less of a 24/7 business district residential community, and limited green space relative to some other major cities)
- As a local government:
 - Structural budget shortfalls
 - Legacy costs of retiree benefits
 - Costs of renewing and replacing aging infrastructure
 - Tax structure marked by high rates, and limited flexibility to share costs with commuters and visitors
 - Inconsistent customer service and ease of doing business with the City

Opportunities

- For attracting and retaining residents:
 - Potential for defense-related IT job growth across the metro area
 - Growth in demographic cohorts attracted to urban environments (empty nesters, Gen Y)
 - Becoming a more competitive location of choice (taxes, services, regulation, schools, quality of life amenities such as recreation centers)
 - Improved public transportation (Red Line light rail)
 - Expanding university and hospital partnerships
 - Greening programs to help comply with stormwater management regulations
 - Redevelopment of blighted properties and/or conversion to parks/open space; ongoing projects taking hold (e.g. Uplands)
- For attracting and retaining jobs:
 - Spinoff economic growth and investment (e.g. Bioscience Initiative, IT and information security, etc.)
 - Hospitality sector modernization (Arena, Inner Harbor, Convention Center, cruise industry growth)
 - Distribution/export-oriented manufacturing (Port of Baltimore)
 - Streamlined and predictable regulatory policies (e.g., the new Zoning Code initiative), incentive programs, and government partnership with the private sector
 - Small business development
- As a local government:
 - Revenue diversification
 - Greater regional coordination
 - Restructuring City assets, and sale of surplus City-owned properties

Threats

- For attracting and retaining residents:
 - Continued population decline would erode City viability (tax base, service levels, quality of life, blight, workforce competitiveness)
 - Deteriorating infrastructure would lead to service disruption
 - Slowed progress on improving schools and quality of life could cause 20-somethings turning 30 to move out
- For attracting and retaining jobs:
 - Continued macroeconomic weakness
 - Potential for federal deficit reduction initiatives to constrain governmental spending in the region
- As a local government:
 - Unaddressed, underfunded pension and OPEB liabilities would continue to erode available resources and/or lead benefits to become unsustainable
 - Decreasing Federal (CDBG) and State assistance (Highway User Revenues, Disparity grant) and potential further cost shifts (teacher pensions) would add to budget pressure
 - Declining representation in Annapolis due to demographic change and redistricting will require strong regional partnerships and communication
 - Federally mandated environmental regulations (water, stormwater, air quality) would add to rate and tax pressures
 - Climate change impacts could create new service demands
 - Decreasing landfill space

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
REVENUE										
Property Taxes	\$768.3	\$759.4	\$767.8	\$784.1	\$803.8	\$828.9	\$842.8	\$870.0	\$901.7	\$934.8
Income Taxes	\$256.1	\$267.5	\$273.1	\$278.6	\$283.9	\$289.0	\$292.2	\$295.4	\$298.6	\$301.9
Recordation Tax	\$20.2	\$21.3	\$22.7	\$24.3	\$26.5	\$29.0	\$31.9	\$35.3	\$39.1	\$43.5
Transfer Tax	\$22.0	\$23.2	\$24.7	\$26.5	\$28.8	\$31.5	\$34.7	\$38.4	\$42.5	\$47.3
Hotel Tax	\$22.0	\$24.0	\$24.9	\$25.4	\$25.9	\$26.5	\$27.2	\$27.9	\$28.6	\$34.2
Telecommunication Tax	\$34.3	\$34.3	\$34.3	\$34.3	\$34.3	\$34.3	\$34.3	\$34.4	\$34.5	\$34.6
Energy Tax	\$38.8	\$39.5	\$40.2	\$41.0	\$41.9	\$42.8	\$43.8	\$44.8	\$45.8	\$46.9
Annual Nonprofit Contributions	\$3.4	\$2.4	\$2.4	\$1.4	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Video Lottery Terminals	\$0.0	\$11.0	\$13.0	\$20.0	\$20.7	\$21.4	\$21.4	\$21.4	\$21.4	\$21.4
Targeted Homeowners Tax Credit	(\$3.8)	(\$18.6)	(\$20.3)	(\$21.8)	(\$24.3)	(\$28.7)	(\$34.4)	(\$38.0)	(\$38.0)	(\$38.0)
Beverage Container Tax	\$5.2	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4
Admissions Tax	\$8.0	\$8.5	\$8.7	\$8.8	\$9.0	\$9.1	\$9.2	\$9.3	\$9.4	\$9.5
State Aid	\$100.5	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0	\$102.0
Licenses and Permits	\$30.9	\$31.5	\$32.0	\$32.6	\$33.2	\$33.9	\$34.5	\$35.2	\$35.8	\$36.5
Fines and Forfeitures	\$28.6	\$32.2	\$29.2	\$27.2	\$27.2	\$27.2	\$27.2	\$27.2	\$27.2	\$27.2
Charges for Services	\$44.5	\$45.1	\$45.7	\$46.3	\$46.9	\$47.5	\$48.1	\$48.8	\$49.4	\$50.1
Use of Property	\$15.0	\$15.4	\$15.7	\$16.0	\$16.3	\$16.6	\$16.9	\$17.2	\$17.5	\$17.8
Interest Earnings	\$0.9	\$1.4	\$2.4	\$4.4	\$4.4	\$4.4	\$4.4	\$4.4	\$4.4	\$4.4
Other Use of Money	\$2.3	\$2.3	\$2.4	\$2.4	\$2.5	\$2.6	\$2.7	\$2.8	\$2.9	\$3.0
Net Parking Revenue	\$27.2	\$25.8	\$25.6	\$25.5	\$25.3	\$25.1	\$25.0	\$24.8	\$24.6	\$24.4
State Highway User Revenue	\$132.0	\$134.4	\$142.6	\$145.9	\$145.9	\$145.9	\$145.9	\$145.9	\$145.9	\$145.9
All Other	\$14.8	\$13.0	\$13.2	\$13.1	\$12.8	\$12.4	\$12.2	\$11.6	\$11.0	\$10.3
Total Revenues	\$1,571.1	\$1,585.9	\$1,612.7	\$1,648.6	\$1,677.4	\$1,711.9	\$1,732.4	\$1,769.1	\$1,814.8	\$1,868.2

Appendix C: Multi-Year Budget Projection Detail

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
EXPENDITURES										
Salaries	\$579.5	\$600.2	\$615.1	\$630.3	\$646.3	\$662.3	\$678.9	\$695.7	\$713.4	\$731.0
Benefits										
Pension Contributions										
FPRS	\$105.2	\$115.3	\$117.3	\$126.6	\$130.9	\$133.6	\$135.5	\$136.8	\$137.5	\$137.8
ERS	\$43.7	\$46.8	\$48.8	\$50.7	\$52.4	\$54.1	\$55.7	\$57.3	\$58.9	\$60.6
EOS	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4	\$0.4
Total Pension Contribution	\$149.4	\$162.6	\$166.6	\$177.7	\$183.7	\$188.1	\$191.6	\$194.5	\$196.8	\$198.8
Health Insurance (Active Employees)										
Medical	\$84.0	\$75.9	\$80.4	\$85.1	\$89.9	\$95.1	\$100.5	\$106.2	\$112.3	\$118.5
Prescription Drug	\$14.5	\$13.0	\$13.7	\$14.5	\$15.3	\$16.2	\$17.1	\$18.1	\$19.2	\$20.2
Dental	\$1.8	\$1.9	\$2.0	\$2.1	\$2.2	\$2.4	\$2.5	\$2.6	\$2.8	\$2.9
Vision	\$0.6	\$0.6	\$0.6	\$0.7	\$0.7	\$0.7	\$0.8	\$0.8	\$0.9	\$0.9
FY13 Health Benefit Savings (Actives)	(\$5.8)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Total Health Insurance	\$95.1	\$91.4	\$96.8	\$102.4	\$108.2	\$114.4	\$120.9	\$127.8	\$135.1	\$142.6
FICA	\$21.8	\$22.9	\$23.5	\$24.0	\$24.6	\$25.3	\$25.9	\$26.5	\$27.2	\$27.9
All Other	\$9.9	\$12.4	\$12.6	\$12.9	\$13.1	\$13.3	\$13.5	\$13.7	\$14.0	\$14.2
Total Benefits	\$276.1	\$289.3	\$299.4	\$317.0	\$329.6	\$341.1	\$351.9	\$362.5	\$373.0	\$383.5
Contractual										
Retiree Prescription Drug	\$38.9	\$35.7	\$37.3	\$38.7	\$40.2	\$41.7	\$43.2	\$44.7	\$46.2	\$47.6
Retiree Medical	\$31.4	\$26.9	\$27.2	\$27.2	\$27.4	\$27.7	\$28.2	\$28.5	\$29.0	\$29.4
FY13 Health Benefit Savings (Retirees)	(\$4.3)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Gas/Electric/Steam	\$22.0	\$21.0	\$22.0	\$22.9	\$24.0	\$25.0	\$26.1	\$27.3	\$28.5	\$29.7
Water & Sewer	\$3.8	\$4.2	\$4.5	\$4.9	\$5.4	\$5.9	\$6.4	\$7.0	\$7.6	\$8.3
Other Contractual	\$176.5	\$176.7	\$180.4	\$185.6	\$191.3	\$197.1	\$203.2	\$209.8	\$217.0	\$222.8
Total Contractual	\$268.3	\$264.5	\$271.3	\$279.4	\$288.2	\$297.4	\$307.0	\$317.2	\$328.1	\$337.9
Supplies, Materials and Equipment	\$42.3	\$45.0	\$46.0	\$46.9	\$48.1	\$49.3	\$50.2	\$51.2	\$52.5	\$53.7
Grants, Subsidies and Contributions										
Contribution to City Schools										
BCPS Local Share	\$204.5	\$204.1	\$210.3	\$212.4	\$219.4	\$226.3	\$233.4	\$240.7	\$248.3	\$256.0
BCPS City Services Transfer	\$4.4	\$4.4	\$4.5	\$4.6	\$4.7	\$4.8	\$4.9	\$5.0	\$5.1	\$5.2
BCPS Severance Pay-Outs	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Teacher Pension Shift	\$12.9	\$16.4	\$14.8	\$17.9	\$18.1	\$18.3	\$18.4	\$18.6	\$18.8	\$19.0
BCPS Retiree Health	\$28.8	\$28.9	\$29.8	\$30.5	\$31.3	\$32.3	\$33.3	\$34.3	\$35.3	\$36.4
Total Contribution to City Schools	\$253.5	\$256.7	\$262.2	\$268.2	\$276.3	\$281.6	\$290.1	\$298.6	\$307.5	\$316.6
Contribution to General Fund Reserve	\$2.0	\$2.1	\$2.1	\$2.2	\$2.2	\$2.2	\$2.3	\$2.3	\$2.4	\$2.4
OPEB Contribution	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5	\$8.5
Workers Comp (Admin, Direct, State)	\$38.2	\$40.9	\$41.8	\$42.7	\$43.6	\$44.6	\$45.6	\$46.6	\$47.6	\$48.6
Other Grants, Subsidies, and Contributions	\$44.9	\$45.7	\$46.6	\$47.6	\$48.6	\$49.6	\$50.6	\$51.7	\$52.8	\$53.9
Total Grants, Subsidies, and Contributions	\$347.0	\$353.8	\$361.2	\$369.1	\$379.2	\$386.6	\$397.1	\$407.7	\$418.8	\$430.1
Debt Service										
General Obligation - P&I	\$77.2	\$66.8	\$63.0	\$67.6	\$70.1	\$67.8	\$73.0	\$79.4	\$86.1	\$91.8
Conditional Purchase Agreement - P&I	\$33.7	\$46.8	\$49.8	\$57.8	\$55.8	\$51.7	\$52.3	\$54.5	\$45.5	\$43.8
Transp. Revenue - P&I	\$13.3	\$11.9	\$12.0	\$11.9	\$12.5	\$12.5	\$12.5	\$12.5	\$12.5	\$12.5
TIF - P&I	\$13.7	\$12.6	\$12.6	\$12.6	\$12.6	\$12.6	\$12.6	\$12.6	\$12.6	\$12.6
Convention Center Hotel - Hotel Tax	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8	\$2.8
Other	\$1.5	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0	\$3.0
Total Debt Service	\$142.3	\$144.0	\$143.3	\$155.9	\$156.9	\$150.4	\$156.3	\$164.9	\$162.6	\$166.5
PAYGO Capital	\$9.7	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0	\$8.0
Interfund Transfers/Other										
Retiree Health Contributions (Transfers in)	(\$10.5)	(\$9.4)	(\$9.6)	(\$9.7)	(\$9.9)	(\$10.1)	(\$10.3)	(\$10.5)	(\$10.7)	(\$11.0)
Other	(\$83.6)	(\$89.7)	(\$94.9)	(\$100.2)	(\$105.5)	(\$110.8)	(\$116.1)	(\$116.5)	(\$116.9)	(\$117.3)
Total Interfund Transfers/Other	(\$94.1)	(\$99.0)	(\$104.4)	(\$109.9)	(\$115.3)	(\$120.9)	(\$126.4)	(\$127.0)	(\$127.6)	(\$128.2)
Beverage Container Tax Expenditures	\$0.0	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4	\$10.4
Total General Fund	\$1,571.1	\$1,616.2	\$1,650.3	\$1,707.1	\$1,751.4	\$1,784.5	\$1,833.4	\$1,890.7	\$1,939.2	\$1,992.9
Surplus/Deficit	(\$0.0)	(\$30.3)	(\$37.6)	(\$58.6)	(\$74.0)	(\$72.5)	(\$101.0)	(\$121.7)	(\$124.4)	(\$124.7)
General Fund Balance (Year End)	\$166.0	\$135.6	\$98.1	\$39.5	(\$34.5)	(\$107.0)	(\$208.0)	(\$329.7)	(\$454.1)	(\$578.8)

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
GROWTH RATES										
REVENUE										
Property Taxes	-1.17%	1.11%	2.13%	2.50%	3.13%	1.67%	3.23%	3.64%	3.67%	
Income Taxes	4.47%	2.10%	2.00%	1.90%	1.80%	1.10%	1.10%	1.10%	1.10%	
Recordation Tax	5.36%	6.60%	7.33%	8.68%	9.57%	10.04%	10.51%	10.78%	11.30%	
Transfer Tax	5.36%	6.60%	7.33%	8.68%	9.57%	10.04%	10.51%	10.77%	11.30%	
Hotel Tax	9.03%	4.14%	1.79%	1.94%	2.50%	2.49%	2.48%	2.47%	19.68%	
Telecommunication Tax	-0.14%	-0.09%	0.00%	0.06%	0.07%	0.10%	0.15%	0.21%	0.26%	
Energy Tax	1.73%	1.89%	2.03%	2.14%	2.21%	2.24%	2.29%	2.34%	2.40%	
Annual Nonprofit Contributions	-29.41%	0.00%	-41.67%	-100.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Video Lottery Terminals	0.00%	18.18%	53.85%	3.50%	3.38%	0.00%	0.00%	0.00%	0.00%	
Targeted Homeowners Tax Credit	389.47%	9.14%	7.39%	11.47%	18.11%	19.86%	10.47%	0.00%	0.00%	
Beverage Container Tax	101.90%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Admissions Tax	7.48%	1.71%	1.66%	1.51%	1.30%	1.25%	1.25%	1.26%	1.25%	
State Aid	1.50%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Licenses and Permits	1.74%	1.80%	1.84%	1.89%	1.89%	1.89%	1.90%	1.90%	1.90%	
Fines and Forfeitures	12.41%	-9.32%	-6.85%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Charges for Services	1.49%	1.25%	1.27%	1.30%	1.31%	1.33%	1.34%	1.35%	1.37%	
Use of Property	2.50%	2.15%	2.11%	1.94%	1.70%	1.65%	1.66%	1.68%	1.69%	
Interest Earnings	64.20%	66.57%	85.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Other Use of Money	1.03%	1.58%	2.52%	3.52%	3.52%	3.48%	3.47%	3.43%	3.35%	
Net Parking Revenue	-5.10%	-0.58%	-0.60%	-0.63%	-0.65%	-0.67%	-0.68%	-0.70%	-0.73%	
State Highway User Revenue	1.79%	6.14%	2.29%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
All Other	-11.85%	1.55%	-0.95%	-2.10%	-3.30%	-1.78%	-4.42%	-5.61%	-6.25%	
Total Revenues	0.94%	1.69%	2.22%	1.75%	2.06%	1.19%	2.12%	2.58%	2.94%	

Appendix C: Multi-Year Budget Projection Detail

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22
EXPENDITURES										
Salaries	3.58%	2.48%	2.48%	2.53%	2.47%	2.52%	2.48%	2.53%	2.47%	
Benefits										
Pension Contributions										
FPRS	9.58%	1.74%	7.91%	3.37%	2.12%	1.41%	0.90%	0.53%	0.26%	
ERS	7.13%	4.27%	3.82%	3.43%	3.16%	2.98%	2.87%	2.81%	2.81%	
EOS	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Total Pension Contribution	8.84%	2.46%	6.69%	3.38%	2.42%	1.86%	1.47%	1.20%	1.02%	
Health Insurance (Active Employees)										
Medical	-9.59%	5.90%	5.80%	5.70%	5.70%	5.70%	5.70%	5.70%	5.70%	5.60%
Prescription Drug	-10.88%	5.90%	5.80%	5.70%	5.70%	5.70%	5.70%	5.70%	5.70%	5.60%
Dental	6.62%	5.90%	5.80%	5.70%	5.70%	5.70%	5.70%	5.70%	5.70%	5.60%
Vision	0.46%	5.90%	5.80%	5.70%	5.70%	5.70%	5.70%	5.70%	5.70%	5.60%
FY13 Health Benefit Savings (Active Employees)	-100.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Total Health Insurance	-3.95%	5.90%	5.80%	5.70%	5.70%	5.70%	5.70%	5.70%	5.70%	5.60%
FICA	5.20%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
All Other	25.67%	1.61%	1.63%	1.64%	1.66%	1.67%	1.68%	1.70%	1.71%	
Total Benefits	4.75%	3.51%	5.86%	3.99%	3.47%	3.19%	3.01%	2.90%	2.81%	
Contractual										
Retiree Prescription Drug	-8.22%	4.31%	3.87%	3.85%	3.70%	3.62%	3.41%	3.36%	3.21%	
Retiree Medical	-14.48%	1.12%	0.00%	0.77%	1.26%	1.59%	1.29%	1.50%	1.63%	
FY13 Health Benefit Savings (Retirees)	-100.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Gas/Electric/Steam	-4.41%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	4.40%	
Water & Sewer	9.09%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	9.00%	
Other Contractual	0.15%	2.07%	2.90%	3.05%	3.07%	3.05%	3.26%	3.43%	2.68%	
Total Contractual	-1.40%	2.57%	2.96%	3.15%	3.21%	3.22%	3.31%	3.45%	2.96%	
Supplies, Materials and Equipment	6.52%	2.09%	2.10%	2.50%	2.37%	1.99%	1.97%	2.49%	2.28%	
Grants, Subsidies and Contributions										
Contribution to City Schools										
BCPS Local Share	-0.17%	3.01%	1.00%	3.31%	3.15%	3.14%	3.13%	3.12%	3.12%	
BCPS City Services Transfer	0.00%	2.00%	2.05%	2.10%	2.10%	2.10%	2.10%	2.10%	2.10%	
BCPS Severance Pay-Outs	0.00%	0.00%	0.00%	0.00%	-100.00%	0.00%	0.00%	0.00%	0.00%	
Teacher Pension Shift Cost	26.75%	-9.50%	20.75%	1.00%	1.00%	1.00%	1.00%	1.00%	1.00%	
BCPS Retiree Health	0.33%	3.12%	2.21%	2.74%	3.03%	3.21%	2.93%	3.04%	3.07%	
Total Contribution to City Schools	1.26%	2.18%	2.26%	3.03%	1.93%	2.99%	2.96%	2.97%	2.96%	
Contribution to General Fund Reserve	1.95%	2.00%	2.05%	2.10%	2.10%	2.10%	2.10%	2.10%	2.10%	
OPEB Contribution	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Workers Comp (Admin, Direct, State)	6.94%	2.20%	2.20%	2.20%	2.20%	2.20%	2.20%	2.20%	2.20%	
Other Grants, Subsidies, and Contributions	1.94%	2.00%	2.05%	2.10%	2.10%	2.10%	2.10%	2.10%	2.10%	
Total Grants, Subsidies, and Contributions	1.95%	2.10%	2.17%	2.74%	1.94%	2.71%	2.69%	2.70%	2.70%	
Debt Service										
General Obligation - P&I	-13.53%	-5.67%	7.32%	3.73%	-3.39%	7.69%	8.87%	8.38%	6.58%	
Conditional Purchase Agreement - P&I	38.82%	6.39%	16.10%	-3.52%	-7.44%	1.30%	4.15%	-16.50%	-3.72%	
Transp. Revenue - P&I	-10.60%	0.55%	-0.25%	4.68%	-0.15%	0.06%	0.02%	0.09%	0.05%	
TIF - P&I	-7.79%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Convention Center	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Other	107.15%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Total Debt Service	1.22%	-0.51%	8.80%	0.67%	-4.17%	3.92%	5.53%	-1.41%	2.45%	
PAYGO Capital	-17.53%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Interfund Transfers/Other										
Retiree Health Contributions (Transfers in)	-11.08%	2.13%	1.25%	1.78%	2.08%	2.28%	2.02%	2.15%	2.20%	
Other	7.27%	5.83%	5.58%	5.30%	5.04%	4.81%	0.32%	0.33%	0.33%	
Interfund Transfers	5.21%	5.48%	5.18%	4.99%	4.79%	4.60%	0.46%	0.48%	0.49%	
Beverage Container Tax Expenditures	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Total General Fund	2.87%	2.11%	3.44%	2.59%	1.89%	2.74%	3.13%	2.56%	2.77%	

2012 Paid Leave and Salary Benchmarking Findings

The following benchmarking data is based on PFM survey analysis and review of collective bargaining agreements for general government (civilian) employees.

	Vacation Leave	Vacation Carry Over
Baltimore City	<6 YOS: 12 days 6 to <11 YOS: 15 days 11 to <14 YOS: 18 days 14 to <19 YOS: 21 days 19+ YOS: 24 days	Employees shall be allowed to accumulate vacation leave up to the maximum number of days earnable for a five (5) year period as determined by their current rate of accrual.
Anne Arundel County	<5 YOS: 10 days 5 to <10 YOS: 15 days 10 to <20 YOS: 20 days 20+ YOS: 25 days	An employee may not carry more than 30 days of annual leave into a calendar pay period.
Baltimore County	1 to 5 YOS: 12 days 6 to 10 YOS: 15 days 11 to 15 YOS: 20 days 16+ YOS: 25 days	Vacation maximum accumulation varies by YOS, ranging from 24 to 50 days.
Harford County	0 to 3 YOS: 12 days 4 to 9 YOS: 15 days 10 to 15 YOS: 21 days 16+ YOS: 24 days	A total of forty (40) days annual leave is the maximum that may be carried over from one (1) calendar year to the next.
Howard County	0 to 5 YOS: 13 days 6 to 10 YOS: 16 days 11 to 20 YOS: 19 days 21+ YOS: 21 days	Employees may carry over no more than 360 hours of annual leave from one fiscal year to the next
Montgomery County	0 to <3 YOS: 15 days 3 to <15 YOS: 20 days 15+ YOS: 26 days	Maximum carryover of 240 hours
Prince George's County	0 to <3 YOS: 13 days 3 to <15 YOS: 20 days 15+ YOS: 26 days	Maximum carryover of 360 hours
State of Maryland	<5 YOS: 10 days 5 to <10 YOS: 15 days 10 to <20 YOS: 20 days 20+ YOS: 25 days	Any days of annual leave not used at the end of a year may be carried forward into the next year. Employees may accumulate unused annual leave and may carry over from one year to the next up to seventy-five (75) days, or six hundred (600) hours.
City of Philadelphia	<5 YOS: 10 days 5 to <10 YOS: 15 days 10 to <20 YOS: 20 days 20+ YOS: 25 days	Vacation leave does not carry over, unless denied or approved by Management
City of Memphis	6 months to <1 YOS: 5 days 1 to <6 YOS: 10 days 1 additional day for each year, up to 25 days maximum after 25 YOS	Maximum of 70 vacation days carryover from year to year
City of Columbus	<3 YOS: 10 days 3 to <6 YOS: 16 days 6 to <13 YOS: 23 days 13 to <20 YOS: 26 days 20 to <25 YOS: 28 days 25+ YOS: 30 days	<3 YOS: 20 days 3 to <6 YOS: 32 days 6 to <13 YOS: 46 days 13 to <20 YOS: 52 days 20 to <25 YOS: 56 days 25+ YOS: 60 days

Appendix D: Paid Leave Benchmarking Results

Vacation Leave - Cash Out Provisions	
Baltimore City	CUB: 60 to 120 days (5 years at current vacation accrual rate) MAPS: 96 to 192 days (8 years at current vacation accrual rate) IAFF: 48 to 96 days (4 years at current vacation accrual rate) FOP: 192 days
Anne Arundel County	Up to 30 days of vacation leave paid at termination
Baltimore County	Up to 50 days of vacation leave paid at termination
Howard County	Up to 45 days (360 hours) of vacation leave paid at termination
Montgomery County	Up to 30 days (240 hours) of vacation leave paid at termination
Prince George's County	Up to 45 days (360 hours) of vacation leave paid at termination
State of Maryland	Up to 50 days of vacation leave paid at termination

	Number of Holidays	Pay on a Holiday Worked
Baltimore City	11	1.5X
Anne Arundel County	14 + Election Day	1.5X
Baltimore County	10 + Election Day	
Harford County	10	1.5X for 7 holidays 2X for 3 holidays
Howard County	12	1.5X for 4 holidays 1X for 8 holidays
Montgomery County	9	1.5X
Prince George's County	12	2X
State of Maryland	10	Straight time compensatory time
City of Philadelphia	11	1.5X
City of Memphis	13	1X
City of Columbus	10	1.5X

	Personal Days	Accumulation
Baltimore City	3	Employees may accumulate up to 8 days of personal leave. Unused personal leave is paid out at separation.
Anne Arundel County	1	No carryover
Baltimore County	6	No accumulation. May cash out personal leave earned but not used.
Harford County	8	No accumulation. May cash out personal leave earned but not used. Maximum of 2 days for all unused personal leave for any separation other than retirement.
Howard County	6	No accumulation. May cash out personal leave earned but not used.
Montgomery County	3	No accumulation. May cash out personal leave earned but not used.
Prince George's County	3.5	No accumulation or cash out of personal leave
State of Maryland	6	No accumulation or cash out of personal leave
City of Philadelphia	4	No accumulation or cash out of personal leave
City of Memphis	None	None
City of Columbus	1	No accumulation or cash out of personal leave

Regional Public Employers Paid Leave Comparisons – Civilian Workers

	Sick Leave	Sick Leave Cash Out
Baltimore City	12	Employees may convert 1 day of unused sick leave for each 4 sick days accrued during the year and at retirement. Days not cashed out carry forward to the next year.
Anne Arundel County*	15	Most employees are not entitled to be paid for disability leave upon separation. On and after September 1, 1986, a management, professional, or confidential employee and employees in the classifications of Fire Battalion Chief and Police Lieutenant shall be paid \$25 for each day of disability leave earned but not taken at separation.
Baltimore County*	15	None
Harford County*	15	None
Howard County	12	Employees who have accrued 12 disability leave days and have used four or less days during the year for personal or family illness or physician's appointments may, at their option, cash in two of their remaining days for one day's pay.
Montgomery County*	15	None
Prince George's County*	15	Sick leave earned after 1997 is not subject to cash payment upon separation.
State of Maryland*	15	None
City of Philadelphia	15	A non-uniformed employee who terminates employment receives payment at current regular rate of pay for 30% of the number of days of accumulated sick leave. The maximum number of accumulated sick leave days is 200 days. In lieu of a cash payment at retirement, a non-uniformed employee may elect to use all or part of his or her accumulated sick leave to purchase an extension of the five (5) year period of retiree health coverage
City of Memphis	<5 YOS: 12 days 6 to 9 YOS: 18 days 10 to 14 YOS: 24 days 15+ YOS: 30 days	Employees are compensated in cash for up to 75 days of accumulated unused sick leave upon retirement.
City of Columbus	12 days	Sick leave may be converted to cash payment upon separation at the following ratio: <950 hours: 1:4 ratio 951 to 1,750 hours: 1:3 ratio

*Accumulated sick leave may be applied toward credited service for retirement purposes in accordance with the rules and regulations of their respective pension system

2012 Health and Retirement Benefits Benchmarking Findings

Hay Group conducted two separate benchmarking analyses for this study, evaluating plan designs as of 2012. The first comparison benchmarked the City's programs against seven local jurisdictions as well as the federal government. The second comparison benchmarked the City's programs against a comparator group of national organizations.

Methodology

Hay Group has developed a method of evaluating benefit plans in terms of a consistent standardized cost of employment. This valuation method is applied to the full range of employee benefits including:

- Pension and Capital Accumulation Plans
- Health Insurance
- Life Insurance
- Disability Insurance and Sick Leave
- Vacations and Holidays
- Statutory Benefits
- Other Benefit

While the standard values developed for such benefits are representative of average costs, they should not be interpreted as the actual costs of any given employer's benefits package. Although actual cost is clearly of vital concern to an employer, attempting to compare benefits across multiple organizations has the following disadvantages which render it less useful for most benefit plan comparison studies, including the type of studies performed for the City and discussed herein:

- An organization's bargaining power and skill as a benefits buyer is one variable making actual cost unreliable as a tool for measuring the relative value of benefits.
- Funding, financing, experience and accounting techniques vary widely among organizations. Therefore, the actual cost of two identical benefits can be different for a host of reasons not related to the benefit itself.
- The employee "mix" can vary substantially among employers. The distribution of employees by age, sex, service, salary level, and relative health is rarely similar from one firm to another — all of which factors significantly impact the actual cost of benefits.

- Complete and accurate actual costs are not always available from survey participants.

For these reasons, Hay Group does not use actual cost in studies comparing benefit values, but instead has developed a technique of "common costs" which permits the assignment of dollar values without the problems associated with using actual costs.

Local Jurisdictions

Following discussions with City representatives, we established that our local governmental benchmarking comparison would include the following governmental jurisdictions:

- Baltimore County
- Montgomery County
- Harford County
- Howard County
- Prince George's County
- Anne Arundel County
- State of Maryland
- US Federal Government

Each of these jurisdictions offers employees a variety of health plan options. For purposes of this study, we valued the most prevalent (or highest enrollment) plan for each jurisdiction.

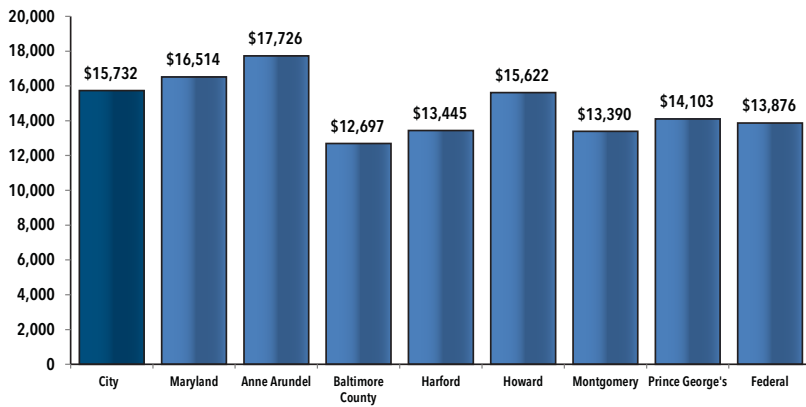
Comparison of Health Care Plans

The chart that follows shows a comparison of the value of the 2012 healthcare benefits offered in the local jurisdictions. As described above, these values represent the standardized cost of employment rather than the actual cost of these programs for each local jurisdiction. In addition, Hay only valued the benefits for the plan offered in each jurisdiction with the highest enrollment.

The values in the chart that follows reflect the 2012 value of these jurisdictions' full healthcare programs, including medical, pharmacy, dental and vision benefits. **As a result of analysis conducted for this Ten-Year Plan, a revised, more affordable health benefits structure has been adopted for 2013 and beyond.**

The City's healthcare benefit program is more valuable than the programs offered in most of the local jurisdictions surveyed. Only Anne Arundel County and the State of Maryland plans have higher values than the City's healthcare programs. The value of the program is most affected by the level of out-of-pocket costs,

Comparison of Healthcare Benefit Values (2012)



Note: The City implemented a new healthcare plan for 2013, with a value of 14,222 (about 10% lower than the 2012 plan).

including deductibles and co-pays, the type of plan offered (HMO, PPO, etc.) and the portion of the premium the employee is expected to contribute. The table on the following page compares several key provisions of the benefits programs in each of the local jurisdictions surveyed.

The value of the Anne Arundel County benefits program is higher than the City's program as a result of a unique triple option plan design. In this program, employees have the opportunity to significantly reduce out-of-pocket costs by using providers in the BlueChoice network. Employees can also use providers in the broader PPN network or select out-of-network providers; however, higher out-of-pocket costs are associated with out-of-network providers. Employees can choose any level of coverage each time they receive services. In other words, an employee could use a combination of Blue Choice, PPN and out-of-network providers throughout the course of the year.² For this analysis, we have used the deductible, copayments, and coinsurance that apply for employees when they take advantage of the BlueChoice network. The out-of-pocket costs for employees who use CareFirst's PPN network are comparable to the out-of-pocket costs for City employees.

The State of Maryland plan is very similar to the City's plan, but the State's plan has a slightly higher value due to lower office visit and prescription drug copayments.

CareFirst's PPN network out-of-pocket costs are comparable to the out-of-pocket costs for City employees.

Examination of the chart of key features that follows indicates that there is no one feature of the City's health plan that stands out as significantly beyond the norms of the group; however, it is the

combination of several features that make the City's health plan one of the most expensive in the local comparator group. Specifically, the City's health plan provides among the higher employer contributions (as a percentage of total health plan cost), with prescription drug coverage being provided at no cost to employees as of 2012, and the City's plan has no deductible, which is significantly more generous than the average deductible of approximately \$140 for individuals. Additionally, the copays in the City's plan are in the mid-range for the group. These features, in the aggregate, contribute to making the City's health plan among the more costly among the local jurisdictions.

With respect to the City's prescription drug plan, as indicated above, the most expensive aspect of the City's drug plan is that 100 percent of the prescription drug plan premiums are paid for by the City. That feature alone more than makes up for the fact that the City's prescription drug copays are among the highest in the local comparator group.

This helps to explain why the City's health plan, with the exception of the State's plan and the anomalous Anne Arundel County plan (which uses CareFirst's triple option), is among the most expensive of the local area jurisdictions surveyed. In particular, the value of the City's plan, on an average value per employee basis, is \$942 higher than the average for this group, and \$1,629 greater than the median for this group. The City's health plan is \$1,629 more expensive, on an average value per employee basis, than the Prince George's County plan; \$1,856 more expensive than the Federal Government's plan; \$2,342 more expensive than the Montgomery County plan; and \$3,035 more expensive than the Baltimore County plan. These are significant differences in plan values.

Note: This benchmarking is for the City's benefit structure prior to 2013 reforms developed through this Ten-Year Financial Plan Process. These reforms will save more \$20 million annually, while retaining competitive benefits valued at above the median for the local public sector comparables.

²The CareFirst triple option is valued as expensive in part because our model assumes people will select the most valuable features, though it is possible for a variety of reasons that such is not the case in practice. However, without additional utilization information, Hay cannot further refine this value.

Appendix E: Hay Group Benefits Benchmarking

Active Health Care Benefit Comparison

	City of Baltimore	Baltimore County	Montgomery County	Harford County	Howard County	Prince George's County	Anne Arundel County	State of Maryland	US Federal Government
Plan Options	6	3 (plus 1 option closed to new members)	4 (plus 1 option closed to new members)	4	3	3	3	8	22 in Region
Prevalent Plan Name (Type)	CareFirst BCBS PPN (PPO)	Cigna Open Access Plus (PPO)	BCBS High Option (POS)	CareFirst BCBS (PPO)	Aetna Open Access Select (EPO)	Cigna Open Access (HMO)	BCBS Triple Option	CareFirst BCBS (PPO)	BCBS Standard (PPO)
Eligibility	1st of the month following 30 days	1st of the month following completion of enrollment	Immediately	1st of the month following 30 days	1st of the month following hire	1st of the month following 45 days	1st of the month following hire	1st or 16th of the month, based on date of first payroll deductions	Enroll within first 60 days of employment
Employer Share of Premium (Single)	80% PPO 90% HMO	80%	75%	80%	85% PPO 90% HMO	78%	80% PPO 90% HMO	80%	68%
Employer Share of Premium (Family)	Same	75%	75%	80%	85% PPO 90% HMO	78%	80% PPO 90% HMO	80%	67%
Annual Deductible	None	\$200 Ind \$400 Family	\$300 Ind \$600 Family	\$250 Ind \$500 Family	None	\$50 per individual	\$100 Ind \$200 Family	None	\$350 Ind \$700 Family
Annual Out-of-pocket max	None	\$1,000 Ind \$2,000 Family	\$1,000 per person	None	None	\$2,000 Ind \$4,000 Family	\$500 Ind \$1,000 Family	None	\$5,000
Inpatient Hospital	Covered in full	Plan pays 85% after deductible	\$150 per admission copay	Covered in full, after deductible	Covered in full	\$250 per admission deductible	Plan pays 95% after deductible	Covered in full	\$250 per admission deductible
Office Visit Physician Specialist	\$20 copay \$25 copay	\$15 copay \$25 copay	\$15 copay \$15 copay	\$30 copay \$30 copay	\$10 copay \$20 copay	\$30 copay \$35 copay	\$5 copay \$10 copay	\$15 copay \$25 copay	\$20 copay \$30 copay

Active Health Care Benefit Comparison – Prescription Drug Benefits

	City of Baltimore	Baltimore County	Montgomery County	Harford County	Howard County	Prince George's County	Anne Arundel County	State of Maryland	US Federal Government
Prescription Drug Benefits									
Plan Type	Separate Plan	Separate Plan	Separate Plan	Included in Medical	Included in Medical	Separate Plan	Included in Medical	Separate Plan	Included in Medical
Copay (\$) or Coinsurance (%)									
Retail									
Generic	\$15	\$5	\$10	\$10	\$10	\$10 copay	\$5	\$10	20%
Preferred Brand	\$30	\$20	\$20	\$25	\$30	Greater of \$20 or 20%	\$15	\$25	30%
Non-preferred Brand	\$40	\$35	\$35	\$45	\$50	Greater of \$40 or 40%	\$25	\$40	30%
Mail Order									
Generic	\$20	\$10	\$10	\$20	\$10	\$20	\$10	\$20	\$10
Preferred Brand	\$40	\$40	\$20	\$50	\$30	Greater of \$40	\$30 or 20%	\$50	\$70
Non-preferred Brand	\$60	\$70	\$35	\$90	\$50	Greater of \$80 or 30%	\$50	\$80	\$70 for first 30 scripts & \$50 thereafter

Appendix E: Hay Group Benefits Benchmarking

National Comparator Group

In addition to the comparison of the benefit values in certain local jurisdictions, Hay also completed a comparison of the City's healthcare benefits against the following major U.S. city governments:

- Atlanta
- Boston
- Philadelphia
- Pittsburgh
- Tampa
- Washington, D.C.

As indicated in the chart that follows, the City's healthcare value is in line with the above sampling of large east-coast cities. The average value of the City's coverage is 98 percent of the large cities comparator group's, and the City's value is exactly at median for the group. That said, there is a significant range of healthcare values, ranging from \$11,994 for Washington, D.C. at the low end, to \$18,136 for Philadelphia; a range that spans 40 percent of the average. This indicates there are significant variations in the surveyed cities' plans. Given the substantial trend toward controlling employers' healthcare costs, there can be little doubt that these cities are in various stages of controlling their healthcare costs. These efforts may be difficult to track because of the timing of renewals of various collective bargaining agreements.

The City's health plan value is above the market median compared to the nationwide comparators. The nationwide comparators offer employees a choice of health plans including PPO and HMO options. The employer share of the premium ranges from 70 to 90 percent. Most of the jurisdictions require a deductible and office visit copays range from \$15 to \$35 for primary care physicians. A higher copayment applies for specialty care. Inpatient hospital services are not covered in full by most jurisdictions, however, a variety of cost-sharing approaches are used including per admission copayments, per day copayments and coinsurance. Each of these jurisdictions offers a comprehensive and competitive health care program. Some cities, however, have taken unique steps to reduce costs while continuing to provide quality benefit programs.

Recent Healthcare Reform

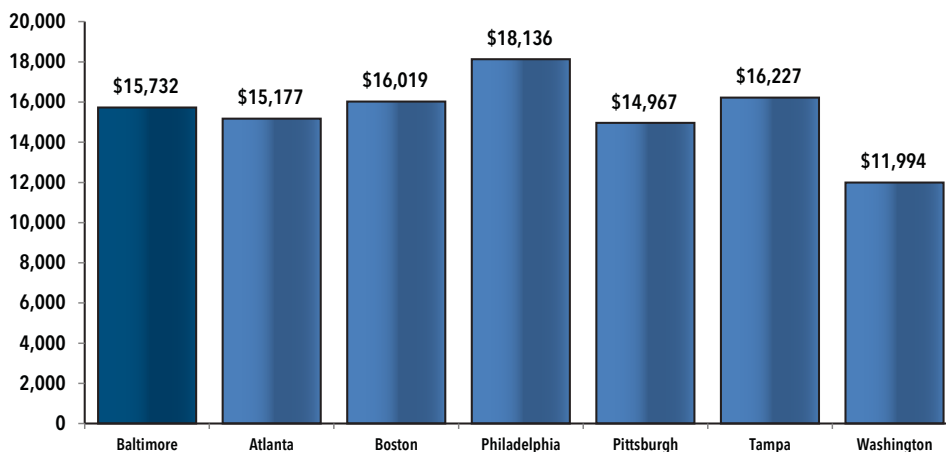
Both nationally and locally, public employers have implemented initiatives to contain fast-growing healthcare costs.

The **City of Tampa** has increased focus on wellness initiatives over the past two years. In 2011, Tampa introduced two Employee Wellness Centers which provide primary, acute and urgent care to employees and non-Medicare retirees and their dependents enrolled in the City's health plan. There is no co-pay for office visits, generic prescriptions or supplies dispensed at the centers. Tampa also offers lower premium sharing and higher first dollar benefit allowance to employees who are tobacco-free and/or complete a personal health assessment. The first dollar benefit allowance is an allowance of money paid by the City that is available to pay for medically necessary services received from

network providers and helps covered members pay for out-of-pocket expenses. The allowance is paid before members begin paying deductibles.

The **City of Philadelphia** does not directly administer health benefits for its four largest unions (FOP, IAFF, DC 33 & DC 47). Instead, the City makes a monthly contribution for bargaining unit members to health and welfare trust funds, which are administered independently by each union. In recent years, the City's contributions to the funds have been reduced, resulting in

Comparison of Healthcare Values (National)



significant cost savings. For example, the City’s annualized per employee contribution to the FOP Trust Fund was reduced from \$15,636 in FY2008 to \$13,980 in FY2009 to \$11,580 in FY2010 — a total cut of over 25% – with a more cost-effective self-insured approach established thereafter. Although the average Philadelphia healthcare value is significantly higher than others (\$18,136), it is equally clear that the example of the contract between the FOP and Philadelphia is a harbinger for that city’s future reductions in healthcare costs.

In the **City of Boston** employees represented by AFSCME have been subject to increased employee health care contributions. Effective January 1, 2009, the City increased employee contributions to health premiums for HMOs from 12.5% to 15.0% of premium, while employee contributions for POS coverage rose from 17.5% to 20.0% of premium.

Employees of the **City of Pittsburgh** now contribute to the cost of health care at approximately 15% of premiums. Prior to 2005, no employee contributions were required.

Montgomery County, Maryland, implemented changes to its health benefits program in FY2012. These changes applied to both civilian and public safety employees and included the following:

- Increased employee contributions toward the CareFirst Standard and High Option POS plans from 20% to 25% of premium.
- Increased employee contributions toward the Caremark Standard Option Rx plan from 20% to 25% of premium. This premium increase resulted in higher employee costs for the Caremark High Option Rx drug plan as well, since it is structured as a “buy-up” based on the cost of the standard plan.

In FY2012 the **State of Maryland** implemented a new prescription drug plan with increased employee and retiree cost sharing, as follows:

- Increased employee prescription drug out-of-pocket maximums to \$1,000 individual/\$1,500 family
- Increased retiree prescription drug out-of-pocket maximum to \$1,500 individual/\$2,000 family

- Increased retail prescription drug co-pays from \$5/\$15/\$25 to \$10/\$25/\$40
- Increased mail order prescription drug co-pays from \$10/\$20/\$20 to \$20/\$50/\$80

Retiree Health Care

Currently, the City provides a subsidy to retirees to offset the cost of retiree medical coverage. The subsidy provided is the same for the retiree and the retiree’s covered dependents. The subsidy is 50% for employees who retire with a minimum of 15 years of service and 20% for employees with 9 to 14 years of service. No subsidy is offered to employees with less than 9 years of service; however, they can choose to participate in the plan by paying the full cost of coverage.

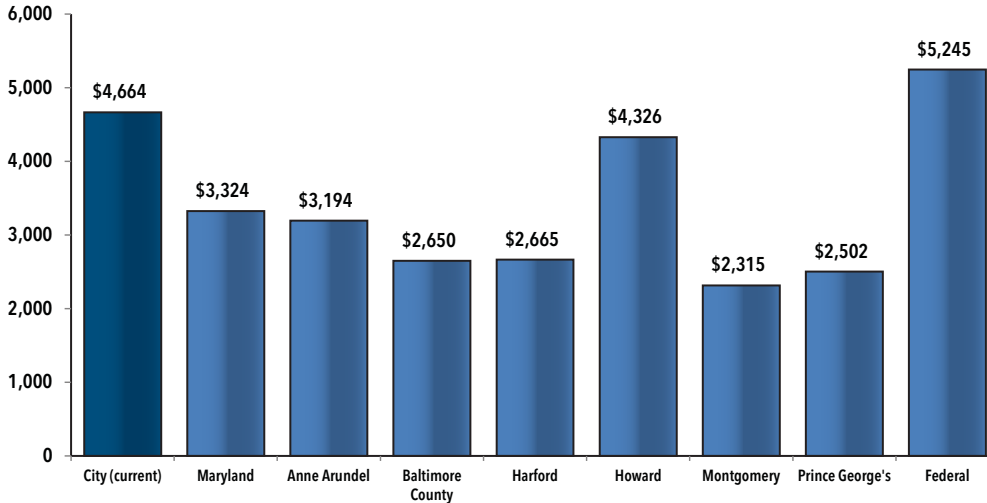
In addition, the City subsidizes 80 percent of the cost of retiree prescription drug coverage.

Most jurisdictions provide the same subsidy for covered dependents. Several of the jurisdictions provide a graduated subsidy which increases based on an employee’s length of service.

	Current Employer Subsidy for Retirees Healthcare	Spouse
City of Baltimore	50% of premium for medical (20% with 9 to 14 Years of Service), 90% for Rx (80% starting 1/1/2012)	Same
Anne Arundel	80% of premium	Same
Baltimore County	Graduated from 25% to 92%	Same
Harford	12-14 yrs 75%; 15-19 yrs 80%; 20-24 yrs 85%; 25+ 90%	Same
Howard	15-19 yrs 50%; 20-24 yrs 75%; 25+ 90%	25%
Montgomery	5 yrs 50%; 10 yrs 60%; 15+ yrs 70%	Same
Prince George's	HMO 78%; POS 73%	Same
State of Maryland	Retired pre-1984 up to 80%; Hired after June 2011; graduated up to 25 yrs	Same
US Federal Government	72% of the premium for the Standard BCBS Plan Option.	Same

Appendix E: Hay Group Benefits Benchmarking

Comparison of Retirement Values at \$40,000 Salary



Pension Benchmarking

As with Healthcare, Hay Group prepared two separate benchmarking analyses for the City's retirement program. Hay compared the City's retirement benefits to the retirement benefits offered by a group of local jurisdictions and a group of national jurisdictions.

The chart above shows the relative value of the City's retirement benefits compared to the local organizations included in this study. Retirement values vary based on the salary of the individual earning the benefit. We have shown a comparison of the retirement benefit values at the \$40,000 salary level for this report. In the local comparator group, only the Federal Government offers a more generous retirement benefit than the City of Baltimore. This is because the Federal Government offers a defined benefit plan which is combined with a defined contribution plan with employer contributions. The main factors that impact the value of the retirement benefit are the benefit formula, cost-of-living adjustments, early retirement provisions and whether the plan requires employee contributions. It is important to note that the values shown reflect the standardized cost of employment rather than the actual cost of providing these benefits or the actual benefit received at retirement.

Comparison of the Main Features for the Local Jurisdiction Retirement Plans

The table below provides a comparison of the main features of the retirement plans offered by the local jurisdictions.

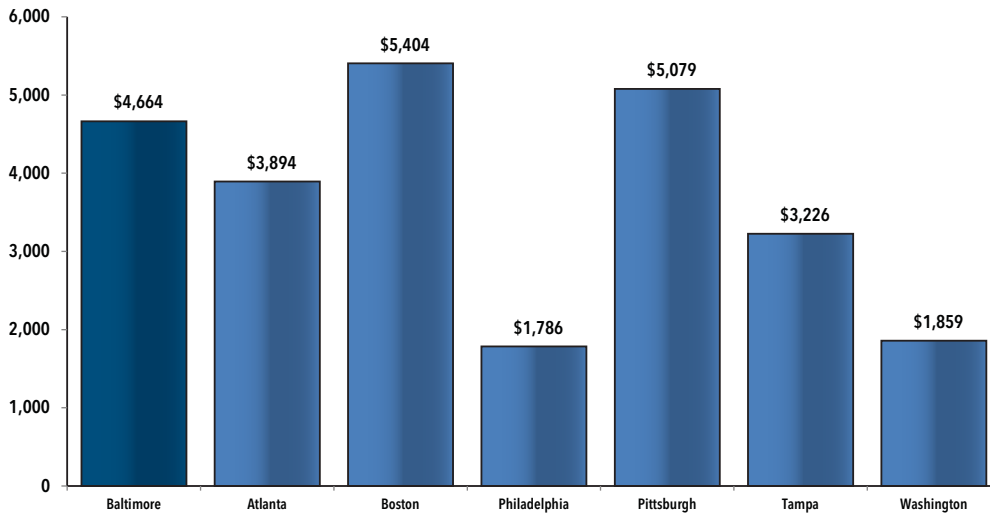
	City of Baltimore	Baltimore County	Montgomery County	Harford County	Howard County	Prince George's County	Anne Arundel County	State of Maryland	US Federal Government
Employee Contributions	None	7% for employees hired after 6/30/2012	4% of pay up to SS integration level + 8% of pay above SS integration level	7.0%	2.0%	5.5%	4.0%	7.0% for service after 6/30/2011	0.8%
Annual COLA	Yes, minimum of 1.5% plus amount based on funds' investment earnings	Yes, if sufficient excess investment income exists. Range from 1 to 3%, based on CPI. Depending on DOH & DOR. Must have 20 or 25 YOS	N/A	Determined during budget deliberations. Not annual	60% of CPI to a max of 2.5%	Yes, tied to CPI. Capped at 2.5% when funds meets or exceeds assumed rate of return or at 1% if assumed rate is not met	100% of CPI up to a maximum of 3%	100% of CPI up to a maximum of 3%. 100% of CPI up to a max of 3%. After 7/1/2011 - capped at 2.5% when funds meets or exceeds assumed rate of return or at 1% if assumed rate is not met	Begin at age 62. Amount is based on CPI.
Normal Retirement Eligibility	Age 65 with 5 YOS or 30 YOS	Age 67 with 10 YOS or 35 YOS	Age 62	Age 62 with 5 YOS or 30 years. For employees hired after 6/30/11 - Rule of 90 or Age 65 with 10 years of Service	Age 60 with 5 YOS or 30 YOS or employees hired after 6/30/11 - Rule of 90 or Age 65 with 10 years of Service	For employees hired after 6/30/11 - Rule of 90 or Age 65 with 10 years of Service	Earliest of 30 YOS or age 62 with 5 YOS or 63 with 4 YOS or 64 with 3 YOS or age 65 with 2 YOS	For employees hired after 6/30/11 - Rule of 90 or Age 65 with 10 years of Service	Age 62 with 5 YOS or age 60 with 20 YOS or MRA with 30 YOS
Benefit Formula	$[(1.6\% \times \text{FAC}) \text{ plus } (.25\% \times \text{FAC} \text{ in excess of covered comp}) \times \text{years of service up to 30}] \text{ plus } 1.85\% \times \text{FAC} \text{ for each year of service above 30}$	1/70th times years of service times FAC 1/70th = 1.428%	Cash Balance Plan: 6% Annual employer contribution with guaranteed interest rate of 7.25%	$[0.8\% \times \text{FAC up to covered comp} \times \text{YOS}] \text{ plus } [1.5\% \times \text{AFC above covered comp} \times \text{YOS}]$	$2\% \times \text{FAC} \times \text{credited service, with max of 60\% of AFC}$	$1.5\% \times \text{FAC} \times \text{Years of Credit}$ (Other formulas apply for employees hired prior to July 1, 2011)	$1.55\% \times \text{FAC} \times \text{credited service}$ (some at 1.66% effective 7/1/11)	$1.8\% \times \text{FAC} \times \text{credited service}$ (Multiplier is 1.5% for new hires after 7/1/11)	$1\% \times \text{hi-3 average pay} \times \text{service}$ (1.1% if the member retires at age 62 or later with 20 YOS or more)
Final Average Compensation	Based on highest 3 consecutive years	Highest 36 consecutive months	N/A	Highest 36 consecutive months. New hires after 6/30/11 - highest 5 consecutive years	Highest 3 out of last 5 years	Average of 5 highest consecutive annual salaries during career	Highest 36 months	Highest 36 consecutive months. New hires after 6/30/11 - highest 5 consecutive years	Based on highest of final 3 years

Appendix E: Hay Group Benefits Benchmarking

National Comparison

The chart below shows the relative value of the City's retirement benefits compared to other national cities.

Comparison of Retirement Values at \$40,000 Salary





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