IN RE WAIVER REQUEST OF MONTGOMERY COUNTY

BEFORE THE

MARYLAND

STATE BOARD

Fiscal Year 2010
Maintenance of Effort

Waiver Request No. 2009-1

# OPINION

## INTRODUCTION

Montgomery County has requested a waiver of its maintenance of effort ("MOE") requirement. To obtain a waiver of its MOE, Montgomery County must show that the county's fiscal condition significantly impedes its ability to fund the MOE requirement. Md. Educ. Code Ann. §5-202(d)(7).

## PROCEDURAL BACKGROUND

On March 23, 2009, the State Board established a process and procedure to the MOE waiver requests that the State Board received on April 1, 2009. As to any requested waiver of the MOE filed on April 1, 2009, the public, including the local board of education, could file a response by April 10, 2009. The county's Reply was due on April 15, 2009. The State Board of Education scheduled a hearing for April 27, 2009 to give the county government, the local school system and a parents' representative the opportunity to make an oral argument.

On April 1, 2009, eight counties requested waivers of their MOE funding obligations. The eight counties were: Anne Arundel, Calvert, Charles, Frederick, Montgomery, Prince George's, Wicomico, and Worcester. As required by COMAR 13A.02.05.04, and by request of the State Board, each county submitted the following information: a narrative statement, the amount requested to be waived, the county's projected fiscal condition, the county's revenue stream, any prohibition against raising revenue, three prior year audited financial statements, projected expenditure plan, additional information, a statement whether the school board supports or opposes the request, and the amount of funding anticipated through the Federal Fiscal Stabilization Act and the American Recovery and Reinvestment Act of 2009 and the positive or negative effect of such funding on local maintenance of effort for schools.

Prior to the April 27, 2009 public hearing, Anne Arundel, Calvert, Charles, Frederick, and Worcester counties withdrew their MOE waiver requests. Anne Arundel County determined that it could fund the Board of Education at the MOE level, even though "this was a very difficult exercise in fiscal management." Calvert County found a way to meet the Board of Education's MOE funding and manage the FY 2010 budget through the "use of available monies in other funds and additional expenditure reductions." Similarly, Charles County has "found a way to fully fund the maintenance of effort." Frederick County spent many hours "working on our budget" before deciding to withdraw its MOE waiver request. Worcester County withdrew its MOE waiver request after staff worked "tirelessly to determine every possible cost saving measure available to reduce expenditures."

Montgomery, Prince George's, and Wicomico counties maintained their waiver requests and presented oral argument on April 27, 2009. Isiah Leggett, County Executive, presented on behalf of Montgomery County. The President of the Board of Education, Shirley Brandman, also presented, conditionally supporting the counties' waiver request. No parent representative submitted a position or argument.

FACTUAL BACKGROUND

**Amount Requested To Be Waived**

Initially, Montgomery County requested a waiver of $94,852,285 from its MOE of $1,529,554,447. At the April 27, 2009, public hearing Montgomery County reduced its waiver request to $79,537,322. With the waiver, the county proposes an appropriation to the local board of education of $1,450,017,125.

**Projected Fiscal Condition – FY 2010**

According to the information and documents that Montgomery County filed, total revenue for fiscal year 2010 is projected to be $3,795,300,000, an increase of $18.9 million from fiscal year 2009. Total expenses are projected to be $4,424,900,000 causing an estimated budget shortfall for FY 2010 of over $600 million dollars. During the public hearing the county asserted that with the current estimated shortfall of $600 million, it was experiencing a $1.2 billion cumulative deficit in its budget, including a $400 million deficit for FY2009 and a $200 million dollar deficit for FY2008.

For fiscal 2010, Montgomery County estimates increased property tax revenue of $1,438,700,000, an increase over fiscal year 2009. Montgomery County also estimates increased revenue from recordation tax with premium for fiscal year 2010 of $51.9 million, an increase from fiscal year 2009. It anticipates an increase of revenue from fines and fees, energy, telephone, and hotel taxes.

Transfer tax revenue for FY 2010 is estimated to be $65 million, a reduction from the fiscal year 2009 estimated revenue. Income tax revenue is expected to decrease to $1,214,800,000 by FY 2010. Montgomery County also anticipates reduced revenue in fiscal year 2010 from highway user fees and investments. Moreover, the Federal Reserve rate cuts have reduced projected investment income by nearly 60 percent.

Since May 2008 the county revised its fiscal year 2009 and 2010 revenue projections down $340 million because of reductions in income tax, transfer tax, investment income, and state highway user aid. It estimates a reduction of 10% tax revenue. The county estimates a revenue stabilization fund ("Rainy Day" fund) of $119,600,000 by the end of fiscal year 2009.

County employers added 1,800 jobs in 2008, a .4% increase. Unemployment increased to 4.6% in January 2009, the highest level since 1990; however the county unemployment rate remains low compared to the State and the nation. Resident employment is stagnant. The county anticipates that an average of 4,350 new jobs to be added between 2008 and 2015. The public sector provides a stable foundation against "significant labor market volatility" nationwide. The large presence of the federal government, in terms of employment, procurement, and federal retirees, generally insulates Montgomery County's economy, from the volatility that is experienced nationally.

Home sales declined 17.8% in 2008, 23.4% in 2007, 20.5% in 2006. During the public hearing, the county stated that it has seen a 25% decrease on the sales of homes, a decline in the price of homes, and an increase in foreclosures. Residential construction declined 8.3% from 2007-08.

**Prohibition against Raising Revenue**

Montgomery County has two constraints to raising revenue. Section 305 of the Montgomery County Charter requires a unanimous vote of the county council to raise property taxes beyond the rate of inflation. The county does not support seeking a property tax increase. The income tax rate is at the State allowed maximum rate of 3.2%.

**Projected Expenditure Plan - - Fiscal Year 2009 and Fiscal Year 2010**

The county projects mid-year reductions of $48.8 million in fiscal year 2009. For fiscal year 2010, the county projects reductions of $130.4 million. It would abolish 400 county government positions, eliminate general wage adjustments, eliminate a $25 million increase in pre-funding of retiree health insurance, and it plans to reduce county reserve by $40 million.

**School Board Conditionally Supports the Waiver Request**

The Montgomery County Board of Education conditionally supports the county's waiver request. The Montgomery County Board of Education stated that it could agree with the waiver request if: 1. No further cuts were made to the MCPS budget; 2. MCPS gets federal stimulus funds per the plan submitted to the county; and 3. The fiscal year 2011 MOE is based on fiscal year 2009 local appropriation. During the April 27, 2009 hearing, the representative of the board of education stated that they had assurances from the County Executive and the County Council that the conditions would be met.

The FY 2010 education budget is $64 million over fiscal year 2009, without the federal stimulus funds. In the County Executive's recommendation for the MCPS FY 2010 Operating Budget, this amount was reduced by $24 million. The County stated, however, that the County Executive's recommended budget for FY 2010 would fund nearly 99% of the BOE request. Both the county and the local board of education agree that reductions do not impact education programs.

The local board of education has reduced fiscal year 2010 expenses by $89 million in cost of living allowance (COLA) payments. The Montgomery County Board of Education will further reduce its budget by $30 million for fiscal year 2010 in addition to $20 million in position freezes and expenditure restrictions in fiscal year 2009.

**Amount of Anticipated Federal ARRA and Stabilization Funds.**

The county stated that the local board of education will receive $6.1 million in ARRA funds for Title I programs and $15.3 million for the Individuals with Disabilities Education Act (IDEA). They assert that the stimulus funds will not have any effect on meeting the State MOE requirement. In addition, there are federal Stabilization Funds that the Governor has appropriated for funding schools in Maryland. The local board of education is expected to receive $36 million in ARRA Stabilization Funds.

LEGAL ANALYSIS

**A. Maintenance of Effort History**

Before addressing the relevance and materiality of the facts presented in this case, we address the law governing our decision. For the first time since the passage of the MOE waiver statute and the waiver regulations, we are called on to interpret that statute and regulations and to explain, not only the evidence we will consider in our decision making, but also the weight we will attached to that evidence. We are guided in our interpretation by the underlying premise for the maintenance of effort requirement. By law, in order to "be eligible" to receive State "foundation program" funding for education, a county government must levy taxes sufficient to provide "the local share of the foundation program" funds. Md. Educ. Code Ann. § 5-202(d). In other words, the State and local governments are to share the cost of providing an education to public school students in each county.

The local governments' MOE requirement has long been a component of the total public school funding law in Maryland. It was added to the public school funding law by the General Assembly in 1984. Chapter 85, Laws of Maryland 1984. *Letter to Ecker*, 76 Md. Op. Atty. Gen. 153 (Mar. 6, 1991). To meet the MOE requirement, the county governing body must appropriate local funds to the school operating budget in an amount no less than the product of the county's full-time equivalent enrollment for the current fiscal year and the local appropriation on a per pupil basis for the prior fiscal year. Md. Educ. Code Ann. §5-202(d)(1)(ii). The local appropriation for the prior fiscal year for a county is calculated on a per pupil basis by dividing the county's highest local appropriation to its school operating budget for the prior fiscal year by the county's full-time equivalent enrollment for the prior fiscal year. Md. Educ. Code Ann. §5-202(d)(2).

The Bridge to Excellence Act, which sets forth the education funding formula, recognizes that the local share will vary depending on the wealth of the county. *See, e.g.*, Md. Educ. Code Ann. §§ 5-502(a)(7) & (8); 5-210. But, State/local sharing of the costs of education is the cornerstone of education funding in Maryland. Indeed, in 2002 when the Commission on Education Finance, Equity and Excellence published its comprehensive report ("a/k/a, Thornton Commission Report") on how to achieve a level of constitutionally adequate funding for education in Maryland, it stated:

> Although meeting the adequacy goals adopted by the Commission will require a significant increase in State aid over the next five years, funding the public schools remains a shared responsibility between State and local governments. Reaching adequate funding, therefore, will require additional local funding for the schools.

Thornton Commission Report at 73.

The Commission addressed the important role of local funding in achieving adequate funding:

> The Commission believes that the current maintenance of effort requirement has generally worked well to ensure a minimum level of funding for the public schools and recommends no change to the requirement. In recent years, aggregate county support for education

> has substantially exceeded the maintenance of effort requirement. Meeting adequacy goals by fiscal 2007 will require that counties continue to exceed maintenance of effort. The Commission estimates that if counties provide increases in education funding comparable to the increases provided from fiscal 1997 to 2000, most school systems would meet or exceed adequacy goals by fiscal 2007. . . . [T]he Commission believes strongly that maintenance of effort only establishes the minimum funding level. Achieving adequate funding will demand that counties continue to display the level of commitment to public education that the majority of counties have repeatedly demonstrated in the past.

*Id.*

Thus, when a county government requests a waiver from paying its maintenance of effort in full, we must consider carefully the full implications of that request, not only at the local level, but statewide as well, because any crumbling in the cornerstone of the State/local share formula for funding education can affect the structural soundness of the education funding formula going forward.

With those guiding principles in mind, we have reviewed the law and regulations that govern the waiver of maintenance of effort. The law establishes that the county may obtain a waiver of MOE if the State Board determines "that the county's fiscal condition significantly impedes the county's ability to fund the maintenance of effort requirement." Md. Educ. Code Ann. § 5-202(d)(7). After that law passed, the State Board promulgated regulations that explained the factors the State Board would consider in making its decision. They are:

(a) External environmental factors such as a loss of major industry or business;
(b) Tax bases;
(c) Rate of inflation to growth of student population;
(d) The maintenance of effort requirement relative to the county's statutory ability to raise revenues.

COMAR 13A.02.05.04(C)(2).

### B. Burden of Proof

In presenting evidence of the factors to the State Board that a county's fiscal condition significantly impedes its ability to fund MOE, the county has the burden of proof by a preponderance of the evidence. COMAR 13A.02.05.04C(3).

The standard of proof by a preponderance of the evidence is defined in the Maryland Pattern Jury Instructions as follows:

> To prove by a preponderance of the evidence means to prove that something is more likely so than not so. In other words, a preponderance of the evidence means such evidence which, when considered and compared with the evidence opposed to it, has more convincing force and produces in your minds a belief that it is more likely true than not true.
>
> If you believe that the evidence is evenly balanced on an issue, then your finding on that issue must be against the party who has the burden of proving it. (MPJI-Cv 1:7)

See also *Coleman v. Anne Arundel County Police Dept.*, 369 Md 108, 127n.16 (2002).

Thus, for the county to prevail in its request for a waiver, we must be convinced that it is more likely than not that events in the county have affected the county's fiscal condition such that it "significantly impedes the county's ability to fund the maintenance of effort requirement" for fiscal year 2010.

### C. Factors for Granting a Waiver

As stated previously, for the first time since COMAR 13A.02.05.04C was promulgated in 1997, we are called on to define the parameters of each of the factors that the Board will consider.

(1) External Environmental Factors

The term "external environmental factors" can be read two ways - - broadly to include a general, severe economic downturn, or narrowly to include only extraordinary economic events unique to the county requesting the waiver. The regulation itself provides some guidance on how to interpret the term "external environmental factors." The regulation qualifies that term with the phrase "such as a loss of major business or industry." That qualification provides an example of the type of external environmental factor that we should consider in deciding the waiver request. That qualification limits the expansiveness of the term "external environmental factor."

Turning to the rules of statutory construction, we are guided by the principle of *ejusdem generis*. Under that rule, when general words in a statute follow the designation of particular things or subjects, the general words will usually be construed to include only those things or subjects in the same class as those specifically mentioned. *Handley v. Ocean Downs, LLC*, 151 Md. App. 615, 637 (2003). Thus, because the regulation defines the class as including events like a major loss of business or industry, we will interpret the term external environmental factor in the narrow way because a loss of major business or industry is an extraordinary event unique to a county.

(2) Tax Bases

The regulation provides no internal guidance on the parameters for consideration under the "Tax Base" factor. The statutory requirement that a county show that its fiscal condition "*significantly*" impedes its ability to fund MOE in full provides guidance to us, however. Because the county must establish that significant impediments exist, we will look for evidence of significant impacts on the county's tax bases. Thus, within the Tax Bases factor we will look for evidence of the complete loss of one tax base or significant losses across all or most of a county's tax bases because such losses could "significantly impede" a county's ability to fund MOE in full.

(3) Rate of Inflation Relative to Growth of the Student Population

For the purposes of the cases before us, this factor does not come into play at all because inflation is not an issue nor is growth in student population.

(4) Maintenance of Effort Relative to Statutory Ability to Raise Revenue

In considering the relationship between the MOE requirement and the county's statutory ability to raise revenue, we note that a separate section of the regulation directs the county to explain "statutory prohibitions for raising revenue." COMAR 13A.02.05.04A(3)(c). The regulation does not establish, however, whether a prohibition on raising revenue should be weighed as a positive or negative factor in favor granting a waiver. In considering this issue, we return to the underlying premise of education funding in Maryland - - that to receive the State share of education funding, the county government must levy sufficient taxes to cover its minimum local share, *i.e.*, the MOE amount.

In some counties in Maryland there are locally imposed caps on taxes and/or other significant locally imposed impediments to increasing taxes. We do not opine on the propriety of those locally imposed prohibitions or impediments. We do opine, however, that based on our understanding of the State/local share requirements contained in Maryland's education funding formula, when we consider a county's ability to raise revenue we will give locally imposed prohibitions little weight in the balance.

We adopt this position because each county and its voters are free to restrict tax increases, but in our view, each is not free to abdicate its responsibility to fund its minimum local share of education costs. If we gave locally imposed prohibitions great weight in our analysis, we envision legal and public policy consequences that could destroy the cornerstone of the education funding formula because any county in Maryland can, by referendum or otherwise, cap its property or other tax bases at a level that would ultimately preclude the county from raising sufficient taxes to fund MOE in full. That is not an outcome this Board could sanction by interpretation of our regulation.

We are guided here again by the Thornton Commission Report and the concerns the Commission expressed on the issue of locally imposed impediments to tax levies.

> The Commission is concerned, however, that some local property tax policies may impede the ability of counties to sufficiently fund education during the five-year phase-in of the Commission's funding proposal. . . .[F]ive charter counties (Anne Arundel, Montgomery, Prince George's, Talbot, and Wicomico) have amended their charters to limit property tax rates or revenue growth. With the exception of Montgomery County, the limits can only be adjusted through a charter amendment. . . . County governments have three basic strategies for enhancing funding: (1) utilize annual increases in revenues from the county's existing tax structure; (2) raise tax rates or levy a new tax; and (3) reorder budget priorities to provide a larger budget share to education. The existence of a property tax rate or revenue limitation may constrain the use of the first two strategies, thereby impeding a county's ability to sufficiently increase education funding to meet adequacy goals.

*Id.* at 73-75.

With all those considerations in mind, we will give little weight to locally imposed prohibitions and impediments to tax levies. We will give great weight, however, to evidence of taxing limitations that the General Assembly imposes on a county by statute. For example, county income taxes are capped by State statute at 3.2%.

(5) Other Factors

As explained above, the regulation lists four factors that the State Board may consider in deciding the waiver request. We do not here exclude the possibility that other factors may be relevant and material. One dominant "other factor" in the cases before us is the recession and its impact on local revenues. When we consider this factor, however, we note that the recession impacts all counties in Maryland and that 21 of the 24 counties have not requested a waiver of MOE. Although three counties have requested a waiver for FY 2010, if the fiscal pressures on all of the counties and Baltimore City become so severe and wide-spread there may be a "tipping point" when a legislative solution rather than a State Board solution may be required.

Thus, to the extent that the recession is a factor, we will look for evidence that the county requesting the waiver has experienced a serious, significant economic impact that is different from the generalized economic impact experienced by other counties in Maryland. For example, evidence that the housing market has collapsed in the county may be given great weight in our deliberations, but downturns in housing market may be given little or no weight.

Again, we take this view of the evidence because, in our opinion, a waiver of MOE requires a showing that extraordinary events in the county have led to the need for such a waiver.

Another factor that this Board weighs in the balances is whether reduction in the minimum local share of education funding comports with the American Recovery and Reinvestment Act (a/k/a "the stimulus package;" "ARRA"). Under that recent piece of federal legislation, Maryland schools will receive over $1.2 billion additional federal dollars. To receive those funds, the local school system and the State must meet specific mathematical MOE requirements set by the federal government. It is too early to tell whether the local school systems will be able to meet those federal MOE requirements if the county reduces its MOE.

It is not too early to consider the other implications of a reduction of the county's MOE. Under the ARRA, to receive federal funds, States are required to make assurances directed at improving education, student achievement, teacher effectiveness, and closing the achievement gap and supporting struggling schools. Reducing the county's financial contribution to its school system could send the unintended message that the county is not on board with the State's assurances.

In addition, Maryland will be one of the States competing for a "Race to the Top" federal grant. In FY 2010, the Department will award $4.35 billion in grants to States in a national competition. The Race to the Top grants will support States that are making significant progress in meeting the four assurance goals and effectively using ARRA funds. The State's meeting its

MOE requirements will be a factor in that competition. A reduction in a county's MOE may cast a shadow on Maryland's competitive position.

### D. Montgomery County's Evidence

1. External Environmental Factors such as loss of Major Business or Industry

The loss of a major business or industry is an extraordinary event unique to the county. Montgomery County did not identify any major loss of business or industry that is unique to the county. It alleges that the current national economic crisis and international crises in credit markets caused its financial difficulty. The county states that it has seen a decline in the residential home sales over the past three years. Home sales in the county have declined 17.8% in 2008, 23.4% in 2007, 20.5% in 2006. In addition, residential construction declined 8.3% from 2007-08. The county points us to a generalized downturn in the housing market that all counties are experiencing. It did not allege or demonstrate that the housing market in the county had collapsed.

The county also points to a decline in retail sales. Retail sales decreased 12.2% in 2008. This also is not unique to the county. We recognize that retail sales have decreased generally in the State, and the nation. This is not comparable to the loss of a major industry or business to warrant the waiver of a portion of the county's share of public school funding.

2. Tax Bases

Montgomery County did not offer evidence of a complete loss of a tax base or significant loss across all tax bases. Instead, the documentation that the county provided demonstrates that its tax bases are more stable than most counties. The county has a low unemployment rate compared to the State and the nation. The large presence of the federal government, in terms of employment, procurement, and federal retirees provides a buffer so that Montgomery County's economy generally does not experience the volatility experienced nationally.

In addition, Montgomery County has a low unemployment rate compared to the State and nation. The public sector industry provides a stable foundation against significant labor volatility nationwide. The county predicts an average of 4,350 new jobs to be added each year between 2008 and 2015. County employers added 1,800 jobs in 2008. The county did identify reductions in tax revenue. While we recognize that the county needs to address these issues, they have not provided evidence of a loss of tax bases sufficient to tip the balance in toward the granting of a waiver from the MOE.

3. Rate of Inflation Relative to Growth of Student Population

Montgomery County's student population increased 1,424 students between September 30, 2007 and September 30, 2008 to 135,970 students. The county did not offer any evidence that the rate of inflation relative to growth in student population was a reason for granting the waiver. As we stated above, the rate of inflation relative to the growth of student population was not an issue regarding the request for a waiver.

4. MOE Requirement Relative to County's Statutory Ability to Raise Revenue

The county identified two constraints to raising revenue. One, Section 305 of the Montgomery County Charter requires unanimous vote of the county council to raise property tax beyond inflation. Two, the income tax rate is at the State allowed maximum rate of 3.2%.

In that regard, we give great weight to the fact that the county is prohibited by State law from increasing the income tax rate. We give little weight to the need for a unanimous vote to raise property taxes.

5. Montgomery County Board of Education Conditionally Supports the MOE Waiver.

The Montgomery County Board of Education and the county sought a collaborative approach to the MOE waiver request. The school board's support was conditional to preserving its priorities for no additional cuts to its budget, federal stimulus funding is provided consistent with the plan submitted to the county, and that the MOE for fiscal year 2011 is based on the fiscal year 2009 local appropriation. At the hearing, the county government affirmed that it was committed to meeting the board of education's conditions. In addition, Educ. Art. §5-202(d)(7) was amended to require a county's MOE for the next fiscal year to be based on the per pupil local appropriation of the greater of the prior fiscal year or the second prior fiscal year. Educ. Art. §5-202(d)(7)(v); Ch. ___, 2009 Laws of Md.

We commend the county and the board of education for working collaboratively to achieve a unified position. A unified position is meaningful, but is not a determinative factor for us to grant the MOE waiver. State law requires the local government to levy sufficient taxes to cover the minimum local share to receive the State share of the foundation program funds. In our view, absent exceptional circumstances, the county government must provide this minimum funding to the local board of education to maintain the structural soundness of the education funding formula.

CONCLUSION

Despite the agreement between the two governmental entities, the evidence and argument presented do not demonstrate by a preponderance of evidence that extraordinary events occurred in the county that significantly impede the county's ability to fund its MOE requirement. When we balance the weight of the evidence under each of the factors, no one factor, nor combination of factors, tips the balance in favor of granting this waiver request. We conclude that the county has not met its burden of proof. Therefore, we deny the request for a waiver of the maintenance of effort.

James H. DeGraffenreidt, Jr.
President

Dunbar Brooks

Charlene M. Dukes

Mary Kay Finan

Rosa M. Garcia

Richard L. Goodall

Karabelle Pizzigati

Ivan C.A. Walks \ TPS

Ivan C.A. Walks

Absent

Kate Walsh

Derek Wu EnK

D. Derek Wu

Dissent:

The Montgomery County case is a unique one. The initial problem was that there was adequate money to fund the schools, but not adequate money to fund both the schools and the county government operations. The local school board, the county executive and the county council have now all agreed on adequate funding for both the schools and the county government operations, but need the waiver they have requested to make the agreement effective. This is an example of good government at work. It ought to be encouraged and supported. The waiver should be granted.

Blair Ewing EnK

Blair G. Ewing
Vice President

Dissent:

I also dissent in this opinion.

Donna Hill Staton \ TPS

Donna Hill Staton

May 15, 2009