

**T50A99**  
**Maryland Economic Development Corporation**

***Financial Statement Data***

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**Maryland Economic Development Corporation Financial Statement**  
**Fiscal 2002 – 2004**  
**(\$ in Thousands)**

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>Change FY 03 - FY 04</u>
Net Assets	\$1,139,297	\$1,538,451	\$1,689,613	\$151,162
Net Liabilities	1,116,621	1,541,414	1,712,806	171,392
<b>Fund Equity</b>	<b>\$22,676</b>	<b>-\$2,963</b>	<b>-\$23,193</b>	<b>-\$20,230</b>
Total Revenue	27,642	49,667	77,172	27,505
Total Expenditures	32,726	75,306	99,151	23,845
<b>Net Income/- Loss</b>	<b>-\$5,084</b>	<b>-\$25,639</b>	<b>-\$21,980</b>	<b>\$3,660</b>

**Maryland Economic Development Corporation Financial Statement**  
**Change in Fund Equity and Net Income by Source**  
**Fiscal 2002 – 2004**  
**(\$ in Thousands)**

	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 04</u>	<u>Change FY 03 - FY 04</u>
Operating Facilities	\$1,105	-\$24,104	-\$46,895	-\$22,791
Other Operations	21,570	21,140	23,702	2,562
<b>Fund Equity</b>	<b>\$22,676</b>	<b>-\$2,963</b>	<b>-\$23,193</b>	<b>-\$20,230</b>
Operating Facilities	-4,923	-25,210	-22,791	\$2,419
Other Operations	-162	-429	811	1,240
<b>Net Income/-deficit</b>	<b>-\$5,084</b>	<b>-\$25,639</b>	<b>-\$21,980</b>	<b>\$3,660</b>

Note: Other operations are comprised of property and equipment rental; and consultant and management fees

Source: Maryland Economic Development Corporation fiscal 2004 financial statements

Note: Numbers may not sum to total due to rounding.

For further information contact: Stacy A. Porter

Phone: (410) 946-5530

## ***Analysis in Brief***

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### **Issues**

***Financial Losses Mount at Rocky Gap Lodge and Golf Resort (Rocky Gap):*** The State has invested a significant amount of money in Rocky Gap; however, the resort has posted a considerable net income loss in each fiscal year since its inception. Currently, the resort is not generating enough cash flow to service the interest burden on the \$26.1 million in senior debt held by the bond investors. **The Department of Legislative Services (DLS) recommends that the Maryland Economic Development Corporation (MEDCO) brief the committees on the losses associated with the Rocky Gap project and the financial outlook for fiscal 2005 through 2006. MEDCO should also comment on the potential impact these losses may have on MEDCO and the State's investment.**

***MEDCO's Involvement in Financing State Agency Projects:*** MEDCO is issuing revenue bonds to finance capital projects for State agencies. Since 1999, the number of State agencies MEDCO has provided financing for has increased from 4.2 to 25% of its total projects in fiscal 2004. Also, 34.8% of MEDCO's fiscal 2004 outstanding debt was issued on behalf of State agencies. The use of MEDCO by State agencies seems inconsistent with its mission to attract and retain business. **Consideration should be given to prohibit MEDCO from financing State agency projects through amendments to budget reconciliation legislation.**

### **Recommended Actions**

1. Nonbudgeted.

### **Updates**

***MEDCO Project Updates:*** The MEDCO 2004 Annual Report describes several recent and ongoing projects that are representative of the corporation's activity. This update gives a brief description of significant projects.

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***Operating Budget Data***

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**Program Description**

The Maryland Economic Development Corporation (MEDCO) is a nonbudgeted entity created in 1984 to allow the State the ability to directly own or develop property for economic development purposes. The corporation is governed by statute under Article 83A, Sections 5-201 through 5-216. A 12-member board of directors appointed by the Governor with the advice and consent of the Senate manages the corporation's affairs and appoints the executive director. The secretaries of the Departments of Business and Economic Development (DBED) and Transportation serve as ex-officio voting members. MEDCO's activities complement the marketing and financing programs of DBED. There are currently eight full-time and two part-time professional staff members.

Enacted as emergency legislation Chapter 338, Acts of 2001 amended MEDCO's corporate powers to conform to current practices. In addition, MEDCO's statutory authority was amended to be more consistent with the Maryland Economic Development Revenue Bond Act (MEDRBA) and economic development revenue bond enabling legislation in effect in other states which are competing with the State for economic development opportunities. For example, Chapter 338 amended MEDCO's legislative purpose to be virtually identical to those of the MEDRBA which governs all local bond issuing authorities (1) relieving the conditions of unemployment in the State; (2) encouraging the increase of business activity and commerce, and a balanced economy in the State; (3) assisting in the retention and attraction of new business activity in the State; (4) promoting economic development; and (5) generally promoting the present and prospective health, happiness, safety, right of employment, and general welfare of State residents.

MEDCO's mission is to assist in the expansion, modernization, and retention of existing Maryland business and to attract new business to the State. MEDCO purchases or develops property that is leased to others under favorable terms. MEDCO also makes direct loans to companies requiring financing to maintain or develop facilities throughout the State, often serving as the conduit for loans administered by DBED. MEDCO borrows money and issues bonds for the purpose of financing this assistance. The debt consists primarily of revenue bonds issued by the corporation – which are not obligations of the State – and notes payable to government agencies such as DBED. The debt represents non-recourse obligations of the corporation because MEDCO is not liable to bondholders and lenders in the event of project or borrower default. Because MEDCO debt is not debt of the State or of MEDCO, and each project has to support itself from its own revenues and no projects are cross-collateralized, there is no implied State guaranty or State obligation to protect bondholders from losses.

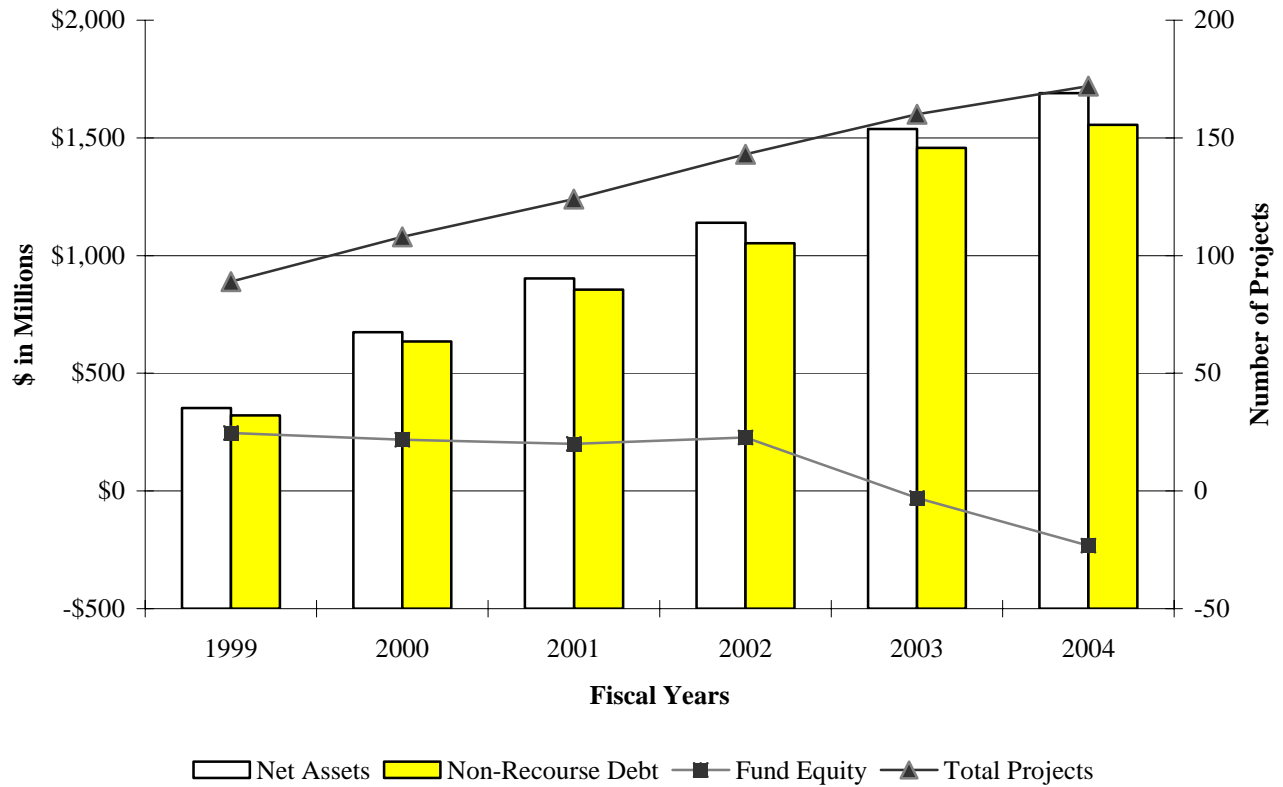
## **Fiscal 2004 Financial Statements**

As shown on page 1, MEDCO's revenues increased \$27.5 million, or 55.4% from \$49.7 million in fiscal 2003 to \$77.2 million in fiscal 2004. The increase in revenues is primarily attributable to an increase of \$16.7 million in operating revenues from the Chesapeake Bay Conference Center (CBCC), and an increase of \$9.1 million due to the completion of five new operating facilities in fiscal 2004. New operating facilities include Frostburg State University Student Housing; Morgan State University Student Housing; University of Maryland, Baltimore County Student Housing; University of Maryland, College Park South Campus Commons; and Compass Pointe Golf Course (not fully open). All five projects were completed and opened in fiscal 2004. Due to financial problems, Anne Arundel County voted to acquire Compass Pointe Golf Course from MEDCO in February 2005. The county may issue \$26.0 million in bonds to assume control of the golf course as early as May 2005.

Losses from operating facilities decreased approximately \$2.4 million in fiscal 2004. The decrease is largely due to reduced losses at CBCC and Rocky Gap. The reduced losses of \$3.1 million at CBCC are primarily due to higher occupancy and higher average room rates in fiscal 2004. The decrease in losses of approximately \$1.0 million at Rocky Gap is mostly due to lower depreciation expense as a result of the full depreciation of some furniture and equipment. The decreases in losses at both facilities are partially offset by net losses of \$3.2 million incurred by the five operating facilities that commenced operations during fiscal 2004. Additionally, interest expense increased 27.6%, or \$10.9 million from \$39.7 million in fiscal 2003 to \$50.6 million in fiscal 2004. The increase in interest expense relates primarily to interest incurred on debt related to CBCC and the new operating facilities. In fiscal 2004 all of MEDCO operating losses are attributable to the accumulated losses of its operating facilities. Exclusive of operating facilities, as shown in page 1, MEDCO's fiscal 2004 net profit was \$811,000. See **Appendix 1** for a complete list of the operating facilities.

Since fiscal 1998 there has been a significant increase in MEDCO's financial assistance activity. The cumulative number of projects assisted by MEDCO has increased from 65 to 172 from 1998 through 2004. As a result, the corporation's debt has also increased significantly. As shown in **Exhibit 1**, the corporation's non-recourse debt has increased from \$321.0 million in fiscal 1999 to \$1.6 billion in fiscal 2004. This compares to growth in assets from \$352.8 million in fiscal 1998 to \$1.7 billion in fiscal 2004. Since 1998 the rate of growth in the corporation's non-recourse debt has exceeded the rate of growth in net assets. The corporation's total fund equity has decreased from \$24.7 million in fiscal 1998 to negative \$23.2 million in fiscal 2004 as a result of continued and growing operating losses at its operating facilities, primarily CBCC and Rocky Gap. However, all of MEDCO's operating facilities are stand-alone projects, no projects are cross collateralized, and each project must support itself by its own revenue generation.

**Exhibit 1**  
**MEDCO Asset/Non-recourse Debt/Fund Equity**  
**Fiscal 1999 – 2004**



Source: Maryland Economic Development Corporation

*Issues*

**1. Financial Losses Mount at Rocky Gap Lodge and Golf Resort (Rocky Gap)**

Rocky Gap consists of a 220-room hotel and conference center and an 18-hole Jack Nicklaus Signature golf course situated on approximately 260-acres within Rocky Gap State Park. MEDCO’s accounting systems control several operating facilities including Rocky Gap. The Financial Statement for Rocky Gap shown in **Exhibit 2**, indicates a significant net income loss in each of fiscal 2001 through 2004. Net losses decreased approximately \$1.0 million, or 15.4% from \$6.6 million in fiscal 2003 to \$5.6 million in fiscal 2004. The decrease in net loss is primarily due to lower depreciation expense as a result of certain furniture and equipment being fully depreciated. Overall net income losses are primarily due to lower occupancy and lower average room rates. In September 2004, Rocky Gap completed the expansion of its meeting and banquet facilities as well as other improvements such as upgrades to the pool, spa, and restaurant. It is hoped that the improvements will significantly increase Rocky Gap’s ability to attract larger groups and improve its financial condition. MEDCO reports that bookings for summer/fall 2005 are significantly higher than summer/fall 2004.

**Exhibit 2**  
**Rocky Gap Financial Statement**  
**Fiscal 2000 – 2004**  
**(\$ in Thousands)**

	<u>FY 2001</u>	<u>FY 2002</u>	<u>FY 2003</u>	<u>FY 2004</u>	<u>Change</u> <u>FY 03 - FY 04</u>
Revenue	\$9,730 *	\$8,707	\$8,212	\$7,727	-\$485
Total Expenditures	13,194	14,156	14,798	13,301	1,497
<b>Net Income / - Loss</b>	<b>-\$3,464</b>	<b>-\$5,451</b>	<b>-\$6,586</b>	<b>-\$5,574</b>	<b>\$1,012</b>
Assets	\$38,027	\$35,767	\$34,968	\$34,458	\$510
Liabilities	38,995	42,186	47,972	53,036	5,064
<b>Equity</b>	<b>-\$968</b>	<b>-\$6,418</b>	<b>-\$13,004</b>	<b>-\$18,578</b>	<b>-\$5,574</b>

\*Additional revenue of \$890,847 derived from capital projects grants from various government agencies reduced net income losses to \$3.5 million for fiscal 2001.

Numbers may not sum due to rounding.

Source: Maryland Economic Development Corporation fiscal 2001 through 2004 financial statements

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Currently, Rocky Gap is not generating enough cash flow to service the interest burden on the \$26.1 million in senior priority debt held by the bond investors. On April 3, 2003, MEDCO, DBED, and the holders of the Project's Series A bonds entered into an amended and restated trust indenture to provide relief from certain provisions of the trust indenture as follows:

- Forbearance by the Series A bondholders from exercising their remedies under the trust indenture through December 1, 2006; and
- An interest holiday through June 30, 2004, to protect the \$4.0 million of working capital funds provided by DBED in 2003. The working capital funds were used to finance the recent capital improvements and to provide working capital. All of the \$4.0 million has been depleted except for approximately \$35,000 that will be used for additional capital improvements.

On July 1, 2004, the trust indenture was once again amended to extend the interest holiday through June 30, 2005. Additionally, the investors have agreed not to pursue foreclosure until at least December 2006.

### **Rocky Gap Exposure**

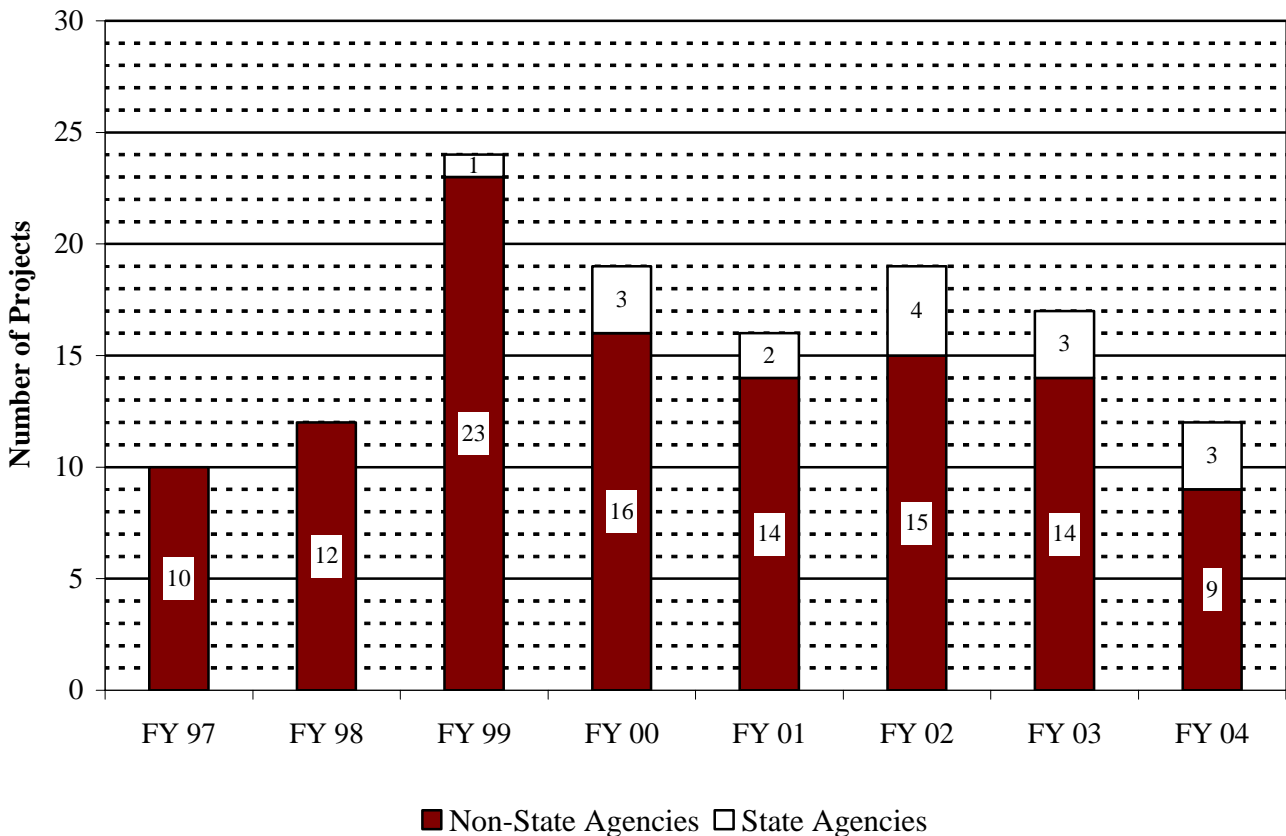
As stated earlier, Rocky Gap is not generating enough cash flows to service the interest burden on the \$26.1 million in senior priority debt held by the bond investors. The public funding provided for the facility is subordinate to senior debt; therefore, since there are not enough funds to service the bond holders, only minor payments have been made in accordance with the original schedules for the public funding. Some of the local obligations, which are paid primarily through room taxes, have not been paid. While the State could default MEDCO loans, there is nothing to be gained. The State is not in default with the investors as this is a non-recourse obligation to MEDCO.

There was no full faith and credit of the State of Maryland to support the bond obligations held by the private bond investors. The bond investors could exercise their rights and remedies provided for in the official statement for the original bond issuance which amounts basically to foreclosure. However, foreclosure is limited to leasehold over the revenues generated by the property – since the property has not generated sufficient revenues to pay even its operating costs, bondholders would receive very little in payment even if they exercised their leasehold over the revenues. Additionally, the underlying ground remains in the control of the Department of Natural Resources (DNR) and at the end of the term of the bonds the assets revert to DNR. Furthermore, foreclosure would result in the bonds becoming taxable rather than tax-exempt. **The Department of Legislative Services (DLS) recommends that MEDCO brief the committees on the losses associated with the Rocky Gap project and the financial outlook for fiscal 2005 through 2006. MEDCO should also comment on the potential impact these losses may have on MEDCO and the State's investment and on options for the State if Rocky Gap is unable to become profitable, including the impact the potential co-location of a slot machine facility nearby.**

## 2. MEDCO’s Involvement in Financing State Agency Projects

MEDCO is issuing revenue bonds to finance capital projects for State agencies. As shown in **Exhibit 3**, since 1999, the number of State agency projects for which MEDCO has provided capital financing has increased from approximately 4.2% of total projects in fiscal 1999 to 25% of total projects in fiscal 2004. Although bonds issued by MEDCO do not constitute a debt, liability, or pledge of the full faith and credit of the State, DLS questions if utilizing MEDCO is the most appropriate source of financing for State agencies, particularly since MEDCO is not subject to State procurement laws.

**Exhibit 3**  
**Number of MEDCO Projects**  
**Fiscal 1999 – 2004**



Source: Maryland Economic Development Corporation

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As shown in **Exhibit 4**, of the \$1.6 billion in MEDCO debt outstanding as of June 30, 2004, approximately \$553.9 million, or 34.8% was issued on behalf of other State entities, including several institutions of higher education and the Maryland Department of Transportation (MDOT). Since all of MEDCO bonds are issued as limited-obligation revenue bonds with a dedicated source of repayment, much of the debt issued on behalf of State agencies is not considered State tax-supported debt and is, therefore, not subject to the debt limit recommended by the Capital Debt Affordability Committee. Also, by using MEDCO to issue revenue bonds for State agency projects such as the MDOT headquarters, the State is paying more in interest expense by virtue of using 20-year debt.

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**Exhibit 4**  
**MEDCO Fiscal 2004 Debt Outstanding**  
**(\$ in Millions)**

<u>Completed MEDCO Project</u>	<u>Amount</u>
MEDCO	\$813.7
Chesapeake Bay Conference Center	161.2
Chesapeake Hills Golf Course	3.9
Compass Pointe Golf Course	18.0
Maryland Technology Development Corporation (TEDCO)	3.8
Rocky Gap Lodge and Golf Resort	38.8
<b>Subtotal</b>	<b>\$1,039.4</b>
<b>State Agencies</b>	
Frostburg State University, Student Housing	\$17.5
Morgan State University, Student Housing	38.3
University of Maryland, Baltimore County, Student Housing	37.5
University of Maryland, College Park, Energy Project	74.0
University of Maryland, College Park Student Housing	52.3
University Village at Sheppard Pratt, Student Housing	31.6
Bowie State University, Student Housing *	21.3
Salisbury University, Student Housing *	16.1
MDOT Headquarters	34.3
MDOT – Maryland Aviation Administration	231.0
<b>Subtotal</b>	<b>\$553.9</b>
<b>Total Debt Outstanding as of June 30, 2004</b>	<b>\$1,593.3</b>

\* Operations have not commenced

Note MEDCO debt includes bonds and notes outstanding as of June 30, 2004, and \$9.4 million of unamortized bond premium.

Source: Maryland Economic Development Corporation

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Additionally, if a State agency project develops financial trouble, the State may feel obligated to step in and provide financial support even though there is no legal obligation for the State to do so. **The use of MEDCO by State agencies seems inconsistent with its mission to attract and retain business, is more expensive, circumvents State procurement restrictions, may aid State debt affordability limits, and could result in State financial intervention in case of project defaults. It seems inappropriate for MEDCO to finance State agency projects. Consideration should be given to prohibit MEDCO from financing State agency projects through amendments to budget reconciliation legislation.**

***Recommended Actions***

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1. Nonbudgeted.

## Updates

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### 1. MEDCO Project Updates

The MEDCO 2004 Annual Report describes several recent and ongoing projects which are representative of the corporation's activity. In 2004, MEDCO provided tax-exempt financing for two manufacturers, one transportation entity, five not-for-profit entities, and three projects requested by either State or local government. MEDCO also funded one federal project with taxable bonds. Below is a brief description of projects MEDCO has highlighted and feels are providing significant economic benefits to the State.

- **Compass Pointe:** In 2002, MEDCO issued \$17.6 million in unrated tax-exempt revenue bonds to finance the construction of the Compass Pointe Golf Course in Anne Arundel County. When completed, the project was to consist of 36 holes of golf, a driving range, and banquet facilities. The first 18 holes of golf were supposed to be completed by May 2003, and the remaining 18 holes were to be completed by December 2003. However, due to inclement weather and the resulting construction delays, the first 18 holes did not open until October 2003, the third 9 holes opened July 2004, and the final 9 holes are not completed. In 2004, Anne Arundel County loaned MEDCO \$1.1 million to cover a shortfall in operating revenue. The project has also incurred \$3.0 million in construction cost overruns. Frustrated by the delayed opening and the need to provide the \$1.1 million loan to MEDCO, Anne Arundel County recently voted to acquire the golf course from MEDCO, and possibly issue \$26.0 million in bonds to assume control of the project.
- **Higher Education Financing:** Due to the State's scarce capital resources in 2002, Maryland's colleges and universities utilized student housing revenue bonds to enable them to construct necessary student/dormitory housing. Because the Internal Revenue Service (IRS) raised certain questions regarding the ownership of student housing projects by out-of-state not-for-profit student housing foundations, MEDCO issued the bonds but also owns several of the facilities until the debt is retired. In all instances but one, the University System of Maryland (USM) will ultimately own the facilities. The IRS ultimately agreed that out-of-state not-for-profit student housing foundations are eligible to own and operate projects in Maryland as well as elsewhere. **Exhibit 5** presents the student housing projects that will ultimately be owned by USM once the debt is extinguished.

**Exhibit 6** presents the student housing project that will be owned by the Sheppard Pratt Health System once the debt is the extinguished.

**Exhibit 5**  
**Owned by MEDCO – To Be Owned by USM When Debt Is Extinguished**

<u>University</u>	<u>Beds</u>	<u>Debt (\$ in Millions)</u>
University of Maryland, Baltimore County	581	\$37.5
Frostburg State University, Allegany County	400	17.9
Morgan State University, Baltimore County	796	38.0
University of Maryland, Baltimore City	337	34.4
Bowie State University, Prince George’s County	470	21.5
University of Maryland, Baltimore County	788	51.9
Salisbury University, Wicomico County	312	16.4

Source: Maryland Economic Development Corporation

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**Exhibit 6**  
**Owned by MEDCO – To Be Owned by the Sheppard Pratt Health System**

<u>University</u>	<u>Beds</u>	<u>Debt (\$ in Millions)</u>
University Village at Sheppard Pratt, Baltimore County	615	\$27.7

Source: Maryland Economic Development Corporation

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In 2000, MEDCO initiated the first projects under the One Maryland Program. The One Maryland Program is funded by DBED and provides economic development assistance to economically distressed jurisdictions. Presently, Allegany, Garrett, Dorchester, Worcester, Caroline, and Somerset counties and Baltimore City are eligible for One Maryland Program assistance. In 2004, MEDCO worked on the following eight projects.

- **Allegany County:** Developed the Barton Farms Industrial Park south of Cumberland on U.S. Route 220. The project includes land acquisition, permitting, providing all utilities including water and sewer, and site preparation. In June 2004 approximately 40 acres were sold to American Woodmark, which is locating a new assembly operation to the site and creating 500 jobs.

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- **Princess Anne, Somerset County:** Construction of a 30,000 square foot industrial shell building, in an industrial park that has seen limited economic success, is complete. MEDCO contracted to have the building designed and built. General Dynamics Network Systems, Inc., a Massachusetts based company, is leasing approximately 2,500 square feet of the shell building. The county is continuing to market the building.
- **Pocomoke City, Worcester County:** Construction of a 43,000 square foot industrial shell building to provide the town and county with new marketable flex space is complete. Mid-Atlantic Foods, a Maryland corporation, is leasing approximately 10,000 square feet of the building and Swales Aerospace, also a Maryland corporation, is leasing approximately 2,500 square feet. The county is continuing to market the building.
- **Baltimore City:** Assisted in constructing a 514-space parking garage which opened in November 2003. The parking garage assisted in retaining Citi Financial in the city and provides general parking. The project was completed and turned over to the City of Baltimore.
- **Baltimore City:** Construction of a parking garage serves Sylvan Learning Systems as well as providing needed parking in the Inner Harbor east neighborhood. Construction is expected to be completed in June 2005.
- **Mountain Lake Park, Garrett County:** Construction of a 30,000 square foot building in the County's Southern Garrett Industrial Park is complete. MEDCO contracted to have the building designed and built. The county lacks available industrial buildings for immediate occupancy, and this building assists in adding needed flexible industrial space to the county inventory.
- **Garrett County:** MEDCO purchased land just off Interstate 68 for the purpose of developing a new industrial park. The county has no industrial land available in the northern part of the county for developable land. Environmental, survey, and purchase negotiations are complete and preliminary engineering is underway. The purchase has enabled the county to attract American Woodmark to locate a dimensional mill on the 87 acre site which will be accessed through this property.
- **Cambridge, Dorchester County:** Construction of a 30,000 square foot building to expand industrial space was completed in September 2004. The building is fully leased.

## **MEDCO Operating Facilities**

Operating facilities in operation during fiscal 2003 and 2004 included the following:

- CBCC – a hospitality project located in Cambridge, Maryland. The project was completed and opened in August 2002.
- Chesapeake Hills Golf Course – a golf facility located in Calvert County, Maryland. The project was acquired in February 2002.
- Compass Pointe Golf Course – a golf facility located in Anne Arundel County, Maryland. The project was completed and opened in October 2003.
- Frostburg State University Student Housing – an apartment project located in Garrett County, Maryland. The project was completed and opened in August 2003.
- Maryland Technology Development Center – an office/laboratory facility designed for use by biotechnology and computer technology companies located in Montgomery County, Maryland. The project was completed and opened in 1999; an expansion of the project was completed in 2002.
- Morgan State University Student Housing – an apartment project located in Baltimore City, Maryland. The project was completed and opened in August 2003.
- Rocky Gap Golf Course and Hotel/Meeting Center – a hospitality project located in Allegany County, Maryland. The project was completed and opened in 1998.
- University of Maryland, Baltimore County Student Housing (UMBC) – an apartment project located in Baltimore County, Maryland. The first phase of the project was completed and opened in August 2003. Construction of a second phase of the project was in progress at June 30, 2004.
- The University of Maryland, College Park (UMCP) Energy and Utility Infrastructure Program – a program under which MEDCO leases land, certain energy conversion facilities and steam, and electricity and chilled water delivery systems at the UMCP campus in College Park, Maryland, and provides energy conversion, delivery, and related services to the University. The program began in August 1999.
- UMCP South Campus Commons – Phase II – an apartment project located in Prince George’s County, Maryland. The project was acquired in July 2003 at which time development of the first of

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three buildings comprising the project was substantially completed. The first building was completed and opened in August 2003. Construction of two additional buildings was in progress at June 30, 2004.

- University Village at Sheppard Pratt – an apartment project located in Towson, Maryland. The project was completed and opened in August 2002.

On June 30, 2004, several operating facilities were under construction and had not yet commenced their planned operations. These projects include apartment/dormitory projects for Bowie State University, Salisbury University, and the University of Maryland at Baltimore, UMBC, and UMCP.