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The State Budget

The major purpose of short sessions of the General Assembly held in even-numbered years is to make mid-biennium adjustments to the state budget. This year's work on the budget was the most difficult since the Great Depression. Before the General Assembly convened on May 28, the state faced a revenue shortfall for the 2001–2002 fiscal year of \$1.6 billion; as of May 1, 2002, state tax collections were down 6 percent from the previous year; and on August, 19, 2002, while the legislature was in the midst of budget deliberations, Moody's Investor Service, a credit rating agency, downgraded the state's credit rating from AAA to Aa1. As a result of this dire financial situation—and the differing views about how to deal with it—the General Assembly was unable to adopt the budget adjustment act until September 20, nearly three months into the fiscal year, making North Carolina the forty-ninth state to adopt a budget for the current fiscal year.

The Budget Process

The bill that was to become the budget modification act, S 1115, was filed in the Senate on May 28, 2002, the day the 2002 session convened. It passed third reading in the Senate on June 19, 2002, and was sent to the House. The House passed its version of the bill, which was quite different from the Senate's, on August 13, 2002. Senate and House conferees were appointed on August 14 and 15 to work out the differences between the two versions, and the House and Senate adopted the conference report on September 20, 2002. The ratified bill was entitled "The Current Operations, Capital Improvements, and Finance Act of 2002." Governor Easley signed the ratified bill on September 30, 2002, and the act was chaptered as S.L. 2002-126.

The 2001 Session of the General Assembly had appropriated \$14,780,657,357 for current operations from the state's General Fund for the 2001–2003 biennium. Clearly, the legislature would have to substantially reduce this amount because of the predicted shortfall in tax revenue for the 2002–2003 fiscal year. Thus the 2002 session faced three difficult issues. First, how would these reductions be made? Second, how much would the reductions be? Finally, would a revised budget include new taxes to increase revenues? In its final product, the General Assembly (1) reduced the current operations appropriation from the General Fund by \$463,954,969 (S.L. 2002-126, Section 2.1); (2) appropriated one-time revenues totaling \$800,000,000 from such sources as the Highway Trust Fund and the Tobacco Trust Account [S.L. 2002-126, Sections 2.2(g) and (h)];

(3) increased significantly the fees charged by many state agencies, including the courts and the Secretary of State (S.L. 2002-126, Part XXIX-A); and (4) authorized counties to levy an additional 0.5 percent sales tax, effective December 1, 2002, and in turn withheld \$333,000,000 in reimbursements to local governments it was obligated to make in compensation for the earlier repeal of various taxes, such as the intangibles tax [S.L. 2002-123 (S 1292)]. As has become its standard practice, the General Assembly included within the budget bill many provisions (referred to as “special provisions”) that have nothing to do with appropriations but rather make substantive changes in other areas of state law. These provisions are discussed in the appropriate chapters that follow.

Budget Highlights

The following are some of the highlights of the modified 2002–2003 budget:

- Step pay increases for public school teachers averaging 1.84 percent
- No pay increases for state employees other than public school teachers and administrators
- Cost-of-living increase for retirees in the Teachers’ and State Employees’ Retirement System and the Local Governmental Employees’ Retirement System of 1.4 percent but no employer contribution to the retirement systems for 2002–2003
- Funding of More at Four preschool initiative at \$28.1 million
- Funding of the first grade class size reduction initiative at \$26.8 million
- Tuition increases at the constituent institutions of The University of North Carolina of 8 percent for in-state students and 12 percent for out-of-state students
- Tuition increases at the community colleges of \$3.25 a semester hour for in-state students and \$17.50 a semester hour for out-of-state students
- In the Department of Correction, closing of the IMPACT boot camps, the Blue Ridge and Henderson Correctional Centers, and the Rowan Diagnostic Center, and elimination of twenty-four positions in the prison chaplain program

The 2002–2003 Budget

General Fund Budget Availability

The state budget is supported by four major sources of funding: (1) the General Fund; (2) the Highway Fund and Highway Trust Fund; (3) federal funds (including matching funds, categorical grants, and block grants); and (4) other receipts (such as tuition payments to universities and community colleges and fees collected by state agencies). Appropriations from the General Fund support virtually all state government programs and services other than highway construction and maintenance. Table 2-1 shows the revenues available in the General Fund as calculated by the General Assembly in S.L. 2002-126. (Items in parentheses indicate reductions in the associated categories.)

Table 2-1. 2002–2003 General Fund Budget Availability

Beginning Unreserved Credit Balance	\$ 25,000,000
Revenues Based on Existing Tax Structure	12,793,950,000
Nontax Revenues	
Investment income	115,300,000
Judicial fees	111,300,000
Disproportionate share	107,000,000
Insurance	46,600,000
Other nontax revenues	98,900,000

Appropriations from the General Fund

The functional allocation of operating funds remains similar to past years. The 2002–2003 operating budget provides \$8.33 billion for education (58 percent), \$3.6 billion for health and human services (25 percent), \$1.5 billion for justice and public safety (10 percent), \$246 million for reserves and debt service (1.7 percent), \$314 million for general government (2.2 percent) and \$339 million for natural and economic resources (2.3 percent).

Table 2-2 sets out the specific revisions S.L. 2002-126 makes in the 2002–2003 budget. Reductions are shown in parentheses.

Table 2-2. 2002–2003 General Fund Appropriation Adjustments

EDUCATION	
Community Colleges System Office	\$ 26,085,931
Department of Public Instruction	(27,635,053)
University of North Carolina—Board of Governors	
Appalachian State University	(2,594,849)
East Carolina University	
Academic Affairs	(3,780,292)
Health Affairs	(1,326,263)
Elizabeth City State University	(636,905)
Fayetteville State University	(904,051)
NC Agricultural and Technical University	(1,794,345)
North Carolina Central University	(1,372,196)
North Carolina School of the Arts	(864,283)
North Carolina State University	
Academic Affairs	(8,298,776)
Agricultural Extension	(1,077,848)
Agricultural Research	(1,361,284)
University of North Carolina at Asheville	(811,533)
University of North Carolina at Chapel Hill	
Academic Affairs	(6,068,562)
Health Affairs	(4,816,196)
Area Health Education Centers	(1,326,559)
University of North Carolina at Charlotte	(3,197,696)
University of North Carolina at Greensboro	(2,790,399)
University of North Carolina at Pembroke	(713,835)
University of North Carolina at Wilmington	(1,916,521)
Western Carolina University	(1,744,797)
Winston-Salem State University	(1,077,326)
General Administration	(2,463,801)
University Institutional Programs	39,815,922
Related Educational Programs	(17,896,363)
North Carolina School of Science and Mathematics	(36,334)
UNC Hospitals at Chapel Hill	(1,168,629)
Total	\$ (30,223,721)

HEALTH AND HUMAN SERVICES	
Department of Health and Human Services	
Office of the Secretary	\$ 19,776,228
Division of Aging	(926,000)
Division of Blind Services/Deaf/HH	(643,013)
Division of Child Development	(7,228,035)
Division of Education Services	(4,104,503)
Division of Facility Services	(748,170)
Division of Medical Assistance	(29,633,097)
Division of Mental Health	(7,707,015)
N.C. Health Choice	7,571,036
Division of Public Health	(6,595,770)
Division of Social Services	(14,183,025)
Division of Vocational Rehabilitation Services	(3,230,105)
Total	\$ (47,651,469)
NATURAL AND ECONOMIC RESOURCES	
Department of Agriculture and Consumer Services	\$ (4,822,458)
Department of Commerce	
Commerce	(10,350,110)
Commerce State-Aid	5,085,000
NC Biotechnology Center	(627,047)
Rural Economic Development Center	(423,851)
Department of Environment and Natural Resources	
Environment and Natural Resources	(9,904,113)
Clean Water Management Trust Fund	(3,500,000)
Office of the Governor—Housing Finance Agency	(540,600)
Department of Labor	(951,725)
JUSTICE AND PUBLIC SAFETY	
Department of Correction	(50,910,108)
Department of Crime Control and Public Safety	(713,318)
Judicial Department	(10,828,966)
Judicial Department—Indigent Defense	8,419,130
Department of Justice	(2,847,391)
Department of Juvenile Justice and Delinquency Prevention	(13,569,384)
GENERAL GOVERNMENT	
Department of Administration	(5,620,309)
Office of Administrative Hearings	(233,742)
Department of State Auditor	(795,965)
Office of State Controller	(1,101,040)
Department of Cultural Resources	
Cultural Resources	(3,610,213)
Roanoke Island Commission	(151,222)
State Board of Elections	209,622
General Assembly	(2,654,234)
Office of the Governor	
Office of the Governor	(504,595)
Office of State Budget and Management	(300,057)
Reserve for Special Appropriations	100,000
Department of Insurance	
Insurance	(1,882,104)
Insurance—Volunteer Safety Workers' Compensation	(2,500,000)

Office of Lieutenant Governor	(53,280)
Department of Revenue	(2,384,400)
Rules Review Commission	(9,981)
Department of Secretary of State	(345,281)
Department of State Treasurer	
State Treasurer	671,618
Retirement for Fire and Rescue Squad Workers	(5,248,601)
TRANSPORTATION	
Department of Transportation	(2,490,841)
RESERVES, ADJUSTMENTS, AND DEBT SERVICE	
Reserve for 2001 compensation increases	(4,247,868)
Reserve for State Health Plan	(12,621,872)
Reserve for legislative, judicial, and teachers' and state employees' retirement rate adjustment	(144,525,000)
Reserve for teachers/principals step increase	51,937,267
Reserve for asst./deputy clerks/magistrates step increase	1,980,700
Reserve for employee severance compensation	5,000,000
Contingency and emergency	0
Reserve for salary adjustments	0
Implementation of recommendations of Governor's Efficiency Commission	(25,000,000)
Reserve for management flexibility	(41,500,000)
Reserve for information technology rate adjustment	(3,414,318)
Mental Health, Developmental Disabilities, and Substance Abuse Services Trust Fund	8,000,000
Ruth M. Easterling Trust Fund for Children with Special Needs	1,000,000
Reserve to implement Health Insurance Portability and Accountability Act	2,000,000
Debt service	
General debt service	(97,750,000)
Federal reimbursement	0
Total Current Operations—General Fund	\$ (463,954,969)

The Highway Fund and Highway Trust Fund

The Highway Fund is funded by the motor fuels tax and other revenue related to motor vehicles. It provides funding for most of the operations of the state Department of Transportation. The Highway Trust Fund is funded by a portion of the per-gallon motor fuels tax and other dedicated revenues. It funds the special program of highway construction authorized by the 1989 General Assembly.

Table 2-3 sets out the funding provided for the 2002–2003 fiscal year.

Table 2-3. 2002–2003 Highway and Highway Trust Fund Appropriations

HIGHWAY FUND	
Administration	\$(90,000)
Operations	0
Construction and maintenance	
Construction	
Primary construction	0
Secondary construction	(1,887,000)
Urban construction	7,000,000
Access and public service roads	0

Contingency construction	5,000,000
Spot safety construction	0
State funds to match federal highway aid	0
State maintenance	13,551,179
Ferry operations	0
Capital improvements	0
State aid to municipalities	(1,887,000)
State aid for public transportation and railroads	14,350,000
Occupational and Safety Health Administration—state	0
Governor’s Highway Safety Program	0
Division of Motor Vehicles	0
Reserves and transfers	(6,039,551)
Total Highway Fund	\$ 29,997,628
HIGHWAY TRUST FUND	
Intrastate system	\$ (159,218,286)
Secondary roads	(18,065,569)
Urban loops	(64,381,244)
Aid to municipalities	(16,705,712)
Program administration	(4,073,189)
Transfer to General Fund	205,000,000
Total Highway Trust Fund	\$ (57,444,000)

Capital Improvements

The relatively little money in the General Fund allocated for capital improvements was appropriated to the Department of Environment and Natural Resources (DENR). For 2002–2003, \$31,158,000 was appropriated for DENR water resource projects, and of that amount, \$20,100,000 would be used for deepening the Wilmington harbor.

Miscellaneous Provisions

Two of the budget modification act’s miscellaneous provisions have important implications for the interpretation of budget items. Section 31.2(a) provides that the Joint Conference Committee Report on the Continuation, Expansion, and Capital Budgets, dated September 18, 2002, shall be considered a part of the act and shall be used to construe the act. Section 31.3 provides that, except for statutory changes and other provisions clearly intending to have effects beyond the 2002–2003 fiscal year, the act’s provisions apply only to funds appropriated for, and activities occurring during, the 2002–2003 fiscal year.

Both the budget modification act, S.L. 2002-126, and the accompanying conference committee report can be found on the General Assembly’s Web site at www.ncga.state.nc.us/homePage.pl.

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