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## The State Budget

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The major purpose of the short sessions of the General Assembly held in even-numbered years is to make mid-biennium adjustments to the state budget. After three years of severe revenue shortfalls, the 2004 session faced the encouraging prospect of a budget surplus of approximately \$300 million. Whereas in the 2001, 2002, and 2003 budget negotiations legislators confronted difficult questions concerning what cuts to make and how large they would be, in the 2004 session they grappled instead with issues such as how surplus funds would be allocated, which appropriations should be increased, and which should be decreased.

### **The Budget Process**

The bill that was to become the budget modification act, H 1414, was filed in the House on May 11, 2004, the day after the 2004 session convened. It passed third reading in the House on June 8, 2004, and was sent to the Senate. The Senate passed its version of the bill on June 24, 2004. House and Senate conferees were appointed to work out the differences between the two versions, and the House and Senate adopted the conference report on July 17, 2004. Governor Easley signed the ratified bill on July 20, 2004, and it was chaptered as S.L. 2004-124.

The act is 203 pages long, and although most of it deals with the appropriation of funds, much of it does not. Rather, as has become the General Assembly's practice, much of the act consists of special provisions, which either amend or create substantive law and have nothing to do with the appropriation of state funds. To give but a few examples, Section 6.1 enacts new G.S. 143-59.1A to give a state purchasing preference to products made in the United States; Section 18.2 transfers the State Boxing Commission to the Alcohol Law Enforcement Division; Section 30.6 enacts new G.S. 20-147.1 to require that passenger vehicles towing other vehicles keep to the right; and Section 30.17 directs the Department of Transportation to construct six median cuts on Catawba Avenue in the Town of Cornelius.

## Budget Highlights

Highlights of the modified 2004–2005 budget include the following:

- Step pay increases for public school teachers averaging 2.5 percent
- Pay increases for most state employees of 2.5 percent or \$1,000, whichever is greater
- Cost-of-living increases of 1.7 percent for retirees in the Teachers' and State Employees' Retirement System and the Legislative Retirement System
- An appropriation of \$50,467,765 to reduce the teacher–student ratio in third grade classes to 1:18
- An appropriation of \$9,057,202 to fund two thousand more places in the More at Four program
- An appropriation of \$62 million to the Clean Water Management Trust Fund

## The 2004–2005 Budget

### General Fund Budget Availability

The state budget is supported by three major sources of funding: (1) tax revenues, (2) federal funds (including matching funds, categorical grants, and block grants), and (3) 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. 2004-124. Amounts in parentheses indicate reductions in the associated categories.

**Table 2-1. 2004–2005 General Fund Availability**

Beginning unreserved credit balance	\$ 271,200,829
Revenues based on existing tax structure	14,755,690,500
Nontax revenues	
Investment income	86,020,000
Judicial fees	136,730,000
Disproportionate share	100,000,000
Insurance	53,900,000
Other nontax revenues	261,517,607
Highway Trust Fund transfer	242,586,830
Highway Fund transfer	16,166,400
Subtotal Nontax Revenues	896,920,837
<b>Total General Fund Availability</b>	<b>\$15,923,812,166</b>
Adjustments to Availability: 2004 Session	
H 1430 Conference Report (Internal Revenue Code conformity)	(2,600,000)
H 1303 Conference Report (reduce privilege and excise taxes)	(2,950,000)
Sales tax refunds and exemptions	(5,200,000)
Research and development tax credit	(4,500,000)
Qualified business investment tax credit	0
Tobacco payments decline—Tobacco Trust Fund	(5,000,000)
Transfer from Fire Safety Loan Fund	250,000
Transfer from Veteran's Home Trust Fund	500,000

Transfer from Office of State Controller, Budget Code 24160	2,180,000
H 1264 Conference Report (finance vital projects), reimburse debt service	5,380,000
Adjust transfer from Insurance Regulatory Fund	4,062,654
Adjust transfer from Treasurer's Office	424,708
Subtotal Adjustments to Availability: 2004 Session	(7,452,638)

**Revised General Fund Availability for 2004–2005 Fiscal Year      \$15,916,359,528**

To achieve a balanced budget this year, the General Assembly made three substantial one-time expenditures: the use of a credit balance of \$271 million, a transfer from the Highway Trust Fund of \$242 million, and a transfer from the Highway Fund of \$16 million. Overall \$529 million out of a total General Fund availability of \$16 billion is not very significant, and spending the credit balance is a long-established practice. The transfers from the Highway Trust Fund and the Highway Fund, both of which are funded through dedicated tax sources, are less easily defended.

### General Fund Appropriations

This year's budget act appropriates all of the \$15,916,359,528 available. In doing so it uses the appropriations act of 2003–2005, S.L. 2003-284, as the base to which it makes additions and reductions in appropriations. Table 2-2 sets out the revisions S.L. 2004-124 makes in the 2003–2005 budget. Reductions are shown in parentheses.

**Table 2-2. 2004–2005 General Fund Appropriation Adjustments**

<b>EDUCATION</b>	
Community Colleges System Office	\$ 31,612,319
Department of Public Instruction	122,269,724
University of North Carolina—Board of Governors	6,386,840
<b>HEALTH AND HUMAN SERVICES</b>	
Department of Health and Human Services	
Office of the Secretary	5,319,802
Division of Aging	3,151,000
Division of Blind Services/Deaf/HH	(30,000)
Division of Child Development	7,925,000
Division of Education Services	10,873
Division of Facility Services	(450,000)
Division of Medical Assistance	(88,729,913)
Division of Mental Health	(5,962,273)
N.C. Health Choice	6,600,000
Division of Public Health	8,226,581
Division of Social Services	(5,561,948)
Division of Vocational Rehabilitation Services	(1,479,294)
<b>Total</b>	<b>\$(70,980,172)</b>
<b>NATURAL AND ECONOMIC RESOURCES</b>	
Department of Agriculture and Consumer Services	100,538
Department of Commerce	
Commerce	(452,263)
Commerce State-Aid	1,950,000
N.C. Biotechnology Center	5,000,000
Rural Economic Development Center	1,144,000

Department of Environment and Natural Resources	
Environment and Natural Resources	1,021,957
Clean Water Management Trust Fund	0
Department of Labor	364,216
JUSTICE AND PUBLIC SAFETY	
Department of Correction	(11,309,897)
Department of Crime Control and Public Safety	3,912,627
Judicial Department	6,741,918
Judicial Department—Indigent Defense	11,000,000
Department of Justice	754,467
Department of Juvenile Justice and Delinquency Prevention	1,734,069
GENERAL GOVERNMENT	
Department of Administration	2,476,330
Office of Administrative Hearings	90,476
Department of State Auditor	(200,000)
Office of State Controller	(99,429)
Department of Cultural Resources	
Cultural Resources	14,944,032
Roanoke Island Commission	0
State Board of Elections	2,197,412
General Assembly	(921,318)
Office of the Governor	
Office of the Governor	42,702
Office of State Budget and Management	401,427
Reserve for Special Appropriations	2,213,382
Housing Finance Agency	1,725,000
Department of Insurance	
Insurance	4,062,654
Insurance—volunteer safety workers' compensation	(1,734,000)
Office of Lieutenant Governor	29,657
Department of Revenue	(1,661,794)
Rules Review Commission	(3,185)
Department of Secretary of State	(110,389)
Department of State Treasurer	
State Treasurer	424,708
Retirement for fire and rescue squad workers	665,000
TRANSPORTATION	
Department of Transportation	(228,056)
RESERVES, ADJUSTMENTS, AND DEBT SERVICE	
Reserve for 2003 compensation increases	(900,000)
Reserve for 2004 compensation increases	260,800,000
Reserve for LEO salary adjustments	2,007,385
Reserve for State Health Plan	(900,000)
Reserve for retiree health benefits	(6,900,000)
Reserve for contributions to benefit plans	(6,230,100)
Reserve for Teachers' and State Employees' Retirement System	9,180,000
Reserve for Consolidated Judicial Retirement System	339,000
Job Development Incentive Grants (JDIG) Reserve	4,500,000
Mental Health, Developmental Disabilities, and Substance Abuse Services Trust Fund	10,000,000

Reserve for Senate Bill 100 compliance	(11,813,949)
Debt Service	
General debt service	(78,268,480)
Federal reimbursement	460,432
<b>Total Current Operations—General Fund</b>	<b>\$367,839,240</b>

### The Highway Fund and Highway Trust Fund

The Highway Fund is funded by the motor fuels tax and other revenues related to motor vehicles. It supports 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 shows the 2004–2005 adjustments to these funds.

**Table 2-3. 2004–2005 Highway Fund and Highway Trust Fund Adjustments**

<b>HIGHWAY FUND</b>	
Transportation Administration	\$ 1,227,072
Operations	0
Match for federal aid	0
Construction Program	
State secondary system	410,000
Small construction	7,000,000
Contingency funds	5,000,000
Spot safety improvements	0
Access and public service roads	0
Maintenance	24,672,591
Capital improvements	0
Ferry operations	1,000,000
State aid to municipalities	410,000
State aid to railroads	0
State aid for public transportation	(436,479)
Asphalt plant cleanup	0
Governor's Highway Safety Program	0
Division of Motor Vehicles	1,218,921
Appropriations to other state agencies	1,030,489
Reserves and transfers	17,842,991
<b>Total</b>	<b>\$ 59,375,585</b>
<b>HIGHWAY TRUST FUND</b>	
Intrastate system	(7,488,716)
Urban loops	(3,028,125)
Aid to municipalities	(785,741)
Secondary roads	236,830
Administrative expense	(439,735)
Transfer to General Fund	66,513
<b>Total</b>	<b>\$(11,572,000)</b>

### Capital Improvements

Considerably more money was appropriated for capital improvements for 2004–2005 than was made available in the previous three fiscal years. A total of \$43,192,000 was appropriated for the following projects:

Department of Commerce—State Ports Authority	
Wilmington Port—replace crane rail	\$ 2,000,000
Radio Island development and improvements	2,000,000
Department of Environment and Natural Resources	
Water resources development projects	26,492,000
North Carolina Museum of Art	
Expansion planning funds	2,200,000
University of North Carolina System	
Center for Design Innovation	2,000,000
Winston-Salem State University—Department of Life Sciences	2,000,000
UNC Greensboro and NC A&T Millennium Campus	4,000,000
N.C. Motor Sports Testing and Research Complex	2,000,000
UNC Wilmington—School of Nursing	500,000
<b>Total Capital Improvements—General Fund</b>	<b>\$43,192,000</b>

## Executive Budget Act Amendments

The 2004 session of the General Assembly made several substantive amendments to the Executive Budget Act (G.S. 143-1 through 143-34.7).

### JDIG Reserve Fund

One of numerous economic development tools devised by the General Assembly over the past several sessions is the Job Development Investment Grant program (JDIG), the details of which are set forth in G.S. Chapter 143B, Article 10. S.L. 2004-124, Section 6.12(a), enacts new G.S. 143-15.3E to require the State Controller to establish a reserve in the General Fund to be known as the JDIG Reserve. The purpose of this reserve fund is to receive appropriations sufficient to meet the anticipated annual cash requirements of the JDIG program.

### Reporting by Non-state Entities

G.S. 143-6.1 contains reporting requirements applicable to non-state entities that receive state funds. S.L. 2004-196 (S 1008) repeals G.S. 143-6.1 and replaces it with new G.S. 143-6.2. One of the new provisions defines a *non-state entity* as any firm, association, local government, or other organization that is not a state agency, department, or institution. Another provision requires the Director of the Budget to take appropriate administrative action if he or she finds that a non-state entity has spent or encumbered state funds for an unauthorized purpose and to report to the Attorney General any indication that a violation of criminal law may have occurred. And a third provision directs the Office of State Budget and Management to adopt rules to ensure the uniform administration of state grants by all grantor state agencies and the grantees and subgrantees. These rules must address several topics, including the establishment of mandatory periodic reporting requirements, grantee maintenance of adequate accounting records, and procedures to recover state funds from grantees unable to accomplish the purposes of a grant.

### Flexible Compensation Benefits

S.L. 2004-199 (S 1225) amends G.S. 143-34.1(d), which authorizes the Director of the Budget to establish a plan of flexible compensation to certain state officers and employees. The current statutory

language prohibits the Director from including in the plan any benefits that already exist by statute. The amendment provides that the plan shall not “replace, substitute for, or duplicate” any of the existing statutory benefits, but it may offer products and benefits additional to those benefits.

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