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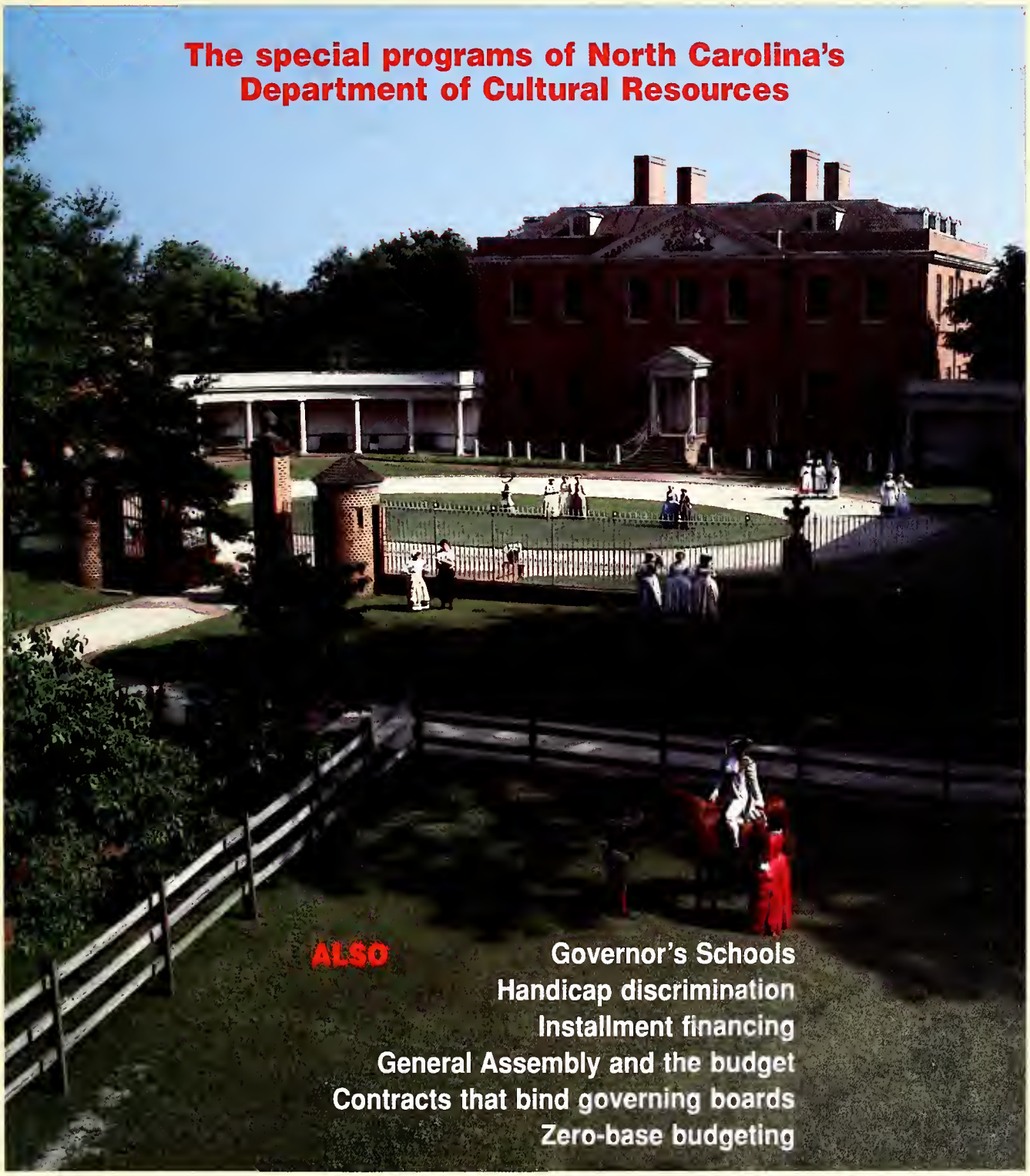

On the Cover

Characters in period dress adorn the lawn of Tryon Palace Restoration in New Bern The thirty-eight room mansion, which served as the capitol of colonial North Carolina, is one of the historic sites maintained by the Division of Archives and History of the Department of Cultural Resources Photograph courtesy of the Department of Cultural Resources.

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The Governor's Schools of North Carolina

Laurie L. Mesibov

First in flight, first in freedom, and first in state-supported residential summer programs for gifted students.[1] If you wonder whether this last achievement rates a place on our state's license plates, just ask the more than 15,000 Governor's Schools alumni who have had a wonderful learning experience there. Ask the hundreds of faculty members who have had an opportunity to teach motivated adolescents in an exciting educational environment. Ask local administrators and teachers who have seen not only changes in individual students but also the sparks set off in class when these students return home. And ask the education leaders in more than thirty-five other states for whom North Carolina's program has been a model of excellence.

Origins

The idea of creating this special summer program originated in the early 1960s with former Governor (and now United States Senator) Terry Sanford and his special assistant, writer John Ehle.[2] Sanford has explained their goals: "We wanted to find a way to do some research [on gifted students] of our own, and we wanted to glamorize superior academic efforts by superior students. . . . We wanted to see what gifted students could do and learn in an unlimited academic environment."[3] The summer program also was created to give educators freedom to try new methods of teaching and new ways of presenting knowledge. It would be a "laboratory of learning" that would demonstrate useful lessons for the entire school system. As Sanford recalled, "It was our intention that it serve that purpose, as well as constituting the capstone of a statewide program of providing additional challenges for students capable of superior achievement."[4]

Sanford submitted a proposal for a residential summer program for gifted students to the Carnegie Corporation of New York, which awarded a grant of $225,000. This amount was matched by eleven Winston-Salem foundations and businesses in less than fifteen minutes at a fund-raising luncheon.[5] The total of $450,000 financed the operation of the program in the summers of 1963, 1964, and 1965 on the campus of Salem College in Winston-Salem. At the end of that three-year experimental phase, the program was taken over by the state and is now a permanent part of North Carolina's education program. It is funded by the General Assembly and administered by the State Board of Education through the Division for Exceptional Children, Department of Public Instruction. A board of governors, appointed by the State Board of Education, acts as an advisory body.

From the start, the Governor's School (so named by the State Board of Education) was a success because of its carefully designed curriculum, strong leadership from dedicated administrators, the faculty, and the students themselves. As Sanford said, "The students at this school compose a most unusual community and are a composite of our needs and reflect so well the hopes we have for the future of our people here in our county and state."[6] Based on what Sanford found, it appears that his initial hopes were realized: "For eight weeks the challenges to unleash their minds were laid before them and all around them. For most of the students this was a completely new approach to education, and their response was overwhelmingly favorable."[7]

The author is an Institute of Government faculty member who specializes in school law. Her older son attended Governor's School East in 1989.

Group discussion is a common method of teaching at the Governor's Schools.

Participants

The school is a public school, with books, room, board, and materials furnished for the students. There is no tuition; students are responsible only for their transportation and spending money. In 1963, 400 rising juniors and seniors representing eighty-five of North Carolina's one hundred counties were selected. In 1989, 800 students from every local school administrative unit and fifteen private schools attended a six-week term. In 1963 all students were on one campus, Salem College in Winston-Salem, now called Governor's School West. Since 1978 Governor's School East has operated at St. Andrews Presbyterian College in Laurinburg (hence the name change from the Governor's School of North Carolina to the Governor's Schools of North Carolina).

Students have always been selected on the basis of merit. Only students identified as academically gifted under State Board of Education criteria are eligible to attend the Governor's Schools. High school principals, teachers, and counselors recommend academically gifted sophomores and juniors to the local school superintendent or headmaster. The superintendent or headmaster nominates individual students according to a quota (based on the total tenth- and eleventh-grade enrollments) of these students. A state selection committee then chooses students for specific areas of study, either an academic discipline (English, Spanish, French, creative technology, mathematics, natural science, or social science) or a visual or performing arts discipline (art, choral and instrumental music, dance, or drama). To ensure statewide representation in the student body, the committee automatically accepts the first two choices of each local superintendent for the academic areas, and then the committee picks additional academic-area students. Students nominated in the performing arts must participate in competitive auditions before a selection committee.

The state's goal is to select students who reflect the racial and sexual composition of North Carolina's school-age population. However, in 1989 black enrollment was only at about 10 percent, perhaps because the proportion of minority students who have been identified as academically gifted is significantly lower than the pro-

Governor's School: A Student's Perspective

Brian Mesibov

Today, nearly six months after my summer in Laurinburg, I still have only positive feelings about the Governor's School program I attended there. I haven't forgotten the hot, humid weather or the difficulties involved in spending time away from home, but somehow the incredible people who surrounded me for those six weeks overshadowed all problems. I have memories of great friends and the good times we shared working, learning, and playing.

The program is not geared to provide mere pleasure, of course. As the name implies, education is the driving force behind the Governor's Schools of North Carolina. I was nominated by a committee at my high school to attend in the area of mathematics, and when accepted, I was proud to have earned the opportunity. I didn't know much about the Governor's Schools then, but my teachers assured me that the experience would be a good one.

When summer finally came, I was excited yet still quite nervous about going. Six weeks away from home seemed like a long time, particularly when the people there would be strangers. Looking back, I suppose I should have been one of the more confident people. After all, I was coming from a fairly large high school, and I'd spent time away from my family and friends many times. Some people at the Governor's School had never really gone beyond the area of their hometowns; they were the ones who really had a right to be scared.

The first few days were as one might expect them to be whenever a group of strangers is brought together. People tried to find other people like themselves to be around, and no one wanted to appear lonely. At first I spent most of my time with my roommate and the people I recognized from my high school. Soon I began to make friends among the people in my classes and those living around me in the dorm. After the first week was over, most people had settled in with a group of friends and felt comfortable on the St. Andrews campus.

The core of the Governor's Schools program is classroom instruction. Each student has an area of concentration and takes two classes a day in that area. For me, that meant one math class every morning and another in the afternoon. I took a beginning Pascal language computer course and a matrix algebra course for the first three weeks, then courses in problem solving and advanced topics in math the second three weeks.

These mathematics courses differed from typical high school classes in a number of ways. Perhaps the most significant difference was the fact that my summer classes had a maximum of fifteen students each, while my calculus class at home had nearly thirty. The smaller group allowed for more individualized teaching and closer relationships between teachers and students. Students also felt very comfortable testing their own limits, perhaps in part because they knew there were no grades or end-of-course exams. Classes moved at a fast pace but without the pressure to cover a set of questions defined by someone outside the program in preparation for an exam. The content of the math courses was special because the topics varied so widely. Most could be taught in high school

The author is a 1990 graduate of Chapel Hill High School. He plans to attend Stanford University in the fall.

portion of minority students in the total high school population.[8]

The Governor's Schools offer a wonderful environment for learning. There are no grades or credits; learning is its own reward. Exploration and self-disclosure are easy in a noncompetitive atmosphere. More important is the active role students play in their education—it is something they do, not something done to or for them. The program encourages collaborative learning and intellectual chemistry between faculty, staff, and students.

The faculty is as exceptional as the students, and their devotion to the program is remarkable. Consider James L. Bray, who began working with the school in 1966, served as director from 1968 to 1978, and has been director of Governor's School West since 1978. He describes his work as "a labor of love."[9] Teachers and staff members are selected from public school systems, private schools, colleges and universities, and private businesses and organizations. Approximately 130 people serve as instructors, counselors, and health care, recreational,

just as they were taught at the Governor's School if teachers had the time, but few teachers ever do.

In addition to classes in the area of concentration, every student takes one course in philosophy and another called Self in Society. These classes meet three times each week, and they stand out in my mind as perhaps the most special parts of the Governor's Schools program.

In philosophy the aim of the instructor was to make students question some things in life that they previously had taken for granted. For example, the entire basis of knowledge and how we know what is "real" was examined closely. We studied topics such as metaphysics, epistemology, and ethics, with classes often involving debates over seemingly silly issues, such as the existence of a clearly visible box in the middle of the classroom. At times I became so confused in that class that I felt as if my brain had overloaded and was ready to shut off.

While philosophy was said to rip students to shreds, Self in Society was there to help put us back together. Values, ethics, and other topics were analyzed as students were encouraged to discover the different factors involved in making them act as they do. My teacher was extremely sensitive to her students' feelings, and her caring brought our class together. Toward the end of the summer we did independent projects through which we each shared an aspect of our personality, and those brought everyone even closer. Movies, including one particularly moving documentary on the My Lai massacre, added to the classroom discussion.

In all of the classes, instructors treated students as equals, a practice not commonly seen in most high schools. Discussion was encouraged over lecture as a method of teaching, and through this students got to know both their subject and their classmates better.

Rooney L. Colfman

Classes at the Governor's Schools are relatively small, so students often receive individual attention.

Everyone got involved in the free exchange of ideas, and without the pressure of tests or grades, pure learning took place.

To supplement the curriculum, different speakers addressed the student body each Tuesday and Thursday. State Superintendent of Public Instruction Bob Etheridge spoke, as did experts in fields ranging from apartheid to students' rights to the fourth dimension. Students were not shy about challenging the speakers. Occasionally, when a speaker disagreed with some students' long-

Continued on next page.

and office personnel. In addition, nationally recognized consultants provide instruction to both students and faculty throughout the summer.

Program

The instructional program is designed especially for gifted students and offers both enrichment, the depth with which a subject is pursued, and acceleration, the pace at which material is presented. As a leading scholar in gifted education explains, "In gifted education, it's enrichment plus acceleration (with special attention paid to critical thinking and problem solving skills) that equals a worthwhile program."[10] The curriculum supplements the regular high school program and emphasizes twentieth century ideas and theories. Classes are structured to take advantage of these students' abilities to comprehend and assimilate knowledge quickly and to see the big picture. By all reports they are curious, flexible thinkers, with an awareness of and sensitivity to the world around

Continued from previous page.
entrenched ideas, the assembly ended in furious exchanges either between students and the speaker or between students themselves. While the main purpose of the assemblies was to challenge us to reconsider our rarely examined beliefs, some students seemed to take the questioning of their beliefs personally, adding to the intensity of the debates.

After classes, we were essentially free to do as we pleased. Sports were the first choice of many students, and intramural basketball and volleyball leagues were organized for friendly competition. We also swam and played tennis, racquetball, soccer, and good old frisbee. There were plenty of other types of activities as well. We had an active student government association, a student newspaper, and clubs ranging from poetry to math.

Evening events included dances on the weekends and movies during the week, as well as performances by the drama, chorus, and orchestra. I was awed by the talents of many of the performers, especially those in drama. The students directed many of their own performances, and the level of acting was extremely high. The chorus and orchestra also were filled with wonderfully talented performers. In some ways these students seemed to become the closest of friends, perhaps because they spent so much time rehearsing and performing together.

The day-to-day lifestyle made me aware of significant differences between living at home and living in a dorm, as I will do next year in college. With all of the freedom, there was, of course, added responsibility. Some students learned how to use a washer and dryer, and all of us were expected to keep up classes and meetings on our own. There were counselors on each hall to keep things running smoothly, but they did not act as baby-sitters. A few students neglected the responsibility of eating good meals and ended up ordering pizza almost every day.

Being on a campus with 400 bright and talented North Carolinians allowed friendships to flourish. While I only spent six weeks with the students there, I can honestly say that I count some of them as being among my closest friends anywhere. At the Governor's School people felt freer to express themselves. Part of the liberation came from the open environment set up through the structure of the program, and part came from the feeling of togetherness produced by spending six weeks in a relatively small and closed society.

Everyone dreaded the day when the bond would finally be broken. On the last morning we all met in the gymnasium for a slide show chronicling our summer. Tears began flowing down the cheeks of people throughout the gym as the pictures faded from the screen, and everyone said their final goodbyes. As the day passed, parents arrived and friends disappeared, and soon the experience was only a memory.

Looking back at the weeks I spent at the Governor's School last summer, I don't remember the specific equations I learned or the topics we debated nearly as well as I remember the people I met and grew close to. I learned a lot about mathematics, but even more about myself, and I know that I am more confident than I was before. I still keep in touch with a number of the friends I made in Laurinburg, and I think we have within us feelings from our experience that no other people in the world can feel. These feelings of love and friendship, in my opinion, are among the greatest benefits the students of our state gain from the program. I feel proud to say that I attended a Governor's School, and I envy those students who will attend in the future. The state of North Carolina will provide them with a tremendous experience.

them: they like challenges and are not frightened by questions that have no right answer. Students develop and enhance their ability to carry on independent study, thought, and activity. They learn from their peers and, at times, are humbled by each other's abilities and insights.

Students attend classes in three areas. Placement in classes in the major area of academic or arts concentration is determined by the student's special interest and talent. In the second area, students move beyond their specialties to a better understanding of abstract ideas through the study of philosophy, epistemology, ethics, and aesthetics. In the third area, students explore values, thinking processes, and social and personal development through the study of self in society. Field trips, such as to the American Dance Festival in Durham or to Discovery Place in Charlotte, and guest speakers are integrated with more formal instruction.

But the school really is a twenty-four-hour-a-day classroom. Students are learning about themselves, their

potential, their place in the world, and their obligation to contribute to society. And students simply enjoy each other as well. As Sylvia Lewis, director of Governor's School East, says, "Number one, they're kids; number two, they're gifted."[11] The summer also has marked the beginning of many lifelong friendships and more than a few marriages. It's not just intellectual chemistry at work here.

There is time for play as well as for work. There is an extensive recreational program, both organized and impromptu, including swimming, tennis, volleyball, basketball, softball, movies, dances, and a talent show. College Day brings representatives of approximately 100 colleges, and Parents Day brings proud families to classes, concerts, an art exhibition, and drama and dance productions. Students produce a newspaper and yearbook. They organize special interest groups such as an environmental awareness group; the Live Poets' Society, where students read their own work or that of other poets; a student government association; and even a chocolate-lovers club.

Achievement

We should take pride in the Governor's Schools. They have met the mission of playing "a small but significant role in preparing these gifted youngsters for their future tasks of creative leadership."[12] They have created a vibrant community of scholars and have been responsive not only to the intellectual but also to the aesthetic, physical, recreational, and emotional needs of students. And in the future, we can expect more of the same, although additional funds are needed to improve salaries, equipment, and activities. The program will continue to have as its primary objective providing a differential education tailored to fit the special talents and needs of academically gifted students. Students will continue to be enriched and motivated by the foundation of knowledge, the habit of critical inquiry, and pleasure in learning. The Governor's Schools also will continue to stimulate schools to establish and improve programs for gifted students by providing leadership in curriculum development and effective teaching techniques. Educators across the state can look to these programs as models for involving students in active learning and as models for a spirit of exploration and experimentation.

In *Self-Renewal* former Secretary of Health, Education, and Welfare and Stanford professor John Gardner says: "Education at its best develops the individual's inner resources to the point where they can learn (and will want to learn) on their own. It equips them to cope with unforeseen challenges and to live as versatile men and women in an unpredictable world. Individuals so educated will keep the society itself flexible, adaptive and innovative."[13] Thus, while the benefits of the Governor's Schools may appear to flow mainly to individuals, we all have been enriched. Surely that is something to celebrate and tell others about. ❖

Notes

1. North Carolina was also the first state to operate a public, residential high school for students with special aptitude and interest in the sciences and mathematics. The North Carolina School of Science and Mathematics opened for students in 1980. The North Carolina School of the Arts, one of the sixteen constituent institutions of The University of North Carolina, offers an arts-training program and liberal arts education at the high school and college levels. It was the nation's only state-supported residential arts school when it was established in 1963. See Marla Carpenter, "The North Carolina School of the Arts," *Popular Government* 53 (Winter 1988): 2–7; and James McDuffie, "The North Carolina School of Science and Mathematics," *Popular Government* 53 (Winter 1988): 8–12.

2. Sanford credits Ehle with significant contributions to education and says, "If I were to write a guidebook for new governors, one of my main suggestions would be that he find a novelist and put him on his staff." Terry Sanford, *But What About the People?* (New York: Harper and Row, 1966), 51. Ehle also proposed state-funded campuses for academically gifted students devoted to the arts, science and mathematics, languages, and the humanities and social sciences. Much of his vision has become a reality. Ehle was awarded an honorary degree (Litt.D.) by The University of North Carolina at Chapel Hill in 1990 for his work as a writer and innovator in education.

3. Sanford, *But What About the People*, 55.

4. Sanford, *But What About the People*, 58.

5. Sanford, *But What About the People*, 57.

6. *The Governor's School of North Carolina* (Raleigh: Department of Public Instruction, 1963), quoting Governor Terry Sanford at the school's inauguration 10 June 1963.

7. Sanford, *But What About the People*, 55.

8. Of the 400 students enrolled in 1963, 30 were black. *Carnegie Corporation of New York Quarterly* 7 (January 1964): 1.

9. Conversation with the author, 31 May 1990.

10. David Fetterman, "Wasted Genius," *Stanford Magazine* 18 (June 1990): 33.

11. Conversation with the author, 11 July 1989.

12. H. Michael Lewis, *Open Windows Onto the Future: Theory of the Governor's School of North Carolina* (Winston-Salem: Governor's School of North Carolina, 1969), 2.

13. John W. Gardner, *Self-Renewal: The Individual and the Innovative Society*, rev. ed. (New York: W. W. Norton, 1981), 26.

Handicap Discrimination in Employment

Stephen Allred

Scott Burgess was a short order cook for a restaurant in Raleigh. In November, 1987, he learned he had the human immunodeficiency virus (HIV) and told his employer. The restaurant manager immediately fired Burgess, solely because he had tested positive for HIV.

Burgess sued the restaurant under the North Carolina Handicapped Persons Protection Act,[1] claiming that his HIV status constituted a handicapping condition and that he was otherwise qualified to perform his job. In early 1990 the North Carolina Supreme Court ruled against him,[2] holding that he was not a handicapped individual as that term is used in the act. Therefore, the restaurant manager did not violate the act when he fired him.

The outcome might have been very different if Burgess had worked for a public employer or had sued under federal law.

The law governing handicap discrimination can be confusing to state and local government employers. They may wonder, for example, who is handicapped? What right do handicapped individuals have to stay employed? May an employer take into consideration how much extra it might cost in deciding whether to hire a handicapped individual? This article describes the statutes under which handicapped people may sue for employment discrimination: the state Handicapped Persons Protection Act and the federal Rehabilitation Act of 1973, as well as a bill now pending in Congress, the Americans with Disabilities Act of 1990. The focus is on handicap discrimination law as it relates to employees with HIV, but the principles apply to all handicaps.

The author is an Institute of Government faculty member who specializes in employment law.

The Handicapped Persons Protection Act

Burgess brought his lawsuit under a North Carolina statute enacted in 1985: the Handicapped Persons Protection Act. This is the third version of legislation prohibiting employment discrimination against the handicapped that the General Assembly has enacted. The original legislation, enacted in 1971 and codified at Section 128-15.3 of the General Statutes (hereinafter G.S.), barred discrimination against any applicant for positions in the state personnel system "based upon any physical defect or impairment . . . unless the defect or impairment to some degree prevents the applicant from performing the duties required by the employment sought." The act further encouraged employment of handicapped individuals. No enforcement mechanism was established by this legislation, however.

In 1973, in the same year in which Congress enacted federal legislation barring discrimination against the handicapped, the General Assembly enacted the Handicapped Persons Act, G.S. 168. That act provided, at G.S. 168-6, that handicapped persons were to be employed by the state, by political subdivisions of the state, and by all other employers "on the same terms and conditions as the ablebodied, unless it is shown that the particular disability impairs the performance of the work involved." Although G.S. 168 prohibited discrimination in employ-

ment against the handicapped. the act did not define handicaps as broadly as the federal act. and it established a fairly low threshold for employers to meet in rejecting a handicapped applicant: that their disability would impair their work performance.

In 1985 the General Assembly repealed G.S. 168-6 (leaving the rest of G.S. 168 intact) and enacted the Handicapped Persons Protection Act. This act. modeled on the federal handicap discrimination statute, covers all employers. including the state and its departments. agencies. and political subdivisions. that have fifteen or more employees. The act provides a private right of action for handicapped employees at G.S. 168A-11. giving them the right to bring a civil action in superior court.

The act defines *handicapped persons* in the same way that the federal statute does. The term includes an individual who (1) has a physical or mental impairment that substantially limits one or more major life activities. (2) has a record of such impairment. or (3) is regarded as having such an impairment.[3] Note. however. that in defining "major life activities" at G.S. 168A-3(1)b. the General Assembly included as illustrations "caring for one's self. performing manual tasks. walking. seeing. hearing. speaking. breathing. and learning" but did not include "working." as was done in the federal regulations. In this way. the North Carolina legislation defines handicapping conditions more narrowly than is the case under federal statute. As a result. an employer is less likely to violate the state act than the federal law.

Like the federal statute. the Handicapped Persons Protection Act requires reasonable accommodation of otherwise qualified handicapped persons. The act [G.S. 168A-3(9)] defines a qualified handicapped person. with respect to employment. as one

> who can satisfactorily perform the duties of the job in question. with or without reasonable accommodation. (i) provided that the handicapped person shall not be held to standards of performance different from other employees similarly employed. and (ii) further provided that the handicapping condition does not create an unreasonable risk to the safety or health of the handicapped person. other employees. the employer's customers. or the public.

Again. the state statute excludes more individuals from the definition of qualified handicapped persons than is the case under federal law. which. once again. makes a violation of the state statute less likely than a violation of federal law.

Finally. the state statute. like the federal statute. imposes an obligation on employers to make a reasonable accommodation for otherwise qualified handicapped employees. Unlike the federal statute. however. the General Assembly has defined the limits of reasonable accommodation with mathematical precision. The act [G.S. 168A-3(10)a.6] provides that the duty of reasonable accommodation does not require an employer to make physical changes to accommodate a handicapped person where

> I. For a new employee the cost of such changes would exceed five percent (5%) of the annual salary or annualized hourly wage for the job in question: or
> II. For an existing employee the cost of the changes would bring the total cost of physical changes made to accommodate the employee's handicapping conditions since the beginning of the employee's employment with the employer to greater than five percent (5%) of the employee's current salary or current annualized hourly wage.

To illustrate. if a wheelchair-bound individual applied for a position as a secretary with a county. at a salary of $15.000 per year. and the county determined that it would cost at least $750 to make physical changes in the work area to accommodate the employee. then the county could refuse to hire the individual without violating the statute. even if the person was otherwise qualified. because the cost of accommodation would exceed the limits of the act. Of course. nothing would prohibit the employer from deciding to hire the employee even though the cost of accommodation exceeded the 5 percent limit. Obviously. the North Carolina General Assembly has taken a much narrower view of the limits of reasonable accommodation than has Congress.

The Handicapped Persons Protection Act also lists certain prohibited practices for employers at G.S. 168A-5. including a general prohibition against refusing to hire someone or dismissing someone who is a qualified handicapped person on the basis of the handicapping condition. In addition. it provides examples of affirmative defenses for employers at G.S. 168A-9. such as the failure of the handicapped person to comply with work rules and excessive tardiness or absence by the handicapped person.

The North Carolina act parallels the federal act in many ways. and it is a marked improvement over previous legislation in providing adequate protection for the handicapped in employment. Still. the federal act is drafted in such a way as to provide greater protection for covered employees.

The Rehabilitation Act of 1973

The Rehabilitation Act of 1973 is the federal statute governing the rights of handicapped individuals. The act has served as the model for states to follow in enacting their own handicap discrimination statutes, and it has been the act most often used to challenge employment decisions as violating the rights of the handicapped.[4]

The act defines the term *handicapped person* very broadly,[5] to include any person who "(i) has a physical or mental handicap which substantially limits one or more major life activities, (ii) has a record of such an impairment, or (iii) is regarded as having such an impairment."[6] By including in the definition of handicapped person those individuals who are "regarded" as handicapped, the act extends protection to people who, for example, are fully recovered from a heart attack and yet may be considered impaired by a potential employer. Excluded from the definition of handicapped person is "any individual who is an alcoholic or drug abuser whose current use of alcohol or drugs prevents such individual from performing" his or her job or who constitutes a direct threat to the property or safety of others.[7]

The act applies only to recipients of federal contract funds. Specifically, Section 503 of the act provides that any person who enters into a contract for more than $2,500 with the federal government for the procurement of personal property and nonpersonal services "shall take affirmative action to employ and advance in employment qualified individuals with handicaps." Section 504 of the act applies to recipients of federal financial assistance and provides that "no otherwise qualified individual with handicaps . . . shall, solely by reason of his handicap, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance." Section 504 has been interpreted by the United States Supreme Court to prohibit discrimination against the handicapped in employment.[8]

In the same case in which the Supreme Court held that Section 504 barred discrimination against the handicapped in employment, the Court also held that Section 504 only applied to the specific program of an employer receiving federal funds. With congressional passage of the Civil Rights Restoration Act in 1988, however, the effect of the 1984 ruling was overturned so that the entire corporation or other covered employer (including a state or local government employer) is covered by the requirements of the act, not just the particular subunit of the employer receiving the federal funds.[9] At least one court has held that the Civil Rights Restoration Act should be applied retroactively to allow discharged employees to bring their handicap discrimination suits.[10]

The Rehabilitation Act protects "otherwise qualified" individuals from discrimination based on handicap. In 1979, in a case arising in North Carolina, the United States Supreme Court defined an "otherwise qualified" person as "one who is able to meet all of a program's requirements in spite of his handicap."[11] That is, an otherwise qualified person is one who can perform the essential functions of a particular job.[12]

Whether a given individual is an otherwise qualified handicapped person is often a difficult question to answer. Each case is unique and of limited precedential value because of the vast variance in individuals and jobs. Nonetheless, a wide range of conditions have been found to constitute handicapping conditions in recent years, giving rise to the act's protections.[13] On the other hand, where the individual is not otherwise qualified, the employer has no duty of reasonable accommodation. For example, one court ruled that a hearing-impaired school bus driver was not otherwise qualified within the meaning of the act, because his inability to localize sounds meant that he could not ensure safety for his riders.[14]

When a handicapped person has been determined to be otherwise qualified, the Rehabilitation Act requires an employer to make reasonable accommodation if that would enable the person to perform the job's essential functions. Sometimes this may be easily accomplished; for example, a local government employer could probably make a reasonable accommodation for an otherwise qualified secretary who was confined to a wheelchair. Accommodation is not reasonable, however, if it requires a fundamental alteration of the job, or if accommodation imposes undue financial and administrative burdens on the employer.[15] Where reasonable accommodation does not overcome the effects of a person's handicap, or where reasonable accommodation causes undue hardship to the employer, failure to hire or promote the handicapped person will not be considered discrimination.

The determination of whether reasonable accommodation is possible for an otherwise qualified person also is not always easily made. For example, when Pennsylvania refused to provide readers for its blind income-maintenance workers in the Department of Public Welfare, the workers sued under the Rehabilitation Act,

claiming that the department's refusal constituted unlawful discrimination.[16] The department argued that the blind employees were not otherwise qualified employees, because they did not possess an essential qualification of the job: the ability to read. At a minimum, the department argued, even if the employees were deemed otherwise qualified, the cost of providing readers would be prohibitive.

The employees responded that they were otherwise qualified, in that in the past they had successfully performed their jobs with the aid of readers, paid for by the employees. In other words, the employees claimed, they were otherwise qualified because, with accommodation, they were able to perform all the job functions associated with their position.

The court agreed with the employees and held that they were otherwise qualified as that term is used in the act. Turning to the reasonable accommodation issue, the court stated that the matter could essentially be reduced to one question: would the cost of providing readers be greater than the act demands? The court said no and held that the department must provide readers for the employees. Judge Pollak, writing for the court, explained why:

> I am not unmindful of the very real budgetary constraints under which the [employer] operates, and recognize that accommodation of these plaintiffs will impose some further dollar burden upon an already overtaxed system of delivery of welfare benefits. But the additional dollar burden is a minute fraction of the . . . personnel budgets. Moreover, in enacting section 504, Congress recognized that failure to accommodate handicapped individuals also imposes real costs upon American society and the American economy. . . . When one considers the social costs which would flow from the exclusion of persons such as plaintiffs from the pursuit of their profession, the modest cost of accommodation—a cost which seems likely to diminish, as technology advances and proliferates—seems, by comparison, quite small.[17]

In this case, then, the court decided that the employees were entitled to the readers, even though there was a substantial cost associated with the accommodation. If the employer were a small North Carolina municipality instead of the state of Pennsylvania, would a court reach the same result? Perhaps not. The regulations implementing the act do not spell out precisely how an employer may demonstrate that an accommodation would impose an undue hardship on its operations, but the regulations do list three factors to be considered in making this determination:

1) The overall size of the recipient's program with respect to the number of employees, number and type of facilities, and size of budget
2) The type of the recipient's operation, including the composition and structure of the recipient's work force and
3) The nature and cost of the accommodation needed[18]

Appendix A to the regulations notes that "a small day-care center might not be required to spend more than a nominal sum, such as that necessary to equip a telephone for a secretary with impaired hearing, but a large school district might be required to make available a teacher's aide to a blind applicant for a teaching job."[19] Thus, a small employer might successfully argue that the cost of accommodating an otherwise qualified handicapped individual is simply unreasonable, even if the same individual could be reasonably accommodated by a larger employer.

The Americans with Disabilities Act of 1990

Currently pending in Congress is the Americans with Disabilities Act of 1990 [H.R. 2273/S.933]. This bill has passed the Senate and the House and, as of this writing, is in a conference committee to reconcile the differences between the two versions. It would extend the prohibition against handicap discrimination currently under Section 501 of the Rehabilitation Act of 1973 to private employers and state and local government employers that do not receive federal funding. For the first two years following the effective date of the act, all employers with twenty-five or more employees will be covered; after that, all employers with fifteen or more employees are subject to the act.

Title I of the act establishes requirements for employers. The act defines disabilities, as under the Rehabilitation Act and under the Handicapped Persons Protection Act, to include "(A) a physical or mental impairment that substantially limits one or more of the major life activities of such individual; (B) a record of such impairment; or (C) being regarded as having such an impairment." The general rule established by the act is that no employer may discriminate against a qualified individual with a disability solely on the basis of that disability. The employer is required to provide reasonable accommodation for qualified individuals with a disability.

Reasonable accommodation is defined as including

> (A) making existing facilities used by employees readily accessible to and useable by individuals with disabilities; and
> (B) job restructuring, part-time or modified work schedules, reassignment, acquisition or modification of equipment or devices, appropriate adjustment or modifications of examinations and training materials, adoption or modification of procedures or protocols, the provision of qualified readers or interpreters, and other similar accommodations for individuals with disabilities.

The act further defines the duty of reasonable accommodation by listing factors to be considered in determining whether an accommodation would impose an undue hardship on an employer. These factors include the cost of accommodation, the financial resources of the employer, the number of employees, the type of operation, and the composition, structure, and functions of the work force.

Like the North Carolina General Statutes, the act prohibits discrimination against a qualified individual with a disability with regard to any term, condition, or privilege of employment. The act provides an affirmative defense for employers: that application of certain qualification standards is necessary and substantially related to the ability of an individual to perform or participate in the essential components of the job or program.

The act is to be enforced by the Equal Employment Opportunity Commission, using the same procedures and with the same remedies as now exist under the Civil Rights Act of 1964 (which prohibits employment discrimination on the basis of race, sex, religion, color, or national origin).

If the Americans with Disabilities Act of 1990 is enacted, the effect on state and local governments would be minimal, as most public employers receive federal funds and thus are covered already by the Rehabilitation Act on which this statute is based.

HIV as a Handicap

What rights does an individual with HIV have under state and federal law? The greatest source of protection for employees with HIV who suffer adverse employment decisions would appear to be the Rehabilitation Act of 1973. The act has been applied to a variety of cases involving HIV in the workplace. The most important recent case interpreting the act, however, is one that involved tuberculosis, not HIV. Nonetheless, the case has important implications for employees with HIV.

In *School Board of Nassau County v. Arline*[20] the United States Supreme Court held that contagious diseases are a "handicapping condition" under Section 504. Although the Court's decision involved a schoolteacher with tuberculosis, the rationale of the opinion strongly supports the argument that HIV also is a disability under the act.

The plaintiff in *Arline* was discharged from her job as an elementary school teacher following a recurrence of tuberculosis. She brought suit against the school board, claiming that her condition was a handicap as defined by the act. The Supreme Court found that Arline was a handicapped individual because she previously had been hospitalized for tuberculosis and therefore had a "record of impairment" within the meaning of the act.

The Court noted that although Arline fit within the broad definition of a handicapped individual, the act only protects people who are both handicapped *and* otherwise qualified. The Court further stated that a person who poses a significant risk of communicating an infectious disease to others in the workplace is not otherwise qualified if reasonable accommodation by the employer will not eliminate that risk.

The determination of whether a person handicapped by a contagious disease is otherwise qualified, under the *Arline* decision, must be based on an individualized inquiry by the reviewing court. The inquiry must rely on reasonable medical judgments about (1) transmission of the disease, (2) the amount of time the carrier will be infectious, (3) the potential harm to third parties, and (4) the probabilities that the disease will be transmitted and will cause varying degrees of harm. The reviewing court usually should defer to the reasonable judgment of public health officials (for example, the Centers for Disease Control) in making these inquiries.

The Court declined to answer the questions of whether an asymptomatic carrier of a contagious disease, such as HIV, could be considered to have a physical impairment and whether such a person, solely on the basis of contagiousness, could be considered a handicapped individual under the act. It is significant to note, however, that the Court cited congressional action that amended the definition of *handicapped individual* to include those who are "regarded as impaired": "Congress acknowledged that society's accumulated myths and fears about disability and disease are as handicapping as are the physical limitations that flow from actual impairment. Few aspects of a handicap give rise to the same level of public fear and misapprehension as contagiousness."[21]

Since the *Arline* ruling, a number of lower federal

courts have considered the question of HIV and acquired immunodeficiency syndrome (AIDS) as a handicapping condition. In *Thomas v. Atascadero Unified School District*[22] the court held that AIDS is a protected disability under Section 504 of the Rehabilitation Act of 1973. This case did not involve an employee, but a child with AIDS who was barred from kindergarten after he bit a classmate. A similar result was reached by the court in *District 27 Community School Board v. Board of Education of City of New York*[23] and in *Ray v. School District of DeSoto County*.[24]

An important federal case involving AIDS in the workplace is *Chalk v. United States District Court Central District of California and Orange County Superintendent of Schools*.[25] In that case a teacher of hearing-impaired children in the Orange County, California, school system, who was hospitalized with pneumonia and diagnosed as having AIDS, won the right to return to his teaching duties. The court relied on *Arline* for the proposition that an employee with a contagious disease is included within the Rehabilitation Act's definition of a handicapped individual. The court also found that Chalk was "otherwise qualified" because he was physically and mentally able to teach and because there was no evidence to demonstrate any appreciable risk of AIDS transmission in the normal classroom setting.

What can a local government employer learn from these decisions? First, the decisions underscore the importance of properly educating employees as to the nature of the disease and the ways in which it can be transmitted. Second, it would appear that an employer who dismisses an employee with HIV or AIDS because of fear of contagion acts at its own peril and may violate applicable state and federal statutes. Third, the federal courts have held, at a minimum, that contagious diseases may be handicapping conditions under the Rehabilitation Act of 1973. Further, each federal court squarely faced with the issue has held that a person with HIV or AIDS meets the definition of a handicapped individual under the act. Local government officials must consider carefully whether a personnel decision adversely affecting an employee with HIV or AIDS could successfully be challenged in federal court under the Rehabilitation Act.

HIV and North Carolina Law

In addition to the requirements of the Handicapped Persons Protection Act discussed above, North Carolina state and local government employers also must be aware of the requirements of G.S. Chapter 130A, Article 6, the communicable disease law.[26] The act provides that "[a]ll information and records, whether publicly or privately maintained, that identify a person who has AIDS virus infection or who has or may have . . . [AIDS] shall be strictly confidential" [G.S. 130A-143]. There are limited exceptions to the confidentiality rule in the statute, such as the one permitting disclosure to health care providers giving care to infected individuals. The act also authorizes the Commission for Health Services to decide who has to be tested. Until recently, the commission limited testing to those who seek it voluntarily. Proposed regulations, however, would partially rescind anonymity of testing.

In 1989 the General Assembly amended G.S. 130A as it relates to people with HIV. It now provides that, except as otherwise provided in the act, (1) no HIV test may be required or performed to determine suitability for continued employment and (2) it is unlawful to discriminate against any person with HIV or AIDS in employment [G.S. 130A-148(i)]. The act authorizes individuals aggrieved by an act or discriminatory practice of an employer to bring an action for relief in superior court within 180 days of the date that the person became aware of the alleged discriminatory practice, but it limits remedies to declaratory and injunctive relief (including orders to hire or reinstate an aggrieved person), as well as retroactive pay and attorneys' fees.

The act's apparent protection for employees or applicants with AIDS or HIV is severely undercut by the remainder of G.S. 130A-148(i), however. The act further states that nothing shall prohibit an employer from (1) requiring an AIDS test of applicants as part of preemployment medical examinations, (2) denying employment to an applicant solely because that person tests positive for HIV, (3) including an AIDS test as part of an annual medical examination routinely required of all employees by the employer, and (4) reassigning or firing an employee who has AIDS or HIV infection if continuation of employment of the employee "would pose a significant risk to the health of the employee, coworkers, or the public, or if the employee is unable to perform the normally assigned duties of the job."

State and local government employers are cautioned that, notwithstanding these provisions of the communicable disease law, the federal handicap discrimination law, as noted above, consistently has been construed by the federal courts to prohibit employment discrimination against persons with AIDS or HIV infection. Thus, the

A Summary of Handicap Discrimination Laws

	Individuals Covered	Employers Covered	Where Found	Chief Effect
Handicapped Persons Protection Act	People with physical or mental handicaps, or with a record of such impairment	North Carolina employers with fifteen or more employees	G.S. 168A	Provides remedies for those not covered by federal law
Rehabilitation Act of 1973	Same, plus those with HIV	Recipients of federal funds	29 U.S.C. §§ 701-796i	Provides remedies for government employees and applicants
Americans with Disabilities Act of 1990	Same, plus those with HIV	All employers with twenty-five or more employees	H.R. 2273/ S. 933	Greatly expands scope of handicap law coverage
Communicable disease law	People with communicable diseases, including HIV	North Carolina employers	G.S. 130A, Art. 6	Permits employment decisions on HIV

changes enacted to the North Carolina law should have little practical effect on public employers.

The Effect of *Burgess*

Let's return to Scott Burgess's case, in which he claimed that his dismissal upon disclosure to his employer that he was HIV positive constituted a violation of the Handicapped Persons Protection Act. The North Carolina Supreme Court, in denying his claim, noted two distinctions between the North Carolina act and the federal handicap discrimination law. First, the court held that although both statutes define handicapped persons as those who are limited in one or more "major life activities," the North Carolina statute does not include working as a major life activity. In other words, because the employee did not show that a major life activity was impaired, he was not "handicapped." Second, the court held that the North Carolina statute, unlike the federal statute, provides that it is not a discriminatory action for an employer to discharge a handicapped person "because the person has a communicable disease which would disqualify a non-handicapped person from similar employment."[27] In the court's view, "proper application of the . . . principles of statutory interpretation compels us to conclude that our legislature did not intend that the definition of 'handicapped person' would include a person solely because he suffers from a communicable disease."[28]

In rejecting the employee's claim, the court relied on the legislature's rejection of a 1987 amendment to the act that would have protected people infected with HIV. The *Burgess* case thus reached a different result than the federal courts had reached on the question of extending the protection of handicap discrimination statutes to people with the HIV infection.

The practical effect of the *Burgess* case on state government as an employer and on local government employers is nonexistent. Given that local government employers are covered by the federal handicap discrimination act, they would still be potentially liable for claims of discrimination against HIV-positive employees or applicants. The *Burgess* case only means that plaintiffs with such claims must invoke the protection of the federal law (as opposed to state law).

If, as is expected, the Americans with Disabilities Act of 1990 is passed by Congress this year and signed into law, the result will be to bring all employers under the same rule: that individuals with HIV are handicapped and entitled to bring claims of employment discrimination. The Congressional Research Service, in analyzing the pending federal legislation, has unequivocally stated

that the act's "provision on contagious diseases or infections would cover persons with AIDS or who are positive for antibodies to HIV."[29]

Conclusion

Three questions were posed at the beginning of this article: Who is handicapped? What rights do the handicapped have to employment? What costs may an employer consider in hiring the handicapped? To answer those questions, first, whether one is handicapped depends on which statute is used to define the term. The federal statute has been interpreted by the courts to reach further in including individuals as handicapped than has been the case under state law. Second, the right one has to employment varies with the nature of the handicap, status as otherwise qualified, and the remedy afforded by federal versus state law. Third, an employer may take into consideration the costs involved in accommodating a handicapped individual in determining whether to hire that person; the limits of reasonable accommodation are more precise under the state statute than under the federal law.

Handicap discrimination law will continue to develop at a rapid pace. State and local government employers are advised to stay current and seek legal advice as necessary in dealing with this difficult area. ❖

Notes

1. G.S. 168A-1 through -12 (1987).

2. Burgess v. Your House of Raleigh, Inc., 326 N.C. 205, 388 S.E.2d 134 (1990).

3. G.S. 168A-3(1).

4. There have been occasional constitutional challenges brought against public employers by handicapped individuals. *See, e.g.*, Costner v. United States, 720 F.2d 539 (8th Cir. 1983) (federal regulation prohibiting people with epilepsy from driving does not violate equal protection clause); Gurmankin v. Costanzo, 11 Fair Empl. Prac. Cas. (BNA) 1359 (3d Cir. 1977) (school board's denial of opportunity for blind applicant to take exam qualifying her to teach sighted students violates due process rights under Fourteenth Amendment).

5. 29 U.S.C. § 706.

6. Major life activities are defined by the U.S. Department of Labor as including "communication, ambulation, selfcare, socialization, education, vocational training, employment, transportation, adapting to housing, etc." [41 C.F.R. § 60.741].

7. 29 U.S.C. § 706. Note that this definition would not exclude people who have a history of drug use but who no longer use drugs [Davis v. Bucher, 451 F. Supp. 791 (E.D. Pa. 1978)].

8. Consolidated Rail Corp. v. Darrone, 465 U.S. 624 (1984).

9. 29 U.S.C. § 794.

10. Leake v. Long Island Jewish Medical Center, 47 Fair Empl. Prac. Cas. (BNA) 783 (E.D.N.Y. 1988).

11. Southeastern Community College v. Davis, 442 U.S. 397, 406 (1979).

12. 45 C.F.R. § 84.3(k)(1).

13. Conditions found to be handicaps include chronic contagious diseases [School Board of Nassau County v. Arline, 480 U.S. 273 (1987)], mental disorders [Schmidt v. Bell, 33 Fair Empl. Prac. Cas. (BNA) 839 (E.D. Pa. 1983)], dyslexia [Stutts v. Freeman, 30 Fair Empl. Prac. Cas. (BNA) 1121 (11th Cir. 1983)], legal blindness [Norcross v. Sneed, 755 F.2d 113 (8th Cir. 1985)], stiffening of the joints [Sisson v. Helms, 751 F.2d 991 (9th Cir.), *cert. denied*, 474 U.S. 846 (1985)], nervous condition [Treadwell v. Alexander, 707 F.2d 473 (11th Cir. 1983)], missing limbs [Vickers v. Veterans Administration, 549 F. Supp. 85 (W.D. Wash. 1982)], coronary bypass [Davis v. Bucher, 451 F. Supp. 791 (E.D. Pa. 1978)], and epilepsy [Smith v. Administrator of Veterans Affairs, 32 Fair Empl. Prac. Cas. (BNA) 986 (C.D. Cal. 1983)].

14. Strathie v. Department of Transportation, 547 F. Supp. 1367 (E.D. Pa. 1982).

15. Southeastern Community College v. Davis, 442 U.S. 397, 410-12 (1979).

16. Nelson v. Thornburgh, 567 F. Supp 369 (E.D. Pa. 1983).

17. *Nelson*, 567 F. Supp. at 382.

18. 45 C.F.R. § 84.12(c).

19. 45 C.F.R. § 84, Appendix A, at 300.

20. 480 U.S. 273 (1987).

21. *Arline*, 480 U.S. at 284.

22. 662 F. Supp. 376 (C.D. Cal. 1987).

23. 130 Misc. 2d 398, 502 N.Y.S.2d 325 (N.Y. Sup. Ct. 1986).

24. 666 F. Supp. 1521 (M.D. Fla. 1987).

25. 840 F.2d 701 (9th Cir. 1988).

26. For a complete discussion of the communicable disease law and AIDS in the workplace, see Jeffrey S. Koeze, "North Carolina's Legislative and Regulatory Response to AIDS," *Popular Government* 54 (Winter 1989): 11–15.

27. *Burgess*, 326 N.C. at 214, 388 S.E.2d at 141.

28. *Burgess*, 326 N.C. at 215, 388 S.E.2d at 140.

29. Nancy Lee Jones, *CRS Report to Congress* 89-433A, "The Americans With Disabilities Act: an Overview of Selected Major Legal Issues" (Congressional Research Service, Library of Congress, July 25, 1989), p.6.

Installment Financing under G.S. 160A-20: New Opportunities and Procedures

A. Fleming Bell, II

During the last decade, North Carolina counties and municipalities have relied more and more on installment financing contracts (also frequently called lease-purchase agreements) to finance the purchase of the equipment, land, and buildings that are needed to provide the services their citizens demand. Under these contracts, a security interest is created in the property being acquired to secure payment of the purchase money.

Section 160A-20 of the North Carolina General Statutes (hereinafter G.S.) has provided the necessary statutory authorization for local governments to enter into such transactions.[1] The property is the financier's main recourse in the event of a default; the statute stipulates that no "deficiency judgment" may be rendered against the local government in an action for breach of the contract.[2]

(Since 1988, G.S. 160A-20 also has authorized water and sewer authorities created under G.S. Chapter 162, Article 1, to engage in secured financings.[3] While this article is concerned only with cities' and counties' transactions, much of what is said also applies to water and sewer authorities.)

The popularity of secured transactions of this type can be attributed to several factors. First, the state constitutional requirement[4] of voter approval that applies whenever a local government "incurs debt" (that is, "borrows money") "secured by a pledge of the faith and credit" (defined as "a pledge of the taxing power") apparently does not extend to G.S. 160A-20 transactions. The statute explicitly provides that "the taxing power of a city or county is not and may not be pledged directly or indirectly to secure any moneys due under a contract authorized by [G.S. 160A-20]."[5]

Second, the interest that a local government pays in a G.S. 160A-20 transaction is exempt from federal income taxation if the transaction meets certain Internal Revenue Service requirements. A correctly structured secured transaction is treated, for federal income tax purposes, in the same manner as a local government bond issue: the Internal Revenue Service considers it to be an "obligation" of the city or county, and the interest on it is exempt from taxation under the Internal Revenue Code.[6] Those financing G.S. 160A-20 transactions find them attractive because of the tax-exempt interest that they can earn. Cities and counties also benefit financially from the transactions, because some of the tax savings are usually passed along to them in the form of lower interest rates.

A perceived third advantage of G.S. 160A-20 transactions is flexibility of structure and cost, as compared with certain other financing techniques such as general obligation bonds. The term of installment agreements can be shorter—and the amount financed, smaller—than would be feasible for bond issues (although longer-term, larger G.S. 160A-20 financings are also possible). Issuance costs, which are related to transaction size, are frequently less for smaller G.S. 160A-20 transactions than for conventional bonds.

As such transactions increased in popularity during the 1980s, certain limitations and questions concerning G.S. 160A-20 became apparent. This led in 1989 to a substantial revision of the statute by the North Carolina legislature.[7] These legislative changes are the focus of this article, which updates an earlier discussion of G.S. 160A-20.[8]

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Prior Limitations and Questions

The prior version of 160A-20 seemed to contemplate that local governments would enter into two-party purchase money security interest transactions with sellers of real or personal property. The seller would supply financing for the purchase of property and would take back a security interest in the property to secure payment of the purchase price.

Although such transactions did occur, the majority of proposed installment purchases involved not two parties but three: a buyer, a seller, and a financing institution. To make use of third-party financing, local governments often resorted to elaborate financing structures to turn a three-party transaction into a two-party "buyer-seller" arrangement fitting the statutory scheme.[9]

Another difficulty involved the scope of transactions authorized by G.S. 160A-20. Purchases of real property could be financed under the statute, for example, while construction or repair of buildings on that same property were not covered by its provisions.[10]

Some cities and counties tried to avoid the latter problem by selling land to private developers and then buying it back through an installment sale arrangement, once a building constructed to the local government's specifications had been built on it. Such arrangements presented other questions, however, regarding proper procedures for disposing of public property and the potential need for compliance with the public bidding and contracting laws in the construction of buildings intended for governmental purchase and use.

Other local governments made use of nonprofit corporations to complete construction projects. Such a corporation would borrow money to finance the construction of a desired building or other structure. It then would lease the completed structure to the city or county, with lease payments set at a level sufficient to retire the debt incurred by the corporation. This type of arrangement, like the sale-buyback structure, raised bidding law issues. It also posed a more general question regarding governmental power: could a local government use a nonprofit corporation to do indirectly what it could not do directly?

The Legislative Response

The new version of G.S. 160A-20 directly addresses the third-party financing and construction or repair financing questions discussed above. In addition, the act clarifies and expands some of the procedural requirements for entering into secured transactions.

Third-party financing authority for purchases

The revised statute makes clear that cities and counties may make direct use of banks and other third-party financing institutions in financing purchases. Specifically, it provides that they "may purchase *or finance the purchase* of real or personal property by installment contracts that create in the property purchased a security interest to secure payment of the purchase *price* [formerly, purchase money] *to the seller or to an individual or entity advancing moneys or supplying financing for the purchase transaction*."[11]

Thus, instead of creating a financing structure where a bank or other financier serves as a surrogate "seller" of the property or is assigned a vendor's contractual rights to receive installment payments,[12] a local government may procure the amount and type of financing it needs directly from a bank. Typically, the governmental unit will execute a promissory note promising to repay with interest the money borrowed and will give the financing institution a security interest in the property to ensure that it does so. (In the case of real property, this security interest will take the form of a deed of trust.)

Construction and repair financing authority

Perhaps the most important provision of revised G.S. 160A-20 is its expansion of financing authority in the construction area. New G.S. 160A-20(b) specifically allows the financing of construction or repair projects (such as new jails, city halls, or water and sewer lines, or the renovation of existing buildings, structures, or other improvements) through contracts that grant a security interest in the fixtures or improvements being constructed or repaired, in the land on which they are located, or in both. The security interest (a deed of trust) secures repayment of moneys that are advanced or made available for the construction or repair work.

Under this provision, a local government may obtain a construction loan to finance needed capital improvements in much the same way that a private individual would borrow money to pay for construction of a house. An important procedural safeguard accompanies this expanded authority, however: contracts under G.S. 160A-20 that involve the construction or repair of

fixtures or improvements on real property must be approved by the North Carolina Local Government Commission under the requirements of G.S. Chapter 159, Article 8, regardless of their size.[13]

Escrow agreements

Another new provision authorizes the use of escrow accounts in connection with the advance funding of G.S. 160A-20 transactions.[14] Escrow accounts increase local governments' flexibility in structuring secured transactions under G.S. 160A-20(a) and (b) by allowing units to borrow money (and perhaps "lock in" an interest rate) in advance of the time that the funds are actually needed as part of a purchase transaction or construction project. Money that is made available in advance by banks and other financiers is held in escrow and invested, pending disbursement as part of a transaction.

The interest a governmental unit earns on such an advance-funding investment often will more than offset the interest cost of the advance loan. However, if the unit uses an escrow account in connection with a secured transaction involving tax-exempt interest income, it also must be mindful of federal arbitrage and rebate regulations. These rules govern the extent to which a local government may retain profits it makes by investing at taxable interest rates money that it borrows at tax-exempt rates.

Prohibition of nonsubstitution clauses

Nonsubstitution clauses attempt to limit local governments' flexibility in making alternative arrangements in the event that an installment financing contract is terminated. They vary in their terms and severity, but generally they state that if the local government has a contractual right to terminate the agreement because of

Capital Financing: Techniques and Statutes

Installment financing under G.S. 160A-20 is only one of several techniques used by North Carolina cities and counties to meet their capital financing needs.

Bonds

The most familiar financing vehicles are *general obligation (G.O.) bonds* and *revenue bonds*. A G.O. bond is a loan obligation backed by the taxing power (the "full faith and credit") of the local government borrower; it usually requires voter approval. A revenue bond is an obligation that is secured by the revenues expected to be earned from the project being financed (for example, a water system or a parking garage).

Another, newer vehicle for borrowing is the *special obligation bond*, which may be backed by a variety of revenue sources other than locally levied taxes. Examples of revenues that may be pledged to secure special obligation bonds include fees, charges, state-shared taxes, and (for cities only) sales tax receipts.

Although G.O. and revenue bonds may be issued for a variety of purposes, North Carolina cities and counties may only make use of special obligation bonds for certain solid-waste facilities. Detailed statutes govern each type of bond (see, respectively, G.S. Chapter 159, articles 4 and 5, and Chapter 159I).

Leases and Continuing Contracts

Other provisions that are sometimes cited as providing statutory authority for specific capital financing transactions are the leasing enabling laws for counties and cities (G.S. 153A-165 and 160A-19) and the county and city enabling statutes for continuing contracts (G.S. 153A-13 and 160A-17).

Leases

The leasing statutes authorize cities and counties "to lease as lessee, with or without option to purchase, any real or personal property for any authorized public purpose." They also specify that all leases with option to purchase of personal property are subject to the competitive bidding laws.

nonappropriation of funds and it chooses to exercise that right, it cannot replace the property being financed with other equipment, services, or facilities to perform the same (or a similar) function. The prohibition remains in effect for a prescribed period, which may be as long as the duration of the original contract. The intended effect of such a clause, quite obviously, is to discourage the local government from exercising any right that it may have to terminate the contract because of nonappropriation of funds.

Such clauses, which in any event may have been unenforceable in most G.S. 160A-20 transactions,[15] are now specifically prohibited. New G.S. 160A-20(d) specifies that no contract entered into under the statute may contain a clause that restricts the governmental unit's right to continue to provide a service or activity, or to replace or provide a substitute for any fixture, improvement, project, or property financed or purchased under the contract.

Public hearing requirement for real property transactions

In apparent recognition that real estate transactions under G.S. 160A-20 may well involve substantial financial commitments for a number of years, the 1989 amendments require that a public hearing be held on *any* G.S. 160A-20 contract that *involves* real property (whether it is a purchase contract or a contract for a construction or repair project).[16] A notice of the hearing must be published once (in a newspaper of general circulation)[17] at least ten days before the hearing date.

Requirements for Local Government Commission approval

Certain G.S. 160A-20 transactions must be approved by the Local Government Commission (LGC) in accordance with G.S. Chapter 159, Article 8, as well as correctly

Although G.S. 153A-165 and 160A-19 do not specifically mention financing arrangements, a number of attorneys think that they provide an independent source of statutory authority to create financing structures for construction or repair projects or for real or personal property acquisition—structures that involve a lease of the property to the city or county as part of the financing plan. Thus, for example, a city or county might lease a completed building from a corporation that finances construction of the building, with the lease payments equaling the principal and interest payments of the corporation, and with title to the building being conveyed to the city or county once the corporation's debt is paid. (Questions about the applicability of the competitive bidding statutes are among the issues that may arise with such an arrangement [see page 17].)

Other experts assert that the leasing statutes probably are intended only to authorize traditional lease agreements—that is, contracts for the rental and use of property—because they make no mention of capital financing. The fact that purchase options are allowed is, in their view, insufficient evidence that financing is authorized.

These experts point out that in other cases where the General Assembly has allowed local governments to enter into capital financing arrangements (for example, the Local Government Bond Act, the Revenue Bond Act, and G.S. 160A-20), it has provided explicit directions and often very detailed rules concerning how those transactions are to be structured. In their opinion, fairly specific statutory enabling authority is needed to uphold particular financing arrangements for local governments, just as such authority is needed to mortgage public property.

Continuing Contract Statutes

G.S. 153A-13 and 160A-17 authorize counties and cities, respectively, to enter into continuing contracts "some portion or all of which are to be performed in ensuing fiscal years." If a city or county enters into a continuing multi-year contract, it is required by the statute to appropriate sufficient funds in each fiscal year to meet that year's continuing contractual obligations.

A disagreement similar to that about the leasing enabling laws exists concerning the scope and meaning of these statutes. While some persons see them as an independent source of authority for creating multi-year capital financing programs, others disagree. They argue that G.S. 153A-13 and 160A-17 should not be interpreted as authorizing particular kinds of contracts, but rather as specifying that contracts *that are otherwise authorized by statute* may extend beyond the current fiscal year. They contend that specific enabling authority is probably required for any type of financing arrangement contemplated by a city or county and that a general authorization to enter into multi-year contracts will not suffice.

structured under G.S. 160A-20. The 1989 amendments to G.S. 160A-20 clarify the law concerning when the LGC approval requirements apply.[18]

First, as noted earlier, LGC approval is required for any secured transaction that involves the construction or repair of fixtures or improvements on real property. In addition, LGC approval is required for any real or personal property purchase transaction under G.S. 160A-20 that meets certain requirements set out in G.S. 159-148(a)(1), (2), and (3); that is, if

1) it "extends for five or more years from the date of the contract," including optional renewal periods;
2) it obligates the local government "to pay sums of money to another;" and
3) it obligates the local government, "over the full term of the contract," including renewal periods, for the lesser of $500,000 or "a sum equal to one tenth of one percent . . . of the appraised value of property subject to taxation" by the local government.

The requirements of Article 8 do not apply to installment contracts "for the purchase, lease, or lease with option to purchase of motor vehicles or voting machines," to contracts entered into between a local government and the state or federal government as a condition for grants or loans to the local government, or to loan agreements entered into by a unit of local government pursuant to the North Carolina Solid Waste Management Loan Program (G.S. Chapter 159I).[19]

A local government that is proposing a G.S. 160A-20 agreement for which LGC approval is required must apply for approval of the contract to the LGC secretary. The secretary may require the unit's governing board or its representative to attend an informal, preliminary conference before the secretary accepts the application. In addition, the unit's finance officer or other designated official must give the secretary a sworn "statement of debt" like that required by G.S. 159-55 in connection with a general obligation bond issue.

Article 8 of G.S. Chapter 159 lists a number of factors that the LGC may consider in determining whether to approve the contract. The contract may be approved only if the unit's net debt, after the contract is executed, will be 8 percent or less of the appraised value of property subject to taxation by the local government. (The amounts to be paid under G.S. 160A-20 agreements and other contracts subject to Article 8 are counted as "debt" for purposes of this calculation.) The LGC must also find that

1) The contract is "necessary or expedient."
2) "[T]he contract, under the circumstances, is preferable to a bond issue for the same purpose."
3) The sums that fall due under the contract are "adequate and not excessive" for the purpose of the contract and can be met without an "excessive" increase in taxes.
4) The local government "is not in default in any of its debt service obligations" and either has good debt-management policies and procedures or has assured the LGC that it will manage its debt "in strict compliance with law."

The unit need not meet all of the listed conditions if it can show that (a) the project is *both* "necessary and expedient," (b) "the proposed undertaking cannot be economically financed by a bond issue," and (c) "the contract will not require an excessive increase in taxes."

If it tentatively decides to deny the unit's application because the information submitted does not provide a sufficient basis for approval of the application, the LGC is to notify the local government and then hold a public hearing on the application if the unit requests one. Article 8 specifies that LGC approval of an application is not to be regarded as an approval of the legality of the contract.

Conclusion

North Carolina local governments will probably continue to expand their use of installment financing agreements in coming years, as a means of increasing their flexibility in paying for the assets they need to perform their functions. In structuring G.S. 160A-20 transactions, care must be taken both to comply with all applicable statutes and to draft contractual terms that adequately protect the local government's interests. With such caution, however, North Carolina local governments should find that secured financing transactions are a valuable addition to the assortment of financial tools available to help them provide governmental services efficiently and effectively. ❖

Notes

1. Local governments in North Carolina have no inherent authority to mortgage or encumber public property [Vaughn v. Commissioners of Forsyth County, 118 N.C. 636, 640–42 (1896)]. Specific statutory authorization is needed for transactions that create a security interest, lien, or mortgage on property that a local government owns or is acquiring or constructing.

2. If one breaches a contract involving a security interest, the financier often can repossess the property securing the financing and sell it to recover some of the money lost because of the breach. A deficiency judgment, which is prohibited in G.S. 160A-20 transactions, is a judgment entered by a court against a breaching borrower for any loss suffered by the financing entity that was uncompensated after the repossessed property was sold.

3. Water and sewer authorities were added to the coverage of the statute during the 1988 regular session of the legislature [1987 N.C. Sess. Laws ch. 981, § 1].

4. N.C. Const. art. V, § 4.

5. G.S. 160A-20(f). The reader shuld be aware, however, that the constitutionality of G.S. 160A-20 is being challenged in a case currently on appeal to the North Carolina Court of Appeals, Wayne County Citizens Ass'n for Better Tax Control v. Wayne County Bd. of Comm'rs, 90 CvS 179 (Wayne County, March 29 and April 6, 1990), *appeal docketed*, No. 9085C577 (Ct. App. June 1, 1990). The plaintiff-appellant asserts that the types of transactions that the statute purports to authorize require voter approval under Article V, Section 4, of the North Carolina Constitution. The trial court held the statute to be constitutional.

6. For a discussion of the federal income tax treatment of the interest paid by local governments under financing agreements, see A. J. Vogt et al., 1 *Guide to Municipal Leasing*, 2d (rev.) printing (Chicago: [Governmental] Finance Officers Association of the United States and Canada, 1985), 54–58. Its coverage of this area, although no longer complete because of postpublication changes in arbitrage restrictions and other provisions of federal tax law, remains generally accurate.

7. 1989 N.C. Sess. Laws ch. 708.

8. A. Fleming Bell, II, "Lease-Purchase Agreements and North Carolina Local Governments," *Popular Government* 49 (Spring 1984): 8–17.

9. A set of documents for creating such a structure is included in A. Fleming Bell, II, *A Model Equipment Lease-Purchase and Security Agreement for North Carolina Local Governments, with Annotations and Appendices* (Chapel Hill, N.C.: Institute of Government, 1985).

10. See A. Fleming Bell, II, "Questions I'm Most Often Asked: To what extent may North Carolina cities and counties make use of lease-purchase financing in real estate transactions?" *Popular Government* 51 (Spring 1986): 33–35.

11. G.S. 160A-20(a). Italicized words indicate new statutory language.

12. See the financing structures discussed in Bell, "Lease-Purchase Agreements," 10–11.

13. G.S. 160A-20(e).

14. G.S. 160A-20(c).

15. See Bell, "Lease-Purchase Agreements," 16, and Bell, *A Model Equipment Lease-Purchase and Security Agreement*, 21–25.

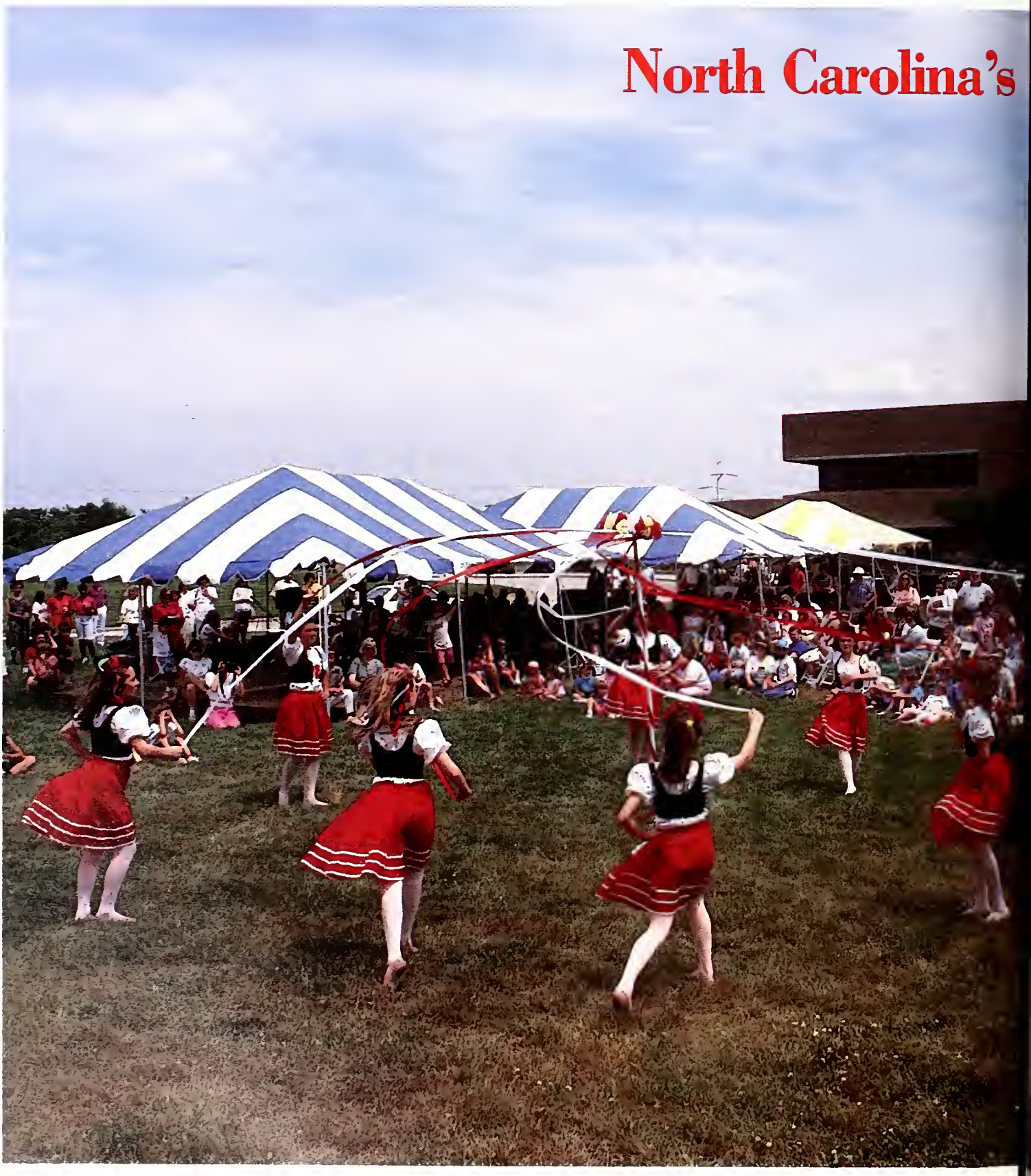
16. G.S. 160A-20(g).

17. See G.S. 1-597.

18. G.S. 160A-20(e). Prior to enactment of this provision, there was a good deal of uncertainty concerning which G.S. 160A-20 contracts, if any, were subject to LGC approval. See Bell, "Lease-Purchase Agreements," 13–14.

19. G.S. 160A-20(e) [see subparagraph (2)]; G.S. 159-148(b).

North Carolina's



Department of Cultural Resources: Special Programs for All Our Citizens

Boyd D. Cathey

Each year millions of North Carolinians use public libraries, visit historic sites and museums, and attend concerts and lectures. How many of us realize that these programs and services, which so often are taken for granted, are in large part made readily available through the support of North Carolina's Department of Cultural Resources?

Created in 1971, the Department of Cultural Resources was the first cabinet-level arts agency established in the United States, and it continues to be the only agency of its kind providing such a diversity of services under one administrative umbrella. The department consists of five divisions: the North Carolina Museum of Art, the State Library, Archives and History, the North Carolina Symphony, and the North Carolina Arts Council. Together they share the mission of enriching the cultural, educational, and economic well-being of citizens and visitors to North Carolina through the preservation, de-

The author is administrative research director for the Department of Cultural Resources. He wishes to thank the division directors for their assistance in preparing this article. Photographs are courtesy of the North Carolina Department of Cultural Resources.

The May Pole Dance is performed during the North Carolina Museum of Art's Festival of Spring, a family program celebrating nature and landscape (left).

velopment, promotion, and dissemination of artistic, historical, and informational resources. The key to fulfilling this mission is outreach—touching the lives of our citizens and offering services that are provided by no other agency of government.

Visitors to the Museum of Art enjoy another family event, the American Folk Art Festival.

North Carolina Museum of Art

In 1947 the General Assembly appropriated $1 million for the purchase of Old Master paintings, making North Carolina the first state in the country to create an art collection for its citizens with public funds. That action ultimately led to the establishment of the North Carolina Museum of Art.

Today the museum's art collections represent 5,000 years of man's artistic achievements, extending back to the ceremonial art of ancient Egypt. The first appropriation bought 139 Old Master canvases in 1952's art market. Years later, in the early 1960s, the Samuel Kress Foundation presented sixty-nine paintings and two sculptures to the museum. Those two acquisitions formed the core of a collection that is nationally recognized for its outstanding examples of European paintings. Collections of ancient, African and New World, Judaic, and twentieth century art have been added since 1960.

The museum mounts twelve to fifteen changing exhibitions annually, ranging from contemporary works by North Carolina artists to the art of other countries and cultures. Major exhibitions have included a 1984 showing of works by Andrew, Jamie, and N. C. Wyeth; a 1987 retrospective of the work of Sir David Wilkie, a Scottish painter; and "Robes of Elegance," a 1988 exhibition of kimonos from the national museums of Japan.

In addition to the exhibits, an array of events and educational activities at the museum are designed for all ages, from day-long family festivals and Friday night feature films to free guided tours offered in English, French, German, and Spanish. The museum also shares staff and volunteer resources through its statewide outreach programs. These free services are educational and include slide lectures that accompany exhibits, workshops and instructional packets for educators, and technical assistance from staff.

Guided tours for schoolchildren often are tied to their specific curricula in history, art history, or art. Under the guidance of the museum's education department, specially trained volunteers called docents present a wide variety of tours structured to cover guidelines provided by the state's Department of Public Instruction. Requests for special program topics are accommodated whenever possible. The education staff also works with the Department of Public Instruction to offer renewal credit summer workshops in art history and criticism for public school teachers.

The state continues to protect its investment by providing annual operating funds, which are supplemented by contributions and earned income by the North Carolina Museum of Art Foundation. This generous state support allows the museum to operate without charging admission.

Archives and History

The North Carolina Division of Archives and History, the third oldest state historical agency in the country, was established in 1903 as the North Carolina Historical Commission. It is one of the largest and most active agencies of this type in the nation. Required by law to "promote and encourage throughout the state knowledge and appreciation of North Carolina history," Archives and History operates programs in archaeology, preservation of historic structures and sites, archives, and historical publications. Publications include books, pamphlets, and a quarterly journal of the state's history. In addition to its Raleigh office, the division has two regional offices in Asheville and Greenville to provide a fuller range of services to the western and eastern parts of the state.

The division operates the Museum of History in Raleigh and regional history museums in Elizabeth City, Fayetteville, and Old Fort. These museums not only offer exhibits that interpret the history of their regions but also provide a broad range of consultative services in such fields as collections management and security to nonprofit museums in their areas. A very popular Tar Heel Junior Historian Club network, sponsored by the Museum of History, enables thousands of high school students to learn North Carolina history and to participate in statewide "History Bowl" competitions that test their knowledge of our state's heritage.

The division's twenty-four owned and maintained historic sites draw nearly a million visitors a year to attractions ranging from the splendor of Tryon Palace to the pastoral beauty of the Zebulon Vance Birthplace. In addition to presenting a vivid picture of North Carolina's varied heritage, our historic sites sponsor special educational and children's programs. A recently opened site is the Charlotte Hawkins Brown Memorial, near Sedalia. Through exhibits, oral histories, and educational programs, the site commemorates Dr. Brown's work as the state's first major black educator. Another significant addition is the Horne Creek "Living History Farm," near Pilot Mountain, which, when fully operational, will provide visitors with a realistic view of farm life in late nineteenth century North Carolina.

The mountain craft of "country woodworking" is demonstrated to a group of youngsters during Pioneer Living Day at Vance Birthplace State Historic Site near Weaverville. The Division of Archives and History maintains twenty-four historic sites in North Carolina.

Of course, North Carolina has many other historical attractions not administered by Archives and History, such as historic Beaufort in the east and the Museum of

The *Elizabeth II* State Historic Site, a square-rigged sailing bark representative of sixteenth century vessels that transported Sir Walter Raleigh's colonists to the New World, is open to visitors in Manteo.

the Cherokee Indian in the west. The division maintains a cooperative working relationship with most of those attractions and provides consultative services, for instance, suggesting techniques on how to restore a historic house or how best to conserve a fragile doll in a museum display.

In addition to its work with museums and sites, the division houses the State Archives. North Carolina has long been known nationally for its archival and records management programs. In 1964 the State Archives received the first national Society of American Archivists' Distinguished Service Award. The division maintains more than one hundred million carefully preserved local and state documents, which are available to citizens for research. Most documents also have been microfilmed for greater accessibility.

North Carolina's archives offer excellent opportunities for genealogists and individuals researching family history. Training sessions are offered annually to assist the public in this popular activity. Legally, county records are required to be offered to the State Archives. Here visitors may examine original wills, deeds, census records, marriage records, and estate settlements.

As with the state, local government records are scheduled for retention or destruction on the basis of recommendations of the division's records managers. In an era in which all kinds of informational data proliferate, our records management staff offers sound guidance on which records need to be retained for future reference and which may be disposed of as duplicative or of little administrative, legal, fiscal, or research use.

In the area of educational outreach, Archives and History engages in cooperative ventures with colleges and public schools in the state, including archaeological digs and special college courses. Nearly one hundred student interns per year perform duties that advance the agency's programs while exposing the students to career possibilities in public historical agency work. From participating in an archaeological excavation to inventorying local historic properties, interns gain practical experience in "hands on" history while learning about the past.

North Carolina Symphony

The North Carolina Symphony is a sixty-eight-member orchestra that performs classical, pops, and educational concerts throughout the year. Since its founding in 1932 by North Carolina composer and conductor Lamar Springfield, the symphony has been dedicated to education and quality entertainment for the people of North Carolina.

The Symphony currently performs nearly 200 concerts each year. Although based in Raleigh, the Sym-

phony travels all across North Carolina. For instance, in fiscal year 1988–89 the orchestra journeyed 21,879 miles, visiting fifty-seven of the state's one hundred counties. Each season the orchestra performs in ten to fifteen counties with low per-capita income; such counties are not often visited by a symphony and do not have local symphony support groups.

Working with the public schools, the orchestra performs educational concerts for schoolchildren. Symphony support staff offer workshops for music teachers throughout the state in preparation for these concerts. Special educational materials enable teachers to prepare their students for the music they will hear.

More than 95 percent of its concerts in Raleigh's Memorial Auditorium were sold through subscriptions for the 1989–90 season, and numerous individual concerts have been sell-outs in recent years. In addition to its high quality of musicianship, the Symphony's popularity also can be attributed to the internationally known guest artists and conductors who join it for performances. A sample of the stars who have appeared in recent years includes Andre Watts, Wynton Marsalis, Kathleen Battle, Kiri Te Kanawa, Pinchas Zukerman, Doc Severinsen, Dizzy Gillespie, and Eric Knight.

Along with the classical and pops concerts in its regular season, the Symphony performs a Young People's Concert Series in various North Carolina communities. Like the in-school educational concerts, these performances are designed to help children learn about classical music. In the future this series will be televised over public television.

The Symphony is supported by funding from the General Assembly, contributions by individuals and corporations, and ticket sales. During fiscal year 1988–89 more than two thirds of the Symphony's income came from ticket sales and private and corporate contributions. At a time when orchestras all over the United States are experiencing financial crises, the North Carolina Symphony enjoys broad support from the citizens of the state. A recently completed $10 million endowment campaign will help ensure future service to North Carolina.

State Library

The North Carolina Division of the State Library is one of the oldest state libraries in the United States. Founded in 1812 to serve the General Assembly, it has evolved into one of the premier institutions of its type in the country. Although the services of a modern state library extend to all citizens of the state, the primary responsibility of the State Library continues to be furnishing information needed by state government to develop policies and programs. Because of the highly

The North Carolina Symphony performs nearly 200 concerts each year throughout the state.

Environment, Health, and Natural Resources Secretary Bill Cobey, Governor Jim Martin, and Cultural Resources Secretary Patric Dorsey share a story with youngsters during the 1990 Summer Reading Program, "Book a Trip to Africa," at the North Carolina Zoological Park in Asheboro. The program is sponsored by the State Library.

technical needs of government, the library provides access to commercial and governmental electronic data bases that offer the most up-to-date information on everything from population statistics to purchasing costs for products used in state offices. Through these electronic networks, the State Library also is able to obtain from other state and national libraries books, periodicals, and other information materials not kept in its own collection.

Since 1909 the State Library has assisted local communities in all parts of the state in developing public library services. Today there is at least one professional librarian managing a public library in all but one of the state's counties. The General Assembly, moreover, extended this development mandate to include professional aid to the state's community college and corporate libraries. Programs ranging from a children's summer reading series to the electronic services of the North Carolina Information Network are provided to public and corporate libraries across the state.

The State Library's North Carolina Information Network links libraries in more than ninety counties to major commercial and state data bases. These include Standard & Poor's, the State Data Center's LINK, the North Carolina Online Union Catalog, and the North Carolina Automated Purchase Directory. Through high speed telecommunications, it offers the private, corporate, and governmental sectors the most up-to-date information available. As a pool of resources, the network represents the financial investment in library materials and electronic information services made by all of the state's public and private institutions. It has become a model for other states creating similar systems because it was the first, and for a long time the only, one to emphasize service to rural communities and small businesses. By providing sources of marketing, sales, and financial data and by developing programs to instruct small-business managers in using the network, the State Library is helping rural counties learn how to use this information in small businesses and local governments.

The State Library also offers special services through its Library for the Blind and Physically Handicapped, which maintains a collection of books and magazines recorded on audio cassettes and phonograph records. To use this library, a person registers for the service, and new titles are automatically sent on a regular basis. Titles are chosen from a general "profile" of reading interests maintained for each customer. Every cassette or record used by a customer is recorded in a data base to avoid sending duplicate titles. The library distributes these braille materials to readers in North and South Carolina. The demand for this vital service continues to increase annually.

One of the State Library's most important tasks is

distributing more than $15 million in state and federal grant funds to public libraries. This money is used to support book and material purchases, automation, electronic data networks, in-service education, and the construction of new public library buildings. Some of these funds also support special adult learning programs, elementary and secondary school student research, and literacy projects. To be eligible to receive funds, library systems must employ professional, certified librarians, and provide matching funds at a minimum dollar-for-dollar level.

North Carolina Arts Council

For many years North Carolina has been a leader in the arts. The first of thousands of thriving community arts councils in the United States was founded in Winston-Salem in 1949. PlayMakers Repertory Company at The University of North Carolina at Chapel Hill was the first state-supported theatre in the country dedicated to the development of American drama. This year the nation's oldest outdoor drama, *The Lost Colony*, presents its fifty-third season in Manteo. And the North Carolina School of the Arts, which has produced many top artists, was the country's first state-supported residential school for the performing arts.

Continuing this strong tradition, the North Carolina Arts Council, formed by executive order in 1961, was one of the first state arts agencies in the United States. Its mission is to enrich the cultural life of the state by nurturing and supporting excellence in the arts and by providing opportunities for every North Carolinian to experience the arts. It fulfills that goal through a network of community arts councils, which operate at the municipal or county level.

These community arts councils receive funding for special projects from the state council. Many of them are designated as local distributing agents for the funding of the Grassroots Arts Program. This program, established by legislation in 1977, was the first per-capita funding program in the country for local arts initiatives. The program provides funds to local arts councils, which use them for community arts projects or for subgrants to other arts organizations or programs.

The Arts Council also provides varying levels of state and federal funding to its 1,500 constituent nonprofit arts organizations. These funds are available through a wide array of grant categories to which organizations can apply and for which they must generally provide a dollar-for-dollar match in local funds. These organizations range from gospel quartets to symphony orchestras, from mime troupes to Shakespearean theatres, from clogging groups to modern dance companies, and from local poetry societies to statewide literary clubs.

"Jubilee-style" gospel singers, the Badgett Sisters (left to right, Connie Stedman, Cleonia Graves, and Celester Sellars), received the 1989 North Carolina Folk Heritage Award. The award program is a project of the North Carolina Arts Council.

To Learn More
about the Programs of the Department of Cultural Resources

Office of the Secretary. Patric G. Dorsey (919) 733-4867

Public Affairs (919) 733-5722

North Carolina Museum of Art (919) 833-1935

Archives and History Administration (919) 733-7305
Archaeology (919) 733-7342
Historic Preservation (919) 733-4763
Historic Sites (919) 733-7862
Historical Publications (919) 733-7442
Museum of History (919) 733-3894
State Capitol (919) 733-4994
Visitor Services (919) 733-3456
Tryon Palace (919) 638-5109
Western Office (704) 298-5024
Eastern Office (919) 752-7778

North Carolina Symphony (919) 733-2750

State Library Administration (919) 733-2570
Information Services (919) 733-3270
Public Library Development (919) 733-2570
Special Services (919) 733-4376

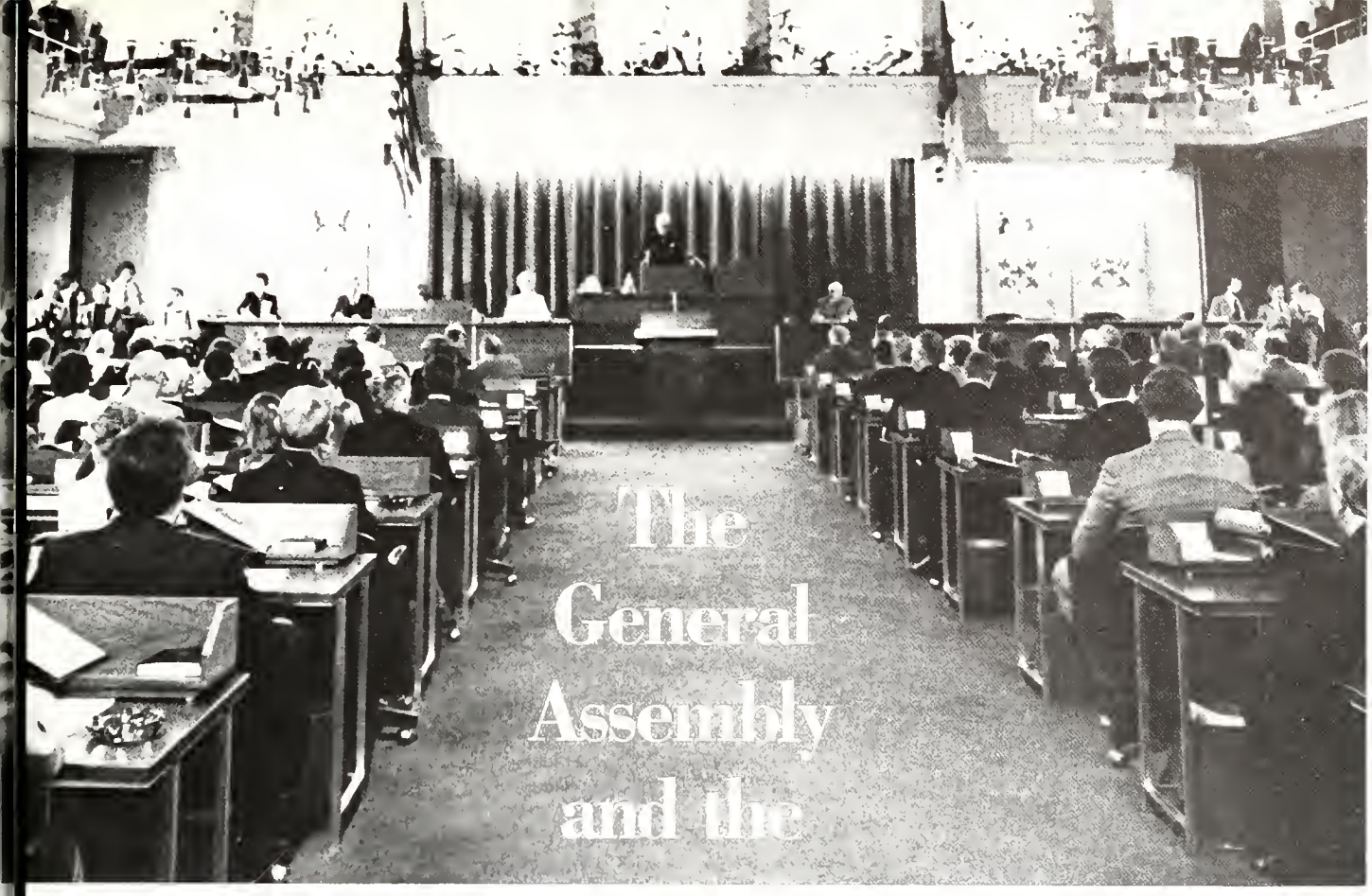
North Carolina Arts Council Administration (919) 733-2111
Community Development, Folklife (919) 733-7897
Literature Arts, Visual Arts (919) 733-2111
Performing Arts (919) 733-2821

Through competitive selection, fellowships of varying amounts are awarded to professional artists (those who have made a career commitment to their art), allowing them to set aside time to work, to purchase supplies and equipment, to achieve specific career goals, and to devote full attention to the creation of their work. In addition, artists on an approved roster can perform residency engagements in the public schools. These schools apply to the Arts Council for funds to support those residencies.

Another highly successful support project, the Visiting Artist Program, places artists in the state's fifty-eight community colleges to serve as arts resources to the surrounding communities. The artists who participate in these year-long residencies offer community workshops and performances, public school educational programs, and a variety of other services.

North Carolina's rich and multicultural heritage in the traditional arts is promoted and preserved through a wide range of programs and projects sponsored by the council. One very special project is the North Carolina Folk Heritage Award Program. These awards are presented annually to folk artists in recognition of their contributions to traditional American culture. Recent honorees include an Appalachian ballad singer, a fiddler, blues guitarists, basket makers, and potters.

The Arts Council also administers the Art Works in State Buildings Program, which allocates one half of 1 percent of construction costs of state buildings for installation of works of art in those buildings. The program greatly benefits not only the artists it employs but also the many citizens of the state who visit or work in those buildings. Artists are chosen through a careful screening process that includes input from the building's architects, its government agency, and representatives of the Department of Administration and the North Carolina Arts Council. ❖



Jim Thornton/Courtesy Durham Herald Company, Inc.

The General Assembly and the Budget

Joseph S. Ferrell

North Carolina, like all states and the federal government, uses a budget to control government expenditures. With few exceptions, state agencies and institutions may spend public money only within the constraints imposed by the budget. The state budget is enacted by the General Assembly and administered by the governor. This article describes the General Assembly's role in the budget process.

Overview of the Budget

North Carolina operates on a fiscal year that runs from July 1 to June 30, and its budget is organized and administered on that basis. The total state budget for the 1989–90 fiscal year was almost $12 billion. That sum included all money that came to and was spent by state government. Of those funds, 20 percent came from the federal government, and 9 percent from agency receipts. Not all of that money was subject to legislative consideration. The General Assembly exercises ultimate control over programs wholly or partially funded from federal dollars, but it does not attempt to regulate the flow of that money in the same way it does revenue from state sources.

Most state revenue and expenditure—$7.4 billion of that $12 billion total—flows through the General Fund. It is this money that claims the lion's share of legislative budget deliberations. Most General Fund revenue comes from the state income and sales taxes; the largest expenditures are for public schools (about 41 percent of General Fund appropriations) and programs administered by the Department of Human Resources (about 15 percent of the General Fund). Spending for public education at all levels (elementary and secondary schools,

The author is an Institute of Government faculty member whose specialties include the General Assembly. The article is adapted from a chapter in the author's forthcoming revised edition of The General Assembly of North Carolina, A Handbook for Legislators, *published by the Institute of Government.*

community colleges, and higher education) consumes two thirds of General Fund revenue.

The other major state funds subject to appropriation by the General Assembly are the Highway Fund and the Highway Trust Fund. Together these funds comprise 10 percent of the state budget. The gasoline tax, the highway use tax, and various fees collected with respect to ownership and operation of motor vehicles are the revenue sources for these funds.

Balanced Budget

The state constitution provides that "the total expenditures of the State for the fiscal period covered by the budget shall not exceed the total of receipts during that fiscal period and the surplus remaining in the State Treasury at the beginning of the period."[1] This means that the state must operate on a cash basis, at least with respect to the revenue side of the ledger, and that state government as a whole may not spend in any given fiscal period more money than comes into the state treasury. To say that the budget must be balanced is a shorthand way of saying that the total expenditures of the state for the fiscal period must be offset on the other side of the equation by an equal amount of revenue. That revenue comes primarily from current tax and fee collections, but it also includes surplus funds on hand at the beginning of the fiscal period, the proceeds of bond issues, federal funds, agency receipts, and other sources.

Both the state constitution and the statutes require the governor, as director of the budget, to "continually survey the collection of the revenue"[2] and to "effect the necessary economies in state expenditures"[3] to prevent expenditures from exceeding revenue. The governor recommends, and the General Assembly enacts, a balanced budget by estimating the revenue side of the equation and appropriating the expenditure side. After the budget is enacted, only the expenditure side of the equation can be controlled with any degree of certainty. The constitution and statutes therefore require the governor to ensure that the balanced budget requirement is observed by curtailing expenditures if revenues fail to materialize in the amounts anticipated.

The statutes say that the General Assembly's appropriations are "maximum, conditional and proportionate."[4] That is, appropriations are maximum in that an agency may not spend more than is appropriated, conditional in that they are dependent on actual revenue collections, and proportionate in that the total amount that all agencies are to spend is proportional to actual revenue collections. The governor is required to monitor revenue collections and determine how much of the money appropriated by the legislature should be allocated each quarter.[5] The governor may, but need not, consult the Advisory Budget Commission in so doing. If necessary to avoid a deficit or overdraft, the Executive Budget Act directs the governor to reduce all appropriations on a pro rata basis.[6] In practice that is rarely done, because it could mean discharging employees or reducing salaries. Instead, the governor typically puts a freeze on filling vacant positions and reduces the amount of money made available to agencies for spending on nonpersonnel items.

Most appropriations not expended or encumbered by an agency at the end of the fiscal year revert to the unencumbered credit balance in the state treasury.[7] Reversions become part of the revenue that the next General Assembly may employ to balance its budget. Appropriations for capital improvements do not revert, even if unencumbered, nor do grants-in-aid. Occasionally special provisions in the expansion budget may provide that certain specific appropriations do not revert.

Preparing the Budget

As ex officio director of the budget, the governor is directed by the state constitution and the Executive Budget Act to prepare a budget for consideration by the General Assembly.[8] Because a new General Assembly is elected every two years, the practice has always been that the governor presents to the first regular session a budget covering two fiscal years.[9] There is no barrier, however, to annual budgeting if the governor and General Assembly choose to operate that way. Since 1974 the General Assembly has held a second regular session in each even-numbered year primarily for the purpose of refining the budget for the second year of the biennium.

The governor is assisted in preparing the budget by the Office of State Budget and Management (OSBM) and the Advisory Budget Commission (ABC). The OSBM is administratively located in the Office of the Governor.[10] It provides staff support for the governor's constitutional and statutory duties as director of the budget[11] and is headed by the state budget officer. In preparation for both the first and second regular sessions, the budget office solicits budget requests from state agencies. It receives and analyzes those requests and compiles such other information as the governor and the ABC need.

The ABC is created by statute[12] and charged with the duty of advising the governor in preparing the budget.[13] Five senators appointed by the president of the Senate, five representatives appointed by the speaker of the House, and five persons appointed by the governor make up the ABC. If the governor appoints any legislators to the ABC, an equal number must come from the House and Senate.

Approximately a year before a new General Assembly convenes, the OSBM sends to state agencies the forms for budget requests for the next biennium. Because that biennium will not begin until July 1 of the next year, about eighteen months away, these initial requests are necessarily somewhat speculative. At this time the governor will also be discussing budget priorities with department heads, and the OSBM will be studying matters not within the jurisdiction of any single department, such as salary increases and retirement and health benefit changes.

To maintain the independence of the judicial and legislative branches from the executive branch, the budgets of the General Assembly and the Administrative Office of the Courts are presented directly to the governor and by the governor to the General Assembly without participation of the OSBM or the ABC, but the governor may make such recommendations with respect to these budgets as he or she may see fit.[14]

Budget requests fall into three categories: continuation, expansion, and capital improvements. The continuation budget (also known as the base budget) is the amount needed to continue existing programs at the current level of service. The amount required for the continuation budget may increase each year because of inflation; statutory increases in matching requirements, such as social security taxes; and the annualization cost of programs previously funded for only part of a year. The expansion budget (also known as the change budget) is the amount needed to expand existing services, establish new programs, provide for salary increases, provide for increases in higher education enrollments, and provide for increases in case loads and institutional populations. The capital improvement budget is the money needed to build new structures or to repair old ones. Throughout the executive and legislative budget process, the continuation, expansion, and capital improvement requests are considered separately.

In addition to being categorized as continuation, expansion, or capital items, budget requests are also informally identified as either recurring or nonrecurring. A recurring item is one that will become part of the continuation budget in the next biennium. The total of all recurring items in the budget is capped by the estimated yield of recurring revenue items, such as taxes, fees, and certain types of federal aid. A nonrecurring item is, as the name implies, one that will not become part of the next biennium's continuation budget. The total of all nonrecurring items in the budget is capped by the total of reversions from the preceding biennium and other one-time revenue items, such as bond issues. All capital projects are treated as nonrecurring items, but the budget usually includes a number of nonrecurring current operating items as well. Categorization of items as recurring and nonrecurring is not required by the Executive Budget Act, but the practice has such proven worth that it has become an indispensable part of the budget process.

Each budget request calling for additional personnel must identify the number of positions to be added. This requirement enables the Senate and House Appropriations committees to comply with a portion of the Executive Budget Act that limits the percentage increase in the number of state employees (other than public school employees hired at the local level) to the average percentage increase in the population of the state over the previous decade.[15]

When departmental budget requests are received, OSBM analysts review them and confer with the departments. The OSBM is especially interested in seeing that requests have been properly labeled as continuation or expansion requests. Although the statute requires that departmental requests be submitted by September 1 of even-numbered years[16] (about four and one-half months before the newly elected General Assembly will convene), the governor usually sets an earlier deadline, often in the spring or early summer.

During the fall before the first regular session convenes, the ABC tours state facilities to assess the need for capital improvements. Representatives of state agencies also appear before the ABC to explain and argue for their expansion budget requests.[17] Throughout this time the ABC is receiving economic forecasts from the OSBM so that revenue estimates may be made. The General Assembly's Fiscal Research Division staff attend these meetings but have no active role at this stage of the budget process. The division's staff members are entitled to attend all ABC meetings and hearings, and the legislative services officer and the director of fiscal research must be given the same notice of meetings, hearings, and

trips that the members of the ABC receive, plus copies of all reports that go to members.[18] Except for the hearings on departmental requests, ABC deliberations are not required by law to be open to the public and usually are not.[19] By statute, the speaker, speaker pro tempore, president pro tempore, and Senate majority leader are entitled to attend ABC meetings.[20]

The governor and the ABC complete their work in December, but their recommendations remain confidential until the governor addresses the new legislature in January. If the governor and the ABC should disagree, the governor's budget is submitted to the General Assembly, and the ABC includes a statement of its disagreement in the governor's report.[21]

Legislative Consideration

Legislative consideration of the budget begins with the governor's budget message, which is delivered at a joint session within the first week or two of the first regular session. Later on the same day the chairs of the Senate and House Appropriations committees will introduce companion bills embodying the governor's expenditure proposals, and the chairs of the Finance committees will do the same with respect to any companion revenue measures. They do this as a courtesy to the governor, not as an indication of endorsement of the governor's proposals. These bills, discussed further below, are explained in the budget message and in the various supporting documents provided by the OSBM.

Committee structure

The budget bills are then referred to the Appropriations committees. Any companion revenue-raising bills are referred to the Finance committees. The president pro tempore and the speaker each appoint about half of the members of their respective houses to an Appropriations Committee and the other half to a Finance Committee. In recent years several members in both houses have served on both committees, with the result that the Senate Appropriations Committee has had as many as forty members and the House Appropriations Committee as many as seventy-one.

The work of the Appropriations committees is always done by subcommittees, though the number, titles, composition, and jurisdiction of those subcommittees vary from house to house and from session to session. Typically the subject-matter subcommittees are Education, General Government, Human Resources, Justice and Public Safety, and Natural and Economic Resources. The 1989 House added subcommittees on Transportation and Capital Outlay and Special Programs to the list.[22]

In the 1989 session, the Senate and House Appropriations committees met jointly to receive budget information from legislative and state agency staff but met separately thereafter and developed their changes in the governor's budget independently of each other. In previous sessions the committees met jointly but voted separately, a practice still reflected in the statutes but no longer observed in practice.[23]

The appropriations subcommittees are at first constituted as a Base Budget Committee to consider the continuation budget. After the full Appropriations Committee in each house acts on changes in the continuation budget recommended by the subcommittees, the subcommittees are then reconstituted as Expansion Budget committees and turn their attention to the governor's expansion budget recommendations. Capital outlay requests are handled in the House by the Capital Outlay and Special Programs Subcommittee and in the Senate by a subcommittee composed of the chair of the Appropriations Committee and the chairs of the subject-matter subcommittees.

The organization of the Finance committees is less elaborate. The 1989 House Finance Committee was organized in permanent subcommittees, as were all other House committees. The Senate Finance Committee used subcommittees on an ad hoc basis. In a typical session the Finance committees will handle many local bills, a large number of relatively minor public bills affecting revenue matters, and one or two major revenue proposals. The Finance committees play a coequal role in the budget process, however, because their actions on revenue measures determine the overall parameters within which the Appropriations committees must work. Like the Appropriations committees, the Finance committees meet jointly to receive information from staff but meet separately when deliberating on measures before them.

In recent sessions it has become customary to enact separate bills for the continuation budget, the Judicial Department budget, the expansion and capital outlay budget, and items of state aid to local governments.[24] Any recommendation for the issuance of bonds is placed in separate legislation, as are any tax measures, because these measures require roll-call votes on separate days while the main budget bills do not. The bills themselves

appropriate money in large, lump-sum totals; to get line-item details on what each agency will do with the money appropriated to it, one must consult the supporting documentation provided by the OSBM. The format of those documents varies from year to year, but generally they distinguish between continuation and expansion items and provide some commentary on the worthiness of the proposed appropriations.

The budget bills also include legislation addressing a great many matters concerning the administration of programs funded in the budget. These portions of the budget bills are called special provisions. The three main budget bills enacted in 1989 contained among them more than 355 special provisions covering 177 pages. The Senate rules provide that no provision changing existing law may be included in the budget bills unless it (1) alters expenditures or salaries, (2) changes the scope or character of a program for fiscal reasons, or (3) modifies a state government function in a way that requires a transfer of funds from one department to another.[25] The House rules have no comparable provision.

In recent years the Appropriations committees have prepared summary reports of items included in the expansion and capital budgets with codes identifying the items as recurring or nonrecurring and indicating how many new positions are being created. These reports are attached to the bills themselves, are incorporated by reference, and may be used to interpret the budget act.[26]

As soon as the budget bills are introduced, OSBM staff members meet with the Appropriations committees in joint session to explain the proposed budget and how to use the supporting documentation. The General Assembly also is assisted throughout its consideration of the budget by its own Division of Fiscal Research.[27] The division's organization and powers are prescribed by statute.[28] It has a professional staff of about twenty-five, which legislators may use to answer questions, objectively review departmental requests, and suggest alternative funding methods independently of the OSBM.

Committee consideration

After the orientation sessions, the Appropriations Committee of each house divides into its subject-matter subcommittees and begins a detailed consideration of the recommended base budget. In 1989 subcommittee meetings were held both in the morning and in the afternoon after the daily session.

Legislators often introduce bills that make appropriations for activities in which they have a special interest. Although formal consideration of these requests must wait until the continuation and expansion budgets are passed,[29] the dollar amounts suggested in special appropriations bills quickly become part of the discussion in the Appropriations committees. Some items suggested in special bills may become part of the budget finally approved by the Appropriations Committee, but most will not be acted on until the main budget package has been completed.

Before 1989 the Appropriations committees approved a budget package that called for expenditure of less than the total revenue estimated to be available for the upcoming biennium. Then the committees decided which special appropriations bills would be funded with the remaining money. For several sessions this process included allocation of a specific sum of money to each member, which that member was permitted to allot to any group or project in his or her district as long as the money was spent for public purposes. The 1989 session did away with these formalized processes, which had come to be known as the "pork barrel."

At some point during the committee's deliberations, the governor may also recommend changes in the budget as originally presented. This is especially likely to happen during the first year of a new governor's term. A newly elected governor takes office just before the legislative session begins and must of necessity submit a budget that has been largely prepared by his or her predecessor.

After the base budget is enacted, which takes about twelve weeks, each Appropriations committee holds a round of joint meetings to hear supplemental budget requests from state agencies, and then the subject-matter subcommittees meet jointly to receive information from staff and separately to consider the requests. After the hearings and lengthy debate on the expansion budget, supplemental requests, and capital budget, the subject-matter subcommittees report their recommendations to the full Appropriations committee in each house.

When the subject-matter subcommittees report to their respective full Appropriations committees, about five months into the first regular session, the total appropriations recommended will frequently exceed the revenue predicted to be available. Traditionally the full committee then creates a special subcommittee mandated to cut and fit the subject-matter committees' recommendations to the funds available to create a balanced bud-

get. The membership and title of this subcommittee varies from one house to the other and from session to session, but its key members are always the chair of the Appropriations Committee and the chairs of the subject-matter subcommittees. For that reason it is known informally as the supersub.

The supersub will consider, but is not bound by, the priorities set by the subcommittees. It may also adopt a revised, slightly more optimistic estimate of revenue in order to ease the problem of balancing. The package that the supersub agrees on after days of intense work and negotiation will be brought back to the Appropriations Committee for approval. The full committee is under no obligation to accept its recommendations, either as a package or individually.

In the past, much of the effective decision making on the budget was done in private. The 1989 General Assembly opened the doors on the budget process. Additions to and changes in the governor's continuation and expansion budget recommendations were generally embodied in bills that were considered in open session by the subject-matter subcommittees, as were drafts of special provisions. Only at the end of the process were some of the conference committee negotiations conducted in private.

Joint House-Senate work

The final Appropriations Committee recommendations are drafted as committee substitutes for the governor's budget bill or some other appropriations bill in the committee's possession and reported to the floor. Because of the known difficulty of balancing the demands for appropriations with responsible estimates of available revenue, and because more than half of the members serve on the Appropriations Committee and participated extensively in developing the bills, budget bills usually receive only a minimum of floor debate in relation to their importance, and successful amendments are few. As each house completes action on its version of the various budget bills, they are sent to the other chamber for concurrence.

Because the House and Senate Appropriations and Finance committees no longer sit jointly to consider the budget, each house develops its budget bills independently. This means that the two houses rarely agree as to all of the items included in the budget bills sent over by the other house. The differences between the chambers must be resolved by conference committee. Typically, each house appoints to the conference committees on budget bills the same members who previously acted as the supersub in developing that chamber's version of the bill at issue. The rules allow the conference committee to consider only spending items or special provisions on which the versions of the bill differ. Once agreement is reached, the conferees report a substitute bill to both chambers, and when that report is adopted, the budget has been enacted.

Second-session revision

The procedure employed in the second regular session to revise the budget for the second year of the biennium is much the same, except that it takes place in a much shorter period of time because only changes, not a whole budget, are being considered. The governor first recommends the changes, usually a few weeks before the session convenes (which may be done with or without participation by the ABC), and the Appropriations Committee may meet in advance of the session to begin its deliberations. The Executive Budget Act was written with the assumption that the budget would be enacted for a biennium and not amended thereafter. Therefore, there is no mandated procedure that the governor is required to follow in developing recommendations for budget adjustments affecting the second year of the biennium.

Joint Legislative Commission on Governmental Operations

Since the 1975–77 biennium, the General Assembly has exercised continuing oversight of the state budget through the work of the Joint Legislative Commission on Governmental Operations. The commission has twenty-two members. The president, the president pro tempore, and the majority leader of the Senate and the speaker and the speaker pro tempore of the House serve as ex officio members. The speaker appoints nine House members, and the president of the Senate appoints eight members of the Senate. Members are appointed for two-year terms, beginning on January 15 of each odd-numbered year. Members who fail to run or are defeated for reelection may continue to serve out their appointed terms, but resignation or removal from office creates a vacancy.[30] The president of the Senate and the speaker of the House serve as cochairs.[31] In practice, the two presiding officers act as chair of the commission in alternate months.

The commission's primary duty is to undertake program evaluation studies of the various components of state agency activity as they relate to (1) service benefits in comparison to expenditures, (2) the achievement of program goals, (3) the use of indicators by which success or failure of a program may be gauged, and (4) conformity with legislative intent.[32] The statute defines "program evaluation" as an examination of the organization, programs, and administration of state government for the purpose of ascertaining whether the programs (1) are effective, (2) continue to serve their intended purposes, (3) are efficient, and (4) require modification or elimination.[33] The commission is staffed by the Fiscal Research Division and other members of the General Assembly's professional staff.[34] ❖

Notes

1. N.C. Const. art. III. § 5(3).

2. N.C. Const. art. III. § 5(3); N.C. Gen. Stat. § 143-25.

3. N.C. Gen. Stat. § 143-25. A balanced budget is also referred to in the general-purpose language of N.C. Gen. Stat. § 143-2.

4. N.C. Gen. Stat. § 143-25.

5. N.C. Const. art. III. § 5(3); N.C. Gen. Stat. § 143-25.

6. N.C. Gen. Stat. § 143-25.

7. N.C. Gen. Stat. § 143-18.

8. N.C. Const. art. III. § 5(3); N.C. Gen. Stat. §§ 143-2, -11, -12.

9. The General Statutes [N.C. Gen. Stat. § 143-12] refer to appropriations and revenues for the "ensuing biennium."

10. Exec. Order No. 38, 1979 N.C. Sess. Laws p. 1510. This order, which transferred the OSBM from the Department of Administration to the Office of the Governor, was not transmitted to the General Assembly before the sixtieth day of the 1979 session, as required by Article III, Section 5(10), of the constitution. Nevertheless, the validity of the transfer has not been subsequently challenged and is implicitly validated by Chapter 1137, Section 37, of the 1979 Session Laws.

11. N.C. Const. art. III. § 5(3); N.C. Gen. Stat. § 143-19.

12. N.C. Gen. Stat. § 143-4.

13. N.C. Gen. Stat. § 143-10.

14. N.C. Gen. Stat. § 143-10.

15. N.C. Gen. Stat. § 143-10.2.

16. N.C. Gen. Stat. § 143-6.

17. N.C. Gen. Stat. §§ 143-6 and -10.

18. N.C. Gen. Stat. § 120-36.6.

19. N.C. Gen. Stat. § 143-318.15.

20. N.C. Gen. Stat. § 143-34.7.

21. N.C. Gen. Stat. § 143-12.

22. N.C. House, *1989 North Carolina General Assembly House of Representatives Rules–Directory* (Raleigh: 1989), Rule 32; N.C. Senate, *1989 North Carolina General Assembly Senate Rules–Directory* (Raleigh: 1989), Rule 27.

23. *See* N.C. Gen. Stat. § 143-14.

24. The Executive Budget Act requires separate bills only for current operating expenses and capital outlay [N.C. Gen. Stat. § 143-12].

25. N.C. Senate, *1989 Rules–Directory*, Rule 42.4.

26. *See, e.g.*, 1989 Sess. Laws ch. 751, § 64; *see also* N.C. Gen. Stat. § 143-12 (final paragraph).

27. During sessions, Fiscal Research staff members are fully occupied in assisting legislators with the appropriations process. Between sessions, staff members undertake research on particular fiscal matters as requested by individual legislators; undertake broad studies of state government operations as directed by simple or joint resolution, the Appropriations and Finance committees, or the Joint Legislative Commission on Governmental Operations; serve as staff to interim study groups; and oversee expenditures and activities within their assigned areas. The Fiscal Research Division's activities generally are controlled by the Legislative Services Commission. By statute, it is required to make studies as directed by the commission, by the Appropriations Committee of either house, or by either house [N.C. Gen. Stat. § 120-36.3(1)].

28. N.C. Gen. Stat. §§ 120-36.1, 120-36.3.

29. N.C. Gen. Stat. § 143-15.

30. N.C. Gen. Stat. § 120-71.

31. N.C. Gen. Stat. § 120-75.

32. N.C. Gen. Stat. § 120-76(1).

33. N.C. Gen. Stat. § 120-72.

34. N.C. Gen. Stat. § 120-79.

Contracts That Bind the Discretion of Governing Boards

David M. Lawrence

Consider the following hypothetical situations.

A citizens group in a small North Carolina town has urged the town board to build a senior center on a vacant lot owned by the town. The board likes the idea, but there is no money available to build the center. In response the citizens have proposed that they organize a private fund-raising campaign to raise half of the amount needed, with the town providing the other half from town resources. The fund-raisers, however, want to be able to assure potential donors that the town will provide its share. Therefore they ask that the board commit the town to doing so. The request creates a difficulty for the board because the fund-raisers expect to take at least two years to raise the private funds and by then a new board will have taken office. No one is quite sure whether the current board can commit a future board to matching the private contributions for the senior center.

A new board has taken office in a North Carolina county. The new chairman is spending a good bit of time in the county office building, and he has come to dislike the background music that is played in offices there. On looking into the matter, he discovers that fourteen months earlier the previous board had entered into a five-year contract with the private company that provides the music. The chairman would dearly like to get out of the contract, but he is not sure that it is possible.

These two situations, disparate as they are, both raise a recurring question in local government: to what extent may a governing board enter into a contract that binds its own future discretion? (This question is frequently phrased in terms of the capacity of the present board to bind its successors, but, as we shall see, that phraseology understates the basic doctrine.) This article addresses that question under North Carolina law.

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The Basic Rule

The leading case in North Carolina—and perhaps the United States—is *Plant Food Company v. City of Charlotte*.[1] Plant Food had contracted with the city to remove sewage sludge from city drying beds, paying the city according to a schedule set out in the contract. The contract extended for ten years, with an option for either party to extend the contract another ten years. But within a year or two of the contract's execution, a new governing board took over in the city and sought to negate the contract. When Plant Food sued the city for breach of contract, the city argued that the previous board had no power to enter into a contract that bound the current one.

The national rule, as developed by the courts of many states, was (and is) that a city may enter into a contract that binds future boards if the subject of the contract is a *proprietary* activity of government. If, however, the subject is a *governmental* activity, such a contract is beyond the power of the local government and therefore void. The city pointed out that sewer services had been held to be a governmental activity in the context of local government immunity from tort liability, and it argued that therefore this contract involved a governmental activity and could not bind a later board. The trial court agreed.

On appeal, the North Carolina Supreme Court accepted the dichotomy between proprietary and governmental activities but refused to simply transfer the distinctions made in tort law to this different context. The

public policies behind the distinctions were different in the two contexts, and the court reasoned that those differences necessarily led to a different placement of the line between proprietary and governmental activities. "The true test," according to the court, "is whether the contract itself deprives a governing body, or its successor, of a discretion which public policy demands should be left unimpaired." If that sort of discretion is not involved, then the contract would not be invalid simply because it extended beyond the terms of office of the original governing board. The court did not find the necessary discretion involved in the Plant Food contract itself. Rather, the contract was an ordinary commercial transaction, and the city was bound by it. If the contract was no longer acceptable to city officials, the city would have to pay damages for its breach.

Future Boards Only?

The city in *Plant Food* made its argument in terms of the capacity of one governing board to enter into contracts that bind a later board with different members. The argument fit the facts of that case, and the doctrine of law under discussion in this article is popularly framed as a limitation on the ability of one governing board to bind by contract the discretion of its successor or successors. But, as noted in the introduction, that framing understates the force of the doctrine. In fact, the doctrine also applies to contracts that purport to bind only the current board.

First of all, to limit the doctrine to contracts that extend past the term of the current board assumes a distinction between this year's board and next year's that is not accepted in the law. The courts have consistently characterized the governing board of a city or county as a continuing body, one that maintains its corporate identity regardless of any changes in its membership.[2] It is this continuity of identity that permits a board to hold a public hearing in October, before an election, and to act on the subject of the hearing in December, after the election, even though an entirely new set of members may have been elected and qualified in the interim.

Second, such a limit on the doctrine suggests that if the contract will be fully executed before the next election, it will be valid even if it does purport to bind the board's discretion. But does anyone really believe that a city council can validly contract in January to rezone a piece of property in a particular way in April or levy a stated rate of tax in June simply because no election intervenes in that period? Certainly not the supreme court. Recall the court's language in *Plant Food*: "The true test is whether the contract itself deprives *a governing body, or its successor,* of . . . discretion."[3] The limitation on contracting powers, that is, applies as much to the present board as it does to a future board. Just as today's board cannot by contract force a future board to adopt a particular ordinance, rezone property in a particular way, open a street, or levy a tax, so it cannot by contract force itself to take any of these actions. The current board must retain that discretion just as much as the future board.

The Nature of Discretionary Activities

The basic rule, then, is that a local government may enter into a contract that binds itself, whether now or in the future, *unless* the contract purports to bind the government on a matter on which public policy requires that the government retain discretion as to whether and how to act. For what kinds of decisions is that continuing discretion necessary?

The court in *Plant Food* did not attempt to define the category of discretionary powers. Rather, it set out a number of examples to "roughly indicate the quality of the power involved," which included the powers

1) to adopt ordinances,
2) to lay out and maintain streets,
3) to preserve order,
4) to regulate rates,
5) to levy taxes, and
6) to levy special assessments.[4]

The list is actually quite narrow. Fundamentally, the listed examples involve the exercise of either the government's police power (adopt ordinances, lay out streets, preserve order, regulate rates) or the government's taxing power (levy taxes or special assessments). (The taxing power also includes the power to appropriate the taxes that are levied—that is, the power to spend money.) Cases from other states suggest one other probable example, the appointment and retention of a board's principal officers, such as a city manager or attorney. But that is about as long as any such list would be.

Understood in this way, the list is consistent with the decided cases in North Carolina. The appellate courts have invalidated contracts that purported to bind a city to keep certain ordinances in force for twenty-five years or to rezone property in a particular way.[5] They have

invalidated contracts that purported to bind a local government to open a particular street; to locate a new highway in a specific location; and to build a boulevard, with side street access, rather than a limited-access highway.[6] They have denied that a city could bind itself not to annex a particular tract of land.[7] And they have denied that a county could be required to levy taxes for a particular activity.[8]

The distinctions made by the North Carolina court in *Plant Food* are also consistent with the results of cases decided in other states in the last two decades. The Nebraska Supreme Court, for example, upheld a twenty-year contract under which a city that operated an electric utility leased space on city-owned electric poles, at a fixed rate, to the local cable television operator.[9] While the city could not have bound itself to a twenty-year rate structure for utility services, pole rental was not such a service. A California appellate court upheld a contract under which a city reserved sewer-treatment capacity for a particular developer.[10] And a Texas appellate court held that a bank services contract involved a commercial, rather than a governmental, activity for the contracting local government.[11] On the other side, courts have invalidated contracts that purported to give multiyear terms to the governing board's attorney, to limit a city's ability to annex, and to require the city to tax property at a reduced rate (multiple tax rates were legal in that state).[12]

Legislative Authorization to Bind a Board's Discretion

The North Carolina courts, in keeping with the courts of other states, have characterized contracts that attempt improperly to bind the discretion of a local governing board as being in violation of the *public policy* of the state. That is, the contracts violate common law doctrines that apply to local government. The courts have not, however, sought to ground the doctrine in the state constitution. They do not cite any provision of the constitution, and the opinions do not imply that these contracts are unconstitutional.

If, then, the contracts are void because they violate public policy, a change in public policy should lead to their being held valid. And the primary source of public policy for the state is the General Assembly. That is, the logic of the cases suggests that the General Assembly may, by specific statutory authorization, permit a local government to enter into a contract that binds its own discretion, because such a statute would represent a change in public policy.

None of the North Carolina cases directly addresses this point, although two or three can be interpreted to support the legislature's power to authorize such contracts. But there is some support in North Carolina legislative practice, and there are examples of such legislation from other states that have been upheld.

A number of North Carolina statutes indicate an assumption that the General Assembly does have the power to authorize contracts that bind a board's discretion. School boards, for example, are authorized to enter into two- and four-year employment contracts with superintendents, their chief executive officers.[13] Cities are permitted to contract with housing authorities and agree to adopt certain ordinances, including zoning ordinances.[14] Counties are authorized to commit themselves to make specific levels of capital outlay appropriations to school boards in future years, in order to support multiple-year construction or equipment purchase contracts.[15] At least one city has been authorized to contract with a property owner to delay the annexation of the owner's property into the city.[16] And the basic general obligation bond pledge, which is authorized by specific statute, permits a local government to contract to levy taxes for many years into the future.[17] Indeed, when we turn to revenue bonds, the General Assembly has sought to limit its own ability to pass laws that weaken the capacity of a local government to pay debt service on such bonds.[18]

Except for the taxing-power pledge of general obligation bonds, however, none of these statutes has been tested in the North Carolina courts. But comparable statutes have been tested in other states, and they have been upheld. Illinois law, for example, permits cities to enter into "preannexation agreements" with property owners.[19] Under such an agreement, the property owner agrees to petition for annexation to the city. In return, the city agrees to zone the newly annexed property in specific ways. These agreements have been upheld and enforced by the Illinois courts.[20] California law permits a county to enter into ten-year contracts with the owners of agricultural land.[21] In return for the owner's commitment to keep the property in agricultural use, the county agrees to tax it at a lower rate. These contracts have been upheld, and a number of courts have upheld other arrangements under which tax exemptions or classifications have been granted by local government

contract.[22] Finally, the New Jersey Supreme Court has upheld a contract under which a city agreed to adopt specific regulatory and zoning ordinances, because the contract was specifically authorized by state law.[23]

Thus, legislative practice in North Carolina and judicial precedent from other states support the ability of the General Assembly to permit local government contracts that bind the governing board's discretion.

Remedies if a Contract Is Invalid

What would be the consequences if a city entered into a contract that was later held to be invalid under the doctrine discussed in this article? If the other party to the contract had made expenditures in reliance on the contract, would the city have to refund the money, or pay for the value of the goods or services rendered?

The most extensive judicial discussion of this question is found in a North Carolina Court of Appeals case, *Rockingham Square Shopping Center, Inc. v. Town of Madison*.[24] The shopping center developers alleged that a contract had existed between the town and themselves, under which they would grade and pave an existing town street, in return for which the town would open and construct a new street. The new street would provide access to the shopping center, and the developers alleged that the purpose of the entire contract was to entice development of the center. The developers did grade and pave their street, but the town never opened the second street. The center eventually failed, and the developers sued the town for damages.

The court held that it was beyond the power of the town to contract to open a street, and therefore the contract was invalid. The developers then argued that it would be unjust to allow the town to reap the benefits of the contract—the graded and paved street—without paying the developers at least for their cost in providing those benefits. The court refused, holding that to do so would permit the developers to benefit indirectly from a contract that was against public policy. Thus, under this decision, any person entering into a contract with a local government that seeks improperly to bind the discretion of that government does so entirely at his or her own risk.

The *Rockingham Square* decision has been cited with approval in other states, and it seems to represent the law of many states on this question. It is not clear, however, that it represents the law in North Carolina. Just three years after *Rockingham Square* was decided, another contract dispute came before the state's appellate courts. The City of Washington had leased waterfront property to Frank Lewis on the condition that he construct public boat slips on the property. For him to make that use of the property, however, it was necessary for the city to rezone the property, and ultimately the city council refused to do so. Lewis sued, seeking either specific performance (that is, a mandated rezoning) or damages (that is, return of his rental payments). The trial court, properly, held the contract to be invalid to the extent that it required the city to rezone property, but that court was ready to allow damages. On appeal, however, the court of appeals refused damages as well, citing *Rockingham Square*.[25]

The case then went to the supreme court. In a very short opinion, that court affirmed the court of appeals decision, but with one modification.[26] Lewis was permitted to make his claim for damages. Because the modification was not accompanied by any explanation, it is not clear why the court made it. But one obvious guess is that the court disagreed with the rule of *Rockingham Square*. That is, the supreme court believes that it would be unjust to allow the local government to retain the benefits of an invalid contract, unless it paid the other party to the contract the value of the goods or services supplied to the government. If that is the correct reading of the supreme court's decision in *Lewis*, then entering into contracts that improperly bind the government's discretion is not a risk-free endeavor for the government.

Our Two Examples

How does the doctrine examined in this article apply to the two examples with which the article opened? Clearly, the first example proposes a contract that would violate the doctrine. In effect, the town is being asked to guarantee to levy a tax at some future point, in order to raise the money necessary to match the private contributions for the senior center. If the town wants to be able to make that guarantee, it will need to seek legislative authority to do so. Just as clearly, the second contract, for the background music, does not violate the doctrine. The subject of the contract is trivial—unpleasant as the music may be—and does not affect the county's discretion in any important matter. If the county wants the music to stop, it will have to pay damages to the company providing it. ❖

Notes

1. 211 N.C. 518 (1938). *Plant Food* is described as the "principal case" in Mariano & Assoc., P. C. v. Board of County Comm'rs, 737 P.2d 323 (Wy. 1987), and is treated as such in C. Antieau, Municipal Corporation Law, §10.18 (1989), one of the leading treatises on local government law.

2. Pegram v. Commissioners of Cleveland County, 65 N.C. 111 (1871); 4 E. McQuillin, Municipal Corporations § 13.40 (3d ed. 1968).

3. *Plant Food*, 214 N.C. at 520 (emphasis added).

4. *Plant Food*, 214 N.C. at 520.

5. Britt v. City of Wilmington, 236 N.C. 446 (1952); Lewis v. City of Washington, 63 N.C. App. 552 (1983).

6. Rockingham Square Shopping Center, Inc. v. Town of Madison, 45 N.C. App. 249 (1980); Johnson v. Board of Comm'rs, 192 N.C. 561 (1926); Bessemer Improvement Co. v. City of Greensboro, 247 N.C. 549 (1958).

7. Thrash v. City of Asheville, 95 N.C. App. 457 (1989).

8. Tilghman v. West of New Bern Volunteer Fire Dep't, 32 N.C. App. 767 (1977).

9. T.V. Transmission, Inc. v. City of Lincoln, 371 N.W.2d 19 (Neb. 1985).

10. Morrison Homes Corp. v. City of Pleasanton, 130 Cal. Rptr. 196 (Cal. Ct. App. 1976).

11. International Bank of Commerce v. Union Nat'l Bank, 653 S.W.2d 539 (Tex. Ct. App. 1983).

12. Harrison Cent. School Dist. v. Nyquist, 400 N.Y.S.2d 218 (N.Y. App. Div. 1977); City of Leeds v. Town of Moody, 319 So. 2d 242 (Ala. 1975); City of Louisville v. Fiscal Court of Jefferson County, 623 S.W.2d 219 (Ky. 1981).

13. N.C. Gen. Stat. § 115C-271.

14. N.C. Gen. Stat. § 157-42.

15. N.C. Gen. Stat. § 115C-441(c1).

16. 1987 N.C. Sess. Laws ch. 201.

17. N.C. Gen. Stat. § 159-46.

18. N.C. Gen. Stat. § 159-93.

19. Ill. Ann. Stat. ch. 24, para. 11-15.1-1 through -5 (Smith-Hurd 1989).

20. Union Nat'l Bank v. Village of Glenwood, 348 N.E.2d 226 (Ill. App. Ct. 1976).

21. Cal. Gov't Code §§ 51240 through 51255 (West 1983).

22. County of Marin v. Assessment Appeals Bd., 134 Cal. Rptr. 349 (Cal. Dist. Ct. App. 1976); "Tax Exemptions and the Contract Clause," I.L.R. 173 (1918):15-249.

23. Terminal Enter., Inc. v. Jersey City, 258 A.2d 361 (N.J. 1969).

24. 45 N.C. App. 249 (1980).

25. Lewis v. City of Washington, 63 N.C. App. 552 (1983).

26. 309 N.C. 818 (1983).

Municipal and County Administration Course Honors Jake Wicker with Scholarship Fund

Members of the 1990 class of the municipal and county administration courses have honored Jake Wicker, who has coordinated the courses for the past thirty-four years, by establishing the Warren J. Wicker Scholarship Fund. Proceeds from the fund will be used to grant a financial aid scholarship to an undergraduate student at The University of North Carolina at Chapel Hill. Greg Jarvies, captain in the Chapel Hill Police Department and the winner of the 1990 George C. Franklin Memorial Award as the outstanding member of the 1990 municipal class, announced the award as part of graduation activities and presented a check for $2,600 to establish the fund. That amount was raised through contributions by members of the municipal and county courses.

The annual courses in municipal administration and county administration are the principal courses offered by the Institute of Government for advanced training of government officials in fundamentals of municipal and county administration. Some 2,100 city, county, state, federal, and regional officials have completed the courses. The 115 members of the 1990 class represented fifty-seven cities, twenty-two counties, two state agencies, and the North Carolina League of Municipalities.

Members of the class hope to increase the amount in the scholarship fund to $10,000, the amount needed to permanently endow the scholarship. They encourage friends of Jake and those who have benefitted from his assistance and advice over the many years of his service at the Institute of Government to contribute to the fund. All contributions are tax deductible. Contributions should be sent to Doug Crutchfield, Office of Scholarship and Student Aid, The University of North Carolina at Chapel Hill, P.O. Box 1080, Chapel Hill, North Carolina, 27514. Checks should be accompanied by a note designating the donation for the Warren J. Wicker Scholarship Fund.

—Barbara G. Johnson, member of the class of 1990, representing the City of Winston-Salem

Zero-Base Budgeting in Mecklenburg County

Gary R. Rassel

Zero-base budgeting (ZBB) has been called the manager's budget because it provides a framework for tying planning and program management to the budget process. It allows budget makers to justify resources for all existing activities as well as for new ones, to analyze the likely effects of different levels of expenditure and performance on the achievement of objectives, and to involve managers at all levels in the budget process.[1] It is credited with providing a large amount of information useful for management and budgeting decisions.[2] It also provides a mechanism for the manager to review all government activities.

A typical ZBB process involves

1) identifying organizational decision or budget units;
2) assessing essential or basic needs;
3) developing decision packages that describe alternative levels of service, giving the
   a) goals and objectives of each activity,
   b) needs for the activity,
   c) measures of performance and work load,
   d) alternative courses of action and levels of activity, and
   e) costs and benefits of alternative service levels;
4) ranking the decision packages; and
5) deciding on the allocation of resources.[3]

When ZBB first received attention in the 1970s as a budgeting technique for governments, it often was presented as a tool for reducing budgets and for cutting government spending. Many governments adopted it for this reason. The rationale was that ZBB would prevent budgeting from focusing only on program increases by requiring that choices be made among alternative service levels developed for each program. Each level would provide a different amount or quality of service and would use different amounts of resources. The alternatives would include decreases in service and funding as well as increases.

In theory, with ZBB the need for each program is justified every budget period and programs compete for resources from a base of zero. That is, decision makers consider what would happen if a program were not funded at all. In practice, however, ZBB systems seldom use zero as the base for ongoing programs; instead, managers choose some level such as 70 percent of the current budget as the base. Budgeting usually proceeds each year with managers requesting small increases to fund existing programs and occasionally adding new ones. The purpose of new or greatly expanded programs and their associated budget requests usually are examined thoroughly, but the purposes of existing programs and relatively small budget increases for them typically are given little consideration. Decreases in funding are usually applied across the board. ZBB was designed to shift the budgeting process away from this incremental approach to consider the priorities of all programs.

ZBB has been used by national, state, city, and county governments. Many that adopted ZBB, however, subsequently discontinued using it. Mecklenburg County has used it successfully since 1982 and is well known for doing so. What accounts for this success when many other jurisdictions have tried and dropped ZBB? Does ZBB

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provide advantages such that other governments in North Carolina might want to consider it?

Mecklenburg County's ZBB System

The county commissioners decided in the late 1970s to use ZBB because they thought that it would provide more information for budget decisions, a system for evaluating the priorities of various services and their overall costs, and improved management of county agencies. A manager experienced in using ZBB was recruited to develop and implement the process.

In Mecklenburg County department activities are organized into budget units and are supervised by unit managers responsible for planning and budgeting. These managers prepare the decision packages as budget requests for the services provided. Pre–budget planning begins in November, with each department submitting a three-year operational needs assessment to the Budget and Resource Management Department. This assessment is a strategic plan outlining needed resources to accommodate ordinary growth in departmental activities and new programs. It sets the framework within which the county will operate for the upcoming fiscal year.

The assessments are summarized and forwarded to the commissioners for their consideration at an annual budget priority-setting retreat held in early January. There the commissioners establish policy goals and priorities and develop a strategic plan to accomplish these.

The official budgeting cycle starts in January with workshop training sessions for all department heads and budget unit managers. Budget manuals and associated materials are distributed at this time. During the first stage of the ZBB process, each budget unit manager must

1) prepare a statement of purpose for the unit;
2) describe the unit's current method of operations;
3) develop and describe alternative methods by which the budget unit can achieve its goals and objectives;
4) describe important links between the unit's operations and those of other budget units;
5) prepare alternative service levels, describing the type and amount of services that would be provided at several levels of service and the resources necessary to fund each level;
6) develop program measures to demonstrate what will be provided at each level; and
7) develop a detailed line-item budget for each level of services.

A unit preparing five service levels, for example, might set them at 70 percent, 85 percent, 100 percent, 105 to 110 percent, and more than 110 percent of the current level. To reduce funding to less than 70 percent of the current level essentially would discontinue the service, at least in its present form. Each service level description shows what will be provided, what it will cost, and the number of personnel required.

Each department ranks the decision packages from all of its budget units and prepares a departmental budget request. The department budgets are then reviewed during a process lasting from February until April. During this period, the county manager meets with each department head to review in detail the department's budget and operations. The department's decision packages facilitate this review and are the focus of the sessions. Analysis of the cost of producing a specific level of service, the rationale used for structuring the service levels, current year accomplishments, and plans for the upcoming fiscal year are discussed. Departments may revise their budgets following this review.

The budget analysts are important in this process. The Department of Budget and Resource Management has a staff of fourteen, eight of whom are budget analysts. Many were trained in accounting and industrial engineering procedures. All of the budget analysts receive additional training in industrial engineering analysis while at Mecklenburg County and are thoroughly trained in ZBB procedures.

When ZBB was introduced in the county, the analysts were trained in its procedures first, and then they in turn trained the departmental staff. Each department is assigned an analyst who works with the budget unit managers to develop their decision packages and with the department head in developing the departmental budget. At the manager's review the budget analyst helps discuss the department's budget. These analysts also work in a Resource Management Program during the year when not involved in the budget, conducting productivity and management studies of agencies. The budget analysts help determine staffing levels and other resource needs for departments and help develop program measures.

Twenty-nine departments submit budget requests to the county manager, along with several nondepartment budget items, such as a market salary survey and employee health programs. These requests include those of 105 budget units, whose managers prepare descriptions for approximately 600 service levels.[1] After the manager

reviews departmental budgets, all service levels are ranked in order of funding priority. In this process service levels are listed in order of decreasing benefit to the county so that top management can recommend where tax dollars should be spent.

The Budget and Resource Management Department initially ranks all of the separate service levels without knowing how much revenue will be available and prepares a computerized, countywide ranking table displaying cumulative funding totals.[5] The county manager, the budget and resource management administrator, and the assistant county managers then use this ranking to produce a final ranking of all service levels for the county. The county manager decides on a cutoff level for funding based on information about revenues and the desire to continue, reduce, or expand current services and add new ones. Current service levels tend to be above the cutoff line and are funded. If level three of a budget unit's service levels is funded, levels one and two usually are ranked above that and also are funded. Level one is the most basic level. The other levels are proposals to increase, from the base level, the amount of service provided. If a current service level is below the funding cutoff, it usually means that the service provided by that budget unit, and hence the funding, is being reduced. The manager recommends a rank for all service levels and submits this to the board of county commissioners as part of the proposed budget.

The manager's proposed budget is presented in three volumes. The first includes basic financial information about the county, service priorities, and capital improvement projects. It also contains the countywide ranking table with summary information for each service level showing the cumulative cost as service levels are included for funding. The second volume contains descriptions for each budget unit: their purpose and operation, objectives, methods of operation, relationships to other units, sources of revenue, and number of positions. The third volume contains the detail for all of the decision packages.[6] Recently, commissioners became concerned that a convenient summary of each program and department, its history, and its future direction was needed. This information will be added in future budget documentation. (The approved budget includes information about each budget unit: a statement of purpose; a comparison of appropriations, revenues, and program measures for the budget year with those of the previous two years; and a brief summary of all funded service levels.)

A formal public hearing is held in May to allow citizens to comment on the proposed budget. Budget workshops are held with the board of commissioners in late May and early June and are followed by formal review and adoption. The board votes on each service level; it can change the manager's ranking of the service levels and the amount recommended for any level. However, to fund more levels than recommended by the manager, which would expand services in some way, the board must increase the revenues available.

During the workshops and the public hearing, the commissioners ask for additional explanation and justification for the budget requests. But attention is directed more toward the amount of services provided for the money and less toward detailed line items in a request, although line-item information is available if the commissioners want to see it. Much of the ZBB process is computerized, so changing and updating service-level information and the total proposed budget, including service-level rankings, can be done quickly.

Strengths of ZBB

ZBB in Mecklenburg County has met the commissioner's original goal of providing better information. For this reason, it also has aided the county manager in overseeing the government of a large, rapidly growing county. Many employees think that ZBB provides a complete, overall picture of the operations, activities, and programs of each department. ZBB is a good educational device for new employees, and the budget documents are a good way to inform the public about county operations. The system provides a great deal of information useful for management and planning as well as for budgeting. To the budget staff, ZBB offers a concrete, objective method of analyzing budgets and aids the county manager in tying budgeting to planning. It also provides considerable information for commissioners.

ZBB allows commissioners to evaluate a total service package or program; they see the funding that goes for providing a certain amount of service rather than just for particular items. However, line-item detail is readily available for analysis. The commissioners can see what services are likely to be diminished if they must reduce the size of the total budget. They also can see which services to add or expand if additional revenue is available.

ZBB decentralizes the budgeting process. It has in-

volved more managers from all levels and has increased the participation of line managers in preparation and execution of the budget. ZBB is also an open system, which suits the current manager's style. The information about purposes, goals, and objectives of each budget unit is available in the public budget documents. The budget unit managers have an opportunity to present their budget requests based on what they see as their needs and objectives. The unit managers know that the manager and the commissioners will see what was proposed even if it was not recommended for funding. The commissioners also know that they will see what was proposed but not recommended for funding.

If budgets must be reduced, ZBB is a good method for helping decision makers identify services to reduce and determine the impact of cuts.[7] However, its real strength lies in the information and the system of management that it provides. ZBB provides a system for review of operations. It aids the manager in structuring information about what the government does and what the budget pays for and in communicating this to the county commissioners, government employees, the news media, and the public.

Weaknesses of ZBB

The ZBB process is labor-intensive. For it to work well, it requires a large budget staff, and it requires those who use it to be well-trained in its procedures. In Mecklenburg County it required budget analysts to work with unit managers in developing the decision packages until these managers became familiar with the process. In developing the plan for implementing ZBB, county staff members concluded that the number of budget analysts would have to be doubled for the system to work properly.

ZBB also is time-consuming, especially in a government as large as Mecklenburg's, where the budget process is lengthy. Mecklenburg's budget cycle has been lengthened since the adoption of ZBB and, in part, because of it. Collecting the information necessary for ZBB and providing for input and review takes time.

ZBB produces a lot of documentation. In Mecklenburg the initial paperwork requirements for ZBB were substantial. Much of the process is now on computer, however, and the county is continuing to automate other parts of it.

A ZBB budget requires developing quantitative measures of performance ("program measures") for each budget unit. Ideally the descriptions of each service level would include different amounts of measurable accomplishments, and as resources increased, more accomplishments would be projected. The program measures developed should reflect this. However, appropriate program measures can be difficult to develop for some county activities (for instance, planning, cultural, human service, and educational activities) because their accomplishments are often difficult to measure numerically.

The Mecklenburg County budget documents are set up such that an overview of departmental goals and objectives is not developed. The ZBB process focuses on the separate budget units and hence gives inadequate attention to pulling this information together for a departmental statement. The commissioners have identified this as a shortcoming, and in the future the process will be changed to overcome it.

To utilize fully the advantages of a ZBB system, elected officials must be willing to evaluate decision packages rather than line items and to leave a great deal of analysis to the manager. Commissioners in many counties may not be able or willing to do this. If commissioners wish to get involved in the detail of expenditures, the system is not likely to work or it will lose much of its benefit.

Why It Has Worked

Mecklenburg County is fortunate to have the resources to invest in the system. The county commissioners who were on the board when ZBB was selected were committed to making it work. They were successful in finding someone with expertise in ZBB, who was well versed in its procedures, and whose management style reinforced its strengths.

County officials planned carefully for implementing ZBB. They studied the likely impact on departments, assessed the need for additional budget staff to make it work, and committed to hiring those staff. It was introduced in careful stages, with ten departments using it on a test basis for a year to help identify and work out problems. The budget staff and unit managers were thoroughly trained and brought into the process early. This commitment to training and assistance was important and has continued. In a 1987 survey of county management staff, a large percentage of respondents commented on the importance of the help of the budget analysts and the support of the commissioners.[8] Studies

of ZBB in other places have shown that thorough training of staff and commitment by top management and elected officials were important for the success of ZBB.

Research also has shown that for budget innovations to work, employees and officials must feel that the new system offers advantages over the old. The commissioners who decided that the county should use ZBB were very dissatisfied with other budgeting systems the county had used. Commissioners and county staff alike have commented on how much better the budget process is with ZBB than it had been previously. This is in part due to the structure of ZBB, the consistent application of procedures, and the style of the current county manager.

Can Other Governments Use ZBB?

Seventy-four percent of those responding to the 1987 survey of managers and budget staff would recommend it, in some form, to other local governments. But would it be a better system for all? It seems that a strong budget staff is necessary to implement and manage ZBB. The number of people needed depends on the size of the jurisdiction and on the amount of detailed information desired. To use ZBB, a county would need to support a high level of budget analysis or operate ZBB in a different fashion than Mecklenburg. Many small governments lack separate staff for budget analysis or have only small staffs. Such governments may also have line-item budgets not requiring the program and productivity measures used by ZBB (although these measures often are developed in jurisdictions using line-item and program budgets).

For smaller governments, ZBB could be modified to suit different conditions and could be scaled back from the system used in Mecklenburg County. It could be done every second or third year. It could be required only for new or expanded programs and could be used only for certain departments. The number of service levels could be limited, for example, to three for each budget unit.

The identification of budget units to organize activities for budgeting, management, and planning is useful, as is the development of program measures. Tying dollar amounts to planned levels of services provides decision makers with information about activities, what each service costs to provide, and what the county should be getting for its money. Much of this can be provided without using the full ZBB process. ❖

Notes

1. John Mikesell. *Fiscal Administration: Analysis and Applications for the Public Sector* (Chicago, Ill.: Dorsey Press, 1986).

2. Allen Schick and Harry Hatry, "Zero-Base Budgeting: the Manager's Budget." *Public Budgeting and Finance* 2 (Spring 1982): 72–88.

3. Sarah Reed, "The Impact of Budgetary Roles upon Perspectives," *Public Budgeting and Finance* 5 (Spring 1985): 83–96.

4. The number of service levels ranked each year varies. It has ranged from as few as 350 to more than 600.

5. Included in the ranking table information are the number of positions for each level, the cumulative total of positions as service levels are included for funding, and the cumulative funding from sources other than the county.

6. Mecklenburg County Manager's Office, "Mecklenburg County Proposed Budget for 1988–89" (1988).

7. A. John Vogt, "Budget Preparation and Enactment," in *County Government in North Carolina*, ed. A. Fleming Bell II (Chapel Hill, N.C.: Institute of Government, 1989), 133–80.

8. Gary Rassel, County Staff and Commissioners' Assessment of Zero-Base Budgeting (Paper presented at the 1987 annual conference of the Western Governmental Research Association, Anaheim, Calif.).

Correction

The two people in the photograph that appeared on page 40 of the Spring 1990 edition of *Popular Government* were identified incorrectly. The caption should have read: "Norma Bodsford (left) reviews the agenda for the upcoming meeting with Commissioner Dot Kearns."

UPCOMING IN Popular Government

Principals' Executive Program

Pricing solid waste collection

Public records and computers

Orange County tax study

Redistricting after the census


UNC Photo Lab

Watts Scholarship Established

Ben F. Loeb, Jr.

The North Carolina Wildlife Officers' Association (NCWOA) has established a scholarship to honor the life and memory of L. Poindexter Watts, Jr., an Institute of Government faculty member from 1957 to 1989. The Watts Scholarship is one of three awarded each year by the NCWOA to children of wildlife officers and to others who plan to pursue careers related to wildlife management and conservation.

The first Watts Scholarship has been awarded to Jennifer Thorson, the daughter of Mr. and Mrs. Brad Thorson of Statesville, North Carolina. Thorson was an honor student at Statesville Senior High School, where she was a Student Council officer and a member of the tennis and softball teams. She has been included in *Who's Who among High School Students* and is now a student at Appalachian State University in Boone, North Carolina. Thorson plans to pursue a career in wildlife management or in parks and recreation.

Dexter Watts, a professor of public law and government and assistant director of the Institute of Government, died in Chapel Hill on January 1, 1989, following a lengthy illness. He was a graduate of Wofford College in Spartanburg, South Carolina, and received his law degree with honors from The University of North Carolina at Chapel Hill School of Law in 1957. While in law school, he was an associate editor of the *North Carolina Law Review* and a member of the Order of the Coif (an honorary law school society for academic achievement).

The author is an Institute of Government faculty member who specializes in criminal law.

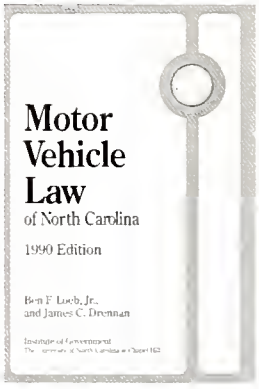
During his Institute career, Watts's principal field of interest was criminal law and procedure, which involved research, consultation, and instruction. He taught a broad range of students, including wildlife officers, district attorneys, and judges. In the early 1960s he assisted in drafting North Carolina's original implied consent (Breathalyzer) law and was a member of the executive board of the Committee on Alcohol and Drugs of the National Safety Council. Watts coauthored a book for wildlife officers and wrote several law review articles, including one dealing with the administration of tests for intoxication. He also served for more than two decades as coordinator of training for North Carolina district attorneys and as their legal advisor.

During his final decade with the Institute, it was wildlife laws and those who enforce them that received his closest attention. He spent endless hours over and above assigned classroom time, working with the new wildlife officers to ensure that they acquired adequate knowledge of laws and regulations to perform their duties. And for present as well as former wildlife students, he was always available to answer legal inquiries and to research complicated legal issues. Watts spent much of his time rewriting and updating the laws dealing with the conservation of marine and wildlife resources, and his appearance before legislative committees dealing with these subjects often drew very favorable news media and editorial comment. Appropriately, the last teaching assignment of his career was during the 1988 Wildlife Basic School held at the Institute of Government. ❖

Off the Press

Motor Vehicle Law of North Carolina
1990 Edition

Ben F. Loeb, Jr., and James C. Drennan



Motor Vehicle Law of North Carolina provides important information for attorneys, law enforcement personnel, and other interested citizens. The 1990 edition contains a discussion and analysis of the more common North Carolina motor vehicle offenses and includes the criminal penalties, driver's license penalties, and insurance points for each offense. Chapters on DWI, driver's license law, and the North Carolina insurance point system are included. [90.06] ISBN 1-56011-103-8, $8.50.

1989 Cumulative Supplement to North Carolina Crimes:
A Guidebook on the Elements of Crime

Robert L. Farb and Benjamin B. Sendor

North Carolina Crimes: A Guidebook on the Elements of Crime, published in 1985, is an important criminal law reference book for lawyers and law enforcement officers. It outlines the elements of several hundred criminal offenses, with each outline explaining the offense, reprinting relevant statutes, and citing relevant case law. It covers criminal states of mind, bars and defenses, participants in crime, and attempts and conspiracy.

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