



NC 2018 Legislative Session Budget and Fiscal Policy Highlights

Fiscal Brief

July 18, 2018

Executive Summary

North Carolina's modified \$23.9 billion FY 2018-19 budget represents a 3.9% increase above the FY 2017-18 budget and provides salary increases for State employees, with particular emphasis on pay raises for prison staff and members of the State Highway Patrol. The modified budget also includes funding for prison and school safety initiatives; a one-time 1% supplement for retirees; and additional funds for the Savings Reserve. This brief highlights the General Assembly's major budgetary and fiscal actions during the 2018 session including S.L. 2018-5, the main appropriations act, and subsequent legislation¹.

Introduction:

During the 2018 short session, the General Assembly modified the second year of the FY 2017-19 biennial budget using an expedited process. Instead of the traditional budget process, both the Senate and House appointed members to a conference committee for Senate Bill 99, and formally began work on the budget in late April 2018. Session convened on the 16th of May and on June 1st, 2018, the General Assembly ratified the bill, modifying the original FY 2018-19 budget. Governor Cooper vetoed Senate Bill 99 on June 5th; the General Assembly subsequently overrode his veto on June 12th, 2018. The bill became Session Law 2018-5, the Appropriations Act of 2018.

The modified FY 2018-19 budget represents a 3.9% increase over the FY 2017-18 budget and a 1.1% increase over the budget originally enacted for FY 2018-19 during the 2017 Session. (See Table 1). The adjustments to each appropriations area are as follows:

Area Committee & Reserves	FY 2017-18	FY 2018-19	% Change
Education	13,062,520,091	13,759,414,134	5.3%
Health & Human Services	5,253,299,542	5,353,212,884	1.9%
Justice & Public Safety	2,701,955,002	2,797,039,761	3.5%
Natural & Economic Resources	587,753,659	602,768,253	2.6%
General Government & Information Technology	461,149,274	496,654,706	7.7%
Statewide Reserves and Capital	963,800,325	910,510,334	-5.5%
TOTAL	\$23,030,477,893	\$23,919,600,072	3.9%

¹ S.L. 2018-76, Health-Local Confinement/Vet. Controlled Sub. (Senate Bill 750) and S.L. 2018-97, Budget Technical Corrections & Study, (Senate Bill 335).

Revenue, Other Availability and Adjustments:

The Fiscal Research Division and the Office of State Budget and Management estimate projected General Fund revenue through a consensus revenue forecasting process. In May, the forecast was revised to \$23.5 billion for FY 2017-18. The May revision increased revenue estimates for the current fiscal year by \$356.7 million.

FY 2017-18

The current-year increase was due to an additional \$282.4 million in projected tax revenue and \$74.3 million in projected non-tax revenue. The tax revenue increase projected for FY 2017-18 was driven primarily by increases in Individual Income tax, Franchise tax, and Insurance gross premium tax. The increase in Individual Income was the result of an increase in final tax payments, which were driven up by some taxpayers shifting income between tax years due to federal tax changes. The Franchise tax significantly outperformed expectations and was up \$81.2 million (13.4%) over projections and the Insurance gross premiums tax was projected to surpass the original estimate by \$56.6 million (11.7%). Sales tax projections were revised downward by \$117.2 million (down 1.6%) due to weaker than projected collections.

Non-Tax revenue projections for FY 2017-18 increased due to an increase in investment income on cash holdings (up \$30.3 million) plus a higher tobacco Master Settlement Agreement payment (up \$23.5 million).

A tax case settlement on the State's former Inheritance tax added an additional \$10.7 million to the projection. Other non-tax revenue sources were expected to be close to the original forecast.

FY 2018-19

Building on the adjustments noted above for FY 2017-18, the revised forecast for FY 2018-19 projects a \$276.5 million (1.7%) increase over last year's forecast, bringing net General Fund revenue to \$23.9 billion. Individual Income tax is expected to increase by \$153.8 million, primarily due to growth in non-withholding income such as business and investment income. Non-Tax collections are projected to increase by \$83.8 million.

Unreserved Fund Balance

The State's FY 2017-18 Unreserved Fund Balance is projected to be an estimated \$1.1 billion prior to legislative adjustments. This is a 17% increase from the year-end FY 2016-17 balance. The \$1.1 billion is derived from:

- \$491 million from the FY 2016-17 Unappropriated Balance Remaining,
- \$275 million in projected Reversions, and
- \$356.7 million in projected Over-Collections for FY 2017-18.

After adjustments of \$155.2 million for capital projects and an earmark of \$64.8 million for repairs and renovations, the remaining Unreserved Fund Balance available for appropriation is \$902.7 million.

Adjustments to General Fund Revenue and Other Availability:

Prior to adjustments to availability, the State's General Fund Availability² was projected to be \$24.8 billion. The Appropriations Act of 2018 included the following adjustments, which reduced availability by \$300 million:

- \$59 million of the revenue reduction is due to the following State tax law changes. These changes were made in response to Internal Revenue Code (IRC) tax provisions enacted in the federal Bipartisan Budget Act of 2018 and the federal Tax Cuts and Jobs Act:
 - Updates the State's conformity to the IRC from January 1, 2017, to February 9, 2018, thereby adopting various federal tax changes, including temporarily reducing the threshold for deducting medical expenses from 10% to 7.5% of income for the 2017 and 2018 taxable years;
 - Decouples from the federal extension of: (i) income exclusion for forgiveness of debt on primary residence; (ii) mortgage insurance deductible as mortgage interest; and (iii) deduction for tuition and expenses;
 - Decouples from the deferral of gain and the exclusion of gain for assets invested in an Opportunity Fund; and
 - Decouples from the inclusion, and deduction, associated with foreign-derived intangible income and global intangible low-taxed income.
- \$221.5 million is transferred to the Savings Reserve, of which \$59.8 million is earmarked for transfer to the State Emergency Response/Disaster Relief Reserve. After these transfers, the total held in the "Rainy Day Fund" will be \$2 billion, the largest balance in the Savings Reserve since its inception³ in 1991.
- \$135 million is transferred to the Medicaid Transformation Fund established in 2015 to facilitate the State's transition from a traditional fee-for-service model to capitated managed care as directed in S.L. 2015-245, Medicaid Transformation and Reorganization (H.B. 372). The \$135 million transferred to the Fund represents the last installment of funds to be transferred and brings the Fund's total to \$435 million, of which \$60 million is appropriated for FY 2018-19.

² General Fund Availability refers to general purpose revenue (i.e., taxes, fees and other miscellaneous revenue) and the unreserved fund balance but does not include agency receipts.

³ S.L. 1991-689, Section 346.

The following table reflects FY 2018-19 Total Availability (including transfers out to other funds) by source.

FY 2018-19 Availability (dollars in millions)		
Source	Amount	% of Total
Unreserved Fund Balance	902.7	3.6%
Taxes:		
Personal Income	12,704.7	51.2%
Sales & Use	7,624.9	30.7%
Corporate Income	709.6	2.9%
Franchise	684.1	2.8%
Insurance	542.6	2.2%
Alcoholic Beverage	373.7	1.5%
Tobacco	258.2	1.0%
Miscellaneous	120.1	0.5%
Non-tax Revenue:		
Judicial Fees	232.7	0.9%
Medicaid Disproportionate Share	163.3	0.7%
Tobacco Master Settlement Agreement	139.4	0.6%
Investment Income	99.4	0.4%
Other Nontax Revenue	277.4	1.1%
Total Availability	\$ 24,832.8	100%
Transfers Out:		
Savings Reserve	221.6	
Medicaid Transformation Fund	135.0	
Total Availability	\$ 24,476.2	

Of the remaining \$24.5 billion in State funds (net of agency receipts), the General Assembly appropriated \$23.9 billion, leaving an unappropriated balance of net General Fund Availability of \$556.6 million⁴.

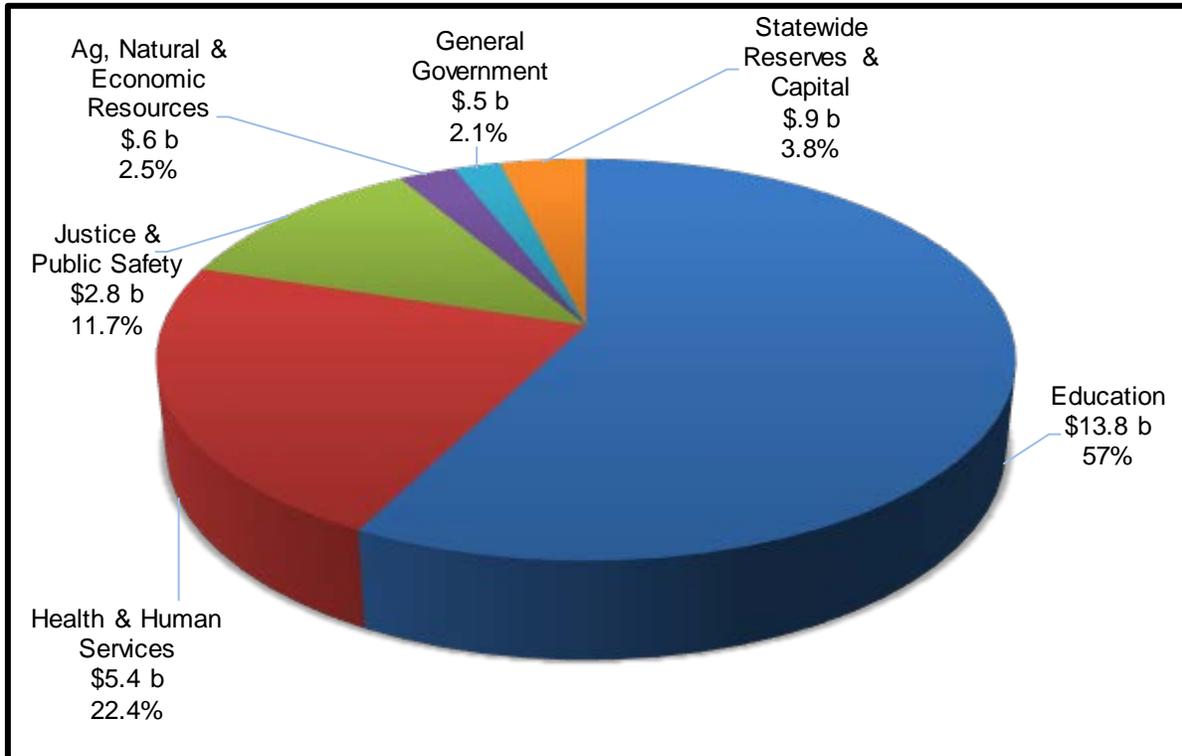
Appropriations by Area and Major Budget Items:

Appropriations by Area Committee

The Senate and House of Representatives Appropriations Committees are subdivided into committees by subject area. The chart that follows illustrates the distribution of funds by area committee, with education comprising the majority of the funds.

⁴ S.L. 2018-5, Appropriations Act of 2018 reflects a remaining balance of \$557.8 million. S.L. 2018-64, Pretax Supplemental Benefits, enacted after S.L. 2018-5, reduced revenue by \$1.2 million, resulting in a subsequent reduction in the Unappropriated Balance of \$1.2 million.

FY 2018-19 General Fund Budget \$23.9 billion⁵



Salaries and Benefits

The budget provides salary increases and benefit enhancements totaling over \$208 million including:

- A 2% salary increase for State employees, excluding University of North Carolina (UNC) employees,
- \$20 million to provide salary increases to UNC employees based on the priorities and discretion of the UNC Board of Governors,
- A minimum salary of \$31,200 for full-time, permanent State employees,
- \$24.1 million to provide salary increases to local community college employees based on the priorities of the State Board of Community Colleges,
- A 2% salary increase for noncertified personnel of local school districts,
- A 6.9% increase in the principal salary schedule, and,
- A \$70 per month increase to the base teacher salary schedule salary for educators with 25 or more years of experience.

The \$31,200 minimum annual salary (or prorated amount) for permanent State employees does not apply to temporary State employees or to State-funded local employees (i.e., local community college, local school district).

⁵ Net General Fund appropriations does not include the appropriation of agency receipts.

Additionally, the modified budget implements most of the S.L. 2017-57 (or Appropriations Act of 2017) intended teacher salary schedule, with greater monthly salary amounts for teachers and instructional support personnel with 25 or more years of experience. The additional \$11.8 million provided in the Appropriations Act brings the total funding provided for teacher and instructional support personnel salary increases under the teacher salary schedule to \$282.7 million in FY 2018-19. The average salary increase for teachers and instructional support personnel who were employed in FY 2017-18 and continue employment in FY 2018-19 is approximately 6.5%. The modified budget also increases average principal pay by providing an additional \$12 million to increase all levels of the principal salary schedule by 6.9%.

Additional benefit enhancements include:

- Full funding of the actuarially-determined employer contribution of the State retirement systems,
- Five bonus leave days for State employees and Community College personnel,
- A one-time 1% retirement supplement for State retirees and beneficiaries,
- An expansion of the line-of-duty death benefit to increase the benefit from \$50,000 to \$100,000 and to include noncustodial employees of the Department of Public Safety killed by an individual in the custody of the Division of Adult Correction and Juvenile Justice.

Emphasis on Specific State Personnel

During the 2018 session, budget writers focused resources on pay raises for certain State public safety personnel.

Correctional Personnel

Starting in 2015, the General Assembly began addressing the longstanding problem of hiring and retaining prison-based correctional staff. The first round of pay increases were enacted in the FY 2015-17 Biennial Budget, which appropriated \$12.8 million for FY 2015-16 and \$25.6 million for FY 2016-17 and implemented a differentiated pay plan based on a prison facility's custody level. The General Assembly appropriated an additional \$16.9 million in 2016 and another \$18.4 during the 2017 regular session.

The Appropriations Act of 2018 again addresses correctional staff pay by appropriating an additional \$27 million to:

- Provide a 4% increase to all correctional personnel based in State adult correctional facilities, including medical, program, maintenance, and administrative staff,
- Establish higher minimum salary levels for:
 - Correctional Officer I (minimum custody) - \$33,120,
 - Correctional Officer II (medium custody) - \$34,220,
 - Correctional Officer III (close custody) - \$36,598, and
- Institute pay differentials ranging from 10-20% of base salary for Correctional Officers assigned to a lower custody-level facility but required to work at a higher-custody-level facility.

Highway Patrol

To address hiring and retention challenges in the State's Highway Patrol, the General Assembly appropriated \$7.2 million to implement a new pay plan for troopers. The new pay plan increases trooper starting pay to \$44,000 and provides 6.5% annual salary increases until a trooper reaches top pay (\$64,202) after 6 years. The former plan included: Trooper starting salary under \$40,000 with 5% annual salary increases; additional 5% salary increases after 3 and 6 years of experience; and top pay (\$62,875) in approximately 8 years.

Additionally, the budget establishes the Trooper Training Reimbursement Program in an attempt to increase employee retention. The program allows the State to seek reimbursement of training costs from former employees in certain situations if an early career trooper leaves the Highway Patrol.

Prison Safety

As noted earlier, the budget includes several salary and benefits enhancements for the State's correctional facility staff. In addition those measures, the budget provides \$15 million to deploy additional prison safety and security measures. The funds will be used to purchase man-down technology for custody and other correctional staff, and to install additional internal and perimeter cameras. Both of these measures are in response to recommendations made by the National Institute of Corrections as part of their Security Operational Assessment conducted in the aftermath of the correctional staff killings at Pasquotank Correctional Institution.

School Safety

The Appropriations Act of 2018 establishes the School Safety Grants Program and provides an additional \$28 million to enhance public school safety. Under the supervision of the Superintendent of Public Instruction, the additional funding will:

- Expand the number of school resource officers in public middle and elementary schools by increasing the State's School Resource Office grant program from \$7 million to \$12 million;
- Serve students in crisis by providing \$2 million in grants for private or nonprofit organizations that partner with local education agencies (LEAs);
- Help train students to develop healthy responses to trauma and stress by providing \$3 million in grants for community partners;
- Enhance school safety by providing \$3 million in grant funds to LEAs, regional schools, innovative schools, and lab schools to purchase safety equipment, such as interlocking door systems and cameras;
- Increase mental health services in public schools by providing \$10 million for grants to LEAs to employ additional school mental health personnel; and
- Provide access to the State's anonymous safety tip line by providing \$5 million for full implementation of the application to all public secondary schools.

The budget also requires all public schools to inform students and employees about the State's anonymous tip line, but allows schools to use another application instead of the tip line as long as the alternative meets State standards.

Disaster Recovery

The Appropriations Act of 2018 includes an additional \$60 million for disaster recovery, bringing the total in State recovery funds to approximately \$360 million appropriated since the original Disaster Recovery Act of 2016.

The budget also expands the authorized purposes for use of the funds to include risk management efforts such as river gauges and landslide mapping and supporting the Division of Emergency Management's State Search and Rescue program, but restricts the use of funds on housing except for hazard mitigation and related efforts.

Lastly, the budget restores a tax deduction for disaster recovery assistance⁶ repealed in 2013 and adds liability protections for volunteer land surveyors who provide professional services following disasters.

Medicaid Transformation

The budget includes the first appropriation of funds held in the \$360 million Medicaid Transformation Reserve. Of the \$360 million, \$60 million in non-recurring funds is appropriated to the Medicaid Transformation Fund for the Department of Health and Human Services to support its efforts to begin implementing managed care. The State funds will also draw down federal funds, for a combined total of \$192 million for information technology, staffing and contracts for the following activities:

- Systems and functions related to beneficiary enrollment,
- Provider credentialing,
- Data management,
- Program integrity,
- Financial analysis and monitoring,
- Technical and operational integration and managed care operations, and
- Prepaid health plan oversight.

More detailed summaries of selected fiscal and budgetary changes can be found at the following link: www.ncleg.net/fiscalresearch/fiscal_briefs/fiscal_briefs.html:

- [Education](#)
- [Health and Human Services](#)
- [Agriculture, Natural and Economic Resources](#)
- [Justice and Public Safety](#)
- [General Government](#)
- [Information Technology](#)
- [Transportation](#)
- [Salaries and Benefits](#)
- [Capital](#)
- [Finance](#)

⁶ S.L. 2013-316, Tax Simplification and Reduction Act.



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