



NC 2015 Legislative Session Budget and Fiscal Policy Highlights

Fiscal Brief

October 30, 2015

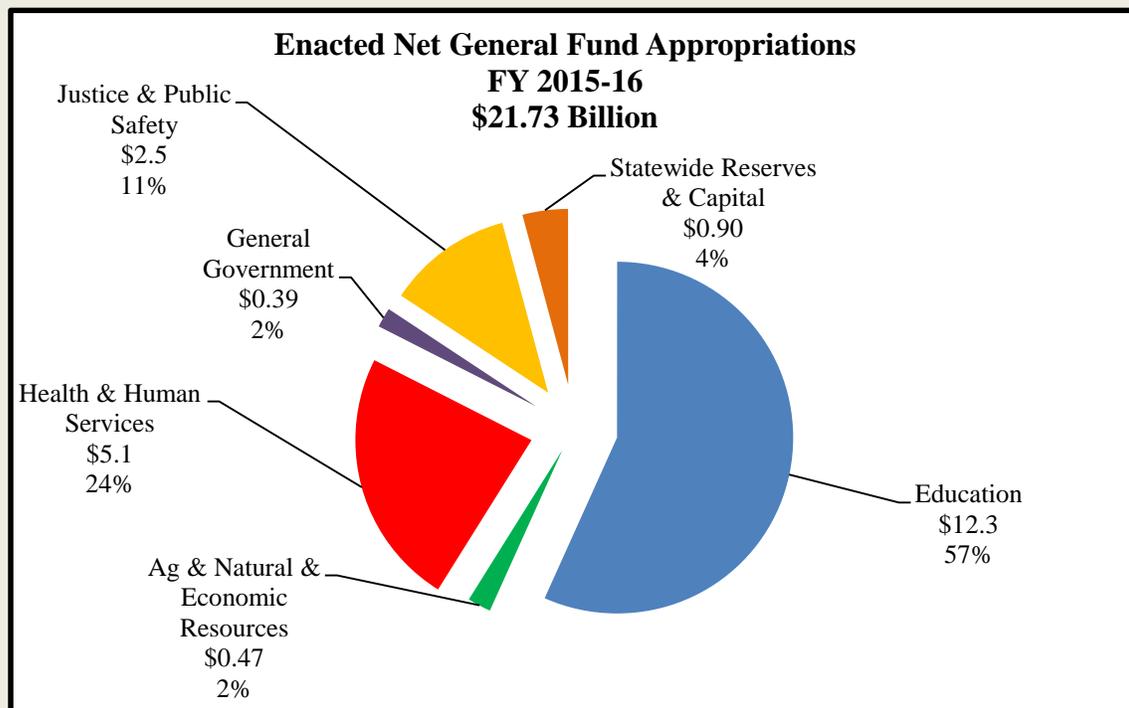
Executive Summary

On September 18th the General Assembly enacted H.B. 97, 2015 Appropriations Act, S.L. 2015-241, appropriating \$21.73 billion and \$21.92 billion for the FY 2015-16 and FY 2016-17 budgets, respectively. In addition to traditional increases to cover growth in Medicaid, public schools and universities, the budget:

- Modifies State tax law to reduce personal and corporate income tax rates, raise the standard deduction, restore medical deductions and expand the sales tax base;
- Raises beginning teacher starting pay to \$35,000 annually, provides other teacher pay increases and a \$750 bonus pay for most other State employees, and addresses select compensation needs;
- Increases funds in the Saving Reserve Account to \$1.1 billion;
- Establishes a Medicaid Transformation Reserve of \$225 million over the biennium to transition the Medicaid program from traditional fee-for-service to a capitated, managed care program; and
- Creates two new cabinet-level departments and consolidates and reorganizes other programs.

This brief summarizes the General Assembly's budget actions as well as other budgetary and fiscal policy actions such as budget transparency and general obligation bonds.

The following chart reflects the distribution of spending by subcommittee/area as enacted in S.L. 2015-241.





Because the General Assembly traditionally adjusts the second year of its biennial budget, this brief focuses primarily on the major fiscal and budgetary legislative actions affecting the FY 2015-16 Budget.

For more detail or additional summaries of the Finance Committee, Appropriations Subcommittee, and other areas of the budget, go to the Fiscal Briefs 2015 Legislative Session section of the North Carolina General Assembly, Fiscal Research Division [website](#).

General Fund Availability

Revenue

The February consensus revenue forecast projected FY 2014-15 collections to be below the budgeted amount by 1.3% and for modest growth to occur during the next biennium. This cautious approach was consistent with the persistent weaknesses in wage growth and the ongoing instability of the global economy.

However, April tax collections produced a positive “April surprise”, delivering significantly better than expected collections for FY 2014-15 and bringing General Fund over-collections to \$445 million. The May revised consensus forecast assumes solid employment gains, improving the prospects for continued income growth over the biennium and moderate, steady overall economic growth. The State’s revenue is projected to grow by 3.7% and 4.2% annually over the biennium resulting in a final projection of \$22.2 billion for FY 2015-16 and \$22.8 billion for FY 2016-17 in recurring revenue.

Adjustments to Availability and Revenue¹

Total General Fund Availability for FY 2015-16 is \$21.7 billion. Significant adjustments to availability include:

- Unreserved Fund Balance² – The State’s unreserved fund balance at the close of FY 2014-15 fiscal year and prior to further adjustments was \$864.6 million. The legislature reduced that amount by \$450 million with the authorization to increase funds reserved to the Savings Reserve Account and by an additional \$150 million appropriation to the Repair and Renovations Account, leaving \$264.6 million available for appropriation.
- Corporate Tax Rate Trigger – S.L. 2015-241 repeals the 2017 sunset on the corporate income tax rate reduction. The tax rate will drop from 4% to 3% when tax revenues reach \$20.975 billion for a fiscal year. The cumulative decrease to the State General Fund from reducing the corporate income tax rate from 5% to 4% is estimated at \$458.2 million over the biennium, \$605 million when fully implemented.
- Tax Law Changes – Various tax law changes reduce revenue by \$81.8 million and \$379.6 million in each year of the biennium, respectively. Key adjustments include:
 - Creation of a new single sales factor apportionment (the method by which multistate corporations are taxed) - effective over three years beginning in 2016.
 - Adjustments to personal income tax – restoring unlimited medical deductions retroactive to January 1, 2015; increasing personal exemptions; and reducing the tax rate from 5.75% to 5.499% in 2017, which reduces revenue by \$117.3 million in FY 2015-16 and by \$445.1 million in FY 2016-17; and;
 - Adjustments to State sales tax – expanding the sales tax base, effective 2016, increasing General Fund revenue by \$159.5 million in FY 2016-17.

¹ A complete General Fund Availability Statement may be found at the end of this brief and in Section 2.2 of S.L. 2015-241.

² The available cash balance effective June 30 after excluding documented encumbrances, unearned revenue, statutory requirements, and other legal obligations.



- Highway Fund Transfer – The General Assembly ended the \$215.9 million transfer from the Highway Fund to the General Fund.
- Medicaid Transformation Fund – The budget establishes a new fund and directes the transfer of \$75 million and \$150 million respectively over the biennium to facilitate the State’s transition from a traditional fee-for-service model to capitated managed care for most of the Medicaid program as directed in S.L. 2015-245, Medicaid Transformation and Reorganization (H.B. 372).
- Other Adjustments – The 2015 Appropriations Act transfers \$10 million of Master Settlement Agreement (tobacco) funds to the Golden LEAF Foundation and adds \$25 million to Availability to reflect a change in accounting for judicial fees previously budgeted in a special fund.

Savings Reserve

The State Budget Act³ directs that 25% of the unreserved fund balance remaining in the General Fund at the end of each fiscal year be reserved to the Savings Reserve Account. For FY 2014-15 that amount was \$216 million. However, the General Assembly directed the State Controller to reserve \$450 million effective June 30, 2015. The total in the Savings Reserve is now \$1.1 billion, 65% of the statutory goal of 8% of the previous fiscal year’s operating budget.

In addition to increasing the Savings Reserve Account, the General Assembly directed that all savings resulting from refinancing of State indebtedness be reserved to the Savings Reserve Account (Section 6.23), effective July 1, 2017. The legislature also directed the Legislative Research Commission to study methods for increasing the amounts reserved to the Savings Reserve Account (Section 6.21).

General Fund Appropriations and Key Areas of Funding

S.L. 2015-241, Appropriations Act of 2015 (H.B. 97), as amended by S.L. 2015-268, General Government Technical Corrections (H.B. 259) and S.L. 2015-264, GSC Technical Corrections 2015 (S.B. 119), appropriates \$21.73 billion for FY 2015-16, 3.1% more than the enacted FY 2014-15 budget. When compared to the base budget for FY 2015-16, the newly enacted budget represents a 4.3% increase. The following table compares appropriations by committee or area.

Comparison: Base and Enacted Budgets
(\$ billions)

Committee/Area	Enacted FY 2014-15	Base FY 2015-16	Enacted FY 2015-16	FY 2015-16 Enacted vs. FY 2014-15 Enacted % Change	FY 2015-16 Enacted vs. FY 2015-16 Base % Change
Education	11.78	11.80	12.33	4.7%	4.5%
Health & Human	5.15	5.02	5.13	-0.3%	2.2%
Justice & Public Safety	2.37	2.39	2.50	5.8%	4.8%
Natural & Economic Resources ¹	0.41	0.43	0.47	14.4%	8.6%
General Government ¹	0.43	0.35	0.39	-8.4%	11.3%
Statewide Reserves and Capital	0.96	0.85	0.91	-4.9%	-12.1%
TOTAL	\$ 21.08	\$ 20.85	\$ 21.73	3.1%	4.3%

Note: ¹Includes adjustments to reflect agency/program transfers.

³ G.S. 143C-4-2



Key areas of funding include:

State Employee and Local Education Employee Salaries

S.L. 2015-241 appropriates \$313 million for salary increases and bonuses for teachers, local education personnel and other select State employee groups. Beginning teacher pay is raised to \$35,000 and funds are provided for other local education personnel pay plans enacted during the 2015 session. An additional \$202 million is for a one-time \$750 bonus to active State employees, teachers, and other local education personnel. The Community College System received additional funds to address salary needs across the 58 campuses, at the local boards' discretion.

Education

The public schools budget grows by 5.1%, the largest funding increase among the State's three education agencies. Significant increases include funds to adjust teacher pay and \$100 million to fund the increase in enrollment.

The University of North Carolina system budget increases by 4.5%, reflecting an additional \$49 million to fully fund projected enrollment growth and another \$27 million provided to fund the one-time bonus for State employees.

The budget also increases the Community College budget by 2.7% to \$1.1 billion for FY 2015-16 due primarily to salary increases and additional funds for instructional equipment and technology.

Justice and Public Safety

The budget increases funding for the Justice and Public Safety agencies by 5.8%, the largest increase of all committee areas. This increase reflects the legislature's focus on correctional staff salaries and funding needs within the judicial branch. An additional \$12.8 million and \$25.6 million in FY 2015-16 and FY 2016-17 respectively is appropriated to the Department of Public Safety to begin addressing salary issues associated with the long-standing problem in recruiting and retaining correctional staff.

The budget also appropriates an additional \$9 million (a 2.7% increase) for the judicial budget to address various court operating needs including information technology, interpreters and expert witnesses.

Health and Human Services

Despite an increase in Medicaid of almost \$300 million, the FY 2015-16 budget for the Department of Health and Human Services (DHHS) appears relatively flat as compared to FY 2014-15. The increased appropriation for DHHS is offset by \$205 million in nonrecurring federal receipts for Medicaid and NC Health Choice and a nonrecurring reduction in funding to regional Local Management Entities/Managed Care Organizations (LME/MCO).

The budget provides an additional \$5 million to facilitate the Medicaid reform initiative mandated in S.L. 2015-245, Medicaid Transformation and Reorganization (H.B. 372). And while not part of the DHHS budget, S.L. 2015-241 establishes a Medicaid Transformation Fund of \$225 million over the biennium, and maintains the \$186 million earmark of unappropriated funds in the Medicaid Contingency Reserve established during the 2014 session.



Transportation

In addition to enacting S.L. 2015-2, Internal Revenue Update/Motor Fuels Tax Changes (S.B. 20) and eliminating the \$215.9 million Highway Fund transfer to the General Fund, the legislature made numerous adjustments to transportation revenues including:

- Revising the motor fuels tax rate formulas,
- Increasing Division of Motor Vehicles fees by an average of 30%, raising an estimated \$185.1 million (annualized);
- Shifting \$150.1 million of motor fuels tax proceeds over the biennium to the Strategic Transportation Investments program.

These funds and other adjustments made available via S.L. 2015-2 provide an additional \$552.1 million in FY 2015-16 to address transportation needs across the State including \$146.8 million to target structurally deficient bridges and \$70 million for modernizing the Wilmington and Morehead City seaports.

Other Budget and Fiscal Policy Highlights

Government Reorganizations

The legislature enacted major changes for certain departments and programs:

- Natural and Cultural Resources – Roughly one-half of the budget (\$88.3 million) for the former Department of Environment and Natural Resources (DENR) is transferred to the Department of Cultural Resources, consolidating the State’s natural and cultural resources programs and services within a newly constituted Department of Natural and Cultural Resources. Programs and services remaining in DENR are now housed in the newly-named Department of Environmental Quality.
- Military and Veteran’s Affairs – Various veteran and military programs and supports are consolidated into a newly created cabinet-level Department of Military and Veterans Affairs.
- Information Technology (IT) – A new Department of Information Technology is established to begin the process of consolidating State IT functions. The new cabinet level agency is responsible for planning, security and other overall IT management functions.

Agency Budget Transparency

Over the last several years there have been legislative and executive initiatives to address budget transparency. During the spring of 2015, the Office of State Budget and Management (OSBM) issued a directive to State agencies laying out the foundation for budget transparency by realigning agency budgets to reflect staffing and spending patterns and history more accurately.

In support of that initiative, the budget directs OSBM to eliminate all positions vacant for more than 12 months (as of April 17, 2015) and to realign State agency budgets with the corresponding savings in accordance with parameters outlined in the budget.



General Obligation Bonds - Connect NC Bond Act of 2015

S.L. 2015-280, Connect NC Bond Act of 2015 (H.B. 943) authorizes the issuance of \$2 billion in general obligation bonds for economic development and infrastructure projects, upon the approval of a majority of the voters. Most of the bonds would be issued for the State's universities. Community colleges, parks, the National Guard, and other programs would also receive funding if voters approve. The bond issue will be included on the NC Presidential Primary election ballot in March 2016.

For additional information, please contact:

Joint Budget Development Team

Karen Hammonds-Blanks Karen.Hammonds-Blanks@ncleg.net
Kristin Walker Kristin.Walker@ncleg.net
Richard Bostic Richard.Bostic@ncleg.net
Evan Rodewald Evan.Rodewald@ncleg.net

*Fiscal Research Division
NC General Assembly
300 N. Salisbury St., Room 619
Raleigh, North Carolina 27603-5925
(919) 733-4910
<http://www.ncleg.net/fiscalresearch>*



General Fund Availability Statement

	FY 2015-16	FY 2016-17
Unappropriated Balance	2,033,330	182,588,544
Over Collections FY 2014-15	445,820,623	0
Reversions FY 2014-15	415,657,138	0
Proceeds from Sale of Dix Received in FY 2014-15	2,000,000	0
Revenue Adjustment as per S.L. 2015-2	(1,000,000)	0
Earmarkings of Year End Fund Balance:		
Savings Reserve	(200,000,000)	0
Repairs and Renovations	(400,000,000)	0
Beginning Unreserved Fund Balance	264,511,091	182,588,544
Revenues Based on Existing Tax Structure	20,981,400,000	21,592,400,000
Non-tax Revenues		
Investment Income	17,100,000	17,400,000
Judicial Fees	227,800,000	225,500,000
Disproportionate Share	139,000,000	139,000,000
Insurance	78,400,000	79,600,000
Master Settlement Agreement	137,500,000	137,500,000
Other Non-Tax Revenues	168,000,000	168,800,000
Highway Fund Transfer	215,900,000	215,900,000
Non-tax Revenues	983,700,000	983,700,000
Total General Fund Availability	22,229,611,091	22,758,688,544
Adjustments to Availability: 2015 Session		
Historic Preservation Tax Credit	0	(8,000,000)
Modify Corporate Income Tax Rate Trigger, Expand Corporate Tax Base, and Repeal Bank Privilege Tax	6,000,000	0
Phase-In Single Sales Factor Apportionment	(7,900,000)	(23,300,000)
Reduce Individual Income Tax (Reduces Rate to 5.499% in 2017, Restores Medical Deduction, and Raises Standard Deduction)	(117,300,000)	(437,100,000)
Expand Sales Tax Base	44,500,000	159,500,000
Transfer Additional Local Sales Tax Revenue for Economic Development, Public Education, and Community Colleges	0	(17,600,000)
Renewable Energy Safe Harbor (S.L. 2015-11)	0	(36,700,000)
Repeal Highway Fund Transfer	(215,900,000)	(215,900,000)
Transfer to Medicaid Transformation Fund	(75,000,000)	(150,000,000)
Standard & Poor's Settlement Funds	19,382,143	0
Master Settlement Agreement Funds to Golden L.E.A.F.	(10,000,000)	(10,000,000)
Department of Justice Tobacco Settlement	2,194,000	0
Transfer from Federal Insurance Contributions Act (FICA) Fund	4,296,802	641,628
Transfer from E-Commerce Fund Cash Balance	3,000,000	0
Transfer from DPS Enterprise Resource Planning System IT Fund	9,000,000	0
Adjustment of Transfer from Treasurer's Office	62,998	18,471
Adjustment of Transfer from Insurance Regulatory Fund	355,915	58,882
Realign Judicial Fees	25,000,000	25,000,000
Subtotal Adjustments to Availability: 2015 Session	(312,308,142)	(713,381,019)
Revised General Fund Availability	21,917,302,949	22,045,307,525
Less General Fund Appropriations	(21,734,714,405)	(21,919,468,078)
Unappropriated Balance Remaining	182,588,544	125,839,447