

Can the Red Headed Orphan Survive on Leftovers?

The Budget Crunch and Capital Spending

by Vance Sanders and Jack Betts

A funny thing happened one day in July as the 134th General Assembly lurched toward adjournment. At a time when legislative leaders were moaning and groaning about paltry revenues and were preparing to put off some major spending requests until a budget session in the fall, taxpayers found out they were going to shell out more than \$4 million to build horse show arenas in Asheville (\$1.6 million) and Raleigh (\$2.5 million).

A few lawmakers, like Sen. Marshall Rauch (D-Gaston), thought the legislative horseplay excessive and in need of reining in. "That's a rich man's sport," Rauch told the Senate. "We have poor people who are not getting a raise next year. As a business proposition I just can't see spending that kind of money on horse shows."

But a majority of the legislators could see spending that kind of money on horses, for two reasons. First, politics has always been a major determinant of where capital funds are spent and 1981 was no exception: Two powerful legislators, House Speaker Liston Ramsey (D-Madison) and House Expansion Budget Committee Chairman Billy Watkins (D-Granville), took a liking to getting these horse projects out of the gates. Beyond politics, though, the horse-barn appropriation resulted from a trend in capital spending so complex and so ominous that building even a new horse barn might have actually been a fiscally prudent act by the General Assembly.

If that sounds strange, listen to Rep. Al Adams (D-Wake), chairman of the House Appropriations Committee and a legislator generally oriented more towards social services than pork-barrel

spending. "We would have funded six horse barns if we'd had proposals for them," says Adams. "I think the Advisory Budget Commission recommended only \$12 million for capital construction this year, and we doubled that. We took every [capital expenditure] we could find."*

Some might argue that spending \$4 million for another type of capital project, like a wilderness camp for emotionally disturbed adolescents or a new wing to a state office building, would help the state more than building two horse barns. But politics determined that choice. Rep. Adams is addressing a different point.

Some types of capital projects, such as horse barns, don't swell with inflation as rapidly as do those involving direct services, explains Adams. "If we put that \$4 million in an operational program," says Adams, "we have to fund it every year. If you put it into capital improvements, it's a one-time expenditure."

But some types of capital expenditures — such as a state office building — cause a ripple effect which does indeed lead to operational expenses. "Once you have a new building, new programs just seem to fill it up," observes one fiscal analyst. Sorting out the role of capital expenditures in the state budget process — whether truly one-time expenses or expenses that lead to more programs — involves first a bit of fiscal history.

The 1981 legislature appropriated a smaller percentage of the total state budget for capital improvements than any other General Assembly in

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* Adams was referring to the legislature's \$24.3 million June appropriation for capital spending out of the general fund. This amount increased to \$30.0 million with the addition of various special provisions for capital projects in the appropriation bill passed in the October session. When road construction and other highway fund appropriations are included, the figure goes to \$328 million.

the last two decades. For the N.C. fiscal year 1982, the state will spend some \$328 million for all capital projects (this figure includes about \$297 million for road maintenance and construction), 5.6 percent of the state budget. If over \$320 million sounds substantial, consider the slice of history presented on pages 22-23, which shows the sources of capital funds and the amounts appropriated for capital projects from 1965 to 1982. In the 1967-68 biennial budget period, the state's capital appropriations totalled \$303 million, 11.1 percent of the budget. And remember, that was 14 years of inflation ago when money could buy a lot more bricks and mortar than it can today. In 1973-74, the year federal revenue sharing became available to the state, capital appropriations peaked at \$501 million, over 17 percent of the state budget.

Since 1974, however, the legislature has committed a declining percentage of funds to capital items. This represents a dangerous trend for North Carolina, say the people in charge of insuring that the state has adequate institutions, like mental hospitals, university buildings, and research facilities as well as sound public properties, like parks and roads. As capital spending declines, the existing physical plant of the state deteriorates. The amount of new capital projects decreases as does the attention to planning for long-term maintenance of the capital plant already in place.

In 1980, state agencies compiled a "wish list" of capital projects. The two-year price tag for what were termed immediate needs topped \$100 million. And fiscal officials within the 16-campus University of North Carolina (UNC) system say that present building plans would require \$650 million to complete. Without adequate capital spending, says UNC Vice-President for Finance Felix Joyner, the results would be devastating: "There's no telling what this figure will be in ten years, with inflation and all. We must meet these needs."

But some argue that the state doesn't need as much new capital building as these figures indicate, that "wants aren't equivalent to needs," as one fiscal analyst puts it. The state should not, for example, be spending \$650 million to expand the UNC system at a time when college enrollment appears to be on the decline, the critics contend. Moreover, when UNC officials and others insert such large figures into the budget process, they intensify the competition among programs for the sharply-declining pot of capital funds and transfer the focus of attention away from the need for long-term maintenance. Consequently, officials at the state level must concentrate more on the political exigencies of a particular budget year than on a long-range maintenance plan. And main-

tenance needs often lose out to flashy new capital projects with strong political backing (see box on page 19).

The difference between what an agency *wants* and *needs* is determined within the state budget process, perhaps the most political process in all of state government and an area extremely sensitive to changing financial trends. Capital budget items face the fiscally conservative Advisory Budget Commission (ABC), the powerful 12-member body that whittles budget requests down into an overall package for the legislature. And in recent years, the sources depended upon for capital spending, such as general revenue sharing and some types of bonds, have been drying up.

In the equation that includes a conservative ABC and a declining source of capital funds, add a growing sentiment against more government spending and the 1981 reductions in federal funding for a wide range of programs. What you get is greater pressure on state and local governments to spend money for running the government — for supporting existing services — rather than for new capital facilities. This equation has begun to operate at a time when much of the state's physical plant is getting old, particularly the roads. Meanwhile, North Carolina is expanding in population — it's now the tenth largest state — and will consequently have increasing demands placed upon its capital facilities.

In 1973 and 1974, the lawmakers had a surplus that totaled close to one-fourth of the total annual budget. While they spent much of it — particularly the newly available federal revenue sharing funds (look at the top line in the chart on pages 22-23, under years 1973-78) — for capital projects, they also put large sums into new state programs. Once these programs became part of the general operations of state government, their fiscal needs were closely tied to inflation rates and to energy costs, both of which began rising sharply in the mid-1970s.

From 1974 to 1982, the state budget more than doubled, from \$2.9 to \$5.9 billion. Maintaining the programs put into place during the "fat" years of 1973-74, perhaps more than any other factor, propelled this rise. And as the cost of running state government zoomed, general revenue sharing — a source of funds that legislators had become accustomed to using for capital projects — ended (see chart, under 1980). Meanwhile, legislators had begun to use funds once reserved for capital projects as a kind of "safety cushion" to meet general operating expenses. As a result of all these political and fiscal trends, legislators have recently made capital expenditures one of their lowest priorities, like a red-headed orphan waiting for the leftovers at the end of the session.

"When things are hard economically, capital improvements are the first to suffer," explains Robert Powell, state budget analyst in the Office of Management and Budget. "If you don't realize your revenues [for operating costs], you can cancel these capital projects at any time." State revenues have increased in recent years, but the operating budget has also grown enormously. And traditional sources of funds for the capital budget "cushion" — which has allowed the state to close the gap between operating revenues and expenses — are drying up.

"We are receiving \$70 million more per year in personal income tax revenue as a result of inflation — what's known as bracket creep," says David Crotts, senior fiscal analyst for the General Assembly. "But we're losing at least \$180 million per year — \$60 million once available in revenue sharing, \$60 million from lost bond-financing potential, and another \$60 million from a five-year highway bond issue that's been depleted." Meanwhile, the overall state budget keeps getting larger and larger.

Examining each of the traditional sources of capital funds provides a way to project what kind of future trends to expect with capital spending.

Revenue Sharing. Often described as former President Richard Nixon's favorite program (he began it in 1972), general revenue sharing pumped billions of dollars into state and local governments for eight years — including \$500 million to North Carolina's state government. Nearly half of that — \$232 million — went straight into capital spending. Alas, Congress cut out revenue sharing to state governments in 1980, and there went \$60 million per year in one fell swoop.

Highway Fund. This account, separate from the general operating fund, has financed much of the state's highways and bridges and paid for other transportation improvements. Since 1973, the amount spent on roads from this fund has hovered at around \$260 million per year, even as the state budget has more than doubled and the cost of building roads has risen with inflation.* The amount jumped to \$297 million for fiscal year 1982 when the legislature approved a three-cent per gallon tax increase and a package of license and fee increases to replenish the fund. But the increase in revenues will barely keep up with necessary road maintenance. Even this three-cent boost — a 25 percent increase in the highway fund base, passed at considerable political carnage —

* The figure swelled to \$281 million in FY 1979 and dropped to \$225 million in FY 1981.

Lag-Time: The Hidden Escalator For Capital Projects

Does delaying capital spending have any real effect? You bet it does, even on relatively small projects like roof repairs. In fact, just clearing the paperwork through the normal process for capital improvement costs the taxpayers millions of dollars.

Take, for example, a simple roof-repair job in which delays cost taxpayers a 66 percent increase in the tab. In August 1976, the Eastern North Carolina School for the Deaf in Wilson formally requested \$300,000 from the state to put up a new roof. When the 1977 General Assembly got to town in January, the project had been approved by the Department of Human Resources, the Office of State Budget, and the Advisory Budget Commission." But the legislature denied the funding request.

The Department of Human Resources didn't give up, however. It kept the project on its list of priorities and asked for it again in the 1979 General Assembly. This time, it got approval — but inflation drove the price tag up to \$501,000.

A few weeks after the legislature approved the request on July 1, 1979, an architect was employed. Eight months later, in March 1980, the construction contract was awarded. The reroofing was finally completed on June 2, 1981 — nearly five years after it was first proposed.

Inflation, running at over 10 percent in the construction business during this period, raised the cost of the contract substantially. And because this capital improvement was not funded earlier, part of the capital funds finally voted for reroofing had to be diverted to repair water damage, including \$10,000 to replace acoustical ceiling tiles.

"Legislators may not be convinced of the need for a capital request the first time they see it, particularly if it is a repair item which has little glamour," says DHR Budget Officer Jim Woodall. "If the ABC members did not visit that institution on their biennial tour, it aggravates the problem."

DHR has had to request some items for as many as eight years before they were funded. As a television car maintenance ad puts it: "You can pay me now or you can pay me later." □

isn't going to be enough for very long. The legislature may be faced with proposals for more tax increases for this fund within a year or two. "The loss of \$30 million to the highway fund as a result of President Reagan's budget cuts will definitely hurt," says Jim Newlin, a senior fiscal analyst at the General Assembly. "The three-cent gas tax increase will not be adequate to meet needs." Indeed, Gov. Hunt recently announced that few, if any, new miles of road will be built in 1982. In the inflationary economy, the highway fund revenues cannot even meet all the road maintenance needs.

Bond Issues. In the last 20 years, nearly \$1

billion worth of bond issues have helped finance almost two of every five dollars spent on capital improvements in North Carolina. In the summer of 1981, several state officials expressed doubt that North Carolina could continue to rely so extensively on bond issues for capital funds. Deputy State Treasurer J.D. Foust pointed to the high level of interest rates: "People don't want to invest in long-term bonds when inflation far outstrips their bond earnings." Fiscal Analyst Crotts worried that the state could rely too much on bonds: "North Carolina's bond rating is currently a high triple-A — the best in the bond market. We don't want to endanger that rating." And State Sen.

Financing With Bonds — Delaying Costs ...Increasing Debts

by Jim Newlin

As one means of financing capital projects, North Carolina issues bonds, a long-term debt instrument which the state pays back with interest over the bond's life. The rationale for bond financing is that it passes on some of the cost of the project to future users. The state issues two major types of bonds, "revenue" bonds and "general obligation" bonds.

Revenue bonds, used for such projects as parking decks or university dormitories, generate income which is used to repay the bonds. Revenue bonds pledge only the revenue generated from the project, not the full faith and credit of the state. Tax funds cannot be used to repay revenue bonds because they have not been approved by the voters.

Certain state agencies or commissions have the authority to issue revenue bonds, usually subject to the approval of the state treasurer and the Local Government Commission and to a feasibility study by a nationally reputable firm that shows that projected revenues will be sufficient to retire the bonds. State institutions or authorities owe some \$602 million in revenue bonds.

The University of North Carolina system, the Housing Finance Agency, and the Medical Care Commission owe most of the debt.

General Obligation bonds are the type of bond to which Sanders and Betts refer in the accompanying article and the type discussed in the rest of this box. These bonds pledge the full faith and credit of the state that they will be repaid. The General Assembly must first approve such a bond issuance. If the amount is greater than two-thirds of the state's indebtedness paid off during the preceding biennium, the voters must then approve the bond issue as well.

Major bond issues requiring voter approval usually have a schedule of issuance, allowing the bond sales to be spread over a period of time, such as five years. This time period is intended to approximate the need for cash for the specific purpose, so the state does not have to pay interest on funds that cannot be spent for several years.

After legislative and, if necessary, voter approval of a bond issue, the state treasurer begins work with bond counsel and underwriters to prepare a prospectus to offer to potential investors. Once the prospectus is offered, bonds are then sold on the market at interest rates which vary with economic conditions and the rating given the bonds. North Carolina general obligation bonds carry the highest rating [Aaa/AAA] offered by rating services, which holds down interest rates charged to the state.

Bonds from any particular issue have varying dates of maturity so that both principal and interest are repaid over the entire issuance period. As soon as the bonds are sold, the state begins interest payments; principal payments usually

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Kenneth Royall (D-Durham), chairman of the Senate Ways and Means Committee, gauged the political mood at that time: "With the interest rates and the debt service we'd have to pay, it just makes [new bond issues] out of the question."

Despite these doubts, the legislature in the October session passed a \$300 million clean water bond, which will have to be approved by the voters before the state can issue the bonds. When federal funds for water and sewer improvements were reduced sharply in the summer of 1981 as a part of President Reagan's budget cutting campaign, Gov. Hunt lobbied hard for the clean water bond in the October session.

Hunt's efforts and the legislature's desire to respond to the cuts in some way helped to pass the bond.

Several bond issues have recently expired (see footnotes 7 and 9 in chart on pages 22-23), leaving the state with a major gap in revenue sources for new capital projects. Generating new capital funds through a bond issue is a far easier step politically than a direct appropriation or new gas tax. But a continued reliance on bonds tends to increase the debt service for the state, a growing part of the annual state budget and an expense that is not as visible as a direct appropriation. Using long-term, interest bearing bonds, the state

begin after two or three years, depending on maturity dates of the bonds.

The Mounting Debt Service

The General Assembly appropriates funds for debt service, which include principal and interest, and the state treasurer is responsible for keeping a schedule of debt service due. In October 1981, General Fund bond indebtedness (principal) amounted to \$589.2 million. Another \$161 million has been authorized, but has not been issued by the state treasurer. Because the state is also paying off bonds each year, the peak indebtedness is only estimated at \$637.2 million in 1984, based on current authorizations. Current General Fund indebtedness dates back to the Public School Facilities Bonds authorized in 1963, which have \$15.2 million outstanding from a \$100 million authorization.

General Fund debt service (principal and interest) on current indebtedness (principal only), is \$61.9 million during the current 1981-82 fiscal year and goes up to \$69.5 million during 1982-83. The state treasurer estimates that issuance of currently authorized bonds will increase debt service to \$80 million in 1982-83, with a peak payment of \$85.8 million in 1984-85.

The General Assembly in October 1981 authorized the issuance of another \$300 million in Clean Water Bonds, subject to the approval of the voters. The state treasurer estimates that issuance of these bonds would increase debt service requirements to \$107.8 million in 1983-84 with a peak payment of \$122.6 million in 1986-87, assuming a 12 percent interest rate on all new bonds. If more bonds are authorized in future years, the peak payment could increase even more.

Highway Fund bonds are general obligation

bonds backed by the taxing power of the state. Since 1949, highway bonds have had an additional backup of a special one cent per gallon motor fuel tax dedicated to debt service; this has led to slightly lower interest rates on highway bonds. Total Highway Fund bond indebtedness (principal only) was \$216 million in June 1981, with an additional \$120 million authorized but unissued.

Legislators face certain tradeoffs when deciding whether or not to use bonds for financing capital projects. In 1977 Gov. Hunt, rather than requesting a gas tax increase, asked the legislature to approve a \$300 million highway bond issue. The bonds would provide \$60 million a year for five years for road construction at a time when inflation was high and Highway Fund revenues were not growing enough to keep up with rising costs. Preventive maintenance of roads was declining.

The choice faced by the legislature was to fund a \$300 million bond issue, at a cost of an estimated \$190 million in interest, or to levy a two cents per gallon gasoline tax for five years, which would have provided a slightly higher amount of funding, but at the political cost of voting for a tax increase. At Hunt's urging, the General Assembly passed the bond legislation, and it was subsequently approved by the voters. In 1981, as the revenue generated by the bond issue was running out, the General Assembly had to levy a three cents per gallon motor fuel tax increase, along with other fee increases, in order to keep road maintenance funded.

Not only did the legislators have to follow the 1977 bond bill with a 1981 tax increase, they also had to appropriate funds in 1981 to pay for the interest and principal of those 1977 bonds. And the debt service on the bonds authorized in 1977 will continue to cost the taxpayers for many years to come. □

defers paying for capital projects. In the long run, this process usually costs the state more than would appropriations from the general or highway fund. (See box on pages 20-21 for an explanation of bonds and their effect on the debt service.)

General Fund. This fund, the main purse of state government, has financed most of the capital improvements over the years. The money comes

from every imaginable tax, but it goes for every imaginable program that state government runs, especially now that legislators use funds once reserved for capital spending as a kind of safety cushion to meet operating expenses. By the time operating expenses are met, there's little left over in this fund for capital improvements — like \$30.0 million for 1981-82, less than one-half of one

Funding for Capital Improvements in North

Biennial Budgets					
A. State Appropriated Funds for Capital Improvements	1965-66	1967-68	1969-70	1971-72	1973-74
1. Federal Revenue Sharing	—	—	—	—	\$105,200,000
2. General Fund	\$ 41,639,578	\$ 112,356,788	\$ 75,588,603	\$ 64,891,192	86,622,446
3. Highway Fund (non-roads)	3,192,800	4,344,600	1,080,000	4,097,293	4,044,500
4. Wildlife Fund	341,254	901,127	140,000	805,986	243,486
5. Federal Funds	3,782,160	19,048,597	11,628,579	1,398,770	3,720,300
6. Self Liquidating	34,074,000	36,023,000	16,731,000	24,000,000	41,589,100
7. Other	—	—	—	—	733,875
8. Highway Fund — Road Construction ¹					
a. State construction and Maintenance	97,000,000	100,000,000	168,000,000	185,000,000	220,000,000
b. State Matching Funds Matched with Federal Aid	34,006,864	30,797,332	35,307,645	67,460,595	38,785,605
TOTAL APPROPRIATIONS FOR CAPITAL IMPROVEMENTS	214,036,656	303,471,444	308,475,827	347,653,836	500,939,312
Total Authorized State Budget ²	2,217,400,000	2,746,600,000	3,589,000,000	4,455,400,000	2,877,900,000
TOTAL APPROPRIATIONS FOR CAPITAL IMPROVEMENTS AS PERCENTAGE OF TOTAL AUTHORIZED STATE BUDGET	9.7%	11.0%	8.6%	7.8%	17.4%
B. Other Capital Improvements Funded by Federal Aid & Bond Issues					
1. Road Construction Funds ¹					
a. Federal Aid	—	60,823,831	74,772,211	110,661,742	96,904,376
b. Road Bonds	—	—	—	—	—
2. Statewide Bond Issues ³	60,000,000 ⁴	40,000,000 ⁴	—	45,995,000 ⁶	—
	17,970,000 ⁵	—	—	—	45,000,000 ⁷
	—	—	—	—	—
	—	—	—	—	—
	—	—	—	—	—
TOTAL BONDS SOLD	77,970,000	40,000,000	-0-	45,995,000	45,000,000
TOTAL BONDS SOLD AS PERCENTAGE OF TOTAL AUTHORIZED STATE BUDGET	3.5%	1.5%	0%	1.0%	1.6%

FOOTNOTES:

¹ Source: Fiscal Section, Dept. of Transportation.
² Summary of the Recommended State Budget, 1981-83, p. 75.
³ Source: Annual Report for FY Ending 6/30/80, Dept. of State Auditor. Amounts are for end of fiscal year. No figures appear for 1981-82 because fiscal year has not ended. Amounts are for bonds *issued*, not *authorized*.
⁴ Issued under \$100 million Public School Facilities Bond of 1963.
⁵ Issued under \$17.98 million Capital Improvements for State Institutions Bond of 1965.
⁶ Issued under \$45.99 million Capital Improvement Legislative Bond of 1971.
⁷ Issued under \$300 million Public School Facilities Bond of 1973.
⁸ Issued under \$2 million Zoo Bond of 1971.

percent of the state budget. (This fund does not pay for road construction.)

Those who argue that current levels of capital spending are far too low point to five possible solutions to the problem: tax increases, new sources of revenue, new bond issues, diverting

general funds, and setting a fixed percentage of the budget for capital funds.

Tax Increases. Political death, right? Maybe so, but be prepared. There are probably more in the offing. There are those who have suggested that an income-tax increase might be forthcoming, but few political observers think that would wash in the legislature — particularly with Congress trying

Carolina by Source of Funds, 1965-82

Annual Budgets

1974-75	1975-76	1976-77	1977-78	1978-79	1979-80	1980-81	1981-82
\$ 47,200,000	\$ 4,713,789	\$ 16,126,358	\$ 26,583,626	\$ 32,230,000	—	—	—
36,165,337	23,948,648	28,969,937	4,749,000	93,778,818	\$ 84,378,719	\$ 99,913,212	\$ 26,848,727
370,000	1,804,500	—	1,625,600	1,533,995	2,707,282	2,767,142	1,200,000
—	—	—	—	—	—	—	—
803,750	1,778,250	5,473,750	2,603,932	1,744,537	2,065,675	2,638,200	—
2,225,000	9,668,000	4,270,000	39,730,000	—	64,446,000	—	—
640,000	32,625	205,625	294,750	780,000	247,600	767,024	3,157,000 ¹³
217,000,000	222,680,022	189,515,053	202,526,769	239,085,854	220,546,132	202,469,807	283,829,644
46,993,248	35,750,287	62,740,266	53,770,401	42,729,448	52,622,297	12,777,486	12,714,934
351,397,335	300,376,121	307,300,989	331,884,078	411,882,652	427,013,705	321,332,871	327,750,305
3,080,900,000	3,247,600,000	3,462,600,000	3,977,300,000	4,410,900,000	5,032,300,000	5,443,100,000	5,864,000,000
11.4%	9.2%	8.9%	8.3%	9.3%	8.5%	5.9%	5.6%
208,630,694	104,143,939	189,477,549	224,500,698	197,827,840	206,058,766	166,141,122	—
—	—	—	60,000,000	60,000,000	60,000,000	45,000,000	—
1,500,000 ⁸	—	—	—	—	—	—	— ³
29,500,000 ⁹	15,000,000 ⁹	35,000,000 ⁹	30,000,000 ⁹	4,000,000 ⁹	28,000,000 ⁹	—	—
105,000,000 ⁷	90,000,000 ⁷	25,000,000 ⁷	16,250,000 ⁷	18,750,000 ⁷	—	—	—
—	—	25,000,000 ¹⁰	18,250,000 ¹⁰	—	—	—	—
—	—	—	—	20,500,000 ¹¹	—	45,000,000 ¹¹	—
—	—	—	—	—	—	—	— ¹²
136,000,000	105,000,000	85,000,000	124,500,000	103,250,000	88,000,000	90,000,000	—
4.4%	3.2%	2.5%	3.1%	2.3%	1.7%	1.7%	—

⁹ Issued under \$150 million Clean Water Bond of 1971.

¹⁰ Issued under \$43.27 million Capital Improvements for Higher Education Bond of 1975.

¹¹ Issued under \$230 million Clean Water Bond of 1977. (More bonds could be issued in the future.)

¹² No bonds have been approved by the voters at this writing under the \$300 million Clean Water Bond authorized by the General Assembly in 1981. Bond issues in notes 4-11 were first authorized by the legislature and then approved by the voters.

¹³ Special appropriation bills approved in fall 1981 session.

This chart was designed and compiled by Vance Sanders, an author of this article, and Center Director Ran Coble. Glenn Kiger and Cathy Garrett, Center interns, assisted with research and computations.

to cut taxes in Washington. Other types of tax increases could also be proposed, such as adding one cent to the local sales tax and increasing the gas tax.

New sources of revenue could help meet some capital budget requirements, but probably not a major share. For instance, imposing a severance tax on minerals mined in North Carolina could produce some \$14 million per year. Another potential source is the acceleration of corporate income tax payments. An idea floating around the legislature since 1971, this change in method of state revenue collections would put corporate income tax payments on the same schedule as federal payments. The one-shot injection could be worth as much as \$100 million, and the legislature could allocate it all to capital projects.

New Bond Issues. As mentioned above, the legislators recently authorized a new \$300 million Clean Water Bond. Submitting this new bond issue to the voters could portend a preference by legislators to go the bond route rather than a tax increase or another route as a way to fund capital improvements. If so, various agencies are already in line with their proposals. The Supt. of Public Instruction and a legislative study commission have proposed a school bond issue to the legislature.*

Diverting general funds, the money currently budgeted for operating costs, could improve the capital improvements picture. Whether based on each agency's budget or on the full operating budget, this approach would meet opposition from many quarters because it would cut into funding for current operations of other programs.

A fixed percentage of each annual budget — say two percent — could be allocated exclusively for capital improvements. Any funds not used immediately could be put into a reserve fund for similar use later. That reserve also could serve as the highly-valued safety cushion which legislators like to fall back upon in lean years. Legislative leaders think this would work but they're leery of being tied to a fixed figure.

"I would not go with any sort of statutory mandate on what the figure ought to be," says Sen. Harold Hardison (D-Lenoir). "But yes, I think there should be some understanding that some substantial amount would be set aside."

Royall, the chairman of the Advisory Budget Commission, agrees: "We've got to have more capital spending, no question about it. With the budget as high as it is now, a percentage figure to shoot for would be as good a way to do it as any."

And on the House side, Rep. Adams concurs:

"I've heard as much as two or three percent talked about. Certainly it should not be less than one percent. Then if you have a short year, you can delay your capital expenditures and get by."

Until one of these alternative solutions, or some combination of them, is adopted, the portion of the state budget allocated for capital projects is likely to continue declining. Some state officials argue for a large increase in capital appropriations as the only way to reverse the decline. Other fiscal analysts contend that this situation calls for more sophisticated long-term maintenance planning at top policy levels and for some rational means of distinguishing between wants and needs. The state has made a good first step towards this long-term planning process by completing "Proposed Six Year Capital Improvement Plans by Departments (Excluding the Board of Governors — University of North Carolina)" for the 1981-83 biennium.* This plan needs to be submitted to further review at the state level as well as within the various agencies so as to make clear distinctions between wants and needs and to distinguish between maintenance needs and new projects. And, legislators need to follow this plan during the appropriation process rather than reacting primarily to the political exigencies of a particular year. Having such a plan available allows legislators to make the tough choices regarding maintenance needs versus new projects in the lean years when there are not enough funds left for capital expenditures.

Regardless of one's position as to the best way to protect the state's physical plant, two important trends are likely to continue eroding the portion of the budget going to capital projects: the drying up of traditional sources for capital projects and the safety-cushion method of using funds once reserved for capital spending to meet operating expenses.

Adding these two trends to such fiscal developments as the federal budget cuts of 1981 (and projected cuts for 1982 and 1983) yields an inescapable conclusion. Only a small amount of funds remain for capital projects at the end of a legislative session. With such small reserves left, politics come into play in a disproportionately high way. After all, if there's barely enough left for horse barns, then what's to become of a leaky roof at a mental hospital? Without a long-term maintenance plan, the state has to make choices based more on politics than on needs. And, all the time, the pot of money is shrinking. □

* Bills to submit a public school bond referendum to the voters were introduced in the 1981 General Assembly (HB 104 and SB 71) but did not pass.

* *Summary of the Recommended State Budget 1981-83 Biennium*, Appendix Table 9, pages 83-106.