During the 2014 legislative session, the General Assembly enacted Senate Bill 744, the Appropriations Act of 2014 (S.L. 2014-100). The Appropriations Act addresses three major budgetary priorities by:

- Responding to revenue undercollections in FY 2013-14 and a downward revision in consensus revenue estimates for FY 2014-15 that together resulted in a reduction of $643.6 million in available funds; and
- Funding an additional $322.9 million required by the Medicaid program during FY 2014-15; and
- Providing $466.5 million for salary increases and a retiree cost-of-living adjustment.

To fund these budget changes, the General Assembly used a $428.8 million unappropriated balance that had been budgeted during the 2013 long session. It also used $396.6 million in unspent funds (reversions) from FY 2013-14. Finally, the General Assembly made funding reductions and other budget adjustments in Education, Health and Human Services, and other State government programs.

The General Assembly also enacted House Bill 1050, Omnibus Tax Law Changes (S.L. 2014-4), which makes technical and clarifying changes to the corporate income tax, creates a new tobacco tax on cigarettes and vapor products, and repeals the local privilege license tax.

### Table 1
General Fund Budget for FY 2014-15
($ millions)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenues and Other Available Funds</td>
<td>21,427.6</td>
<td>21,082.1</td>
</tr>
<tr>
<td>Appropriation</td>
<td>20,998.8</td>
<td>21,082.1</td>
</tr>
<tr>
<td>Unappropriated Balance Remaining</td>
<td>428.8</td>
<td>-</td>
</tr>
</tbody>
</table>

As shown in Table 1, S.L. 2013-360 appropriated $20,998.8 million from revenues and other available funds of $21,427.6 million, leaving an unappropriated balance of $428.8 million at the end of FY 2014-15. These funds provided a budgetary cushion that helped the General Assembly address changes in revenue collections and Medicaid spending and provide salary increases during the 2014 Short Session. In S.L. 2014-100, the General Assembly appropriated $21,082.1 million from revenues and available funds of the same amount, leaving no unappropriated or unreserved balance.
**Revenues**

In FY 2013-14 the State collected $452.6 million less in revenues than had been forecast in 2013, largely due to undercollections in personal income taxes. Personal income tax collections were lower than expected due to:

- Unexpectedly slow wage and salary growth;
- Timing of taxpayer adjustments to changes in tax laws; and
- Larger-than-expected shifts in taxpayer income from the anticipated expiration of federal tax cuts that had been in place since 2001.


**Medicaid**

The implementation of two new information technology systems caused delays in the processing and payment of Medicaid and Health Choice medical provider claims. These delays resulted in the accumulation of $64.2 million of cash at the end of FY 2013-14, but also required the General Assembly to appropriate the same amount in FY 2014-15 in order to pay these claims. S.L. 2014-100 also included $72.3 million to address a shortfall in the Medicaid budget from FY 2013-14. Between these two items, S.L. 2014-100 provides a total of $136.2 million to address prior year Medicaid needs.

In addition to the amount S.L. 2014-100 appropriates for FY 2013-14 Medicaid expenses, the bill also reserves $186.4 million to cover potential FY 2014-15 Medicaid shortfalls. Per section 12H.38 of S.L. 2014-100, this Medicaid Contingency Reserve may not be expended until appropriated by the General Assembly.

**Salaries**

S.L. 2014-100 appropriates $466.5 million for salary increases for active employees and a retiree cost-of-living increase. Of this amount, $282.3 million funds a new salary schedule that will provide, on average, an approximately seven percent increase for current State-funded educators relative to the salary schedule for FY 2013-14. Most other permanent and full-time State employees receive a $1,000 salary increase. Retirees of the State of North Carolina receive a one percent cost-of-living adjustment (COLA).

**Funding Budgetary Priorities**

The collective General Fund impact of these three budget priorities exceeds $1.4 billion:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Downward revisions to revenue forecasts</td>
<td>$643.6 million</td>
</tr>
<tr>
<td>Medicaid shortfall in FY 2013-14 and Contingency Reserve</td>
<td>$322.9 million</td>
</tr>
<tr>
<td>Salary increases for State employees and COLA for retirees</td>
<td>$466.5 million</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$1,433.0 million</strong></td>
</tr>
</tbody>
</table>

To balance the budget while addressing these issues, the General Assembly drew on several sources of funds:

- The unappropriated balance of $428.8 million from S.L. 2013-360, shown in Table 1;
- Reversions of $396.3 million in funds that were appropriated but unexpended in FY 2013-14; and
- Budget reductions and other adjustments in Education, Health and Human Services, and other State government programs. Excluding increases for salaries, benefits, and Medicaid, the reduction from all other budget adjustments in S.L. 2014-100 is $607.9 million.
### State Agency Budget Adjustments

**Department of Health & Human Services (DHHS)**

Although S.L. 2014-100 increases the appropriation to Medicaid by $136.5 million (to address liabilities from FY 2013-14), it increases overall appropriations to DHHS by only $10.5 million. In other words, S.L. 2014-100 includes not only increases in funding for DHHS but also partially offsetting reductions. Some of the major budget reductions in DHHS are:

- The replacement of $33.8 million in General Fund appropriations to the PreK and Child Care Subsidy Programs with federal block grant funds;
- A reduction of $16.0 million for contracts and administrative expenses;
- The elimination of $16.6 million in nonrecurring funds for the new Broughton Hospital, the opening of which has been delayed until May 2016;
- The replacement of $15.1 million in General Fund appropriations with funds retained from financial assessments on hospitals;
- A reduction of $10.8 million for in-patient hospital services by establishing a single base rate for all hospitals; and
- A reduction to Health Choice of $14.5 million resulting largely from revised estimates due to lower enrollment and utilization as children shift from Health Choice to Medicaid.

**Education**

S.L. 2014-100 appropriates $11,775.3 million for Public Education, the University System, and Community Colleges. This amount represents a $112.8 million increase over the General Fund appropriation of $11,662.5 million in S.L. 2013-360. The increase is due, in part, to $400.9 million in salary and benefit increases for all three systems. Excluding salaries and benefit increases, the change in the overall education budget is a reduction of $288.1 million. Within education, the major budgetary changes are in the public schools, as follows:

- A technical adjustment revising the budget for certified personnel based on salary data updated to reflect actual experience saves $64.9 million.
- Another technical adjustment reflecting updated public school enrollment saves $37.5 million.
- Budgeting additional lottery receipts to fund teacher assistants and classroom teachers saves $147.3 million in General Fund appropriations.
- A reduction to the allotment for teacher assistants saves $105.1 million.
- A reduction in student class sizes in kindergarten and first grade requires a $41.9 million increase in the funding allotment for classroom teachers.

**Other Major Budget Adjustments**

Other significant budget adjustments included in S.L. 2014-100 are:

- $56.4 million in savings from elimination of a reserve for future benefit needs previously funded by S.L. 2013-360.
- $22.0 million in savings from a reduction to the State Health Plan.
- $49.9 million in savings by eliminating funds earmarked for the Savings Reserve and Repairs and Renovations under S.L. 2013-360.
- $38.3 million in increased General Fund availability from special fund transfers and other changes to revenues and available funds.

The adjustments and reductions discussed above, together with the $428.8 million unappropriated balance from S.L. 2013-360, $396.3 million in reversions, and other smaller increases and reductions resulted in a budget that allowed the General Assembly to provide salary increases while addressing lower revenue estimates and higher Medicaid spending.
Total General Fund appropriations in S.L. 2014-100 are $21,082.1 million. Table 2 shows how these funds are distributed. Education and Health and Human Services combined receive 80% of General Fund appropriations.

Omnibus Tax Law Changes

The General Assembly also enacted House Bill 1050, Omnibus Tax Law Changes (S.L. 2014-4), which makes the following changes:

- Simplifies the calculation of the loss deduction under the corporate income tax.
- Repeals the authority for cities and counties to levy the local privilege license tax effective for taxable years beginning on or after July 1, 2015.
- Imposes an excise tax of five cents per milliliter on the consumable portion of vapor products, commonly referred to as electronic cigarettes.

For additional information, please contact:

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