

EASLEY BUDGET HIKES TAXES

2002-03 Spending, Revenue Ideas Deserve Scrutiny

Summary: Gov. Mike Easley's proposed budget adjustments for FY 2002-03 help to frame the coming fiscal debate in North Carolina. The plan relies primarily on increasing revenues — including more than \$400 million in tax hikes, \$250 million from a theoretical state lottery, and \$210 million from raiding the state's Highway Trust Fund — rather than on budget savings. And contrary to the governor's assertion, his plan would increase state spending in the midst of a fiscal emergency.

Gov. Mike Easley released his proposed budget adjustments last week as the North Carolina General Assembly was preparing to convene for its 2002 session. Most of what was in the package had been telegraphed days or weeks ahead of time, including the creation of a state-run lottery by mid-year, a transfer of \$210 million from the Highway Trust Fund, other assorted fee increases, and an acceleration of the "sales tax for local reimbursement" swap enacted in 2001 (which represents at least a temporary increase in sales taxes of as much as \$400 million).

The budget plans of any governor are often treated as little more than a "first draft" of the final product. Easley's 2002-03 plan will be no different. But it does help to frame the budget debate. The governor's plan relies mostly on more revenue (\$938 million) rather than lower spending (a net of \$439 million after expansion items are funded) to close the projected \$1.4 billion budget gap. (Media reports of a \$2 billion deficit are misleading — they refer to the difference between projected and revised revenues, not the difference between revised revenues and authorized spending.)

A key point to consider is that if the General Assembly is *not* prepared to raise taxes or to enact a state lottery immediately, without a general-election referendum, then it must come up with an additional \$652.3 million in budget savings to balance Easley's 2002-03 budget. Moreover, even if it does embrace Easley's revenue increases, additional budgetary prudence may be warranted given the questionable nature of the \$250 million lottery number and the possibility that additional tax hikes would damage the state's weakened economy and thus shrink the tax base further.

Another issue deserves clarification. In announcing his 2002-03 proposal, the governor claimed that it would "decrease the operating budget for the first time in 30 years."

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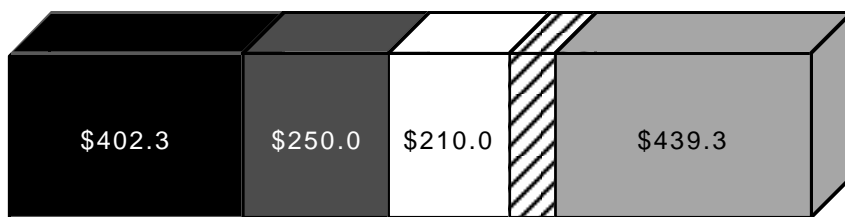
This statement is misleading. The governor's proposed authorization of \$14.3 billion would be about 1 percent lower than the \$14.5 billion authorized for FY 2001-02. But the latter budget, enacted in September, has long since fallen by the wayside. Revenue shortfalls required the governor to hold actual spending well below the authorized amount. Even if a significant portion of the proposed \$14.3 billion budget authorization "reverts" — that is, remains unspent — by June 30, 2003, it is likely that the governor's 2002-03 budget will result in an increase in actual state spending of hundreds of millions of dollars.

It is fair to note, however, that by this method of measuring state spending, Gov. Easley *can* fairly claim to have reduced year-to-year spending by nearly \$80 million, but this occurred in early 2001 as the governor was forced to adjust the last budget proposed by his predecessor, Jim Hunt.

— John Hood, President

HOW EASLEY'S PLAN CLOSSES STATE BUDGET GAP

In Million of Current Dollars



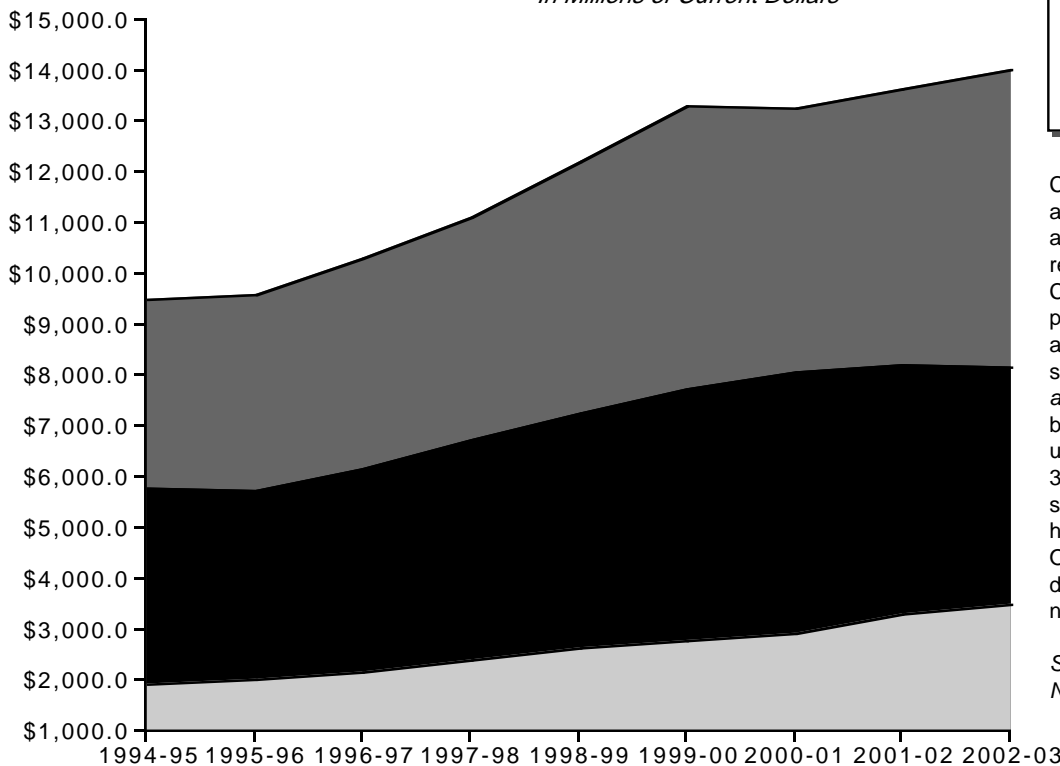
Total New Gen. Fund Revenue: \$938.4 million

- Tax Increases*
- Creating a Lottery
- Raiding Highway Funds
- ▨ Other Revenue Hikes
- Net Budget Savings

* Includes "local" sales tax hike and repeal of 2001 tax cuts.
 DATA SOURCE: Office of State Budget, Planning & Management

ACTUAL GENERAL FUND APPROPRIATIONS, FY 94-95 TO FY 02-03 (PROJECTED)

In Millions of Current Dollars



- Total Operations
- Education, All Levels
- Health/Human Services

Changing the focus from authorized to actual appropriations helps to clarify recent fiscal history in North Carolina. The governor's proposed \$14.3 billion authorization for FY 2002-03 falls slightly below last year's *authorized* budget of \$14.5 billion, but even assuming an unspent surplus of funds by June 30, 2003, actual spending will surpass spending in 2001-02 by hundreds of millions of dollars. On the other hand, the governor did reduce actual spending by nearly \$80 million in FY 2000-02.

SOURCES: Fiscal Reserch Div., NCGA, and OSBPM.