



POLICY REPORT

AGENDA 2008

*A Candidate's Guide to Key Issues
in North Carolina Public Policy*



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INTRODUCTION

As we enter the 2008 campaign season, candidates for public office in North Carolina are faced with the daunting and possibly overwhelming task of developing informed positions on dozens of public policy issues. *Agenda 2008* is part of an ongoing series begun a dozen years ago and published every two years by the John Locke Foundation. These reports are meant to provide a concise and easily digestible public policy guide for candidates for state and local offices in North Carolina.

In 1946 Henry Hazlitt wrote *Economics in One Lesson*, his now classic and timeless introduction to economics and economic policy. In writing the introduction to the “50th Anniversary” edition in 1996 (three years after Hazlitt’s death), Steve Forbes noted, “every tenet of the new economics that Hazlitt dispels continues today to rear its head in one form or another.” In comparing the topics and issues covered in *Agenda 2008* to those covered in our previous reports, it is quite clear that the same could be said for the actions of North Carolina’s state government.

Most of the same topics that were covered in 2006 and even in 1996, when our first *Agenda* was published, “continue to rear their ugly heads.” Concerns about misplaced spending priorities, high and increasing overall levels of spending, and a tax burden that punishes productive activities are continuing problems that plague North Carolina’s citizens. Education finance and performance, the abuse of private property rights through eminent domain and annexation, Medicaid, and economic development policy all continue to cry out for reform. Unfortunately, it appears that these issues, and too many others, will be a part of our *Agenda* concerns for years to come.

There are, however, several new issues for lawmakers to contend with. *Agenda 2008* includes new sections reflecting these. Several were not even on the policy radar screen in 2006. These new sections reflect how changing events can shift the focus of policy makers in a matter of months or even weeks. New for *Agenda 2008* are sections on:

- “Energy”
- “Water and Drought”
- “TIF (Tax Increment Financing) Reform”
(Inspired by the Randy Parton Theatre debacle in Roanoke Rapids)
- “Mental Health”
- “The Education Lottery”
- “Transparency”
(making information regarding government easily accessible to citizens)

What unifies the John Locke Foundation’s analysis of these issues is our fundamental commitment to free markets, private property rights, individual liberty, and limited government. The overarching goal of all of our recommendations is to advance these ideals. In doing so the citizens of North Carolina will not only be freer but also more prosperous.

Agenda 2008 is a joint effort of the policy analysts that make up the research staff at the John Locke Foundation, each of whom has special expertise in one or more of these fields.

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A Candidate's Guide to Key Issues in North Carolina Public Policy

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THE STATE BUDGET

The state budget is out of control. Gov. Mike Easley and the General Assembly call it “fiscal restraint” to spend the tax surplus when the economy is good and raise taxes when the economy is bad. Until state leaders learn to exercise real fiscal discipline or to impose discipline on themselves through an expenditure limit, the “spend and tax” pattern of budgeting from the past decade will continue.

SPENDING GROWTH

During the last ten years, general fund spending on operations has grown 81 percent, to \$20.4 billion in fiscal year (FY) 2007-08 from \$11.3 billion in FY 1997-98.

This was 22 percent faster than the combined rate of inflation and population growth, which translates to \$1,845 more spending in real terms per person, or \$7,378 for a family of four. Spending in FY2008-09 will be at least \$21 billion.

PRINCIPLED, PRACTICAL PRIORITIES

The John Locke Foundation’s *Freedom Budget 2007*, an alternative budget for the FY2007-09 biennium, would save more than \$2 billion in FY2008-09 compared to the certified state budget.

Some of the steps recommended in *Freedom Budget 2007*:

- Redirect \$47 million from non-teaching positions to fund teacher pay raises.
- Raise tuition so students pay 35 percent of costs of their UNC education as part of \$330 million in savings in the university system.
- Save \$365 million by bringing the state Medicaid program in line with the average of six southeastern states.
- Eliminate \$161 million in business subsidies often referred to as corporate welfare.
- Reduce debt service by \$78 million by delaying bonds and selling state-owned assets such as state-owned ports and railroads.
- Restructure and merge state departments to save \$127.5 million.

- End the yearly transfer of \$172 million from the Highway Trust Fund to the General Fund, rededicating the money to major road construction.

TEST EXISTING AND PROPOSED PROGRAMS

All lawmakers should test existing programs and any proposed programs by asking these questions:

- Should the state government be doing this program, or is it best left to private firms, charities, or families?
- Is another agency or level of government already doing this?
- Has this program received significantly more money with little or no better results?
- Does this program create or expand an entitlement that cannot reasonably be taken back in the future?
- Does this program use public money for political advocacy or to discriminate against racial or ethnic groups?

PROTECTING TAXPAYERS

One way to force lawmakers to set priorities and answer (or at least ask) these difficult questions would be with a tax and expenditure limit that pegs allowable spending growth to changes in population and inflation. In North Carolina, a proposed Taxpayer Protection Act (TPA) would allow per capita spending after inflation to remain constant. Versions of the bill have passed the House but never the Senate. If a TPA had been in place during the past ten fiscal years, the state’s General Fund appropriations would have been more than \$2.4 billion lower in FY 2007-08.

RECOMMENDATIONS

1. Enact — or submit as a constitutional amendment to voters — a tax and expenditure limit such as the Taxpayer Protection Act.
2. Set fiscal priorities each year. Search the base budget for items or programs to cut if new spending

is needed in other areas.

In particular, lawmakers should target corporate subsidies, pork-barrel earmarks and discretionary accounts, excessive costs for entitlement programs

such as Medicaid, non-teaching expenditures in public schools, and programs best left to local governments or private institutions.

Chart 1: General Fund Spending in FY 2008 was \$3.7 Billion Higher than Needed Based on Inflation and Population Growth Since FY 1998

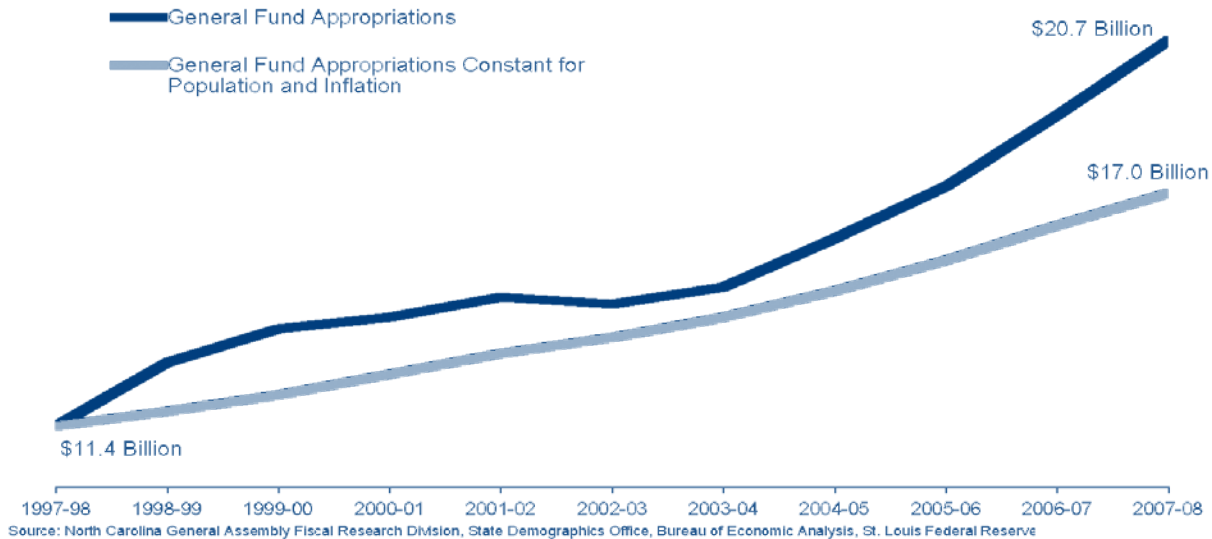
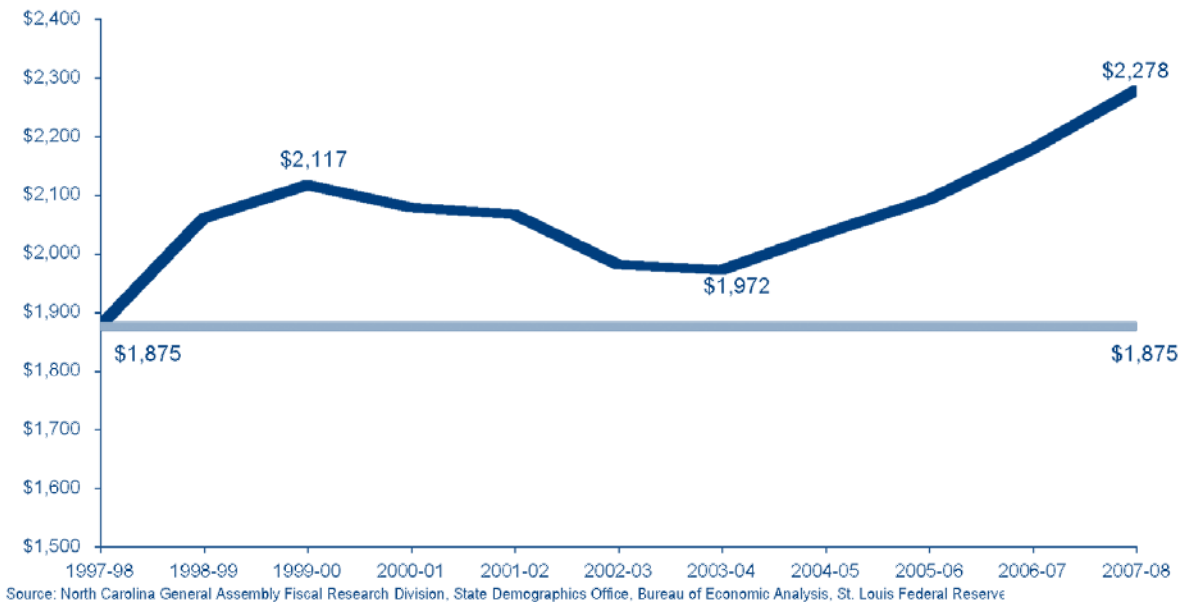


Chart 2: General Fund Spending per Capita Adjusted for Inflation in FY 2008 was \$403 Higher than in FY 1998 or \$1,612 for a Family of Four



THE STATE TAX BURDEN

Taxes are the price we pay for government, so a reasonable tax burden is of benefit to the citizens who consume the services those taxes fund.

Unfortunately, the price of government in North Carolina has grown dramatically over the past two decades and is no longer reasonable. Even with the expiration of some of the 2001 temporary tax hikes, state taxes have climbed more than \$1.3 billion under Gov. Mike Easley.

MORE TAXES, HIGHER TAXES

North Carolina's top marginal tax rates on individual (7.75 percent) and corporate (6.9 percent) income are the highest in the Southeast and ninth highest in the nation. The beer tax is fourth highest in the nation. North Carolina's gasoline tax is second only to Florida in the Southeast.

The combined state and local sales tax rate of 7.05 percent is ninth highest among states that also have an income tax. North Carolina's estimated tax burden in 2008, 9.8 percent of personal income, is among the highest in the South and 20th among all states.

Research has demonstrated that high taxes discourage out-of-state businesses and individuals from locating to a state. Although North Carolina continues to perform well economically, per capita personal income since 2001 has not kept pace with past growth.

RECENT STATE ACTIONS

Between 1983 and 1994, the General Assembly approved five major tax increases (including hikes in sales taxes, income taxes, motor fuels taxes, and excise taxes). The last two, implemented in 1990 and 1992, had a combined fiscal impact of more than \$1.8 billion in 2001. Subsequent cuts beginning in 1995 saved taxpayers \$1.4 billion in 2001, meaning that, over the decade, the state tax burden actually rose by about \$427 million.

Furthermore, while tax increases in the early 1990s hiked marginal tax rates, the 1990s tax cuts

focused primarily on exemptions, deductions, and credits, leaving our high marginal tax rates intact.

The situation worsened considerably from 2001 to 2005. In each of those five years, the General Assembly enacted budgets that increased the tax burden — by roughly \$500 million in 2001 and then more than \$1 billion annually in the following years.

The increases, some permanent and some temporary, included higher taxes on personal income, retail sales, employers, health insurance, satellite television service, and even children's candy. It took until 2006 for the temporary income and sales tax hikes to begin matching their names, although half of the sales tax increase is now permanent.

RECOMMENDATIONS

North Carolina policymakers should make it a goal at least to reduce taxes enough to bring our tax burden in line with that of our neighbors, which would require state or local tax cuts of approximately \$2 billion. Of particular concern are high income tax rates.

The Locke Foundation's 2007 budget proposal made the following proposals with those goals in mind:

1. Reduce personal and corporate income taxes to a flat rate of 6 percent, saving \$908 million.
2. Give families \$295 million in tax relief for education and health expenses.
3. Eliminate \$321 million in selective exemptions, deductions, and other tax biases.

Chart 1: North Carolina State/Local Tax Burden, 1987-2007

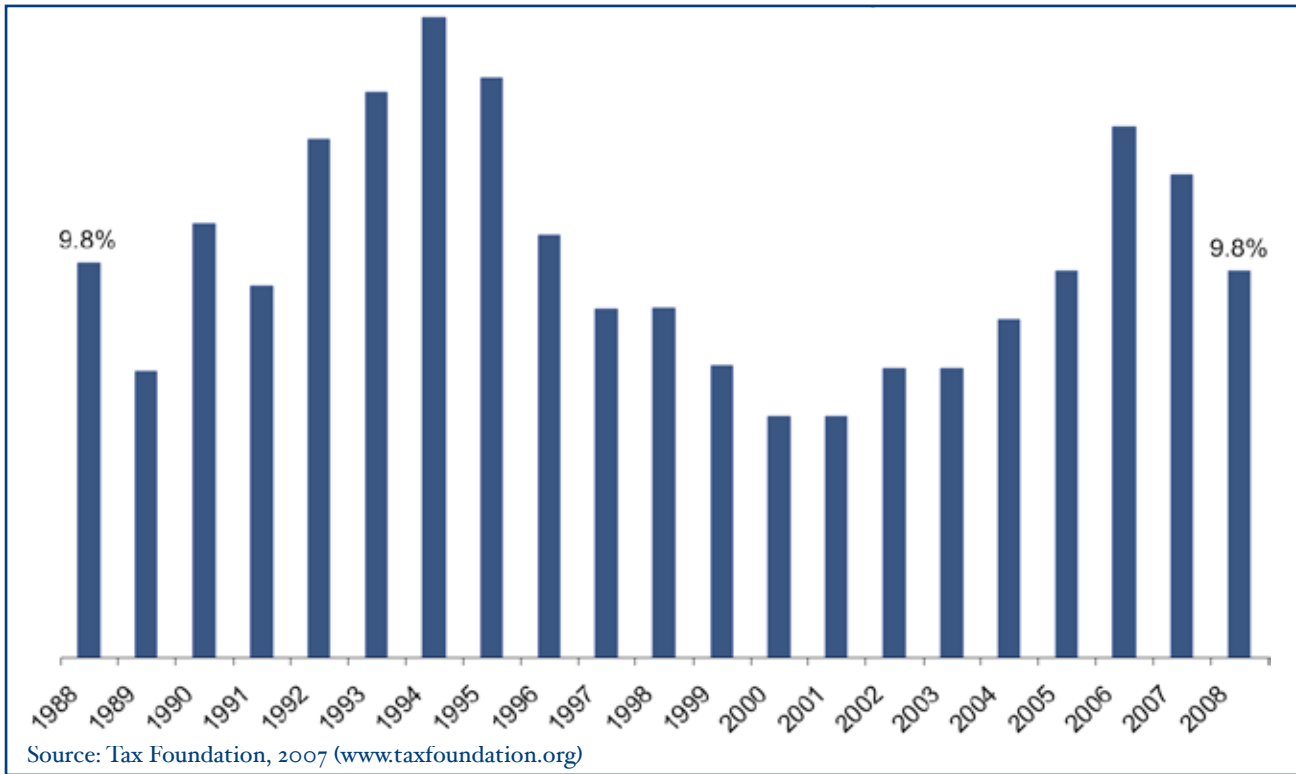
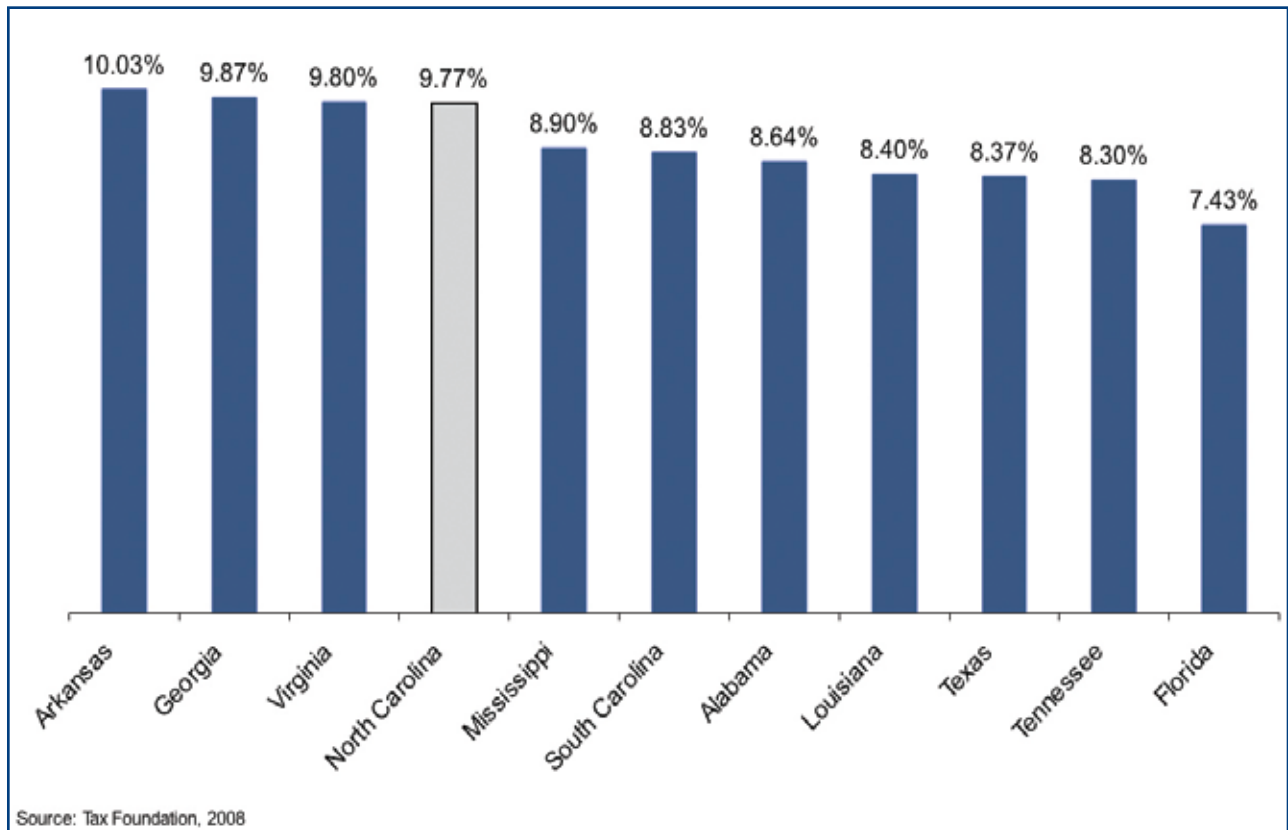


Chart 2: State/Local Tax Burdens, Southern U.S. States (2008)



STATE TAX REFORM

North Carolina has a high tax burden by regional standards, and its top marginal tax rates of 7.75 percent for individual income and 6.9 percent for corporate income are among the highest in the United States.

Tax cuts in the late 1990s did not fully make up for tax increases earlier in the decade, and the General Assembly has raised taxes by more than \$1.5 billion since 2001.

Clearly more needs to be done to gain control of the spending that leads to higher taxes. State policymakers must also consider whether the current tax code is efficient, equitable, and understandable to the average taxpayer.

Groups from left and right, the Institute for Emerging Issues, and the legislature's State and Local Fiscal Modernization Commission have all addressed the need to reform North Carolina's tax system. Proposals include eliminating the death tax, shifting the balance of responsibility between the state and local governments, and expanding the sales tax to cover services as well as goods.

PROBLEMS WITH THE TAX CODE

The current state tax code violates the basic principles of a fair and efficient tax system. It developed piecemeal with explicitly lower rates, deductions, and tax credits for favored behavior such as job training and higher rates for undesired behaviors such as smoking. The tax code, intentionally or not, penalizes saving and investment more than consumption.

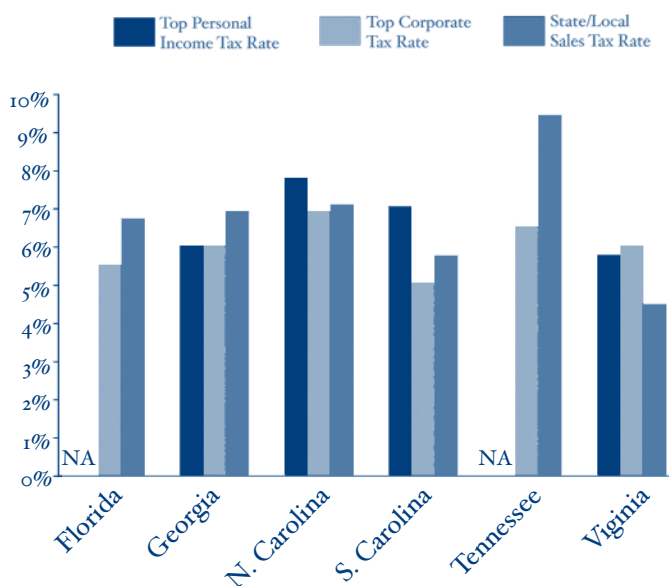
In short, North Carolina is saddled with a system that is complex, biased, and inequitable – opposite the goals of good policy.

1. *Simplicity.* The tax code is too complex for even professionals to understand. Individuals cannot plan for the future and often feel that they are paying more than they should. Resources devoted to avoidance, compliance, and enforcement are a drag on the economy.

2. *Neutrality.* The tax code favors home buyers over renters, pensioners over workers, large companies over small ones, new companies over existing ones, and borrowing over saving and investing. The tax code should not benefit or penalize any individual, group, industry, or economic decision more than another.

3. *Equity.* The tax code's progressive rates based on one's "ability to pay" are nothing more than income redistribution or, less charitably, larceny. Equity demands that users pay for services, such as highways, that are not constitutional entitlements. A flat-rate consumption tax and a flat-rate property tax would each be equitable, and each would be a way to approximate demand for public goods. Progressive income taxes and regressive housing impact fees are not. Corporate taxes are not equitable; corporations merely collect taxes from their workers, investors, and customers.

Chart I. N.C.'s Income Tax Rates — Highest in the Region



A PLAN FOR REFORM

One tax that fits all three principles is a flat tax on consumed income. A single rate applied to yearly spending and not yearly saving is understandable and

makes future taxes more predictable for the taxpayer.

Excluding capital gains and interest income from taxation, or excluding income that is saved or invested, would make the tax code neutral by ending the current pro-consumption bias. Some spending on education and health care should also be considered investments that produce future income and should be excluded from taxation, although direct cash payments to individuals would promote these activities better without distortions.

Establishing a consumed income tax eliminates the bias in the current sales tax favoring the purchase of personal and other services as substitutes for products.

Business purchases of equipment and other goods should be exempt from the sales tax to preserve the principle of equity. These purchases eventually are embodied in the goods and services purchased by consumers, and any tax paid on these purchases also becomes embedded in that price. Finally, because corporations are only intermediaries

in the tax system, the state should end the corporate income tax.

RECOMMENDATIONS

1. State policymakers should remove tax provisions from the state tax code that are inconsistent with principles of simplicity, neutrality, and equity. In every case, the goal should be to lower tax rates while offsetting at least some of the revenue loss by broadening the tax base to eliminate bias.

2. North Carolina should reform its income tax system to create a single-rate, easy-to-understand tax on consumed income that ends multiple layers of taxation on savings and investment. This reform would either make corporate dividends entirely tax-deductible or abolish corporate income taxes. It could also offer tax exclusions for household investment in education, health, and other private human-capital formation.

Chart 2. How Income Taxes Penalize Saving and Restrain Economic Growth

<p>Income taxation reduces the returns to saving twice, the returns to consumption just once. To demonstrate: a person with \$1,000 of pre-tax income faces the choice to spend now or save (with a 10 percent interest rate) and consume later. Without income taxes, his choice is to spend \$1,000 now or save it and have \$1,100 available for spending next year (Figure 1). With his income taxed, his \$1,000 is reduced to \$900 to spend or save. If it's saved, next year he could have \$981 to spend, because the \$90 interest is also taxed. The income tax reduces the return to savings twice: from \$100 to \$90 when the initial \$1,000 is taxed, then from \$90 to \$81 when the interest is taxed (Figure 2). Under a consumed-income tax, the return on investment would return to 10 percent, as it would be without taxes (Figure 3).</p>	Figure 1: No Tax			Figure 2: Current Income Tax			
		<i>Consume</i>	<i>Save</i>		<i>Consume</i>	<i>Save</i>	
	Year 1	Income	\$1,000	\$1,000	Income	\$1,000	\$1,000
		Saving	0	1,000	Saving	0	900
		Tax (0%)	0	0	Tax (10%)	100	100
		Net Income	1,000	1,000	Net Income	900	900
		Spend	1,000	0	Spend	900	0
	Year 2	Interest (10%)	\$0	\$100	Interest (10%)	\$0	\$90
		Tax (0%)	0	0	Tax (10%)	0	9
		Spend	0	100	Spend	0	81
	Saving Penalty	0.0%	0.0%	Saving Penalty	0.0%	9.0%	
	Figure 3:			<i>'Traditional IRA'</i>	<i>'Roth IRA'</i>		
	<i>Consumed-Income Tax</i>	<i>Consume</i>	<i>Save</i>	<i>Save</i>			
Year 1	Income	\$1,000	\$1,000	\$1,000			
	Saving	0	1,000	900			
	Tax (10%)	100	0	100			
	Net Income	900	1,000	900			
	Spend	900	0	0			
Year 2	Interest (10%)	\$0	\$100	\$90			
	Tax (10%)	0	10	0			
	Spend	0	90	90			
	Saving Penalty	0.0%	0.0%	0.0%			

TRANSPARENCY AND ACCOUNTABILITY



Transparency in government is critical to a free society. In addition to providing services to the citizenry, governments should also allow citizens to understand how they pay for those services. As budgets have become increasingly complex, however, citizens are less able to monitor how their taxes are spent.

A PATH TO CORRUPTION

Hiding the manner in which government operates is the simplest path to corruption. Abuses of power over the past decade with Department of Transportation funds, state grants to nonprofits, a state vision plan, money for Johnson & Wales University, and unresponsive public information officers have stemmed from the lack of transparency in state government.

Belated transparency helped expose problems with the Randy Parton Theatre in Roanoke Rapids, community support services designed for those with mental illness, and the governor's travel habits in Italy. One response has been that the state auditor's office now monitors nonprofits that receive state funding and conducts more investigative audits of state agencies.

THE STATE BUDGET AND STATE AGENCIES

The \$21 billion state budget is often difficult for legislators to understand even in broad strokes; understanding the specific line items is still more of a challenge.

To understand total spending in any area, a legislator or citizen must first consult the certified budget from the Office of State Budget and Management (OSBM). Then he must find the final budget bill and committee report approved by the General Assembly, which together show additions and subtractions from continuing spending.

If it is the second year of the biennium, such as the fiscal year that started July 1, 2008, the interested person will also have to find the previous year's budget bill and committee report, the budget Highlights publication from the General Assembly's

Fiscal Research Division, or the Post-Legislative Summary from OSBM. To find what has actually been spent, the intrepid citizen needs to contact the Office of the State Controller. If the citizen wants to understand better what is done with the money, he has to go back to the governor's budget proposal with results-based measures and extrapolate from the spending in fiscal 2006.

Many state agencies provide useful information for consumers of their services, as seen in the relative ease in finding school enrollment and graduation rates at education-related agencies' Web sites.

No agency, however, not even the Office of State Budget and Management (OSBM) or the Office of the State Controller, which monitor the entire budget, has a simple way to track revenues and expenditures online.

OSBM's recently updated site has the governor's recommended budget for the biennium as an Excel spreadsheet or a pdf. It also has the entire certified budget online, but in a format that is more difficult to access than a pdf would be. The Controller's Web site has monthly and annual financial reports available in pdf format.

In a review of state agencies and departments earlier this year, the John Locke Foundation found they generally had information available on senior staff and often had staff directories as well, but they lacked salary information.

More specific information on grants and contracts was nearly impossible to find in nearly every agency except the Department of Public Instruction/State Board of Education and the Department of Cultural Resources. Even with the governor's emphasis on results-based budgeting, most agencies provided no way to see this information.

EFFORTS IN OTHER STATES

North Carolina took the first steps long before other states, but Kansas, Missouri, Texas, and South Carolina have set the bar for transparent government much higher. The federal government has



also become more transparent both on its own and through outside Web sites that make federal spending easier to follow. Other states, from Louisiana to Alaska, Hawaii to Nebraska, are following suit.

Transparency Report Card for Selected State Agencies

	Avg.	Detailed Line-Item Bdgt.	Check Register	Govt. Con-tracts.	Grants to Non-Profits	Employ. & Salaries
K-12 Schools*	D	F	F	C	C	F
Comm. Colleges*	F	F	F	F	F	D
UNC System*	F	F	F	F	F	F
Labor	D	B	F	F	F	D
State Bdgt & Mgmt	D	B	F	F	F	C
Revenue	D	B	F	F	F	D
Cultural Resources	D-	F	F	F	C	D
Admin.	D-	F	F	D	F	C
Crime Control/ Pub. Safety	D-	D	F	F	F	D
Health & Human Svcs	D-	D	F	F	F	D
Agriculture	D-	F	F	F	D	D
Judiciary	D-	F	F	F	D	D
Controller	D-	F	F	F	F	C
DENR	F	F	F	F	F	D
Commerce	F	F	F	F	F	D
Insurance	F	F	F	F	F	D
Corrections	F	F	F	F	F	D
Treasurer	F	F	F	F	F	D
Auditor	F	F	F	F	F	D
Justice	F	F	F	F	F	F
Transport.	F	F	F	F	F	F

* If the categories of School Enrollment and School Graduation Rates are taken into account, the grade for each agency would be a "B," making the avg. grade for K-12 Education a "C-," Comm. Colleges and the UNC System a "D."

These states provide online check registers, searchable databases, and user-friendly sites that allow citizens to follow their tax dollars. Already managers in government agencies have used the new tools to find efficiencies in their operations, and vendors have found areas where their products or services can help improve service for less money. States can also provide this information at little additional cost.

Oregon State University gives an example of an institution that has unilaterally opened its books. Its system, created in less than three months by a student for less than \$10,000, has ten years of historical transactions with daily updates available. It is available to all students, faculty, and staff, though not yet to the general public. There is no reason the UNC system could not undertake a similar effort within even more beneficial results if applied across campuses, a step that would make direct comparisons possible.

The ability to compare across institutions within a state and across states is one of the network effects of transparency efforts. It is now difficult for a state employee or a citizen to compare activities across state lines. With transaction-level detail, however, it can become clear what states are getting for their money in a number of areas.

RECOMMENDATIONS

1. North Carolina should create a state transparency portal with transaction-level information with daily spending updates from the Office of the State Controller for all of state government, and daily revenue updates from the Department of Revenue.

2. Every state agency and department should make its check register available online and provide a link to the state transparency portal.

3. To make budgets more transparent, the legislature should enact a 72-hour "cooling off period" between the time a budget bill leaves the appropriations committee and when the first vote occurs.

4. To complete the transparency cycle, agencies should report and be accountable for program outcomes as they relate to program objectives.

STATE AGENCY CONSOLIDATION



The constitutional offices of North Carolina state government have changed little since 1900. As a reaction first to the tyranny of royal governors and then to the Civil War, the state has divided executive power among a number of separately elected offices. At the same time, governors and legislators have created many agencies under their direct control.

The result has been a lack of coordination and focus on major functions, wasteful administrative spending, and a lack of accountability to the public.

THE NEED FOR CONSOLIDATION

State government departments need to be reorganized and consolidated. Departments or agencies that perform similar functions should be grouped together, both to reduce cost and to improve the delivery of services. At the same time, the number of separately elected executive branch officers should be reduced to three at most — the governor and lieutenant governor, who should run as a team, and an independent state auditor. By electing too many officers to fixed four-year terms, the current system limits immediate accountability for poor performance by department heads and creates confusion among citizens and lawmakers.

For example, there are five major departments or offices that oversee state finances: the Department of Revenue, State Treasurer, State Controller, State Auditor, and the Office of State Budget, Planning, and Management. Most of these separate units could be merged into a Department of Finance, headed by an appointed secretary. It would include divisions similar to the previous departments, but would not require the staff or funding now necessary.

Similarly, there are currently six departments or agency categories that attempt to regulate business activities in North Carolina. These should be consolidated (when not eliminated outright) to form a single Department of Commerce devoted to providing consumers with reliable information and protection from fraud.

Other opportunities for savings include forming

a single statewide police force within a consolidated Public Safety Department and merging all disability services within the Health and Human Services Department.

Under the state constitution, the governor has constitutional authority to reorganize state government. If the reorganization affects existing law, the governor must file the changes as executive orders with the General Assembly during a legislative session. Those orders become effective at the end of the session unless at least one chamber votes them down.

Furthermore, if the governor and General Assembly wish to proceed with administrative reorganization that eliminates the major duties of the Council of State, they can do so. While the constitution mandates that Council of State offices be elected, it does not define their duties. The offices could be made part-time advisory positions with no administrative duties.

The governor could reassign their duties by executive order, and he could even appoint Council of State members to head departments in his or her administration.

GOAL

Consolidate state departments to eliminate unnecessary bureaucracy, clarify responsibility for governmental functions, and concentrate departments around core state functions (see charts).

RECOMMENDATIONS

1. Consolidate functions and reduce the number of major administrative departments to 13 from 26. These and other agency reorganizations could save taxpayers as much as \$54 million a year.

2. Amend the state constitution to eliminate all elected state executives except the governor, lieutenant governor, and state auditor, and to downsize and streamline accountability for appointed state boards.



Chart 1: North Carolina State Government As Currently Organized
(Major State Agencies and Their Functions)

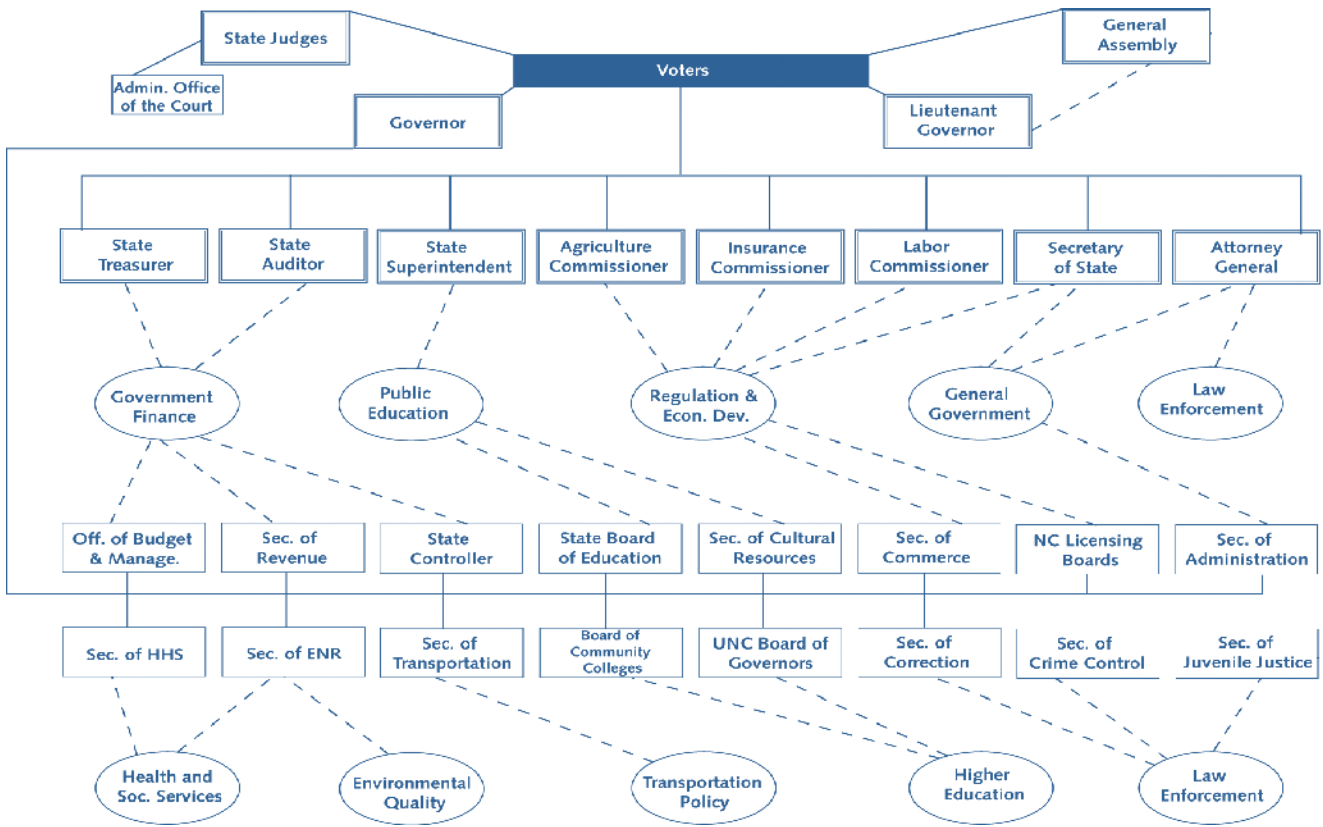
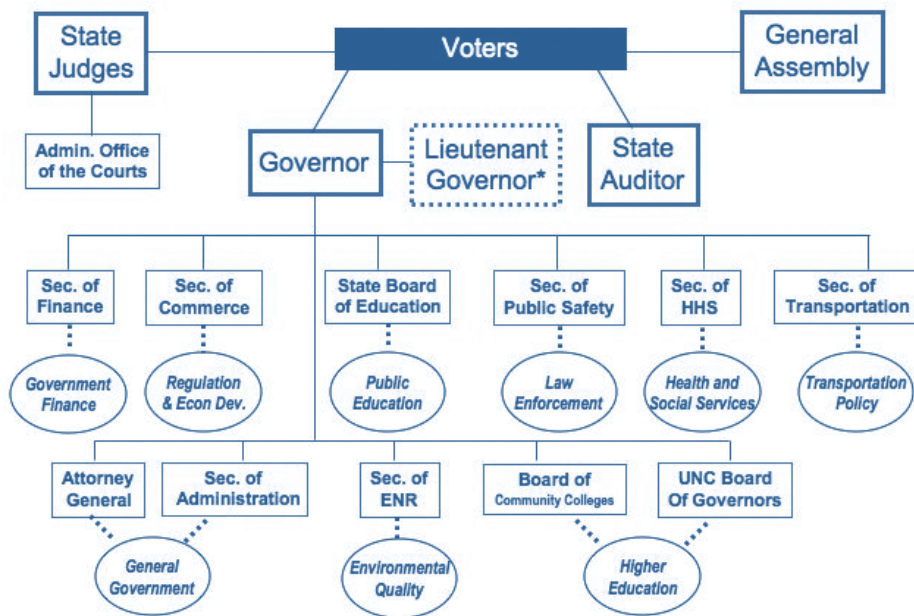


Chart 2: North Carolina State Government — After Consolidation



SCHOOL STANDARDS AND TESTING



With the implementation of the ABCs of Public Education, the Excellent Schools Act, charter school legislation, and other reforms, North Carolina lawmakers have put education at the top of the priority list. But even after some recent progress, repeated problems with the state testing program and disappointing performance from our high school students suggest that more fundamental changes are needed.

IMPROVEMENT — TO MEDIOCRITY

In 1996, the General Assembly approved the State Board of Education's plan for a school-based management and accountability program called the ABCs. The program began with end-of-grade reading and mathematics tests for grades 3-8 and a writing test at grades 4 and 7. In 1998, the state added end-of-course mathematics, English, science, and social studies tests for grades 9-12. Most recently, the state added an 8th-grade computer skills test in 2001 and a 10th-grade writing test in 2002. Taken together, North Carolina has one of the oldest and most comprehensive testing programs of any U.S. state.

Although the ABCs testing program reflects the state's commitment to statewide testing and test reporting, the ABC tests do not adequately assess student achievement. State education officials were embarrassed in 2001 to discover that their new math tests were absurdly easy to pass — a product of poor judgment and a flawed system of field-testing. To achieve "grade level" often means that students need only get half the questions right, so they can expect to pass simply through educated guessing. And while both state tests and the well-respected National Assessment of Educational Progress (NAEP) use four levels of achievement, the performance necessary to earn Level 3 on state tests is lower than the NAEP's Level 2. In other words, North Carolina's expectations are too low.

A related concern is that state testing results don't square with scores on independent national tests. For example, North Carolina's own tests show

a significant improvement in reading achievement since 2002, but NAEP results show a sizable decline for 4th-graders (from a scale score of 222 to a score of 218) and a huge decline for 8th-graders (from a scale score of 265 to a score of 259). On the other hand, North Carolina has clearly made significant progress in mathematics performance. Since 2000, NAEP scale scores in mathematics increased from 230 to 242 among 4th-graders and from 276 to 284 among 8th-graders. If our students are going to be globally competitive, we must do a better job producing graduates who are proficient in reading and mathematics.

Despite some signs of improvement, our public schools still have a long way to go. The final outcome of public education is measured in high-school performance, and it remains disappointing. Only 70 percent of North Carolina's students graduate high school *in five years*. Our college-bound students' performance on the SAT lags far behind the nation. In 2007, North Carolina's total score on the SAT (1004) was far lower than the national average (1017) and ranked 39th in the nation.

If our average performance is mediocre, the situation faced by our minority students can rightly be called a crisis. Among 4th-graders, 32 percent of black students and 16 percent of Hispanics lack basic math skills, while 55 percent of blacks and 51 percent of Hispanics lack basic reading skills. By the 8th grade, 47 percent of black students and 39 percent of Hispanics lack basic math skills, and 47 percent of blacks and 44 percent of Hispanics lack basic reading skills. Worse yet, only 61 percent of black and 54 percent of Hispanic students graduate from North Carolina high schools in four years.

TEACHER STANDARDS

State education leaders tout teacher testing and certification requirements as the way to maintain high standards for public school teachers and improve student performance. Yet, study after study shows that these factors do not guarantee good



teachers. To be granted certification, teachers in North Carolina are required to pass one or more Praxis tests that evaluate a teacher's knowledge of subject-area content and pedagogy.

Nevertheless, the scores required to pass individual Praxis tests are relatively low. Despite the fact that the state granted certification or licensure to nearly 93 percent of the teacher workforce, there is no evidence that the process has separated the wheat from the chaff.

Furthermore, the state urges teachers to participate in the National Board Certification program as a way to improve student achievement. As this certification process exists today, the required portfolio of student work, videotapes of teaching, and "reflective" essays say little about a teacher's potential deficiencies, such as poor knowledge of the subject matter.

Studies that assess the relationship between national board certification and student achievement show mixed results across student subgroups and ability levels. Although there appear to be no instructional gains for teachers and no consistent academic gains for students, the incentives for teachers to pursue certification are too good to pass up. Teachers receive full payment of the assessment fee, paid leave, continuing education credits, and a 12 percent pay increase for 10 years.

RECOMMENDATIONS

1. The state's end-of-year and end-of-course tests should be replaced with an independent, field-tested, and credible national test of student performance. There are a number of norm-referenced tests available for students in grades K-12, including the Basic Achievement Skills Individual Screener (BASIS), Metropolitan Achievement Tests (MAT 8), and the Stanford Achievement Test Series, 10th Edition (Stanford 10).

2. North Carolina should also set an intermediate goal of at least half of students showing proficiency and 90 percent testing at the "basic" level as defined by reputable national tests such as the National Assessment of Educational Progress.

3. In addition to measuring, reporting, and rewarding overall growth in school test scores, the state and local school districts should reward individual teachers based on the value they add to the performance of their students.

4. State policymakers should deregulate and decentralize public schools while maintaining accountability for results by abolishing teacher tenure and rigid certification rules.

4-Year Cohort Graduation Rate, 2005 - 2007

<i>Subgroup</i>	<i>2005-2006</i>	<i>2006-2007</i>
All Students	68.3	69.5
Male	64.0	65.1
Female	72.6	73.9
Native American	51.1	55.6
Asian	75.2	78.9
Black	60.4	61.4
Hispanic	52.3	53.7
Multi-Racial	66.0	65.4
White	73.5	75.0
Economically Disadvantaged	55.6	66.0
Limited English Proficient	55.0	52.1
Students with Disabilities	50.0	49.5

Note: Entering 9th graders graduating four years later.

Source: North Carolina Department of Public Instruction.

SCHOOL CHOICE AND COMPETITION



Public education is a core function of state and local government. The state constitution, in the words of the N.C. Supreme Court, recognizes the right to a “sound, basic education” for every child in the state. But public education need not and should not be delivered by government monopolies, as diverse magnet, charter, and private schools are demonstrating across the country and here in North Carolina.

Affluent families already exercise choice. They can move to neighborhoods where assigned schools are of good quality, or afford to pay twice for better education — once for private school tuition and then again in taxes to fund schools they don’t use.

Middle-income and poor families have few such options. Nor do school-aged students have as much choice as do preschoolers or college students, who have long been able to use tax funds to help defray the cost of private, even religious, instruction. If a preschooler can stay in a church-run day care center, or a student attend a religious university, and receive public funds for doing so, why can’t a poor, inner-city child needing effective instruction or special attention attend a private school without financial penalty?

In the end, no system for delivering goods and services functions well without providing a means for consumers to make their desires known and express their level of satisfaction.

EDUCATIONAL OPTIONS IN NORTH CAROLINA

Increasing numbers of North Carolina’s students are exercising choice. Several districts — including Mecklenburg, Wake, Forsyth, and Cumberland — have established magnet schools or choice-based enrollment policies. A 1996 law established a new category of public schools, called charters, that receive public operating funds and thrive only to the extent they attract students. In 2007-08, there were more than 30,000 students enrolled in North Carolina charter schools.

Research suggests that increasing the number

of charter schools in North Carolina will further improve the performance of students who choose to remain in traditional schools. In a study of North Carolina charter schools, researchers George M. Holmes, Jeff Desimone, and Nicholas G. Rupp found that competition from charter schools raised the performance of nearby traditional schools substantially. Charter school competition raised the performance of students at traditional schools who were at or near the cutoff score for grade-level proficiency. In addition, Holmes, Desimone, and Rupp found that school choice is a more cost-effective alternative to lowering class size. Lowering class size increased student performance by 0.36 percentage points, while school choice increased student performance by 1.0 percentage point.

Among the state’s private schools, enrollment was about 95,785 in 2006-07, up 16 percent from ten years earlier. Home-school enrollment skyrocketed from 18,400 to 68,700 during the same period. Overall, the proportion of students who attend charter, private, and home schools increased 83 percent during the past decade — but at 13 percent, enrollment in non-district schools of choice remained low compared to district school enrollment.

THE CONSTITUTIONALITY OF SCHOOL CHOICE

North Carolina’s Constitution specifies that the public school system must be “general and uniform.” This provision does not mean that all schools must be public schools. Instead, this merely establishes a minimum standard for the state, a standard that is not at odds with establishing alternative schools and programs that are not a part of the public school system. Years of legal precedent have decreed that a “general and uniform” school system is one that improves the education of the state’s citizens, which a school choice program would do. Therefore, school choice would not violate the “general and uniform” provision in the North Carolina Constitution.

More importantly, the North Carolina Constitution is one of the few state constitutions that do not



contain religious clauses that would prohibit school choice for religious schools. The constitution does not contain an Establishment Clause or a “compelled support” clause (also known as a Blaine Amendment) that restrict the government’s ability to support sectarian organizations or churches.

Although the North Carolina Constitution does not contain restrictive religious clauses, a school choice program in North Carolina would still have to comply with religion clauses of the U.S. Constitution. In *Zelman v. Simmons-Harris* (2002), the U.S. Supreme Court ruled that school choice does not violate the separation of church and state because the parents, not the state, determine their child’s school. Therefore, neither the state nor federal constitution would prohibit a comprehensive school choice program in North Carolina.

TAX CREDITS

Education tax credits would enable low- and middle-income parents to exercise school choice. A family education tax credit would reduce the state income tax liability of families that incur out-of-pocket expenses for private school tuition and educational services and expenses. A philanthropy education tax credit would reduce the state income tax liability of individuals and business that donate to scholarship funding organizations. Research has shown that both types of tax credits are educationally and fiscally sound.

Currently, seven states operate education tax credit programs, and the savings to taxpayers in these states has been substantial.

For example, tax credits have produced cumulative savings of \$144 million in Pennsylvania, \$18 million in Arizona, and \$42 million in Florida. A legislative analysis found that North Carolina would save between \$3 million and \$19 million a year in the cost of educating special needs students, so long as at least 5 percent of the special needs students enrolled in public schools used a special needs tax credit to transfer to a private provider or facility.

RECOMMENDATIONS

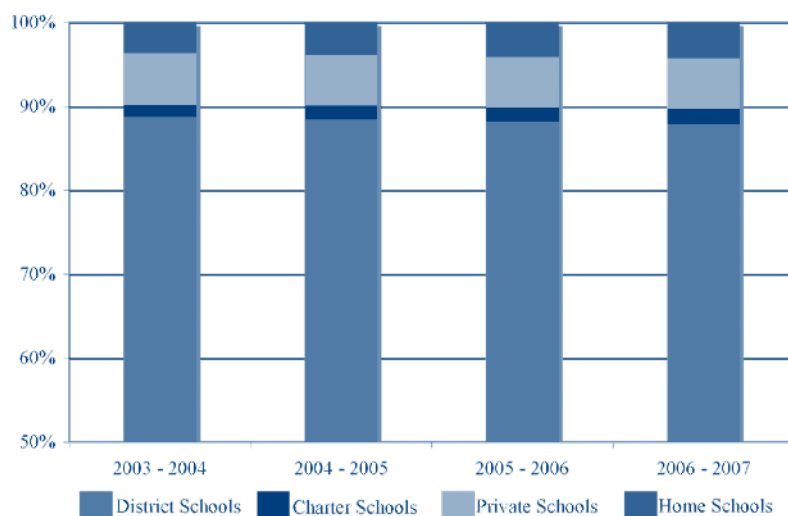
1. The General Assembly should give parents an “Education Bill of Rights” that attaches funding to the student and gives parents the right to send their children to any public, charter, or private school in the state.

2. North Carolina school districts should make greater use of open enrollment and magnet schools, using choice and competition as tools to improve academic performance and allow diverse learning communities to form. Forced busing for social engineering is poor public policy, but voluntary busing for educational excellence provides children with the opportunity to receive the sound, basic education to which they are entitled.

3. The legislatively imposed statewide cap of 100 charter schools should be lifted, allowing the number of charters to grow as long as parents, educators, and oversight agencies ensure accountability for results.

4. All North Carolina families should be allowed to set up educational savings accounts, with an annual tax-deductible deposit of \$4,500 per child, from which they can withdraw funds tax-free for educational expenses such as textbooks, educational materials, or tuition incurred at any time from preschool through college. Needy students in public schools where fewer than 60 percent test at grade level should get \$4,500 scholarships to attend private schools.

School Enrollment by School Type, 2003-2007



EDUCATION SPENDING

Will Rogers said, “Lord, the money we do spend on Government and it’s not one bit better than the government we got for one-third the money twenty years ago.” This is especially true for money that we spend on public education. Despite billion-dollar increases in education spending, it has become clear that more money alone will not yield better results.

Although state education leaders and advocacy groups contend that public schools do not receive enough money, taxpayers think otherwise. Both national and regional polls suggest that more and more taxpayers believe their local school districts are inefficient and wasteful, not underfunded. This is clearly one of the benefits of state accountability efforts like the ABCs and federal programs like No Child Left Behind, but accountability alone will not tame the public school bureaucracy. As long as there is no incentive for public schools to spend money more wisely, they will continue to complain about funding shortfalls while draining the public purse.

CONTROLLING THE PURSE STRINGS

The system of funding schools in North Carolina is different than in many other states because most public school funding comes from the state, not local, government. This means that control over public education in the state is highly centralized, allowing the state legislature, governor, and North Carolina State Board of Education to exercise a great deal of power over public schools. North Carolina ranks sixth in the nation and first in the South for the highest percentage of funds from state revenue. In North Carolina, 64.8 percent of the funds come from the state, compared to a national average of 47.6 percent. Local funds make up 25 percent and federal funds 10.2 percent of K-12 education expenditures in North Carolina.

State, federal, and local education spending continues to grow much faster than student enrollment. From 2001 to 2007, student enrollment in North Carolina public schools increased nearly 10 percent. On the other hand, state public school funding has

increased by 34 percent, from \$5.9 billion in 2001 to \$7.9 billion in 2007. During the same period, federal funding to North Carolina public schools has increased 53 percent, thanks to significant increases in No Child Left Behind funding (\$212.5 million increase since 2001) and special education funding (\$128.5 million increase since 2001). Finally, local public school funding posted a 28 percent increase, adding an additional \$594 million to the state’s public schools since 2001.

SALARIES AND BENEFITS

Much of the money spent on public education in North Carolina pays for employee salaries and benefits. For the 2006–07 school year, the state spent nearly 91 percent of funds appropriated for public education on salaries and benefits. Since 1992, there has been a 100.8 percent increase in base teacher salaries, compared to a 52.8 percent increase in inflation.

Despite legislative efforts to get North Carolina teacher pay above the “national average,” teacher compensation is well above the national average when properly adjusted for cost of living, pension contribution, and years of experience. A 2008 study by the John Locke Foundation found that the average teacher compensation in North Carolina ranks 10th in the nation and was \$55,731, or nearly \$5,400 more than the national average.

MORE MONEY, DISAPPOINTING RESULTS

Despite much of the political rhetoric about the need to increase education spending, funding increases alone will not improve education in the state. There has been a \$3.6 billion increase in state, local, and federal public school spending since 2000, but only 70 percent of North Carolina students graduated high school in four years. In 2006–2007, more than 23,500 students dropped out of school, the highest number of dropouts since 2000. Moreover, the state’s 5.24 percent dropout rate for 2006–2007 was the highest dropout rate in five years.

Simply throwing more money at high schools is not the answer to the dropout crisis. In 2006, Gov. Mike Easley commissioned the “North Carolina High School Resource Allocation Study” to determine if high schools in North Carolina were using existing levels of funding efficiently and effectively. After two years of exhaustive study, a team of researchers from UNC-Chapel Hill and East Carolina found that the effect of total per pupil expenditures on student performance is very small. For example, they pointed out that a \$500 increase in total per pupil expenditures in a school would lead to a miniscule 0.06 increase in average test scores in the school.

RECOMMENDATIONS

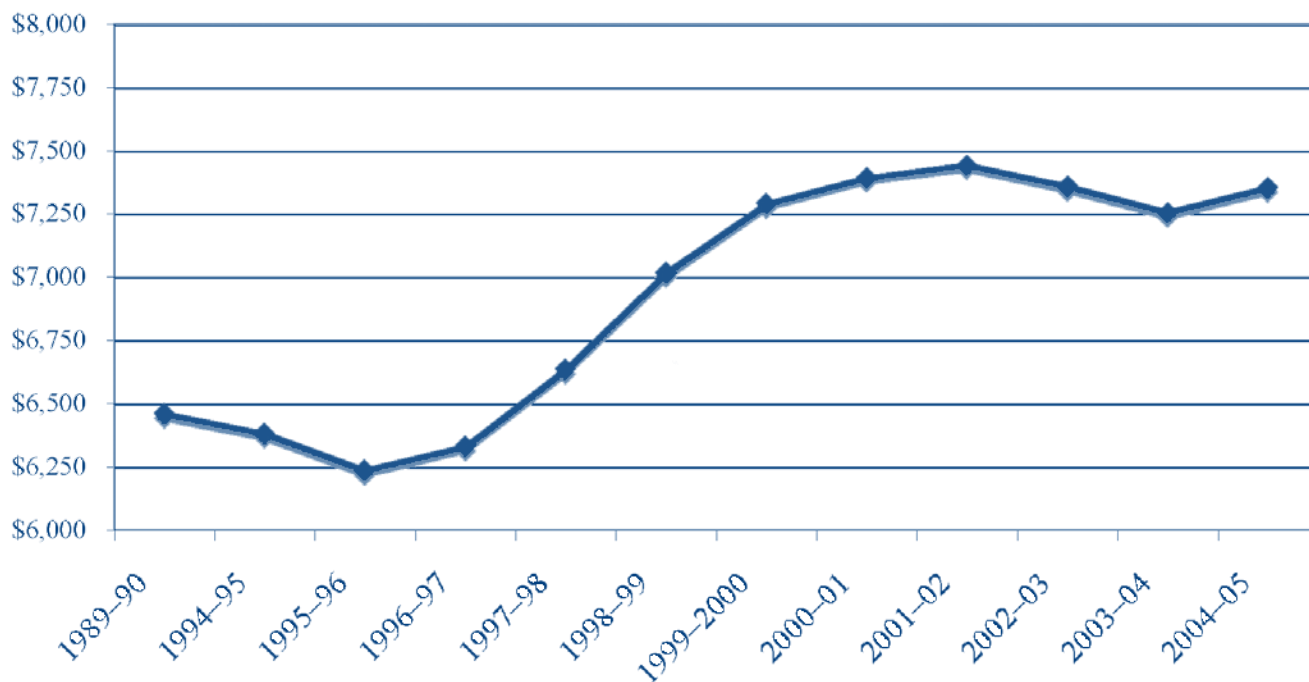
1. Change the way that North Carolina funds public education by attaching funding to the student, rather than allocating funds to each school

district on a per-pupil basis. Coupled with open enrollment for schools statewide, this will ensure that schools of the parents’ choosing receive funds necessary to educate each child and nothing more.

2. Reallocate lottery revenue to provide additional funding to high-growth school districts for school construction and renovation and for cost saving incentives related to capital expenditures. Lottery revenue should also be distributed to charter schools, which do not receive funds for capital expenditures.

3. Implement a merit pay system for teachers that will pay a portion of their salary based on the value that they add to their students’ academic performance, rather than on years of experience and credentials.

Average Per-Pupil Expenditure for North Carolina Public Schools, 1989-90 through 2004-05



Note: In constant 2006-2007 dollars
 Source: Digest of Education Statistics 2007

CHILD CARE AND EARLY CHILDHOOD EDUCATION



One of the most controversial issues in the past few years has been the proper role of the state in providing child care and preschool opportunities to North Carolina children.

The Smart Start program was intended to be an innovative public-private partnership to facilitate local coordination of children's services, but the program is mostly state-funded and focuses mainly on the minority of preschoolers in paid child care. North Carolina also affects the market through a tax credit for child-care expenses and through rules on personnel, facilities, amenities, and location of centers and homes that raise the price of care.

SMART START'S SHAKY DEBUT

Smart Start was created in 1993 to help get North Carolina preschoolers ready to learn and thus boost educational performance. Until recently its effectiveness as a school-readiness intervention was impossible to estimate. This has not stopped some politicians from proclaiming Smart Start a "success." In 1999, for example, Gov. Jim Hunt attributed apparent gains in North Carolina reading scores on 1998 national tests to the existence of Smart Start, even though the highest grade that students from Smart Start-supported preschools could have reached by 1998 was third grade and the reading tests were of fourth-graders.

Since early 1998, a number of studies of Smart Start's impact on school readiness have been published that can provide fair-minded observers with critical information about its effectiveness. Although portrayed by news reports and elsewhere as proving Smart Start's success, the studies, when closely read, suggest a far different conclusion.

In 1998, the Graham Center conducted a study of Smart Start in Orange County. A flawed study because it lacked a true control group, it still found no statistically significant impact on non-poor children and a modest gain for poor ones. A more valid study was conducted in 1998 in Mecklenburg County. It found no statistically significant impact on those

who spent a single year in a Smart Start center. It did find a measurable gain for kids who stayed in such a center for three years, but once again, the gain was relatively small two percentage points on one measure and seven percentage points on another. In early 1999 the Graham Center released a study of 200 Smart Start-supported centers that showed gains in child care quality but no impact on kindergarten readiness.

Due to these severe limitations in research design, researchers are unable to attribute educational or developmental gains to participation in Smart Start or More at Four. For example, the Graham Center's 2003 evaluation of Smart Start concluded that causality between Smart Start participation, child care quality, and child outcomes could not be established. The most recent evaluation of More at Four, a pre-kindergarten program for at-risk 4-year-olds, offered the same warning. Worse, researchers have no plans to conduct new and improved evaluations of student academic preparation for either program.

MORE AT FOUR

More at Four has been in operation since 2002, so it has not existed long enough to show that children enrolled in the program exhibit lasting gains in academic performance. A February 2008 report published by the Frank Porter Graham Child Development Institute assessed More at Four children from the beginning of their pre-kindergarten year to the end of their kindergarten year. This report found that most children retained the skills that they learned over this two-year period.

While that finding is not surprising, there is little guarantee that these children will maintain these skills into middle and high school, where students are most susceptible to falling behind their peers academically. In fact, research suggests that children who received an advantage by attending a preschool program often do not retain that advantage by the time they reach middle school.



CAROLINA ABECEDARIAN PROJECT

Advocates of state-funded early childhood education point to studies like the Carolina Abecedarian Project to justify expanding government expenditures on preschool programs. The Abecedarian study tracked the academic performance and occupational status of two groups of low-income students from infancy to age 21. A group of 57 children received high quality child care from infancy to age five, and a group of 54 children received no intervention at all. When the two groups were compared, the children who received high quality child care generally outperformed those who did not.

Because of the limitations of the study, we should be careful not to draw unwarranted conclusions about early childhood education programs for at-risk children. Some of the gaps between groups were not large or statistically significant. On cognitive tests, the gap between the two groups began to narrow or “fade out” as students entered high school. More importantly, the small sample of children, a problem in itself, was provided *high quality* child care. It is unlikely that More at Four sites are able to deliver the same kind of superior care to 20,000 children that Abecedarian Project researchers provided for 57.

PRESCHOOLERS AND DAY CARE

Families are by far the most important providers of child care and preschool services. They do the most to get their children “ready to learn,” whether it be purchasing a book, making a visit to a doctor, or sacrificing significant income to rear their children at home. All of these investments in child development deserve the same subsidy, if any, given to those who choose services provided for pay outside the home. Furthermore, parents, relatives, and neighbors supply the vast majority of care provided to preschoolers, and on a non-paid basis. Thus, day care and Smart Start subsidies offer little help to most families. A better approach would be to fund refundable tax credits for each preschool child.

RECOMMENDATIONS

1. Smart Start and other subsidy programs and tax credits for child care and preschool expenses should be eliminated in favor of a refundable Smart Start tax credit for preschool children. Parents should also be able to make tax-deductible contributions into Educational Savings Accounts for use in paying preschool expenses or accumulating assets for the future educational needs of their children. For a smaller subset of desperately poor preschoolers who lack functioning parents, a carefully designed state intervention may be justified.

2. Policymakers should limit regulation of day-care operations to health and safety requirements only, letting parents make their own decisions about the trade-off between price and child-staff ratios or qualifications.

3. Yearly evaluations of Smart Start and More At Four should be resumed but redesigned using quasi-experimental research methods. In addition, longitudinal studies should be conducted to determine if state pre-kindergarten programs produce lasting social and educational benefits as children progress through school.

Enrollment and Per-Capita Spending on
Preschool Education, 2005–2006

<i>State</i>	<i>Percentage of 3- and 4-year-olds enrolled in preschool</i>	<i>State per-capita spending on pre-school education</i>
Georgia	50.8	\$3,899
Florida	49.8	N/A
Louisiana	49.6	\$4,235
Virginia	47.9	\$3,420
South Carolina	47.7	\$1,374
North Carolina	47.6	\$4,058
Mississippi	47.5	N/A
<i>U.S. Average</i>	<i>46.1</i>	<i>\$3,551</i>

EDUCATION LOTTERY

The North Carolina Education Lottery was born of corruption, from its inception as a bill, to its lobbying, to its rushed enactment in the N.C. House and Senate in the face of the state's constitutional requirement that revenue bills face multiple votes on successive days, to its false promise to and exploitation of the state's poorest citizens.

LOTTERIES LEAD TO LOWER PER-CAPITA SPENDING ON EDUCATION

At the request of the North Carolina Legislative Black Caucus' Economic Development Committee, the Office of State Auditor conducted a performance audit of the lottery, released April 10, 2008, which "identified significant performance management weaknesses ... no documented revenue forecasting methodology, no strategic plan, no ongoing market research, and no full-cost accounting of promotional events."

The audit's finding of a lack of performance methodology cuts to the very heart of the lottery's ostensible purpose. As stated in the audit, "It is important to develop a reliable revenue forecasting methodology because schools and students were promised Lottery receipts for new construction, class size reduction, and scholarships."

Nevertheless, lottery sales and education transfers for 2007 fell short of projections by more than 25 percent, and despite projections being set about 20 percent lower apiece for 2008, by mid-year lottery sales and education transfers were still trending below expectations.

These shortfalls are exacerbated by appropriation replacement – an inevitable byproduct of state lottery revenue schemes whereby the new funding from the lottery *replaces* rather than amplifies state appropriations for, in this case, education.

There's an old principle that governments raise taxes not to support key functions, but to support the most trivial ones – i.e., ones that lawmakers would cut in the name of efficiency and good government, but decide to keep in the name of higher

taxes. The wisdom of this observation is illustrated to absurd extents by appropriation replacement, as funds that once would have gone to education now find their ways into various other public programs, liberated as it were by the lottery revenue.

The replacement problem first raised its head in North Carolina in early 2006, when *The News & Observer* reported that lottery revenues would supplant more than \$200 million in general funds devoted to schools. It turned out that the original bill included language intended to prevent new lottery proceeds from replacing existing school revenue, but that language was dropped from lottery provisions in the state budget bill (not that legislation could effectively stem the replacement problem, owing to the fungibility of money).

Older state lotteries begin to compound the problem of supplanting through something lottery researchers have termed *lottery fatigue*. Numerous studies have shown that state lottery sales almost always fall after the first few years. Lottery proceeds flatten not only because their novelty fades, but also because residents initiated into gambling branch out into other forms of gambling, including online gambling and anything offering quicker payoffs than lotteries.

In the long run, studies have shown, lottery states are left with lower per-capita spending on education than states without lotteries. This is the next step for N.C.'s lottery.

MORAL PROBLEMS

Studies have repeatedly found another undesirable byproduct of state lotteries: by far the biggest purchasers of lottery tickets are the poor, minorities, elderly, and high school dropouts.

This is not unknown to state lottery commissions; indeed, more lottery advertisements and sales outlets target low-income neighborhoods, even as revenue from those sales generally support wealthier students. As lottery fatigue sets in, that problem exacerbates, as lottery commissions spend more money

on advertisements.

This problem is also infesting North Carolina's lottery. A JLF study last year found that the best predictors of a county's lottery sales to adults 18 or older were its poverty rate, property tax rate, and unemployment rate (see chart).

Beyond taking advantage of the poor to raise revenue, which already offends the mores of many concerned North Carolinians, the lottery also keeps the state in the position of endorsing and promoting an activity that many of its citizens believe is immoral.

One need not oppose legalized gambling to oppose a state lottery. At least privately operated casinos, horse tracks, or friendly poker games do not implicate government officials in swindling anyone and have the virtue, unlike a government-monopoly lottery, of offering choice and competition to improve the odds of winning.

Moreover, at least with horse racing there is the potential for rural communities in North Carolina to expand their horse breeding and training industries.

Another concern has to do with children and families. Lottery advertisements by design constitute a massive effort to communicate what would appear to be a government-approved message to young people that the way to get ahead in life is not to study and work hard, but to gamble.

For the vast majority of people, this message offers a false hope and, if heeded, could result in significant harm. It also clashes in a fundamental way with what most North Carolina parents seek to teach their children.

RECOMMENDATIONS

1. End the North Carolina Education Lottery. Its origin is suspect, its performance is subpar, its history is doubtful, and its manifold negative effects are sure.

2. If that is not feasible, then end the lottery as it is and consider legalizing other forms of gambling that can then be

taxed. This option would remove the state from endorsing and promoting an activity many North Carolinians find immoral, let alone counterproductive to the responsible message that society rewards education and hard work.

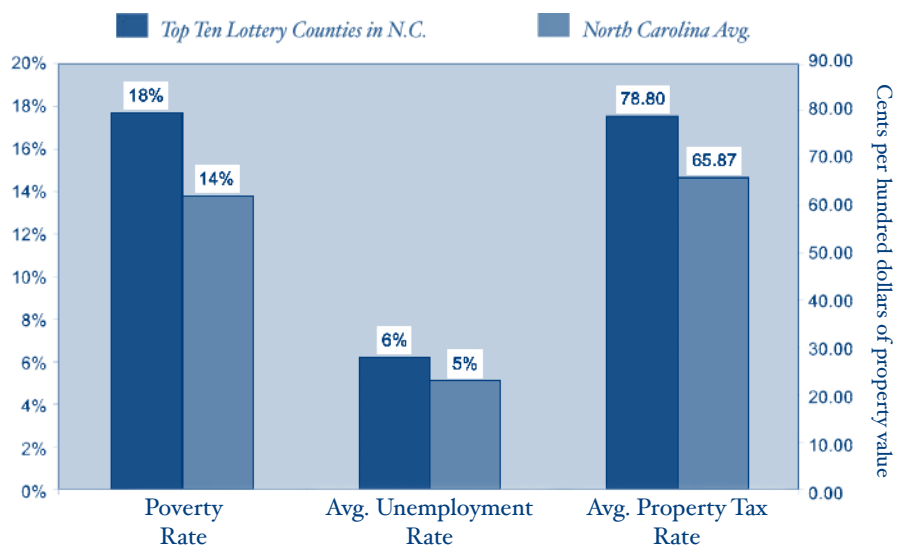
It would also end the exploitation of the poor and allow for new industries (horse breeding and training, for example) to build within the state.

3. If that is not feasible, then end the lottery as it is, then recraft and pass a lottery bill the right way, in accordance with the state Constitution. The next recommendation will offer a reform for the lottery formula also worth considering here.

4. If ending the lottery is not feasible, then at least pass legislation that puts lottery proceeds to proven good uses of education money. The current lottery formula places much greater emphasis on class-size reduction and pre-kindergarten programs — programs the state's own assessment has found haven't improved students' performance.

A reformed lottery formula would focus especially on construction (with emphasis on high-growth school districts) and also include funding for charter schools and incentives programs to reward school districts and administrators who find innovative, low-cost solutions to facilities needs.

The Best Predictors of a County's Lottery Sales to Adults: Its Poverty, Unemployment, and Property Tax Rates*



* Numbers through 2/10/07.

Source: Joseph Coletti, "Eastern NC's Lottery Bug," John Locke Foundation *Spotlight* No. 316, March 21, 2007, www.johnlocke.org/spotlights/display_story.html?id=165.

HIGHER EDUCATION POLICY



North Carolina's system of public higher education absorbs a substantial part of the state's budget — in Gov. Easley's 2007 budget recommendations, almost 18 percent went to higher education. State spending on higher education is usually justified on public-benefit grounds, namely that increased education and training for those who attend colleges and universities actually benefit everyone because the graduates will add so much to the economy and culture.

In terms of governmental appropriations for higher education, North Carolina is one of the states that most heavily subsidizes its university system, with more than 48 percent of the dollars spent on state colleges and universities coming from government appropriations. The median for the country is 37 percent.

Some states manage to run their higher education systems with only about one quarter of the funds coming from government appropriations. In Michigan, for example, only 26 percent of the funding comes from the state; in Colorado, only 22 percent.

The cost of higher education — both to taxpayers and to families paying tuition — has many people asking about the relationship between costs and benefits.

ARE THE EDUCATIONAL BENEFITS DECLINING?

It is generally assumed that earning a college degree significantly enhances an individual's knowledge and skills — his "human capital" — and thereby enables him to obtain good employment and contribute more to society. While that assumption may have been sound several decades ago, more and more evidence points to a persistent erosion of the college curriculum and academic standards. Because of what has been called the "dumbing down" effect, the benefit of the government's subsidization of higher education has become questionable.

The percentage of young people who go to college has increased dramatically since World War

II. Whereas only about 10 percent of high school graduates went to college in the 1940s, today it is about 70 percent. In their desire to expand, many colleges lowered their admission standards.

At the majority of schools that are non-selective, a large number of students are, as one professor calls them, "disengaged." They resist reading and doing written assignments, and instead they focus their attention on finding the courses that are the easiest. To keep such students happy, many professors have watered down their courses and inflated their grades. For those students, college is not about learning, but just having fun while buying a degree.

Evidence of the academic erosion is very clear in the most recent National Assessment of Adult Literacy (NAAL) report, issued in December 2005. That study evaluated more than 19,000 adults, many of them college graduates, as to their literacy in three different domains: prose, document, and quantitative. The findings were shocking. In prose literacy, for example, only 31 percent of college graduates scored in the "proficient" range (which required a score of only 70 percent).

When the same study was done in the early 1990s, 40 percent had registered as proficient — a clear indication that college standards have gone down. At the same time, the NAAL showed an increase in the percentage of college graduates with only "basic" or even "below basic" literacy. That means that a significant number of college graduates have the literacy skills of grade schoolers — a poor testament to the educational value of their studies.

GRADUATION DOESN'T ENSURE A GOOD JOB

Data from the U.S. Department of Labor confirms what one would expect from the NAAL findings, namely that we now have many college graduates doing work that calls for no advanced education. According to federal statistics, for example, 47 percent of fitness and aerobics trainers now have college degrees, as do 25 percent of retail sales supervisors, and 31 percent of airline flight attendants.



Further evidence of the decline of standards in higher education comes from the 2003 Report of the National Commission on Writing, which found widespread dissatisfaction among employers with the writing skills of college graduates.

It costs society a lot to put students through college, but many of them learn little and end up competing for mundane jobs. This brings about the problem of “credential inflation,” which is when employers insist that applicants have educational credentials that have little or no bearing on the ability to learn the job. In turn, that encourages still more people who don’t really have an interest in education to spend a lot of time and money in getting a degree.

RECOMMENDATIONS

1. The institutions of the University of North Carolina system should stop the practice of admitting academically weak students who need remedial course work. For those students who have academic weaknesses that can be overcome with a semester of work in English or mathematics, it is more efficient to have them do that in a community college or a private educational service.

2. The UNC system should implement a policy of assessing students’ fundamental knowledge and skills at the time of entrance and again at the time of graduation so as to determine how much educational value was added. High scores would be a plus for students who earned them; such a program would also identify university strengths and weaknesses.

3. UNC schools should reinstitute the idea of a rigorous core curriculum for students. Presently at many institutions, students can fulfill their general education requirements from a huge array of courses, many of which are narrow or trendy.

4. Both to save money and to improve instruction, UNC schools should reverse the trend toward lighter teaching requirements for professors by having them teach more courses and rely less on graduate assistants.

Annual Cost of Attending a Four-Year Public University

<i>Least Expensive</i>			<i>Most Expensive</i>		
<i>Rank</i>	<i>State</i>	<i>Cost</i>	<i>Rank</i>	<i>State</i>	<i>Cost</i>
1	Nevada	\$2,671	41	Maryland	\$7,045
2	Wyoming	\$2,874	42	Delaware	\$7,074
3	Florida	\$2,941	43	Illinois	\$7,158
4	Hawaii	\$3,226	44	Massachusetts	\$7,290
5	Utah	\$3,445	45	South Carolina	\$7,337
6	North Carolina	\$3,631	46	Ohio	\$8,457
7	Georgia	\$3,632	47	New Hampshire	\$8,458
8	Louisiana	\$3,679	48	New Jersey	\$8,649
9	New Mexico	\$3,701	49	Pennsylvania	\$8,710
10	Oklahoma	\$3,806	50	Vermont	\$9,279

Source: *The Chronicle of Higher Education—Almanac Issue*, 2007-08, August 31, 2007, Vol. LIV, No. 3, pp. 38-95

JOB TRAINING

For state and local policymakers, the issue of job training requires a significant amount of rethinking. In 2005-06, total expenditures for job training and placement services in North Carolina exceeded \$476 million, including federal and local grants. The state budget of 2008-09 included more than \$49.2 million's worth of appropriations for job training and placement programs. Government training and placement programs in this state span 13 state departments and divisions and include 27 programs. Those numbers don't include spending on post-secondary education, degree-based training, and receipt-based adult education through the state's community colleges and universities.

Despite vast sums of public monies being spent on such programs, the benefits are difficult to quantify. The problem is not specific to North Carolina, however. Over the years, economic research in job training has so consistently found government-training programs to be wasteful, inefficient, and sometimes even counterproductive that the focus of recent research has been to understand why they are so ineffective. In stark contrast, the benefits of private and company-sponsored job training are demonstrably positive and significant.

GOVERNMENT PROGRAMS FAIL

Most government training programs provided specifically to disadvantaged or other targeted populations fail to provide significant, long-term benefits. The Government Accountability Office studied 61 job-training programs in 38 states. Its conclusion was that those programs helped program beneficiaries find only "dead-end jobs." The GAO did not find that the poor in those programs received either the education or the training necessary to advance.

One study of the Job Training Partnership Act (JTPA) found that the program had no statistically significant effect on either the average earnings of young females or their employment, and even had a large (7.9 percent) negative effect on the earnings of young males.

In North Carolina, these programs have also provided little benefit. The most recently obtainable outcome data for North Carolina's programs continue to show only modest benefits. Only about one-fourth (29 percent) of JTPA clients entered employment as a result of being in the program, and 26 percent were still employed after 90 days. That same proportion of Employment Security Commission (ESC) job office clients were placed in jobs. About two-fifths (41 percent) of Vocational Rehabilitation clients found employment after completing the program.

State agencies have ceased publishing those outcome data, however. It's not too much to speculate that the reason could be that their demonstrable benefits — especially weighed against their exorbitant costs — are so slight.

Why don't these well-intentioned programs work? Many analysts believe that government training programs, regardless of their design, are doomed to failure because they lack the incentives that a private-sector trainer — or a public college competing for students, for that matter — has to place trainees in jobs successfully.

Private and company-sponsored training is fundamentally enhanced by ownership in the training process by both trainee and trainer. Private providers are also more likely than government to keep up with the latest occupational trends and needs.

A large source of private job training is on-the-job training. For example, an estimated 31 percent of workers received formal professional and technical training from their current employer, and 28 percent received informal professional and technical training from their current employer.

The returns to on-the-job training are rather obvious. Employers ensure that employees learn the skills that are necessary to accomplish tasks in their jobs, and employees gain not only those skills but also the assurance of job stability, since an employer would not invest in a resource he intended to jettison. Employers *and* employees exit the process with more useful resources now and in the future.

Skills, regardless of where or how they are acquired, show the strongest correlation with economic success. If one wants to improve the employment and earnings potential of workers while getting the best return on postsecondary education and training expenditures, the key is to match occupational choices with an appropriate provider of job training, which is, more likely than not, an employer rather than a school or training center.

Studies show that many workers learn their most valuable skills on the job, and are thus best served simply by having good job opportunities available rather than access to government-run training programs.

Even charitable providers of training for the “hard to employ” prove to have greater placement results than government training and placement programs. Often, these charitable programs start by addressing “soft skills,” which are those life skills that make a person employable at any job: timeliness, proper attire, good hygiene, good work ethic, respect for others, a good attitude toward superiors and colleagues, good communication skills, sobriety, etc.

Why that fundamental approach works is because poverty in America is mostly *self-inflicted*, owing to poor decisions and behaviors, especially a weak work ethic. Those programs are aimed at adults already having made many of those poor choices, however.

To help prevent the next generation of adults from making poverty-inducing choices, the state’s education system should allow concerned educators to augment their curricula to meet localized needs, including teaching personal responsibility, the importance of soft skills, and other such ideas where there is particular community need or parental interest.

More charter schools, competition among area schools, and school choice would be vital to this effort.

RECOMMENDATIONS

1. State leaders should consolidate state training programs as much as possible to reduce redundancy and increase oversight. Employees and contractors should be compensated according to performance, such as by paying them a percentage of the income their clients subsequently earn. Those eligible for

training should have the option of converting some of their aid into cash to subsidize private employment at a (low) training wage.

2. All North Carolinians should be allowed to save money tax free in an educational savings account (ESA) for future post-secondary education and training investments, including retraining after a job loss.

3. The state cap on charter schools should be lifted to allow educational innovation and competition to flourish, and school districts should contribute to school choice and competition through open-enrollment policies and the end of forced busing, allowing voluntary busing to district schools of the parents’ choice.

North Carolina Job Training, Job Placement, and Related Programs and Services* (Actual Requirements, 2005-2006)

<i>State Dept. or Division</i>	<i>Reqs. (\$)</i>
Dept. of Labor	\$1,621,377
Dept. of Administration	\$2,137,354
Dept. of Env't. and Nat'l Resources	\$667,639
Div. of Central Mngt. and Support	\$15,589,903
Div. of Aging and Adult Srvs.	\$2,088,345
Div. of Social Services	\$2,624,550
Div. of Srvs. for the Blind, Deaf, and Hard of Hearing	\$14,103,339
Div. of Vocational Rehabilitation	\$104,122,187
Dept. of Correction	\$3,867,584
Comm. Coll. System Office	\$19,041,717
Dept. of Labor	\$56,662
Dept. of Juvenile Justice and Delinquency Prevention	\$61,475
Dept. of Commerce	\$310,166,304
Total	\$476,148,436

* Includes federal, state, and local grants.

Source: Jon Sanders, “Job Training That Works,” John Locke Foundation *Spotlight* No. 344, Feb. 28, 2008.

ECONOMIC DEVELOPMENT



While economic development has dominated the agendas of many governors, legislators, and local elected officials in North Carolina, it is one of the most misunderstood activities that governments undertake.

Politicians love to attract attention to themselves through job announcements and ribbon cutting, but those are a poor substitute for less glamorous policies that promote free markets, entrepreneurship, and overall economic growth.

Such policies would allow for the maximum amount of opportunity and prosperity for all North Carolinians, not just a favored few at the expense of everyone else. They would respect the rule of law, protect private property, promote competition, and allow markets to operate freely.

ANALYSIS

The idea of economic development policy has come to mean policies meant to funnel tax and other kinds of subsidies to businesses and/or regions in the state with the purpose of expanding economic activity, particularly employment.

The problem with this approach is that while subsidies may benefit the targeted business and entice it to locate its operations within the state or a particular county or region, they harm existing businesses and other taxpayers. Such policies do not generate net benefits for the state. Instead they simply hurt some and help others.

There's no such thing as a free subsidy. First, when the state, city, or county decides to use tax dollars to entice a new company to set up shop, that money has to come from somewhere. Other businesses and their employees must pay more in taxes and other costs to support the subsidized industry. This is why such programs are often referred to as corporate welfare.

Since higher taxes are an added cost of doing business, these subsidies depress economic growth for those businesses not receiving the subsidy. In reality the subsidies end up being a mechanism for

transferring wealth from existing businesses and other taxpayers to the subsidized businesses and the people who work for them.

Higher taxes for the state at large are not the only way existing businesses must pay the cost of these subsidies. The subsidized entrants into the market add to the demand for resources, such as workers and land. This drives up costs for all businesses.

In the area of labor the pressure would be felt by any business that is employing similarly skilled workers in the area of the state where the subsidized new business locates. This effect is particularly pronounced if the unemployment rate is already low. It means that the existing businesses not only have to pay for the subsidies through higher taxes, but, adding insult to injury, they may also face higher production costs.

If the economic development subsidy involves exemptions from local taxes, then the effect is to shield the subsidized businesses from bearing some or all of the costs of infrastructure needs that their presence generates. These include the costs of road construction, police and fire services, new school construction, and other public facilities.

It has also become clear that many communities will have to make additional investments in reservoirs and other new sources of water. Bonds will be floated to pay for all this, which will have to be paid back with future property and sales taxes. Corporate welfare schemes, under the guise of economic development policy, simply allow these new, subsidized businesses to be free riders. Again, this adds to the tax burden for the rest of the community and the state.

A partial list of corporate welfare programs would include:

- overseas advertising subsidies in the departments of Commerce and Agriculture;
- special marketing programs for industries as varied as film production and meat goat farming;
- state subsidies for private ventures such as the N.C. Biotechnology Center's venture capital fund;

- state services offered below cost to agricultural and other businesses;
- regional subsidies such as the state's investment in the Global TransPark in Kinston; and
- special tax breaks for "job creation" in distressed communities, worker training, and research and development.

Programs that support all of this activity include the Golden LEAF Foundation, The William Lee Act, and the One North Carolina Fund.

ECONOMIC GROWTH, NOT ECONOMIC DEVELOPMENT

Economic development policy, as it has developed, has become simply a term used for state management of entrepreneurial activity and an excuse for funneling favors to privileged businesses and industries.

The fundamental premise behind it is that the state will reward specific companies that it deems worthy. If a company will run its business the way politicians and state economic development planners think it should be run, then the subsidies will flow in its direction.

If it locates in the right place, if it hires the right amount of workers, if it compensates the workers with the correct mix of salary and benefits, and if it is producing the right products or providing the right services, then it will qualify for the privilege of being subsidized by the citizens of North Carolina. This is government central planning, plain and simple.

The entire focus of policy should shift away from this approach and toward a concern for statewide economic growth. That is, it should focus on creating an economic environment that will maximize gross state product (GSP).

A growing economy will create jobs, lift people out of poverty, provide consumers with affordable products, etc. It is about creating wealth and prosperity and not shifting it from less favored businesses and taxpayers to those who are more favored.

The general approach to policy should be as follows:

- Eliminate disincentives to investment and entrepreneurship, typically brought about by regulations and taxes.
- Create an overall environment that is conducive to efficient, market-motivated investment.

- Create conditions statewide such that all businesses, entrepreneurs, and investors have an equal opportunity to compete for capital, resources, and labor based on efficiency and success in satisfying customers.

RECOMMENDATIONS

1. Eliminate tax biases and multiple layers of taxation against saving, investment, and entrepreneurship. This could be accomplished by adopting a low, flat-rate, consumed income tax. That is, all income used for saving and investment would be exempt from taxation.
2. Abolish the corporate income tax or at least dramatically lower the rate.
3. Eliminate all estate and inheritance taxes, which are additional layers of taxation on saving.
4. Lower the overall level of taxation by cutting state spending.
5. Keep the regulatory burden to a minimum. All proposed regulations should meet a rigorous test of benefit-cost analysis with the presumption that no new regulations are implemented unless the benefits from their stated objectives outweigh the costs to the state's consumers and businesses.
6. The state should devote its resources to core functions and to making sure that the services that it is providing are of high quality, are consistent with the citizens' desires, and are conducive to economic growth. This would especially include safety and law enforcement, education, water and sewer services, and roads.

REGULATORY REFORM

Regulation is the “hidden tax” that governments impose on families and private firms. While state and local governments clearly have an interest in developing sensible regulation, regulations often are developed without examining their costs and their impact on all regulated entities.

REGULATORY BURDEN

Although state agencies certainly develop burdensome regulations, the state legislature is more responsible for creating the massive regulatory burden hurting North Carolinians.

In a 2005 JLF survey of more than 600 North Carolina business leaders, they ranked the regulatory burden as the second most important factor reducing the state’s economic competitiveness (the tax burden was ranked No.1). About 81 percent said that the cost of most government regulations exceeded their benefits. Those results are consistent with JLF’s 2004 survey in which regulatory burden also was ranked second. In 2002, regulatory burden was ranked fourth, however — indicating that the problem is only getting worse.

A great example of North Carolina’s disregard for any type of cost-benefit analysis is the so-called Clean Smokestacks bill enacted in 2002. Designed to impose strict regulations on coal-fired power plants, the bill passed even though its benefits will be limited or nonexistent.

Air quality in North Carolina has generally been improving for decades, and violations of even the tighter federal standards on ground-level ozone have also been declining. The new state regulations will not appreciably affect human health, but they will further inhibit the state’s economic growth.

N.C. REGULATION RESTRAINS COMPETITION

Regulation is supposed to promote competition and protect the interests of consumers. In North Carolina, as in other states, however, some regulation exists to reduce competition and, in effect, raise prices for consumers. Here are two examples:

- *Certificate-of-Need Laws.* State law mandates that health care providers must obtain a certificate of need to do such simple things as replace outdated equipment. A hospital must get permission from a government agency to add even a single bed to its facility. Absent government approval, new hospitals cannot be built, and existing hospitals cannot expand to meet the needs of local citizens.

- *Occupational Licensing.* North Carolina requires licenses for numerous occupations, such as barbers, landscape architects, and acupuncturists. But state licensing is frequently unnecessary, and a less restrictive approach — such as a private and optional certification system — would be more appropriate. An optional system would give consumers the choice between certified professionals and others who decided, for whatever reason, not to seek certification.

Barber licensing is one example of an occupational law that should be eliminated. North Carolina’s barber licensing law is so extreme that it requires almost anyone engaged in “barbering” to have a certificate. In North Carolina, if you give a friend, cousin, or anyone who isn’t an immediate family member a facial for free, but you don’t have a barber’s license, you are breaking the law.

REGULATION’S IMPACT ON SMALL BUSINESS

According to the U.S. Small Business Administration (SBA), “More than 92 percent of businesses in every state are small businesses, which bear a disproportionate share of regulatory costs and burdens.” Small businesses have different resources and compliance capabilities than larger businesses.

For this reason, the SBA has been encouraging states to adopt “regulatory flexibility acts”: statutes that require agencies, when developing regulations, to take into consideration the unique factors that small businesses will face when trying to comply with them. Unfortunately, North Carolina does not have a small business regulatory flexibility act.

As part of its model legislative language, the SBA

identifies five factors any state should consider in its small business regulatory flexibility analysis in order to reduce the impact of the proposed regulation on small businesses:

1. Establish less stringent compliance or reporting requirements for small businesses.
2. Establish less stringent schedules or deadlines for compliance or reporting requirements for small businesses.
3. Consolidate or simplify compliance or reporting requirements for small businesses.
4. Establish performance standards for small businesses to replace design or operational standards required in the proposed regulation.
5. Exempt small businesses from all or any part of the requirements contained in the proposed regulation.

HOW MUCH REGULATION DOES N.C. HAVE?

One measurement of regulatory growth is the number of pages published in the North Carolina Register each year. The annual rate roughly doubled between 1987 and 2007 (see chart, “Measuring the Trend in State Regulatory Activity”).

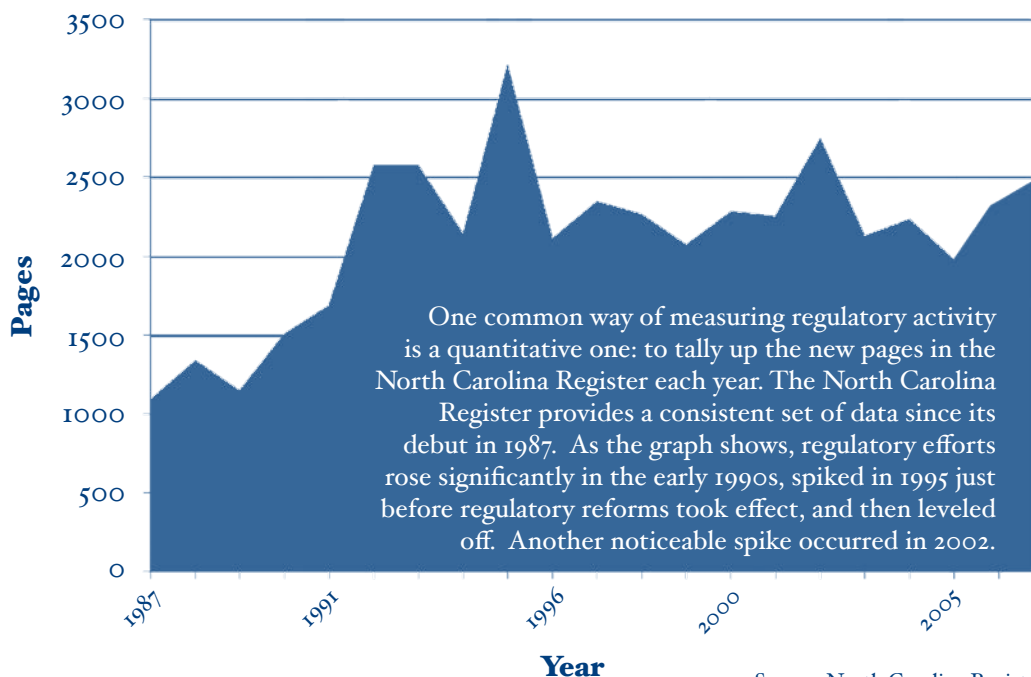
In 1995, the North Carolina General Assembly began to address the state’s role in regulatory overkill by enacting a bill that gives the Rules Review Commission the power to review proposed regulations before they became law. But before the law became effective Dec. 1, 1995, some 24 state departments and boards filed more than 2,250 proposed rule changes to beat the deadline. This breathtaking exhibition of the cavalier attitude state bureaucrats have toward regulatory reform is but one more reason lawmakers should take more extensive action to reform state rule-making and enforcement agencies.

The 1995 reforms certainly helped, but the numbers still are about double what they were in 1987. The agencies remain a major source of regulatory overkill, but as mentioned previously, the legislature is the primary source of excessive regulation.

RECOMMENDATIONS

1. Eliminate regulations other than those necessary for promoting public health and safety and combating fraud in markets such as financial services. Where possible, employ compliance mechanisms other than fines, such as consultations with private firms and educational programs for professionals. Sunset all new state rules after two years to allow an assessment of their real-life costs and benefits.
2. Review existing regulations and eliminate redundant, outdated, and unnecessary regulations.
3. Repeal laws that create government restraints of trade, such as the certificate-of-need laws and unreasonable occupational licensing laws. Regulations should help promote competition, not restrict it.
4. The legislature should do its own cost/benefit analysis on proposed legislation that would have even a modest economic impact on North Carolinians. This analysis could be similar to the fiscal notes developed by the fiscal research staff.

Measuring the Trend in State Regulatory Activity, 1987-2007



One common way of measuring regulatory activity is a quantitative one: to tally up the new pages in the North Carolina Register each year. The North Carolina Register provides a consistent set of data since its debut in 1987. As the graph shows, regulatory efforts rose significantly in the early 1990s, spiked in 1995 just before regulatory reforms took effect, and then leveled off. Another noticeable spike occurred in 2002.

Source: North Carolina Register

PROPERTY RIGHTS

Property rights have received renewed attention in large part because of the *Kelo v. City of New London* case and the resulting public outcry. In that case, the United States Supreme Court held that the government could seize private property solely for economic development reasons.

In other words, if the government can find a better economic use for your house, it can seize it and transfer the property to a private developer.

This opinion has sent shockwaves throughout the country. If anything good came out of *Kelo*, it was putting eminent domain abuse and other property-rights violations (e.g., forced annexation) on policymakers' radar screens.

EMINENT DOMAIN: A CONSTITUTIONAL AMENDMENT IS NECESSARY

Eminent domain is the government's power to seize private property. The Fifth Amendment of the United States Constitution states "Nor shall private property be taken for public use, without just compensation." After *Kelo*, the term "public use" basically has been deleted from the U.S. Constitution.

In response to *Kelo*, seven states already have passed constitutional amendments to protect against eminent domain abuse, including neighboring states Georgia and South Carolina (see chart).

The North Carolina House passed an eminent domain constitutional amendment in 2007, but the amendment died in the Senate, as is usual with anything that protects property rights. There was bipartisan support for the amendment — the vote was 104-15.

This bipartisan support demonstrated the critical need for an amendment in North Carolina. The state constitution has the weakest property rights protections in the country.

It is the only state in the country that does not have an express constitutional provision that limits the taking of private property for a public use with just compensation.

FORCED ANNEXATION

In North Carolina, a city may force property owners living in unincorporated areas to become a part of the municipality. Under state law, these affected property owners have no say about the annexation — there is no vote or representative process.

Cities must be allowed to grow through annexation, but this type of forced annexation is undemocratic and an embarrassment to the state. Only a handful of states still have this type of forced annexation. Virtually every state in the country has abandoned this outdated practice.

Municipalities can do almost anything they want when it comes to forced annexation because the law allows them to. The major problem with forced annexation is not municipalities abusing the law, but the law allowing municipalities to abuse citizens.

A SHAM OF A LAW: THE WATER AND SEWER EXAMPLE

One of the "best" examples of the abusive nature of the annexation law is how the provision of water

States that Passed Constitutional Amendments Protecting Against Eminent Domain Abuse in 2006

State	Voting Results	
	percent in favor	percent opposed
Florida	69.1%	30.9%
Georgia	82.7%	17.3% †
Louisiana	55.0%	45.0%
Michigan	80.1%	19.9%
Nevada*	63.1%	36.9%
New Hampshire	86.0%	14.0%
North Dakota	67.5%	32.5%
South Carolina	86.1%	13.9%

* In Nevada, voters overwhelmingly approved a new amendment, but it requires passage in two consecutive general elections to become law.

† These results were based on 98 percent of precincts reporting.

Source: Castle Coalition

and sewer service is handled. Many people think that water and sewer must be provided to property owners within two years after the effective date of the annexation.

The reality is that the two-year requirement only applies to when municipalities must construct major water and sewer lines, not the connecting lines that travel through neighborhoods and eventually hook up to properties.

If affected property owners do not know about an obscure detail to request water and sewer within five days after the public hearing, they may not be provided water and sewer for more than a decade. This is precisely what is happening to the thousands of people in Fayetteville who are likely to wait as long as 15 years for water and sewer service, if not longer.

FORCED ANNEXATION: FAILING TO MEET ITS PURPOSE

According to the North Carolina Supreme Court in *Nolan v. Village of Marvin* (2006), the primary purpose of involuntary annexation, as described in the annexation statute, is to provide meaningful and significant municipal services to fringe geographic areas.

This purpose has been lost. Municipalities provide services to areas that do not need services, in many instances duplicating services. They target affluent areas, by their own admission, because of the additional tax revenue. The opposite is true as well. Municipalities ignore communities that do need services. As research from the UNC Center for Civil Rights and the Cedar Grove Institute for Sustainable Communities shows, many minority communities that need services have been excluded from municipalities.

RECOMMENDATIONS

I. Pass a constitutional amendment that would, among other things:

- Expressly prohibit the seizure of private property for economic development and for all private uses (except as necessary for common carriers). A general prohibition on seizing property for economic development and private reasons, though, is not enough protection because the government always will come up with an alternative reason for taking property.

In fact, there genuinely may be multiple reasons for taking property. An amendment must recognize this problem and close end runs around the law. It must ensure that if there is some economic development reason for taking property, it is clearly incidental to a public use.

The most common pretext for taking property for economic development reasons is “blight.” Blight or urban redevelopment laws have been abused for two primary reasons. The definition of “blight” often is subjective and excessively broad, and property in pristine condition can be seized so long as it is in a “blighted area.”

North Carolina’s legislature amended the state’s urban redevelopment law a couple of years ago to address these critical problems — however, an amendment is needed to protect against this pervasive form of eminent domain abuse.

- Clearly define “blight” so that only properties that cause a clear health and safety risk can be seized.
 - Define just compensation to ensure that individuals are made “whole.”
 - Require the government to have the burden of proof to demonstrate that (1) a taking is necessary and no reasonable alternatives exist, (2) a taking is legal, and (3) the compensation offered is just.
2. Reform the state’s annexation law:
- Allow citizens in the affected area to have a vote or some form of meaningful representation (such as county approval) prior to the passage of an annexation ordinance.
 - Codify the clear holding of the North Carolina Supreme Court case *Nolan v. Village of Marvin* (2006): Prohibit a municipality from being able to annex an area unless it provides meaningful and significant benefits to affected property owners.
 - If an area already has major municipal services (such as water and sewer) and a municipality is unable to prove that the services are inadequate, then it should not be able to annex that area, except through voluntary annexation.
 - Prohibit a municipality from annexing any contiguous area if another contiguous area is in more dire need of municipal services — this will help protect against the problem of minority communities being excluded from municipalities.

TRANSPORTATION POLICY



Highways and transportation facilities are some of the most visible programs that state and local governments operate. But they are not without controversy. Some believe that North Carolina has invested too much money in highways and not enough in mass transit, but others observe continuing declines in road conditions, rising congestion, controversial project selection, and directionless system management. The state's needs are estimated at \$50 billion to \$70 billion over 25 years.

Transit systems receive significant capital operating subsidies, yet they attract less than 1 percent of commuters. Massive investments in light rail in Charlotte have failed to stem rising congestion. And major highway projects such as outer loop highways and the Global TransPark in Kinston have sparked debate about the proper level of spending and the ability of investments to spur development.

Reforming the scandal-ridden Department of Transportation also must be a priority. Transportation Board votes display lockstep logrolling for pet projects while real needs languish. Projects are approved without cross-state comparisons of worthiness or impact. The state's formulas for distributing money favor sparse rural areas at the expense of congestion-plagued cities. Discretionary "loop" projects get priority in small regions while those of large regions get delayed.

TRENDS IN TRANSPORTATION SPENDING IN NORTH CAROLINA

North Carolina taxpayers pay for state highways through taxes on motor fuels and vehicles. Expenditures from the state's highway funds have grown significantly in nominal dollars during the past 20 years to \$2.3 billion in FY 2006-07, and North Carolina currently levies the 15th highest tax rate on motor fuels in the nation. The rate increased from 24.2 cents per gallon in 2004 to 30.2 cents per gallon in 2008. But adjusted for inflation and vehicle-miles traveled, highway expenditures actually decreased during the past two decades. Per-capita state and lo-

cal spending on transportation grew at a slower rate than spending on education, health care, and overall government spending.

A recent national study for the Reason Foundation by UNC-Charlotte's David Hartgen found that North Carolina's highway system, ranked eighth in the U.S. in 1987 for quality and efficiency, had fallen to 36th by 2003. Although the state has recently improved its overall ratings, only two states have a higher share of congested urban interstates — California (83 percent) and Minnesota (79 percent) — than North Carolina (70 percent). The state also ranks 41st in deficient bridges, 25th in the condition of urban interstates, 40th in rural interstate condition, and 39th in the condition of rural primary roads.

A detailed study of congestion in the state's 17 major cities, also by Hartgen, found that congestion was rising rapidly in all regions and was expected to double in the next several decades. In the largest cities (Charlotte, Raleigh, and Durham), transportation plans would not even keep up with traffic growth, and 40-60 percent of funds were targeted to transit which carries less than 1 percent of commuters.

But the Board of Transportation, the governor, and the General Assembly have ignored the dismal condition of North Carolina roads. Since 2002 they have diverted about \$1 billion from the Highway Trust Fund (HTF) to the General Fund. The HTF obtains 99 percent of its funds from drivers and is supposed to be used for building roads.

Given the continuing deterioration of North Carolina's road system, there is no good reason to continue forcing drivers to drive on inadequate roads while their gasoline tax funds and other tax funds are used to subsidize other government spending. The state is risking its economic future by permitting its road system to decline.

THE TRANSIT DISTRACTION

According to a recent Locke Foundation transportation study from Hartgen, the ten largest transit



systems in the state cost \$127 million and are on target to reach \$200 million in operating costs by 2010. All that spending impacts only about one-quarter of one percent (0.28) of the travel in these areas, however. What is worse, the promised reductions in congestion and air pollution do not exist. If all ten public transit systems stopped service tomorrow, congestion and air pollution in these cities would increase by only one-quarter of one percent.

Building rail systems in Charlotte, the Triangle, and the Triad will not have the promised results. Charlotte's new light rail line, costing more than \$500 million, carries about 11,000 riders daily, less than 1/2 the capacity of a single lane of freeway and just 1/10 the traffic on nearby Interstate 77. It has had no effect on even nearby road traffic. Yet Charlotte's long-range transportation plan proposes to spend more than half its money on transit expansions. Raleigh's proposed transit plan would spend more than \$2 billion but the federal government has previously indicated that it will not meet funding criteria.

More promising actions for relieving traffic congestion and pollution include new computer technologies and the use of "congestion pricing" on limited-access highways to charge variable tolls depending on the time of day and amount of congestion. North Carolina should also pursue public/private partnerships to build new highways and high-occupancy-toll (HOT) lanes on existing highways using electronic "no toll booth" collection technology. However, these actions alone will not relieve growing congestion. The sober truth is that more road capacity will be needed.

RECOMMENDATIONS

1. State officials should focus their attention on improving the efficiency and quality of North Carolina's highway system. More highway capacity, new technologies, and tollways should be used to relieve congestion and promote economic development. Projects should be selected according to worthiness, not geography.

2. The state should end all subsidies for the Global TransPark. Furthermore, the state should issue a request for proposals for the sale of the state ports at Wilmington and Morehead City and the state-owned North Carolina Railroad.

3. The Department of Transportation should be restructured to perform its job better. Reforms should include downsizing the Board of Transportation and making it an advisory panel only, merging highway divisions and eliminating bureaucracy, using competitive contracting for design and planning functions, and giving a portion of gas taxes collected directly to local governments for local needs. A state infrastructure bank should be established for assisting localities, as South Carolina has done.

4. State lawmakers should end the diversion of highway user fees to non-highway uses. All revenues from motor fuels and auto-sales taxes should be dedicated to road construction and maintenance. The "loop" program should be ended and replaced with project selection based on worthiness criteria. Together with reductions in low-priority road building, administrative savings, and the use of public and private tollways, dedicating gas and car taxes only to their appropriate uses would yield \$470 million a year in additional highway spending. That would eliminate the gap between legitimate needs and expected revenues over eight years, according to an analysis conducted for the John Locke Foundation in 2000.

5. Innovative designs for major roads should be considered, to reduce impacts but provide needed capacity. The state should insist that local planners spend state dollars on major state roads, rather than delay them in favor of less important local projects.

Overall Road Quality and Efficiency Ranking, 2006

<i>State</i>	<i>Rank</i>
South Carolina	6
Georgia	10
Virginia	16
Tennessee	19
North Carolina	23
Alabama	29
Florida	41

Source: David T. Hartgen and Ravi Karanam, "Progress Continues: Performance of State Highway Systems, 1984-2006," Reason Foundation, June 2008. On the web at www.reason.org.

TORT REFORM

There is a legitimate need for lawsuits. Citizens should be able to go to court and get fairly compensated for the harm caused by negligent acts of individuals or businesses. However, the civil justice system is being abused. Plaintiffs receive damages beyond what is necessary or appropriate. Individuals and businesses that should never be sued find themselves paying large attorneys' fees to defend against frivolous lawsuits.

North Carolina has several specific problems that should be addressed. First, there is a medical malpractice crisis in the state because physicians are paying exploding premium costs. These increases serve only to drive up the costs of health care for patients. Second, businesses and other defendants are forced to pay large sums of money for noneconomic damages that go well beyond compensating victims. Third, the tort system has rules in place that are grossly unfair to defendants. Significant civil justice reform (or tort reform) is a critical way to alleviate the extensive legal costs that ruin businesses and stifle innovation.

MEDICAL MALPRACTICE CRISIS

According to a 2007 report by the American Medical Association (AMA), North Carolina is one of 17 crisis states "where medical liability insurance rates force physicians to retire early, eliminate high-risk procedures or leave the state." The AMA, when previously describing the problems in North Carolina, identified the tripling of the annual number of settlements greater than \$1 million in medical liability cases between 1993 and 2002, the massive increase in liability insurance premiums (see chart, "Base Premium Rate for N.C. Medical Professional Liability Insurance"), and the fact that the state does not cap noneconomic damages.

NONECONOMIC DAMAGES

Generally, there are two major sources of damages in tort cases, compensatory damages and punitive damages. First, compensatory damages, which

are designed to compensate plaintiffs for their losses, generally consist of economic damages and noneconomic damages. Economic damages represent the actual economic harm that has been or will be sustained by plaintiffs, such as lost wages and medical expenses. Noneconomic damages are awarded to plaintiffs for issues such as pain and suffering, loss of consortium, and mental anguish. Second, punitive damages are awarded to punish a defendant for severe behavior such as intentional torts.

In 1995, North Carolina took a big step to reform the civil justice system by placing a cap of \$250,000 on punitive damages. However, the state also needs a cap on noneconomic damages. Noneconomic damages are a subjective way to measure an individual's pain and suffering. As a result, excessive sums often are awarded, based mostly on subjective emotional factors. Noneconomic damages are not supposed to be awarded to punish a defendant, like punitive damages, but to help make the plaintiff "whole."

A 2004 JLF report summarizes the need for a cap on noneconomic damages: "But a cap of two times that amount [two times \$250,000] (as exists in Maryland, for example) would preclude jury awards of '\$1 billion in pain and suffering,' as sometimes happens when juries are precluded (as they are in North Carolina) from granting huge punitive awards. A cap on noneconomic damages, in other words, prevents 'pain and suffering' from becoming an end run around caps on punitive damages, such as North Carolina's. Such a cap is thus sorely needed in the TarHeel State."

UNFAIR TORT RULES

There are two rules in particular that create a grossly unfair system for defendants. First, there is the collateral source rule. North Carolina's collateral source rule prohibits a judge or jury from considering the fact that a plaintiff may have received compensation from a third party (usually a plaintiff's insurance company). As a result, the plaintiff

can receive money twice, from the defendant and the insurance company. Juries and judges should be required to consider compensation from collateral sources. In addition, for fairness purposes, they also should be required to consider any subrogation rights of third-party collateral payers (rights that require the plaintiff to pay back any compensation to the collateral payer, such as an insurance company, before the plaintiff receives any compensation).

Second, there is the rule of joint and several liability. This rule requires a defendant who may be found by a jury to be, for example, 5 percent responsible for the harm caused to the plaintiff to pay 100 percent of the damages, if the other defendants are not able to pay the plaintiff. Defendants should only have to pay a proportional amount of the damages based on the harm they caused — in other words, their fair share.

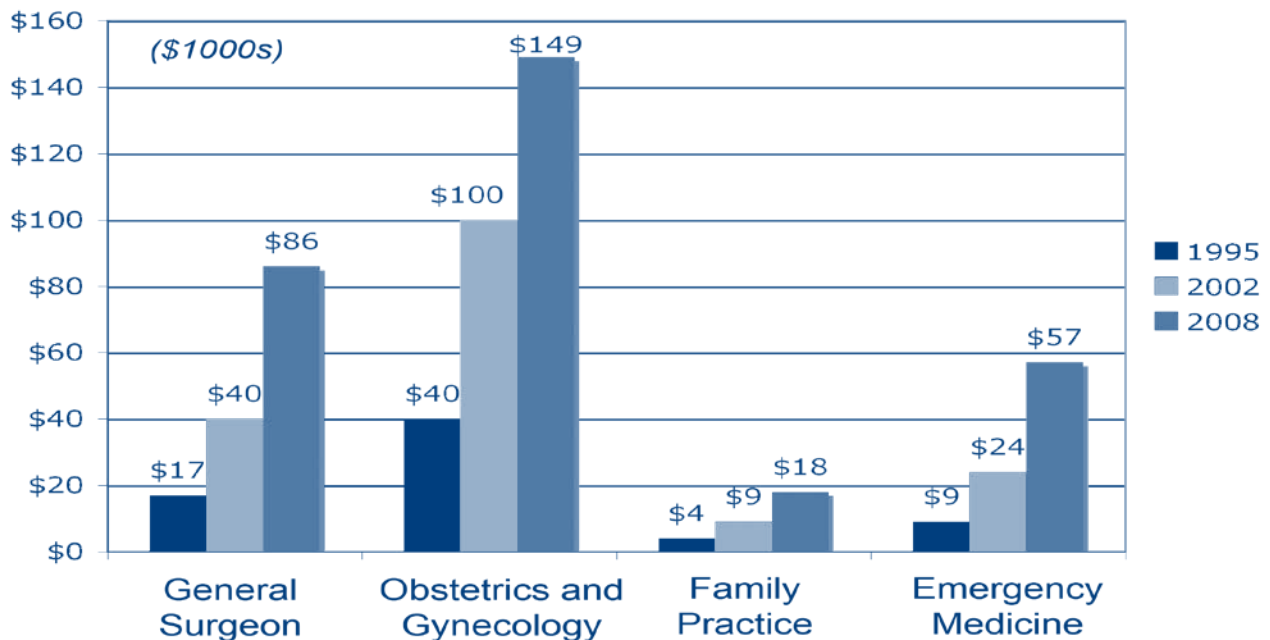
Generally, the defendant on the hook for 100 percent of the damages can sue the other defendants to try to get money from them. That still is an extreme hardship on the defendant, however. Some

argue that repealing this rule would hurt plaintiffs. It is unfortunate when plaintiffs are unable to recover damages from defendants, but this does not justify the government requiring a defendant paying more than his fair share.

RECOMMENDATIONS

1. North Carolina needs civil justice reform across the board, including reform to address the medical malpractice crisis.
2. Noneconomic damages should be capped at \$500,000.
3. The collateral source rule should be repealed.
4. The rule of joint and several liability should be repealed.

Base Premium Rate for North Carolina Medical Professional Liability Insurance: 1995, 2002, 2008 (Projected, in Thousands of Dollars)



Note: From 1995 to 2002, the actual increases were 127 percent for General Surgeons, 137 percent for Ob/Gyns, 115 percent for Family Practice physicians, and 153 percent for Emergency Medicine physicians.

Source: Medical Mutual Insurance Company of North Carolina (the state's largest medical malpractice insurer).

ENERGY POLICY

Energy is not only critical to the economy, but also to our health, safety, and general welfare. Energy is an input into every good and service. Our hospitals need electricity to operate the high-tech machines that provide us medical care. Fuel provides us the means to drive vehicles that give us the mobility that has transformed the nation.

We need to promote policies that ensure low-cost and reliable energy. Low-cost energy is not a luxury but a requirement to fill our most basic needs. As John Reinker of GE Global Research stated in a recent presentation titled “Future Energy”:

Societies have continually increased productivity through the harnessing of different energy sources, which has allowed for economic expansion and the development of the modern world The availability of abundant, low-cost energy is key to a modern society and a necessity for continued economic expansion.

SHOOTING OURSELVES IN THE FOOT

Despite the critical importance of low-cost energy, state policymakers have gone out of their way to increase the price of energy artificially, while wringing their hands about energy prices.

In 2007, the North Carolina legislature passed a controversial law, Senate Bill 3, which was literally drafted by special-interest groups. This bill mandates that utility companies generate 7.5 percent of their electricity through renewable sources of energy, such as wind and solar power.

According to the North Carolina Utilities Commission’s own estimate, the “partial” costs of this bill are staggering: by 2021 when the law is supposed to be in full effect, electricity customers will bear a cost of \$500 million a year.

North Carolinians are being forced to pay extra for their electricity (i.e., electricity taxes) so that renewable energy providers can have a guaranteed market for their cost-prohibitive and unreliable electricity.

THE NEXT ROUND

The North Carolina legislature is likely to consider numerous policy recommendations in the name of fighting global warming that will drastically increase energy prices (a detailed discussion of global warming can be found in the preceding chapter, Climate Change).

One of the primary policy recommendations coming from global warming extremists is a state or regional cap-and-trade program. It would limit the total amount of carbon dioxide that can be emitted by regulated parties. Because carbon dioxide emissions are primarily a result of burning fossil fuels to produce energy, cap-and-trade systems are effectively a limit on the amount of energy that can be produced.

The National Association of Manufacturers and the American Council for Capital Formation have studied the primary cap-and-trade bill recently considered by Congress (S. 2191). Their analysis helps provide a sense of what such a program could mean to North Carolina — there would be a devastating impact on North Carolina — Charts 1 and 2 show the impact the cap-and-trade program would have on gasoline and electricity prices in North Carolina, respectively.

GLOBAL WARMING ALARMISM AND ENERGY POLICY

Even global warming alarmists admit that there is no way to have any meaningful effect on temperature. To adopt policies that increase energy prices and thereby significantly harm the welfare of every North Carolinian is beyond irresponsible; it is unethical.

The need for wealth is critical to solve whatever problems North Carolina and the United States may face in the future. Low-cost energy is critical to wealth and to providing innovators the means to solving environmental problems.

On December 13, 2007, in an open letter to the Secretary-General of the United Nations, nearly one

hundred international scientists, economists, and leading scholars, including some Intergovernmental Panel on Climate Change (IPCC) members, argued:

It is not possible to stop climate change, a natural phenomenon that has affected humanity through the ages. Geological, archaeological, oral, and written histories all attest to the dramatic challenges posed to past societies from unanticipated changes in temperature, precipitation, winds, and other climatic variables. We therefore need to equip nations to become resilient to the full range of these natural phenomena by promoting economic growth and wealth generation...Attempts to prevent global climate change from occurring are ultimately futile, and constitute a tragic misallocation of resources that would be better spent on humanity's real and pressing problems.

RECOMMENDATIONS

1) Adopt policies that promote low-cost and reliable energy:

- Reduce the obstacles for the construction of coal and nuclear power plants.
- Pressure Congress to permit offshore drilling.

2) Fight policies that increase energy prices, such as a cap-and-trade program, and:

- Repeal Senate Bill 3.
- Do not force consumers to pay for costly and unreliable sources of electricity, such as wind, solar, and biomass.
- Protect the public from efforts to build grid-connected wind power plants that increase electricity prices, undermine the reliability of the electricity grid, and harm local communities.
- Eliminate costly energy-related subsidies that are just special-interest handouts.
- Require more transparency from the North Carolina Utilities Commission.
- If Senate Bill 3 still exists, require the extra costs (i.e., taxes) associated with renewable energy and energy efficiency to be itemized clearly on customer bills.
- Restructure the Public Staff — the Public Staff is supposed to be the consumer advocate for electricity customers, but instead has taken on environmental goals. It has even pushed for energy solutions that would drastically increase prices for consumers.

3) Recognize that energy independence regarding oil has nothing to do with renewable energy sources for electricity such as solar and wind. Based on 2006 Energy Information Administration data, electricity generation accounted for only 1.5 percent of all petroleum consumption in the country. Drawing a distinction between renewable energy for electricity and renewable energy for transportation, such as alternative fuels, is critical.

4) Do not get fooled into using the global warming excuse to destroy our way of life.

Chart 1. Gasoline Price Estimates Under Cap-and-Trade in N.C.

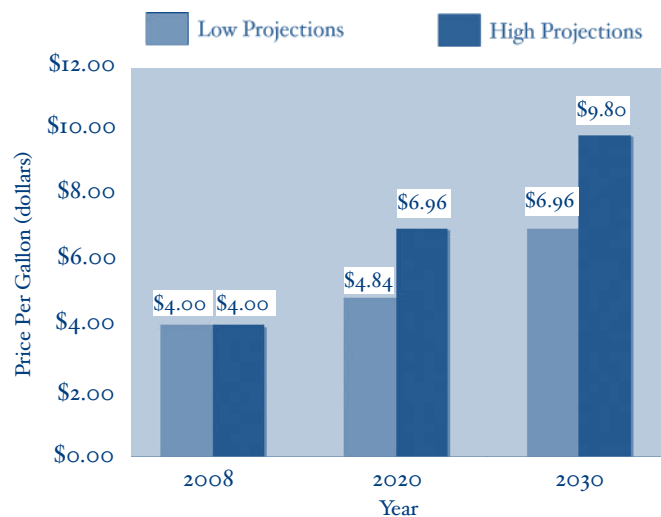
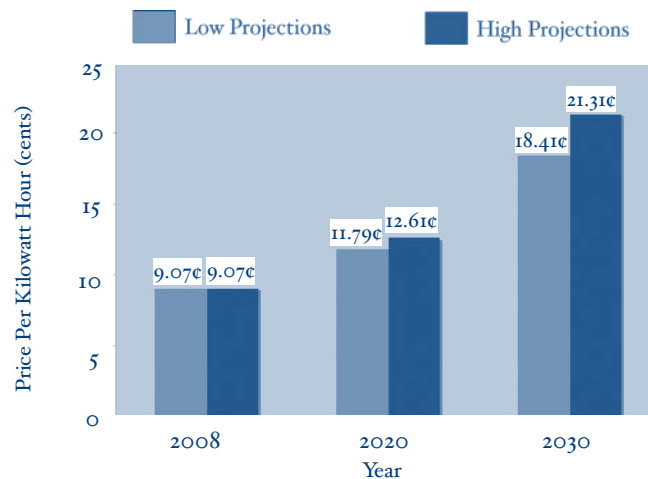


Chart 2. Residential Electricity Price Estimates Under Cap-and-Trade in N.C.



- NAM/ACCF estimate that a cap-and-trade program would raise gasoline prices in N.C. 21 to 74 percent by 2020 and 74 to 145 percent by 2030, and residential electric prices 30 to 39 percent by 2020 and 103 to 135 percent by 2030.

- Gas price estimates are based on a current statewide average gasoline price of \$4.001 (Source: AAA, July 22, 2008); residential electricity rates are based on an average rate of 9.07 cents/kWh (Source: U.S. Energy Information Administration, February 2008).

- All estimates are made in constant 2007 dollars.

CLIMATE CHANGE

The most significant environmental policy initiatives that legislators will face in North Carolina in the coming two years will be related to attempts to reduce carbon dioxide (CO₂) emissions ostensibly to ward off future global warming.

N.C. CANNOT AFFECT GLOBAL WARMING

In 2005, the legislature created a global warming commission, the N.C. Legislative Commission on Global Climate Change (LCGCC) to evaluate the issue and to determine what, if any, policies the state should pursue. As of April 15, 2008, the time expired on the commission's legislative mandate without completing its work, after already being extended by more than a year in 2006. An extension has been voted on and passed during the 2008 session.

In addition to the LCGCC the North Carolina Department of Environment and Natural Resources (DENR) established its own study group made up of various special interests, from environmental advocacy groups to public utilities and other companies. This group is called the Climate Action Plan Advisory Group (CAPAG). The goal of CAPAG has been to devise policy proposals meant to reduce CO₂ emissions.

In order to facilitate this process DENR hired a consulting group called the Center for Climate Strategies (CCS), primarily with funds from private foundations. All of these foundations have invested heavily in left-of-center environmental groups who espouse the view that global temperature increases since 1975, which leveled off after 1998, were caused by CO₂ emissions. These emissions are generated by humanity's use of energy to light, cool, and heat their homes, power their automobiles, run their factories, and facilitate their leisure activities. CCS is among these organizations. It should be noted that CO₂ is what humans exhale and what plants need to grow. It has no toxic effects.

As part of its work for the state, CCS devised a set of 56 policies meant to curb energy-using activities of all kinds. CAPAG has adopted these policies,

and the LCGCC is now examining them with the expectation that most or all of them will be recommended to the General Assembly for possible adoption.

It should be noted that CAPAG, in discussing these policy recommendations made by CCS, was not allowed to bring up any of the scientific issues surrounding global warming. Its mandate was to assume the same scientific assumptions made by CCS regarding human activities and global warming.

For example, the hypothesis that much of the global warming from the last century is due to natural causes, such as changes in the sun's intensity, were not allowed to be considered. Indeed no scientific opinions that contradicted those held by CCS and the foundations that have paid it for its North Carolina work were allowed into the process.

ANALYSIS

An important point — one that has not been disputed by any testimony before the climate commission — is that there is nothing North Carolina can do, either by itself or in conjunction with other states, that will have any noticeable impact on the climate.

If all 56 CAPAG proposals were adopted by not just North Carolina but all states in the Union and all countries of the world, there would be no noticeable impact on the climate. Dr. Thomas Wigley at the U.S National Center for Scientific Research, an adviser to Al Gore, in a 1998 Geophysical Research Letter article calculated that if there were 100 percent compliance by all countries that were party to the original United Nations treaty on global warming (the "Kyoto Protocol"), the effects would be "small" and "undetectable for many decades."

Wigley calculated that by 2100, with 100 percent compliance from all Kyoto Protocol parties, global temperatures would increase by only 0.27 degrees F less than they would if nothing were done at all.

This scientific fact should be considered along-

side the conclusions of economic analysis done by a team of economists from Suffolk University's Beacon Hill Institute in Boston.

That analysis estimated that by adopting only a portion of the 56 CAPAG/CCS recommendations, North Carolina would lose more than 33,000 jobs and more than \$4.5 billion in gross state product. The real disposable income of North Carolina's citizens would fall by \$2.2 billion. All this would occur in a three-year period. These policies would be all costs and no benefits for the citizens of North Carolina.

RECOMMENDATION

The best thing the state of North Carolina can do to help citizens to cope with the vagaries of future climate-related problems, whatever their cause and however severe, is to imple-

ment policies that promote economic growth and prosperity for the citizens of the state. This means lower taxes, fewer regulations, and a policy that promotes inexpensive energy. None of the 56 proposals being offered by CAPAG should be adopted.

Economic Impact Estimates for CAPAG Proposal Recommendations for 2011

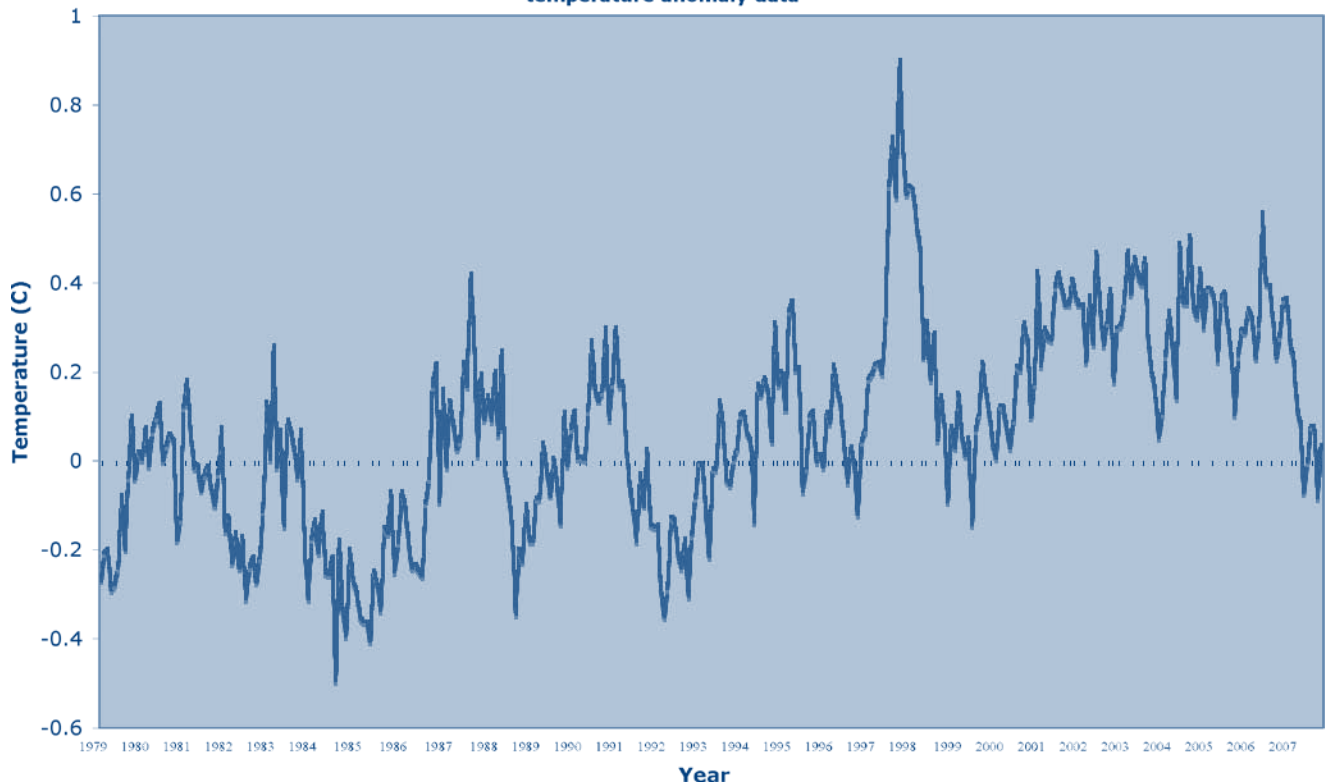
	<i>Energy Demand & Supply</i>	<i>Transportation</i>	<i>Cap & Trade</i>	<i>Total*</i>
Net Employment	-2,473	-1,202	-29,808	-33,483
Investment (\$ millions)	-76.7	-27.7	-397.9	-502.4
Real Disposable Income (\$ millions)	-242.5	-46.5	-1,976.5	-2,265.5
Real State GDP (\$ millions)	-360.3	-168.0	-4,002.6	-4,530.9
State and Local Revenue (\$ millions)	170.3	-17.5	-337.3	-184.6

* minor differences are due to rounding.

Source: Beacon Hill Institute, Suffolk University.

Global Temperature Change, 1979-2007

RSS (Remote Sensing Systems of Santa Rosa, CA) RSS Microwave Sounder Unit (MSU) global temperature anomaly data



WATER AND DROUGHT



North Carolina's drought in 2007 and 2008 may have been the worst on record, but droughts of some kind have been a fairly regular occurrence since 2000. This latest drought led to a number of local restrictions on water usage, proposals for the state to take, a manipulative public service announcement from the governor's office, and two of the goofiest mascots this side of the Olympics.

Some cities have considered adopting tiered water rates, but no city was able to raise prices during the drought. Private water suppliers also had little ability to raise prices temporarily even if they had wanted, as they must get permission from the state Utilities Commission, but the Commission has no easy way to approve temporary price increases in response to low water levels.

WATER RATES AND USAGE

A number of water systems in the state, such as Greensboro and Charlotte, already charge higher rates to customers who use more water. Under this "increasing block pricing," the water system charges higher rates in steps. This has proven to be an effective way to encourage users to conserve water without sacrificing much revenue.

The Town of Cary uses tiered prices, direct billing of renters for water consumption, and non-price conservation policies to reduce water demand in the town. The combination of policies was more successful than expected: conservation was so great that revenues were less than anticipated, and the city needed to raise rates in 2005. Other municipal water systems, from Asheville to Wilmington, charge a single rate for each gallon, regardless of volume.

Raleigh and Durham had among the lowest prices in the Triangle area and were also among the hardest hit by the drought. Neither system had enough reservoir capacity, nor had they built adequate connections to systems drawing from Jordan Lake or alternate sources. Among the difficulties the capital city faces, Raleigh stopped drawing from the Lake Benson and Lake Wheeler reservoirs in 1987, but will

be unable to start drawing from Lake Benson again until the Dempsey Benton water treatment plant is complete in 2010. The plant took 5 1/2 years from proposal to groundbreaking.

When Raleigh Mayor Charles Meeker proposed a 50 percent drought surcharge for water, city council roundly rejected the idea. Even if the surcharge had passed, it would not have taken effect until May 1, by which time Falls Lake was full and the city had returned to the lowest level, Stage One, restrictions.

Worse yet, the city would not have been able to begin block pricing until July 2009, 18 months after first proposed.

RESTRICTIONS WITHOUT PRICES

Without adequate supplies and with no way to adjust prices in a reasonable period of time, municipal water suppliers resorted to nonprice water restrictions. Whether voluntary or mandatory, restrictions on water use that do not rely on price limit the ways people can save water.

Instead of saving by taking shorter showers or finding other efficiencies, people without lawns who never wash their cars at home can ignore the problem. No neighbors will stop by to check the length of their showers, whether their dishwashers are full, or if they turn off the water while shaving or brushing their teeth.

Even mandates on water-saving devices from low-flow toilets and showerheads to high-efficiency washers have limited effects. In some cases, alternate watering days actually lead to more water usage as consumers water longer and are more conscientious about watering when they are limited to using water only on certain days.

Beyond the problems of enforcement, nonprice conservation efforts starve water systems of needed revenue, which leads to permanent water rate increases during the next budget cycle. Cary faced this in 2005. Charlotte and Raleigh will raise water rates 15 percent. High prices alone are no guarantee against rate hikes in response to conservation, as the



Orange [County] Water and Sewer Authority (OWASA) plans a 25 percent increase starting July 1.

PRIVATE SOURCES TARGETED

Farmers and other users who draw from private wells also face more regulation. The General Assembly approved an extensive well monitoring program in 2007, and Gov. Easley wants more information from more farmers on the water they use. In addition to these attempts to regulate private water usage, the state also is taking steps to socialize water resources along the Yadkin River.

RECOMMENDATIONS

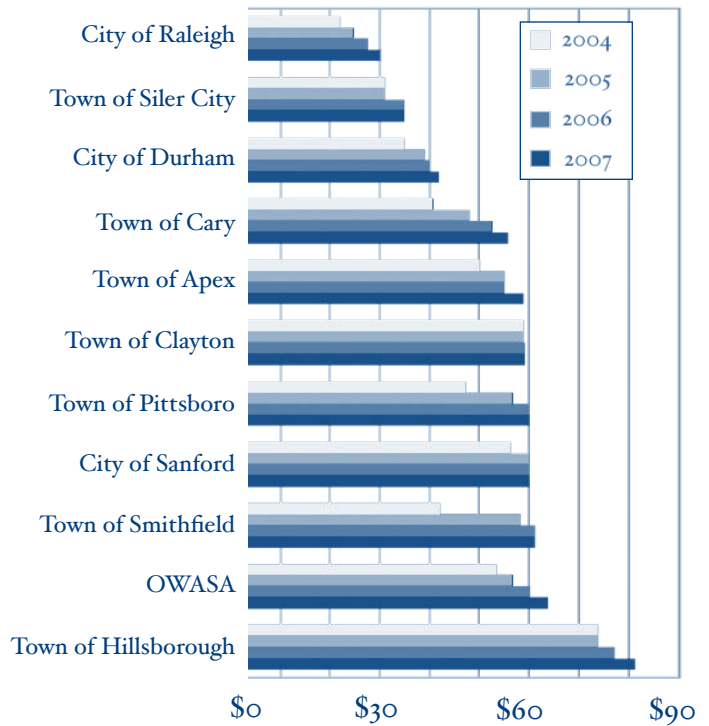
1. State policy should support increasing block pricing as a more efficient, effective, and welfare-enhancing way to match supply and demand for water. Arbitrary limits on how and how much water individuals and businesses use can lead some to use more water or force others to stop using water that is essential to their continued operation.

2. State lawmakers should make provisions to allow water prices to rise when supplies fall, just as the Utilities Commission now allows other utility prices to rise when their input costs rise. Conservation without higher prices leaves utilities with less revenue but the same costs. Prices usually rise again after periods of conservation and rise permanently at that time.

3. State policy should also make possible

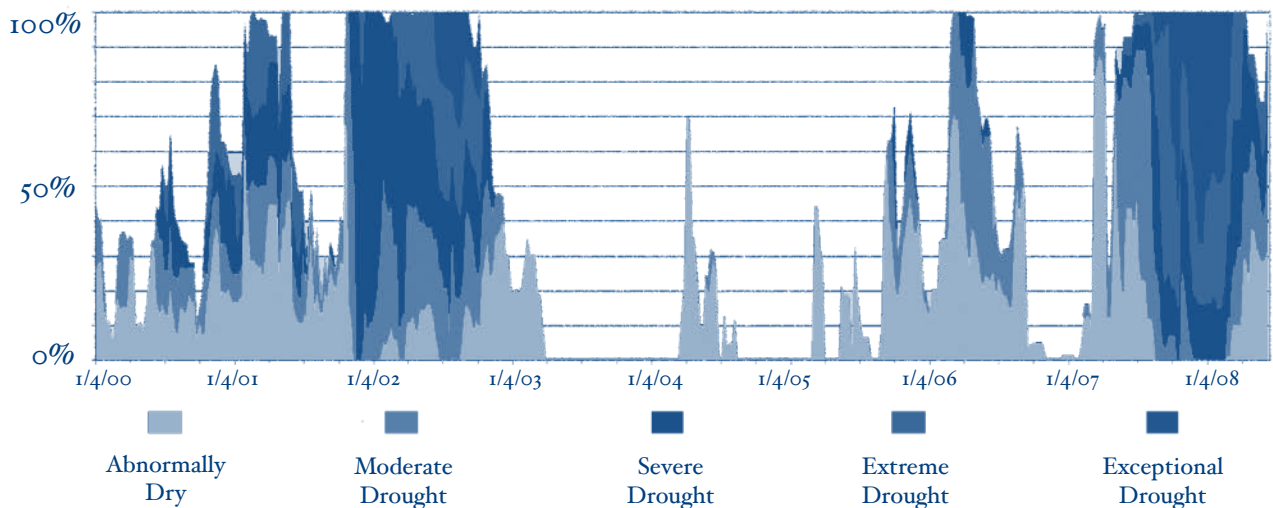
innovations tried elsewhere to reclaim and treat wastewater for use as drinking water, to treat and transport potable and nonpotable water separately, and to privatize the water infrastructure as a way to increase investment.

Chart 1. Water & Sewer Rates in the Triangle 2004-2007



Source: Triangle Joint Council of Governments

Chart 2. North Carolina is in its Fourth Drought Since 2000 (percent of state in drought conditions)



Source: U.S. Drought Monitor, http://www.drought.unl.edu/dm/dmtabs_archive.htm

HEALTH CARE REFORM



Rapidly rising medical costs are making health care insurance more expensive and less available to individuals. Workers are less likely to find insurance through their employers, and those who receive coverage face higher premiums, copays, and deductibles. It should be no surprise, then, that health care is a top concern among voters nationally and in North Carolina.

Many proposed changes to the health care system focus on making health insurance more affordable for some groups. In their efforts to expand access, however, these proposals often contribute to rapidly rising health care costs, which in turn limit access. Would-be reformers who simply want to expand access to Medicaid or mandate that people purchase insurance, should focus on promoting competition among providers and insurers as ways to expand access and lower costs.

WHAT DRIVES HEALTH COSTS?

Four factors are driving health care costs higher, two positive and two negative:

- *Innovations.* New pharmaceuticals, better diagnostic tools, and less-invasive forms of surgery often increase costs even as they improve health.

- *Demographics.* An aging, growing, and increasingly diverse population has more health care needs, and those needs are more varied.

- *Insurance.* Most people with insurance have premiums subsidized by their employers for low-deductible policies that hide the true cost of care. When care is nearly free, people have little reason to limit how much they use.

- *Government.* This is also a problem with government health programs such as Medicare (for seniors), Medicaid (for the poor), and North Carolina Health Choice (for children). As a result, governments at all levels are looking for ways to push the cost someplace else.

Government regulations such as certificate of need limit the availability of doctors and medical facilities throughout the state and particularly in rural

areas, restricting access and driving up prices where services are available. Other regulations privilege inefficient employer subsidies for insurance over individual purchases, mandate benefits, and prohibit insurance sales across state lines. These regulations increase the cost of health care and insurance by limiting the insurance individuals can choose.

The result is one group of workers earning good wages at large companies who are not just insured but insulated against medical costs, and another group earning lower wages at small companies who are uninsured or underinsured. Those with insurance often face “job lock” and are stuck in the wrong job for fear of losing their insurance or having to pay the full premium on their own.

LETTING COMPETITION WORK

Any reform needs to fix the entire market for health care and health insurance, rather than trying to expand insurance to uninsured subgroups. Simply mandating that all individuals have health insurance, as Massachusetts has tried, will not work. Instead of getting people to purchase insurance, the state merely encouraged them to take free coverage through the state, driving costs to \$78 million instead of a forecast \$21 million. The policy board overseeing the Massachusetts Connector decided not to fine individuals without insurance because, without deregulation of insurance benefits, policies are still too expensive for lower-income individuals to afford.

In 1995, the N.C. General Assembly moved toward market-based reform by rolling back some insurance regulations, passing a limited tort reform bill, and endorsing the concept of medical savings accounts (MSAs), which paved the way for health savings accounts (HSAs). A good way to ease the tort system’s burdens and provide relief to patients who have been harmed is with waivers of liability as proposed by David Hyman at the University of Illinois.

In 1998, the legislature passed limited tax credits for child health care insurance purchased directly by



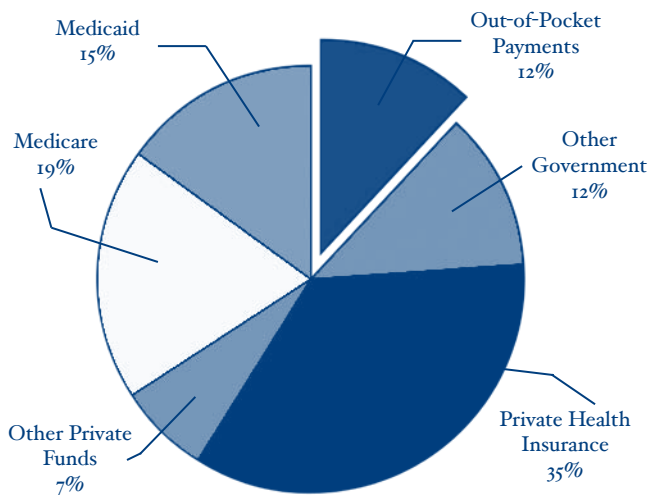
parents and for long-term care insurance, though unfortunately a subsequent legislature eliminated both as part of a tax-increase package passed in 2001. The long-term care tax credit was revived in 2007. Broad tax credits to offset the tax penalty for individuals whose employers do not provide health insurance would be a welcome next step.

Also in 2007, the legislature passed legislation to create a high-risk pool for those with conditions that might otherwise make them too expensive to insure. Legislators used money from the tobacco settlement-created Health and Wellness Trust Fund to pay for the pool instead of new taxes or fees. As important, the law included a health savings account option for those in the pool. This could provide some impetus to incorporate health savings accounts more broadly, including incorporating into the state health plan.

Health savings accounts (HSAs), which allow employers and employees to save pre-tax dollars for health needs and to earn tax-free returns on their unspent funds, were created as part of the 2003 Medicare Modernization Act.

Already more than 6.1 million people, including 128,000 in North Carolina, have enrolled in HSA-eligible insurance plans with deductibles as low as \$1,100 for an individual or \$2,200 for a family. Companies that had not previously offered insurance have taken up HSAs as have individuals who were uninsured.

Chart 1. Patients Pay Out-of-Pocket Less Than \$1 Out of Every \$8 Spent on Health Care



Source: Center for Medicaid and Medicare Services, National Health Expenditures.

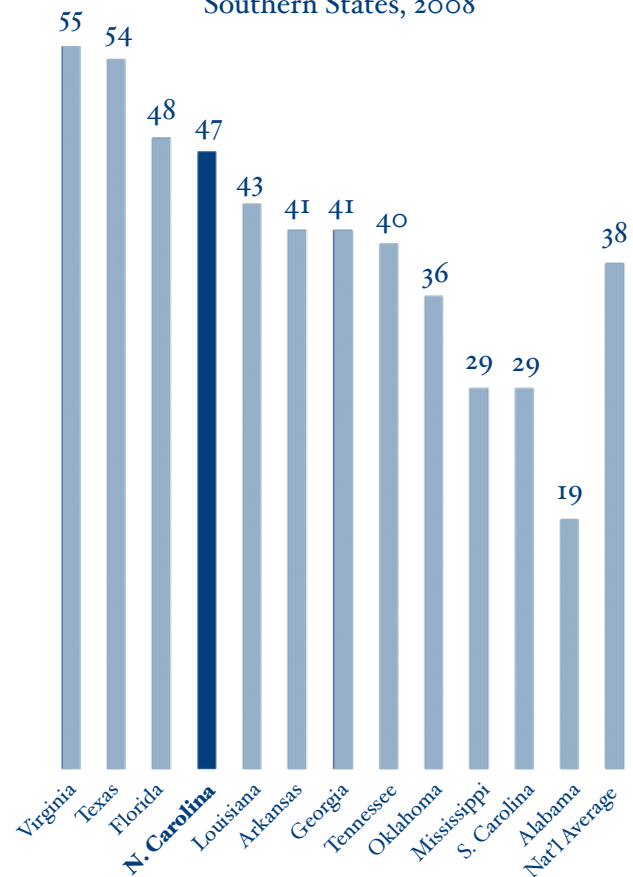
RECOMMENDATIONS

1. The goal of health reform should be to provide greater access to quality care, not to enroll more people in health insurance schemes. State lawmakers should reinstate and expand the tax credit for child health insurance by giving a refundable credit of \$250 per person, up to \$1,000 per family. The state's health plan for state employees and retirees should also include an HSA option to provide greater choice and help constrain the plan's exploding costs.

2. State policymakers should end certificate-of-need regulation and eliminate state benefit mandates on health insurance. The state should also reduce licensing restrictions on non-physician providers.

3. Lawmakers should enact changes in the tort system — such as a waiver of liability — to reduce medical-malpractice costs and improve the ability of harmed patients to receive just compensation.

Chart 2. Mandated Health Benefits in Southern States, 2008



Source: Council for Affordable Health Insurance.

MEDICAID AND HEALTH CHOICE



State and federal expansions of Medicaid since 1989 have helped make North Carolina's Department of Health and Human Services one of the state's fastest growing institutions.

With one of the most expensive Medicaid programs in the region, North Carolina desperately needs to inject large doses of market competition and common sense into its medical assistance efforts.

THE MEDICAID EXPLOSION

Congress created Medicaid in 1965 to pay for the health care of poor Americans. Four decades later, Medicaid is now four welfare programs in one. Today Medicaid covers:

1. poor adults and children
2. nonpoor children and pregnant women
3. disabled adults and children
4. elderly users of long-term care.

Also, Medicaid pays for nearly half of all births and three-quarters of all nursing home bills.

In the past, the state has focused on ways to maximize federal Medicaid matching dollars. The federal agency that administers Medicaid has signaled that it will resist future efforts to do this. There have also been suggestions that federal Medicaid money should become a fixed amount that grows at a set rate rather than supplementing new state spending.

Even without federal limits, the future affordability of North Carolina's Medicaid program is in serious doubt. Total spending on Medicaid in North Carolina has nearly tripled in the past decade to \$11.3 billion in FY2007-08, including \$2.9 billion in state funds, \$500 million in county funds, and \$7.9 billion in federal funds.

Worse, this increased spending has done little to help the uninsured. Instead, Medicaid eligibility expansions largely "crowded out" private insurance as workers of modest means chose to cancel family plans for which they previously paid in order to get free Medicaid coverage. The Congressional Budget

Office estimates that for every ten children added to SCHIP, six will lose private insurance. Unfortunately, many efforts to counter this have little effect, and some actually increase crowd-out.

INCENTIVES THAT MOVE PEOPLE FROM PRIVATE INSURANCE TO PUBLIC ASSISTANCE

North Carolina Health Choice, created under the State Child Health Insurance Program (SCHIP), has similar problems. The main effect of the free or low-cost insurance, offered to nonpoor families, was to induce some either to drop their private coverage or avoid buying coverage after leaving Medicaid. Health Choice, in other words, has allowed lower- to middle-income families to shift the cost of their children's health care to taxpayers. The percentage of children without insurance in the state has actually grown since 1999, despite a large increase in coverage by Medicaid and Health Choice.

Neither Medicaid nor Health Choice provides recipients with incentives they need to leave the public assistance rolls. The benefits packages are nominally more generous than those that most North Carolinians purchase individually or at the workplace, and are free or virtually free to recipients. No time limits, work requirements, or payback provisions are imposed on able-bodied recipients. As a result, recipients are rewarded if they stay enrolled and consume high levels of care. In addition, recipients are also penalized with extremely high effective marginal tax rates when they earn enough to no longer qualify for the program. Benefit phaseouts merely extend the range of the tax penalty but leave high effective marginal tax rates for recipients. This violates every principle of sound public policy.

The other fiscal time bomb in Medicaid, besides expanding eligibility rules, is increasing use of long-term care. Because most families expect that their elderly members will be able to tap Medicaid funds should they need long-term care, few are purchasing long-term care insurance, building their savings, or using reverse mortgages to pay for care. The federal



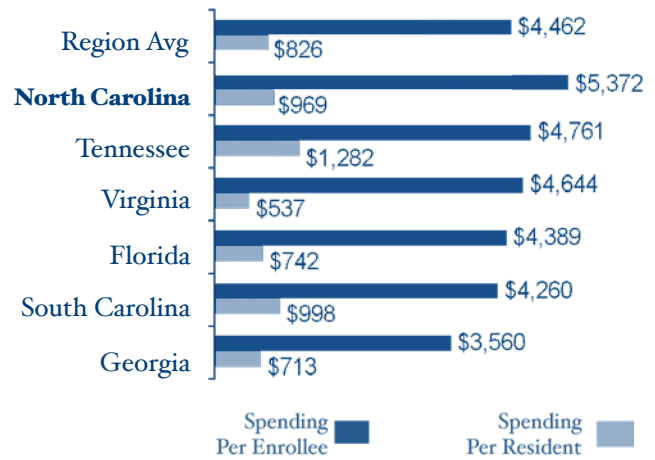
2006 Deficit Reduction Act included provisions to tighten eligibility rules for long-term care, which could help make this more rational, but North Carolina has yet to take advantage of the opportunity.

Medicaid and Health Choice all too often moved people from private insurance to government-paid care. The General Assembly has intermittently offered tax credits for individuals who purchase health insurance for their children or long-term care insurance for themselves. Although research indicates that subsidies such as tax credits do not produce large increases in private insurance enrollment, removing these subsidies while expanding Medicaid and Health Choice eligibility provided an incentive for many to move from private insurance to these government programs.

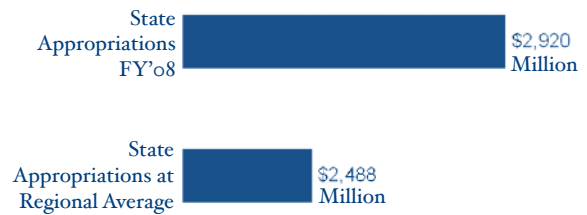
RECOMMENDATIONS

State policymakers should significantly restructure Medicaid. The benefits package should more closely resemble private plans and be limited to services mandated by Washington. Poor families should be offered vouchers or refundable tax credits with which to purchase private insurance, enroll in managed care, or deposit in HSAs. The Health Choice program should be significantly curtailed or eliminated, with the savings used to offer tax credits to families for private health care.

Chart I. Health Care Spending Per Enrollee and Per Resident

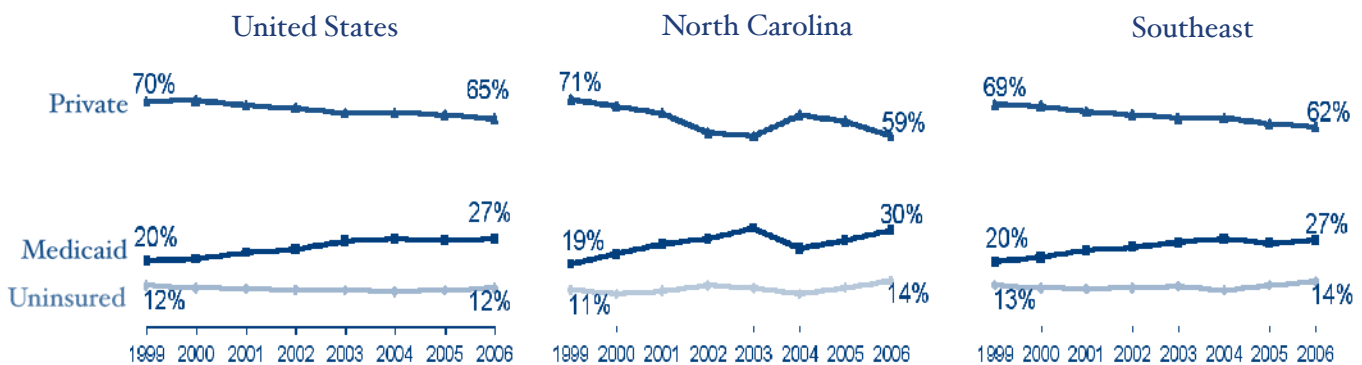


Total N.C. Spending if at Regional Average Per Capita



Source: Kaiser Family Foundation, StateHealthFacts.org.

Chart 2. The Percentage of the Uninsured in North Carolina Has Grown Despite Medicaid Expansion



Note: Respondents to the survey can fall into more than one category.
 Source: U.S. Census Bureau, Current Population Survey 2000 to 2007 Annual Social and Economic Supplements
<http://www.census.gov/hhes/www/hlthins/historic/hihist5.html>

MENTAL HEALTH

Mental health reform began in 2001 with a goal of moving from a hospital-based public system to a community-based public system, but has had disappointing results. Despite claims to the contrary, privatization is not the problem.

The main problem is hubris among reformers who too often have forgotten the first rule of medicine – do no harm.

Each reform so far has provided an initial shock to the system followed by new problems and another round of revisions. Even when well intentioned, these changes have tended to make the system more complicated and less responsive to consumer needs.

Reforming mental health the right way depends on establishing responsibility at the right level and providing the right incentives for everyone in the system to seek better patient outcomes.

HOSPITALS

Reformers hoped the state would be able to consolidate to three hospitals from the current four. Poor planning and timing, however, have left state mental hospitals more taxed than before reform.

Instead of building the community-based system first and ensuring its viability, the 2001 reforms counted being able to close beds and save money in state mental hospitals to pay for the new community care options.

The result was a perverse incentive early in the reform process for state hospitals to reduce their res-

ident populations by discharging long-term patients into the community and dealing only with the immediate crisis for many newly admitted individuals.

Half of discharges in fiscal 2007 were patients who were in the hospital for one week or less, compared to less than one-third before reform.

LMEs

Local Management Entities (LMEs) are supposed to direct patients to the most appropriate source of care, work to build the network of providers available, and ensure that patients receive appropriate care from one of those providers.

Without the care provision function, LMEs were virtually shut out of a significant portion of the Medicaid payment system. This portion grew as providers realized that once they were approved by the LME for services they could bill straight to Medicaid.

Community support services have been criticized for wasted spending, but much of this was outside the control of LMEs. Higher Medicaid payments directly to providers reflect the increase in community support services. Piedmont Behavioral Health (PBH) controlled its own Medicaid spending, so it did not have the same problems the rest of the system had in this area.

In contrast to PBH's prudent management of resources, Southeastern Center for Mental Health, Developmental Disabilities, and Substance Abuse

Chart 1. Stays of One Week or Less as Share of All Discharges from State Hospitals

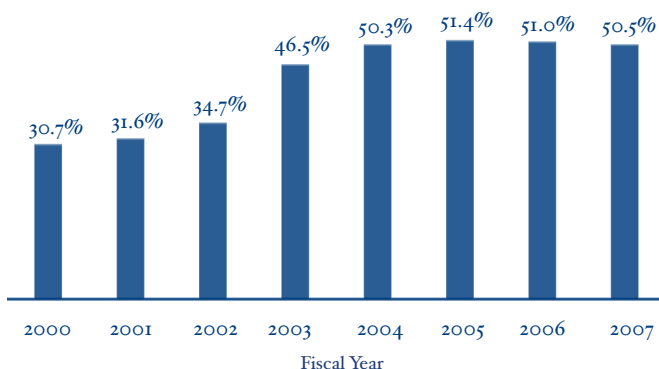
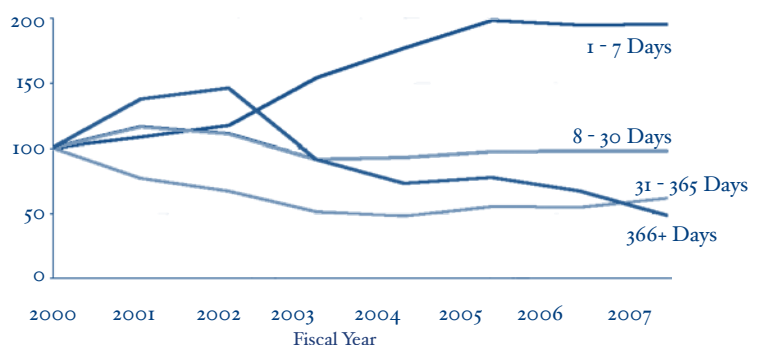


Chart 2. Long-Term Discharges Spiked Early in Reform
(Discharges by length of stay FY2000 = 100)



Services and the ten-county Albemarle Mental Health Association in northeastern North Carolina provided egregious examples of LMEs gone wild.

Southeastern failed to spend one-third of its state allocation in fiscal 2007, but was surprised when its funding for fiscal 2008 did not return to the previous level. Also, the ten-county Albemarle Mental Health Center was earlier investigated over the \$319,000 it paid Director Charlie Franklin.

Secretary of Health and Human Services Dempsey Benton presented a plan in April 2008 that would give much more power to the state government in overseeing LMEs and directing mergers between LMEs, but the number and scale of care management organizations is less important than the ability of those organizations to manage care.

This means not just getting control of the multiple money streams, but also ensuring that staff in the organization have the authority and resources to work with consumers in an effective way.

JAIL DIVERSION

Crisis intervention teams (CIT) improve treatment outcomes and public safety with less recidivism. The police officer or deputy trained in this technique, as a first responder, can evaluate a situation himself and act instead of waiting for a social worker or others to arrive, and can keep a situation in check with less risk of violence or injury.

Because the intervention occurs in the field, it can preempt all of the costs of jail for some of the 16 percent of inmates with serious mental illness. This last is significant because jail inmates with mental illness cost more to detain per day and have longer detentions than other inmates.

Post-booking methods, such as mental health courts, are for individuals who cannot be diverted earlier but for whom mental health treatment could be an acceptable alternative to a criminal sentence, with actual prison time the next step if a person does not comply.

PROVIDERS

Local crisis centers closed as the providers formerly tied to LMEs lost their ability to cross-subsidize services. Advocates and the North Carolina Psychiatric Association say that community psychiatrists went into private practice or other venues instead of taking a risk in an LME-supported provider.

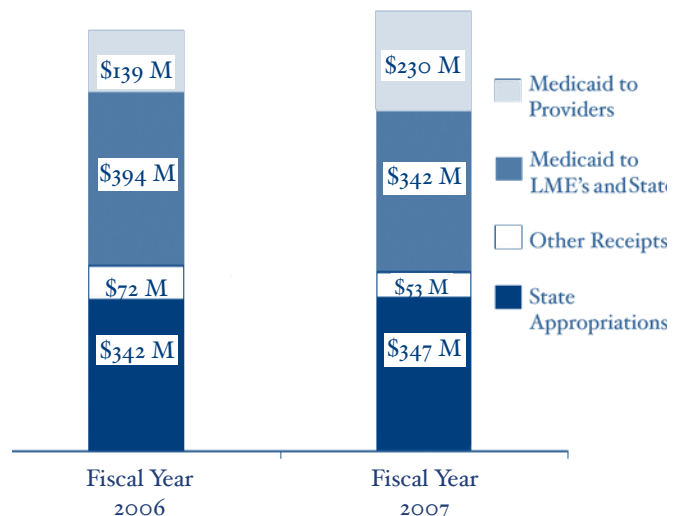
Despite these difficulties and a decline in the number of psychiatrists per 10,000 population since 1999, North Carolina still ranked in the top 20 states on this measure in 2004.

Easing regulations to incorporate primary care physicians and allied health professionals such as nurse practitioners in the continuum of mental health care could improve access, particularly in 17 counties with no psychiatrists and the 65 counties with less than one psychiatrist per 10,000 residents.

RECOMMENDATIONS

1. Expand the 1915(b) waiver currently used by Piedmont Behavioral Health to other local management entities (LMEs).
2. Allow LMEs to compete and expand across geographic boundaries.
3. Encourage more counties and LMEs to adopt crisis intervention teams as a way to improve the community-care system, improve public safety, and allow jails to be used for other offenses.
4. Ease restrictions on scope of practice that limit the ability of nurses and doctors to provide access to psychiatric care in more places at less cost.
5. Keep Dorothea Dix Hospital open indefinitely, and adjust staffing and training at state mental hospitals to the evolving role of hospitals as crisis centers with some long-term patients.

Chart 3. Medicaid Paid 55% of Public Mental Health Services, 23% Directly to Providers in FY '07



COMPETITIVE SOURCING



Throughout North Carolina, state and local governments struggle with two conflicting demands: a plea for lower taxes and a desire for better services. However, under the traditional model of public sector management, these two goals are diametrically opposed.

In order to lower taxes, government must reduce the number and quality of its services. But to improve services, citizens must be willing to “invest” more tax dollars. With competitive sourcing, this problem is solved. Competitive sourcing benefits taxpayers by reducing costs for government and improving the quality of services provided.

WHAT IS COMPETITIVE SOURCING?

Competitive sourcing is the competitive process for determining the most efficient and effective source — private or public — for performing specific governmental functions or services. Competitive sourcing is not the same as privatization.

Instead, the state defines a service or a function and takes bids from private and public providers. The lowest bid wins. Whether the service stays in-house with government employees or is contracted out to a private provider, taxpayers are the victors.

The competitive process ensures that the service is provided at the lowest price. As such, it provides a powerful tool for state officials to cut costs while providing essential governmental services. Savings of 5 to 50 percent due to competitive sourcing have been reported, with savings in the amount of 20 to 30 percent being common.

HOW COMPETITIVE SOURCING SAVES MONEY

The general public knows almost by instinct two essential and interrelated economic principles: competition and specialization save money. But these principles are often forgotten when it comes to providing governmental services. There is a misguided belief that state services can be provided only by state agencies operated by state employees. Additionally, there is a misconception that large state

agencies can operate efficiently even though they don't face competition.

Competition is essential in both the private and public sectors to ensure that goods and services are provided at the lowest cost. The quality of services is also improved due to the threat of competition. The introduction of competition into a formerly public-sector market helps taxpayers by providing better services at lower costs.

Many states have implemented competitive sourcing in an effort to lower taxes and improve services. The results have been positive in these states and have saved taxpayers a great amount of money.

EXAMPLES FROM OTHER STATES

- *Indiana.* Indiana Gov. Mitch Daniels first introduced competitive sourcing through the state's prison system. After the previous governor built an expensive new prison, Indiana didn't have the money to house inmates and had to send them to a private facility in Kentucky.

When Governor Daniels was elected, the state contracted with private firms to manage the prison Indiana had already built. This resulted in an increase in jobs and taxpayer savings of \$2 million a year. The prison's food service contract was awarded to a private company, as well. That saved the state \$0.43 per meal and allowed the prison to cut out middle management positions.

Indiana also leased the Indiana Toll Road, which had been losing money for many years, to a private company for \$3.85 billion. This allowed the state to decrease the size of government by 3,000 jobs and seven departments. It also gave Indiana the chance to focus on badly needed transportation projects that had previously been ignored due to budget shortfalls.

Indiana has used competitive contracts with the private sector for a number of other services, as well. The state is saving \$500,000 every year with private janitorial services. By hiring a private firm to collect delinquent taxes, the state receives a 16:1 return. As



of 2006, Indiana was also considering competitive bidding for the administration of entitlement programs, including Medicaid, food stamps, and welfare.

- *Florida.* During his tenure as governor, Jeb Bush saved Florida taxpayers approximately \$600 million through competitive sourcing. He also was able to cut taxes by \$20.3 billion in eight years. With bidding, Gov. Bush's goal was to improve the performance of state-run services.

With 2006's Florida Efficient Government Act, the legislature encouraged state agencies to provide their services in the most efficient manner possible. It promoted the employment of private firms when they could supply services in a more cost-effective manner. The act also established the Council on Efficient Government to advise on possible outsourcing projects and explore ways to increase government productivity and decrease costs for taxpayers. Under Gov. Bush, Florida used private providers for more than 138 public services.

- *South Carolina.* South Carolina Governor Mark Sanford has also led the way for state-based competitive sourcing initiatives, helping his state save \$100 million dollars in 2005. When South Carolina saw a drop in the number of mental health patients (from thousands to only 200), the state sold the \$50 million property where it had formerly institutionalized patients.

The state also contracted with private companies to provide services for mental health patients. This has benefited not only the patients, but the taxpayers, as well.

Competitive sourcing also saved taxpayers money when South Carolina sold Port Royal, which moved very low volumes of goods compared to the state's busier port in Charleston.

In addition, the state has used bid contracts to provide many other services, including government car fleets, golf courses, and bait-and-tackle shops formerly run by the state.

- *Virginia.* Virginia has used competitive sourcing in various aspects of its transportation system. In 2006, the General Assembly passed a bill to allow the state to contract out toll operations.

Virginia has since leased the Pocahontas Parkway, a Richmond toll road, to the Australian com-

pany, Transurban, for 99 years. This contract allowed the state to pay back the debt incurred from the construction of the toll road. It also allowed Virginia to build an important connector road to the Richmond airport. The state has contracted with private companies to do highway maintenance, as well. All of this has resulted in savings for taxpayers and improvements on Virginia's transportation system.

RECOMMENDATIONS

1. The state should establish an aggressive competitive sourcing policy that includes most, if not all, government services.

2. Lawmakers should establish competitive sourcing offices that will set up a framework for introducing competition to government services.

These offices should accept unsolicited bids from private companies who believe they could provide a publicly run service in a more efficient, less costly way. By doing so, many cities and counties, as well as the state, may find ways to reduce taxes and decrease the strain on government that comes from operating these services.

3. State and local governments should also eliminate the barriers that prevent private companies from entering the market for these types of services. Many laws and regulations stand in the way of private sector involvement. Lawmakers should remove these hurdles in an effort to encourage competition.

For example, Wake County chose not to open up its school bus operation to competition because the county found it would be more expensive than leaving it as a public service. However, state regulations on insurance and other issues hid the true cost of public-sector provision. Had these regulations not been in place, taxpayers may have been able to save money through competitive sourcing.

TIF REFORM

In 2004, North Carolina voters narrowly approved a constitutional amendment referred to as Amendment One. This amendment permits local governments to use a form of public debt financing called tax increment financing (TIF). The stated purpose of TIF is to promote private economic development in designated districts through the development of public improvement projects.

To put it simply, by developing a public improvement project, such as water and sewer lines, this allegedly will help attract private developers who otherwise would have ignored an area. The public improvement project would be financed through the extra property tax revenue (incremental revenue) that would exist due to the new private development.

THE MYTH OF TIF: NOT FREE MONEY

Because incremental tax revenues pay the TIF debt instead of general revenues as in a certificate of participation or general obligation bond, TIFs do not affect a government's credit rating. This, however, makes repayment less assured, so lenders charge

higher fees and interest, making TIFs the most expensive way to borrow money (see Chart 1 for a comparison of public debt instruments).

Advocates say TIF bonds (TIFs) do not impose a cost on taxpayers. This is not true. While it is true the government does not pay TIF debt from the general fund, this is only because the revenue never makes it to the general fund in the first place. This has no cost in the same way that having taxes deducted from a paycheck has no cost to the employee.

When using TIFs, the tax revenue is used to pay off the debt at the expense of paying for other needed services. If the private development would have occurred anyway, the local government loses revenue that could have gone to pay for critical services instead of paying for the debt incurred by the TIFs.

LACK OF OVERSIGHT LEADS TO DISASTER

North Carolina's experience to date with TIFs has been nothing short of a disaster. The first TIF project was the Randy Parton Theatre in Roanoke Rapids. It has been both a financial failure and a source of controversy and alleged corruption (see Chart 2 for a list of the lowlights of the project).

Roanoke Rapids reversed the whole concept of TIFs. Instead of the public improvement project (i.e., the theater) helping to lead to new private development, the city used the TIFs so that existing development would help with the theater. The Local Government Commission (LGC) that is supposed to provide oversight on TIF projects also failed to do its job properly (the LGC is a nine-person state commission that approves local government bonds).

REQUIRE A VOTE

Requiring voters to approve TIFs would make a major difference in providing much-needed oversight. Amendment One expressly stated "these instruments of indebtedness may be issued without approval by referendum." Because of the use of the word "may" instead of "shall" in the constitutional

Chart 1. Features of Debt Instruments

General Obligation Bonds (GO Bonds)

Lowest cost, straightforward accounting; voter approval needed, clearly paid from General Fund; repayment schedule not tied to revenues.

Certificates of Participation (COPs)

Higher cost than GO Bonds, do not require voter approval, can be structured so repayment depends on revenue availability; clearly paid from General Funds, assets provide collateral.

Tax Increment Financing (TIFs)

Do not require voter approval, payment linked to new tax revenues — not General Fund, not counted as debt by some; highest cost, hidden obligation, rely on growth for repayment.

language, a referendum certainly could be required if the legislature passed a bill to this effect.

There is nothing inherent in TIFs that requires ignoring the will of the people — TIFs simply are a form of financing that can exist with voter approval just like general obligation bonds. The legislature can and should require that voters have a voice when it comes to TIFs.

FIX THE LGC RUBBER-STAMPING PROCESS

The TIF statute creates what can fairly be described as a rubber-stamping process. There are two sections outlining the TIF approval process. The first section simply permits, but does not require the LGC to consider relevant matters regarding a TIF proposal. The second section is even worse because it requires the LGC to *approve* a TIF if certain conditions are met.

The statute should instead be changed so that the LGC is required to review the critical issues regarding TIFs — meaningful oversight by the LGC should not be optional as it is now. As a general matter, when there is a TIF or a bond project, a city or county should be required to prove the merits of the project to the LGC. There should not be a presumption, as currently exists in the TIF statute, that the project is appropriate.

Further, TIFs need a high degree of scrutiny because the projects, as of now, do not require voter approval, unlike general obligation bonds. Since most TIFs do not specifically pledge funds from the general tax base, they also may not receive the same scrutiny from local government officials.

RECOMMENDATIONS

The whole issue of tax increment financing can get very confusing. The recommendations, fortunately, are nothing more than common-sense and easy-to-understand policies for honest and open government:

1) Vote: The best form of oversight is to permit citizens to vote on TIFs.

2) Real LGC Oversight: The LGC needs to have real oversight powers and not be a rubber stamp for local governments.

3) Ethics: There are too many ways for self-deal-

ing to take place when it comes to TIFs — the TIF statute needs strong protections against conflicts of interest and other possible ethical risks.

4) Transparency: The public is provided far too little information about the true nature of TIF projects, including the risks of the projects. The TIF statute should have strong protections to ensure the public has accurate and detailed information about TIFs.

Chart 2. Lowlights of the Randy Parton Theatre TIF Debacle

- The Local Government Commission (LGC) apparently ignored key points of the feasibility study for the \$21.5 million theater project.
- The feasibility study assumed that there would be two additional hotels with 400 rooms and a retail center with 200,000 square feet of space before the theater even opened. The hotels and retail center did not exist when the theater began operating in July 2007. One new hotel has been completed, but no retail space has even been started. *More importantly, TIF projects are supposed to be the catalyst for private development, not the other way around.*
- Randy Parton's theater management company, Moonlight Bandit Productions, did not have any experience in managing a theater and was not selected through an open and competitive process.
- As reported, the president of the state-funded regional economic development organization (Northeast Commission) was the business manager of Moonlight Bandit Productions at the same time he was recruiting the company to Roanoke Rapids.
- Moonlight Bandit Productions was fired by the city after less than six months of shows, in part due to very low attendance.
- The city of Roanoke Rapids paid Moonlight Bandit Productions \$750,000 to settle any future claims it may have against the city for its dismissal.
- The city of Roanoke Rapids hired a new theater management company and then terminated that contract within a few months.
- A Roanoke Rapids city council member and a member of the North Carolina Department of Transportation have resigned due to issues related to this failed project.

CRIME AND PUNISHMENT



Preventing crime is the most basic of government functions. It's one in which North Carolina governments have made some important progress recently but still have far to go. From 1991 to 2006, the crime rate in North Carolina fell 22 percent. Despite this recent decline, the crime rate — the number of reported crimes per 100,000 in population — is nearly three times higher (273 percent) than what it was in 1961. In high-crime areas of the state, the goals of education reform or economic development will be difficult to achieve without making more progress in improving safety.

WHY THE CRIME RATE ROSE

For much of this past century, state and local officials increasingly favored sentence reduction and lighter punishments over increased incarceration. Even after the state began to address its prison overcrowding problem in the mid-1970s, it failed to make incapacitating criminals a high enough priority.

A 1994 study by the American Legislative Exchange Council found that from 1980 to 1992, the 10 states with the largest increases in their incarceration rates (250 percent) experienced an average eight percent reduction in crime rates. The 10 states with the lowest incarceration rate increases (15 percent) experienced an average 51 percent increase in crime.

In that time, ALEC found, North Carolina was the only state whose overall incarceration rate declined (by six percent). The state's crime rate rose by 25 percent, the nation's second-highest increase.

Instead of new cells, North Carolina had pursued alternative punishments (including parole and probation), designed to rehabilitate criminals or simply keep them from the "dehumanizing" state prisons. By 1990 only one-fifth of state convicts were actually serving prison time, and one-third of new prison admittees each year were convicts incarcerated for violating the terms of their alternative punishments.

The 1980s saw two initiatives — making parole more prevalent and the infamous prison cap of '87 — in response to federal lawsuits alleging violation of

prisoners' constitutional rights. By 1994 the average sentence for misdemeanants in North Carolina was 23.9 months — but the average time served was 1.4 months (about six percent of the sentence). For felons, the average sentence was 8.8 years, but the average time served was 8.1 months (about eight percent). In the 10 years from 1985 to 1994, the number of prisoners paroled ballooned from 48.7 percent of imprisoned convicts to 83.4 percent.

In 1994 Gov. Jim Hunt called a special legislative session on crime, and the General Assembly responded by enacting "Structured Sentencing," touted as the solution to the state's crime problem. It was to increase time served, both to incapacitate criminals and deter others from becoming criminals. The result was a decline in reported crimes.

The new laws increased time served by violent offenders by doing away with parole. Unfortunately, the laws actually decreased sentence lengths for some nonviolent crimes, ignoring that career criminals often start with petty crimes, then go to more serious offenses.

INCARCERATION AND BEYOND

Still, building additional prisons and lengthening sentences have resulted in lower crime rates (see chart). Local policies also helped. Many cities have deployed additional police officers and used innovative "community policing" techniques to discourage petty crimes and build community trust.

They also yield positive economic returns for the community. A 1996 paper by North Carolina State University economist Dr. Mike Walden, written for the John Locke Foundation, found that investing tax dollars in public safety generated far stronger economic returns than government expenditures on even public education or highways (all other public expenditures drew negative economic returns, by the way).

Local economies grow new businesses and opportunities faster where insurance costs aren't sky-high and people aren't afraid to shop, work, and live.



To maintain these positive trends, North Carolina must continue to expand prison capacity as quickly and efficiently as possible so that more criminals can receive just (that is, longer) sentences. This need not be a budgetary burden, if inmate labor is used and larger, more cost-effective prisons are built.

Privately built and operated prisons also can provide significant cost savings. One study found that privately operated prisons cost 35 percent less than publicly operated ones, while actually providing higher quality services in many areas.

A significant concern is North Carolina's judicial system, which is inadequately positioned to address the state's law and order needs. Clogged courts, outdated technology, and overworked and undervalued personnel mark our judicial system. The state simply must reallocate more resources to its primary responsibility to the people. Combined with lax treatment of beginning criminals, the system fosters an "untouchable" mentality in offenders that stirs them on to greater, more violent crimes.

We must also focus on preventing crime by addressing the conditions that give rise to it. But that does not mean increasing government spending on jobs programs or social programs. The real cause of crime is not a poverty of resources but a poverty of values. Research has clearly documented a relationship between out-of-wedlock births and the likelihood that those children will grow up to be criminals. A successful crime-prevention strategy will therefore include welfare reform and other measures to reduce government dependency and illegitimacy.

State leaders should also prevent new opportunities for crime by resisting Smart Growth initiatives and other "New Urbanist" planning mandates that force people to live in crowded, dense areas and "open" established neighborhoods with more streets, alleys, and bike and foot paths. As economist Randal O'Toole and Stephen Brown, co-author of *Design Against Crime: Guidance for the Design of Residential Areas*, show in a February 2005 *Reason* article, these initiatives lead to increases in crime. Densely packed living areas lead to greater crime, as do increasing access into (and "escape paths" out of) private neighborhoods. Along those lines, the U.S. Justice Department recently published a report titled, sufficiently, "Closing Streets and Alleys to Reduce Crime."

Brown and O'Toole argue in favor of Defensible

Space planning, pioneered by architect Oscar Newman with support from the National Science Foundation. Defensible Space planning recognizes that "the safest neighborhoods maximized private space and minimized common zones."

RECOMMENDATIONS

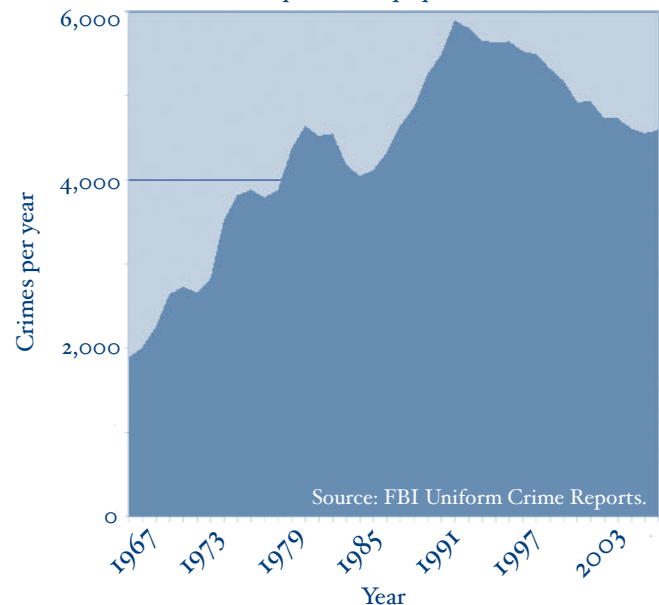
1. State leaders need to devise a comprehensive plan for identifying and incapacitating the career criminals who commit a disproportionate share of crime in North Carolina. The state needs to build enough prison space to lengthen sentences for serious crimes, but should use prison labor, larger regional prisons, and privatization where appropriate to reduce the cost to taxpayers.

2. Local leaders should employ community policing, volunteers, and other ways to deter criminal activity in their communities, including measures to reduce government dependency and the consequent poverty of values that lead to criminal behavior.

3. State and local officials should reallocate more resources to fixing the problems plaguing the judicial system.

4. Local leaders should pay heed to Defensible Space principles of neighborhoods maximizing private space and minimizing common zones instead of putting their communities under crime-inviting Smart Growth mandates.

North Carolina Crime Rate, 1967-2006
(Crimes per 100,000 people)



CIVIL RIGHTS AND EQUAL OPPORTUNITY



Civil rights and discrimination are among the most controversial subjects that state and local leaders must discuss. But they are also crucial issues that involve the core values of our political system: equality before the law, personal freedom, and the dignity of the individual. Affirmative action, originally proposed as a device for extending educational and employment opportunities to minorities and women previously excluded from fair and open competition, has in far too many cases become discrimination itself. Likewise, unconstitutional policies by public universities to outlaw intolerant speech on grounds of race, gender, etc., run serious risks of discriminating against viewpoints. The resulting disaffection and anger threatens to pull our society apart at the seams.

DISCRIMINATION AND ITS ENEMIES

Discrimination against women, racial minorities, and other groups is not only a historical legacy in North Carolina — it continues to be a reality in many workplaces and communities. When businesses discriminate on the basis of race or other factors, they are putting their own prejudices before the goal of maximizing profits and performance and will pay the price in the marketplace. In governmental services such as education and health care, the continued existence of discrimination is unjust, costly, and embarrassing, and it should never be tolerated in a state and nation devoted to principles of individual liberty and dignity.

Some of the tools currently used to combat discrimination, however, have themselves become egregious violations of the principle of individual liberty and equal opportunity. In state government, a 1987 executive order established a goal of buying four percent of state goods and services from minorities, women, and the disabled. The General Assembly has created a separate 10-percent goal for state highway and other construction projects. Formal and informal employment targets and quotas exist throughout state government. Furthermore, many

local governments in North Carolina have contracting and employment quotas of their own.

Race-based discrimination is especially prevalent in the University of North Carolina system. UNC awards so-called “minority presence grants” to black students who attend majority-white institutions as well as to whites who attend majority-black institutions. At least some UNC campuses also use race as a factor in the admissions process. A 2004 study by public policy Professor David J. Armor of George Mason University presented before the Virginia Association of Scholars annual meeting found that at North Carolina State University, the odds of a black student being admitted were 13 times greater than the odds of a white student being admitted with the same qualifications.

Discrimination at the admissions level also makes it more difficult for those admitted for factors besides academics to achieve their goal of graduating. Most of those students would likely end up at other UNC campuses, such as Greensboro or Charlotte, or other public or private colleges geared toward their preparation levels for collegiate work. Of course, the black students who are academically prepared to succeed at Chapel Hill or Raleigh would not be affected. But studies have consistently found that students admitted for reasons unrelated to their own academic preparation, such as race, drop out at higher rates. The plight of black students in North Carolina is caused not by a lack of affirmative action at the college level, but instead the poor preparation they receive in public schools (see chart).

The stated goal of affirmative action is unassailable, but the way affirmative action is practiced today is only increasing racial animosity. The principles of equal opportunity aren't breached by such commendable policies as outreach programs to ensure applicants of all racial and ethnic backgrounds are aware of opportunities for employment, contracts, and education. Using merit-based selections after making sure to “cast the net widely,” states and localities can best serve the interests of all citizens.



Racial preferences also fail to help the most disadvantaged minorities, for whom hiring and higher education preferences are irrelevant. The state could address their needs far more directly by solving these problems: (1) public schools not effectively preparing them for citizenship and employment, (2) state and local law enforcement failing to protect them from criminal predators, (3) programs fostering dependency over self-sufficiency, and (4) government limiting their economic options by imposing barriers to economic growth and entrepreneurship.

FIRST AMENDMENT RIGHTS AND DISCRIMINATION AGAINST SPEECH

Most UNC system campuses want to combat discrimination by speech codes that prohibit “statements of intolerance” (N.C. Central), “offensive speech ... of a biased or prejudicial nature” (UNC-Pembroke), “disrespect for persons” (UNC-Greensboro), etc. A 2005 study conducted for the Pope Center for Higher Education Policy by the Foundation for Individual Rights in Education, “The State of the First Amendment in The University of North Carolina System,” found that 13 of the 16 UNC schools had at least one policy that “both clearly and substantially restricts freedom of speech” and could not survive a constitutional challenge. The report stated that UNC “member institutions have run roughshod over [constitutional] rights in the name of tolerance and civility.”

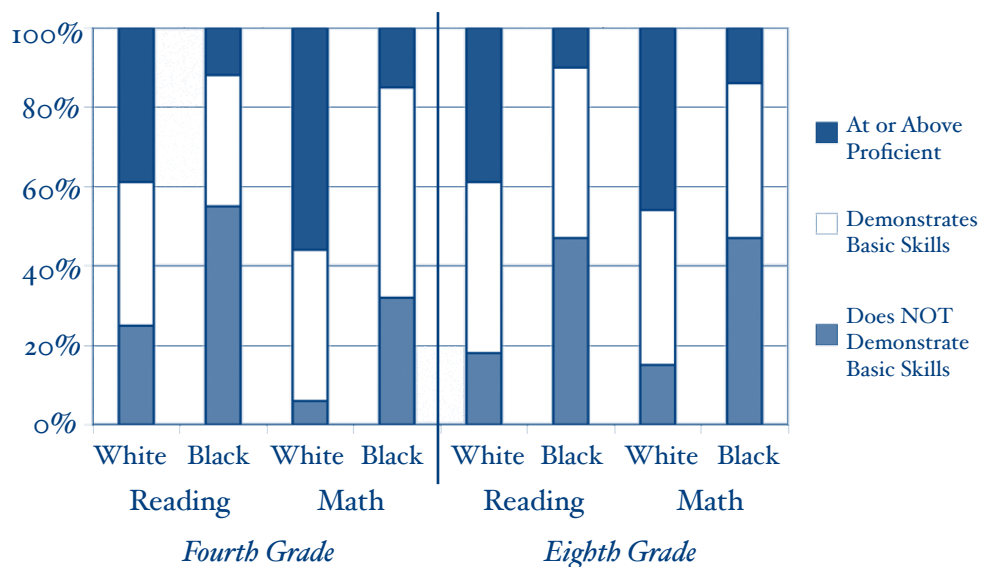
By and large, UNC officials seem to share former UNC-Chapel Hill Chancellor James Moeser’s view that they must resolve “tension” between the First Amendment’s protection of speech and the Fourteenth Amendment’s equal-protection provisions. As public universities, however, UNC campuses are bound to uphold all of the Constitutional rights of its students. Since the Pope Center report was released, both Appalachian

State and Fayetteville State have repealed unconstitutional portions of their policies regarding speech.

RECOMMENDATIONS

1. North Carolina state and local governments should eliminate all preferences, quotas, goals, and targets for suppliers, employment, and school admissions. Instead, government should vigorously enforce existing laws promoting equal opportunity and respect for the rights of all North Carolinians.
2. To expand opportunities for racial and other minorities in North Carolina to provide for themselves and their families, state and local leaders should offer private-school scholarships to students in low-performing school districts, expand efforts to combat crime, and promote true economic development across the state.
3. State and UNC system leaders should vigorously uphold the First Amendment’s protection of speech rights, and they should teach as well as model for the next generation of scholars and leaders that the best way to smother the fires of offensive ideas and speech is not with tyranny, but with better ideas and speech.

N.C. Scores on 2007 National Tests, by Race



Source: National Association of Education Progress (NAEP), 2007

CAMPAIGN FINANCE REFORM



While the issue of campaign finance reform barely registers in public opinion polls, many politicians and the media tell us reform is critical to the future of democracy in America. It is clear, however, that they believe that is true only insofar as we accept the version of reform demanded by these same politicians and the media — public financing, contribution and expenditure limits, extensive regulation, and even prohibitions on issue advocacy and independent expenditures.

This version of reform will have little impact other than to stifle political debate and to further corrupt our political system. The legislature has created artificial restrictions on speech and artificial limits on contribution levels. The First Amendment's protection of speech, to many, is simply seen as an inconvenience. Political speech is under attack.

Serious reformers should accomplish the effective liberation of campaigns and elections from arbitrary limits on the flow of money, information, and access.

MONEY IS VITAL TO DEMOCRATIC ELECTIONS

Money is part of the system and always will be. Money allows candidates to get their messages out and allows challengers to compete with incumbents.

As the U.S. Supreme Court in *Buckley v. Valeo* stated: "A restriction on the amount of money a person or group can spend on political communication during a campaign necessarily reduces the quantity of expression by restricting the number of issues discussed, the depth of their exploration, and the size of the audience reached. This is because virtually every means of communicating ideas in today's mass society requires the expenditure of money."

Money supports campaign advertising. A recent article in the *American Journal of Political Science* stated: "Specifically, our findings show that exposure to campaign advertising produces citizens who are more interested in the election, have more say about the candidates, are more familiar with who is running, and ultimately, are more likely to vote."

UNETHICAL SYSTEM V. UNETHICAL BEHAVIOR

Many reformers want to "fix" the campaign finance system by continually restricting the ability of candidates to raise the money necessary for political speech. They also want to do whatever they can to undermine the speech of independent organizations that support candidates.

Ironically, by creating artificial restrictions (such as contribution limits) on activities that are neither wrong nor immoral, the reforms themselves increase the number of lawbreakers and unethical behavior. That serves only to decrease the faith citizens have in the political system. It becomes a vicious circle: the legislature passes artificial restrictions to address the illegal behavior caused by the artificial restrictions that the legislature created in the first place.

The behavior is unethical only because it is illegal, not because it is wrong in and of itself. For example, a candidate who receives contributions above what the law allows is doing something illegal. It certainly should not be condoned. But it is hard to argue that if it were legal, trying to fund a campaign to support one's speech is somehow morally wrong.

In fact, the moral wrong is government limiting funding and thereby political speech.

NORTH CAROLINA'S FAILED TAXPAYER-FUNDED JUDICIAL CAMPAIGN SYSTEM

Public financing — more accurately called taxpayer financing — is a "cute" way to get around campaign contribution limits. The idea behind the system is that candidates for appellate judgeships get taxpayer funding in return for agreeing to limit their spending. If their "traditional" opponents (those who do not take taxpayer money) spend beyond a certain level, the subsidized candidate gets additional taxpayer funds — called "rescue funds" — to counter their opponents.

This system has been a disaster. It was supposed to be funded voluntarily, but because there was so little support, the legislature instead took General Fund dollars to subsidize the system.



Besides usually meaning higher taxes, taxpayer financing has serious First Amendment free-speech problems. When taxpayers subsidize candidates, they are funding at least some candidates and speech they oppose. If that is not illegal, it is unethical, because they are being forced to support candidates and speech they don't believe in.

A candidate who doesn't take taxpayer subsidies might curtail his own political speech, because in spending a certain level of money to support his message, he would find himself funding the opposition. That effect is chilling speech. Even worse, the "rescue fund" system actually could allow a taxpayer-subsidized candidate to spend more than a traditional candidate — and still receive rescue funds.

Despite this failed system, in 2007, the legislature expanded taxpayer financing through a pilot program that covers three Council of State races: state auditor, insurance commissioner, and superintendent of public instruction.

COMMON CAMPAIGN-FINANCE MYTHS

• *Creating equality in funding is good for democracy.* The U.S. Supreme Court in the 2008 case *Davis v. FEC*, which may provide the basis for striking down the public financing laws, explained "in *Buckley* we held that '[t]he interest in equalizing the financial resources of candidates' did not provide a 'justification for restricting' candidates' overall campaign expenditures, particularly where equalization 'might serve... to handicap a candidate who lacked substantial name recognition or exposure of his views before the start of the campaign.'"

Equalization means an artificial spending limit is keeping a candidate from spending money to advertise and educate voters. In creating an artificial limit, legislators, some acting in their own self-interests, are determining what is an appropriate amount of money to be spent in all elections. They could try to set up low limits that might make it easier for incumbents to win elections.

The only democratic way of funding is to allow citizens to decide for themselves whom to assist financially. If a candidate does not have support and is unable to raise money, that is a good thing, not a bad thing. This ensures only credible candidates are on the ballot. At least citizens and not legislators will be making funding decisions.

• *Taxpayer-financed systems lead to more faith in gov-*

ernment. The belief is that a state that took the drastic step of taxpayer financing would see a significant increase in citizens' confidence in state government. But a GAO report on the early experiences of Arizona and Maine with their taxpayer-financed systems found the following: In Arizona, only 21 percent had more confidence in state government, while 33 percent said the system had no effect and 15 percent said they had less confidence. The findings were basically the same in Maine. Only 17 percent had more confidence, 39 percent said the system had no effect, and 8 percent said they had less confidence.

RECOMMENDATIONS

1. First and foremost, protect political speech.
2. Policymakers should follow a simple rule when considering campaign finance reform: *If the reform undermines freedom of speech, then disregard it.*
3. Disclosure should be the cornerstone of campaign finance reform. Require full and immediate disclosure of all contributions to state campaigns. If campaign treasurers say they cannot comply with this rule because they do not keep their records on a computer, give them an order form and even a coupon if need be for the appropriate software. No excuses.
4. The State Board of Elections needs to compile and organize the campaign finance data so it is easily searchable on the Internet, so anyone can quickly find what they are looking for. Currently, the data are provided through large files that certainly are not user-friendly. Disclosure is effective only if people can make sense of the reported data.
5. Public officials worried about the corrupting influence of campaign contributions should work diligently to decrease the reach and authority of government at all levels so that so-called "special interests" will no longer feel required to curry favor with legislators and executive branch officials.
6. Keep it simple. Recognize that money is going to be part of the system. Do not fight this reality by wishing it away with bad legislation. With clear disclosure rules and without artificial barriers to obtaining contributions, the system will work better.

JLF REPORTS & SUGGESTED RESOURCES



The brevity of this briefing book obviously precludes lengthy discussion of many of the important and complicated issues that face state and local policy-makers. We recommend that interested North Carolinians visit the following Locke Foundation Policy Reports and Spotlights, and that they contact one of the public policy research organizations in the next section for additional information.

JOHN LOCKE FOUNDATION REPORTS

BUDGET, TAXATION, AND ECONOMIC DEVELOPMENT

- “Fiscal Transparency in N.C.: Surveying state and local governments,” http://www.johnlocke.org/spotlights/display_story.html?id=199
- “Freedom Budget 2007,” http://www.johnlocke.org/policy_reports/2007042483.html
- “A Better Bargain: Meeting North Carolina’s needs without a \$1 billion tax hike,” http://www.johnlocke.org/policy_reports/display_story.html?id=81
- “Spend and Tax: A history of General Fund crises in N.C. and how to prevent them,” http://www.johnlocke.org/policy_reports/display_story.html?id=75
- “Compensation Model Cannot Keep Good state Employees,” http://www.johnlocke.org/spotlights/display_story.html?id=136
- “The Political Spending Cycle: Spending binges lead to high-tax hangovers,” http://www.johnlocke.org/spotlights/display_story.html?id=125
- “They Can’t All Be Teachers: N.C. government employment high and rising,” http://www.johnlocke.org/spotlights/display_story.html?id=108
- “Leading By Not Doing: Few counties and school districts receive donations, even from pro-tax residents,” http://www.johnlocke.org/spotlights/display_story.html?id=186
- “Bad Credit: State earned income tax credit would

do little good at great cost,” http://www.johnlocke.org/spotlights/display_story.html?id=155

- “End All Tax Biases: Report on tax expenditures misses half the story,” http://www.johnlocke.org/spotlights/display_story.html?id=120
- “Liberty and Economic Growth: Principles for reforming North Carolina’s tax system,” http://www.johnlocke.org/policy_reports/display_story.html?id=52
- “Fiscal Transparency in N.C.: Surveying state and local governments,” http://www.johnlocke.org/spotlights/display_story.html?id=199
- “Common-Sense TIF Reforms: Ways to Avoid Randy Parton Theatre-Like Debacles and Other Disasters,” http://www.johnlocke.org/spotlights/display_story.html?id=200
- “Debt is Debt: Taxpayers on hook for TIFs despite rhetoric,” http://www.johnlocke.org/spotlights/display_story.html?id=187

K-12 EDUCATION

- “Reading, Writing, and Handbells: Course enrollment in the era of No Child Left Behind,” <http://www.johnlocke.org/spotlights/20070913181.html>
- “The ABCs of Public Disgrace: North Carolina’s school-accountability system has misled parents and taxpayers,” <http://www.johnlocke.org/spotlights/20061101146.html>
- “Raise the Bar, Not the Age: Why raising the compulsory school age won’t reduce dropouts,” http://www.johnlocke.org/spotlights/display_story.html?id=170
- “Better Instruction, Not More Time: A longer school day and year will be North Carolina’s next education fad,” http://www.johnlocke.org/spotlights/display_story.html?id=177
- “Honey, I Shrunk the Class!: How reducing class size fails to raise student achievement,” http://www.johnlocke.org/spotlights/display_story.html?id=123



- “The Solution Is School Choice: We already know what to do about North Carolina’s school facilities crisis,” http://www.johnlocke.org/spotlights/display_story.html?id=175
- “Education Tax Credits in North Carolina: Innovation in education,” http://www.johnlocke.org/policy_reports/display_story.html?id=149
- “Why Charter Schools Are Good for North Carolina,” http://www.johnlocke.org/policy_reports/display_story.html?id=84
- “Annual Report on Teacher Pay: N.C. teacher compensation is more than \$5,000 higher than the national average,” http://www.johnlocke.org/spotlights/display_story.html?id=190
- “Public School Hiring Frenzy: As personnel increases, so does bureaucracy,” http://www.johnlocke.org/spotlights/display_story.html?id=133
- “A Lottery That Helps Students: How lottery proceeds should be spent for education,” http://www.johnlocke.org/spotlights/display_story.html?id=127
- “Don’t Bet On It: A state lottery would not be an alternative to taxes,” http://www.johnlocke.org/spotlights/display_story.html?id=98
- “Eastern NC’s Lottery Bug: Counties with higher taxes and unemployment play more,” http://www.johnlocke.org/spotlights/display_story.html?id=165
- “Job Training That Works: Public programs stagnate, which private and charitable training excels,” http://www.johnlocke.org/spotlights/display_story.html?id=194

HIGHER EDUCATION POLICY

- See various reports at the John William Pope Center for Higher Education Policy, www.popecenter.org

GOVERNMENT REGULATION AND PROPERTY RIGHTS

- “Eminent Domain in NC: The Case for Real Reform,” http://www.johnlocke.org/policy_reports/display_story.html?id=85
- “Ten Myths of the Annexation Process: The truth is, N.C.’s annexation law lets municipalities run wild,” http://www.johnlocke.org/spotlights/display_story.html?id=204
- “Flawed and Undemocratic: Forced Annexation Is

Good for Municipal Leaders, But Bad for the Public,” http://www.johnlocke.org/spotlights/display_story.html?id=172

- “Consumer Protection Blackout: Why the Public Staff Should Be Reformed,” http://www.johnlocke.org/spotlights/display_story.html?id=161
- “The Tort of Medical Malpractice: Is It Time for Law Reform in North Carolina?,” http://www.johnlocke.org/policy_reports/display_story.html?id=50

TRANSPORTATION POLICY

- “No, Fix the Roads First: How N.C. has taken transportation out of transportation policy,” http://www.johnlocke.org/spotlights/display_story.html?id=185
- “Traffic Congestion in North Carolina: Status, Prospects, and Solutions,” <http://www.johnlocke.org/site-docs/traffic/>
- “Policy versus Performance: Directions for North Carolina’s Largest Transit Systems,” http://www.johnlocke.org/policy_reports/display_story.html?id=71
- “TEA-21’s Impact: Performance of State Highway Systems 1984-2003,” http://www.johnlocke.org/policy_reports/display_story.html?id=55

ENVIRONMENT, ENERGY, AND CLIMATE CHANGE

- “Low-Cost Energy: Critical for the Economy and Our Way of Life,” http://www.johnlocke.org/spotlights/display_story.html?id=196
- “A Wind Power Primer: Emission reduction negligible for land-intensive, unreliable, noisy, ugly bird-killing turbines,” http://www.johnlocke.org/spotlights/display_story.html?id=195
- “Electric Shock: North Carolinians would be required to pay for electricity in other states,” http://www.johnlocke.org/spotlights/display_story.html?id=178
- “Renewable Energy At All Costs: Legislation ignores the will of the public and would have unintended consequences,” http://www.johnlocke.org/spotlights/display_story.html?id=174
- “The Economics of Climate Change Legislation in North Carolina,” http://www.johnlocke.org/policy_reports/display_story.html?id=169

- “Taxes, Subsidies, and Regulation: A guide to North Carolina’s proposed global warming policies,” http://www.johnlocke.org/policy_reports/display_story.html?id=147
- “A North Carolina Citizen’s Guide to Global Warming,” http://www.johnlocke.org/policy_reports/display_story.html?id=86
- “Happy Earth Day: North Carolina’s air is worth celebrating,” http://www.johnlocke.org/spotlights/display_story.html?id=166
- “Drought-Resistant Water: Variable prices can work better than mandatory restrictions,” http://www.johnlocke.org/spotlights/display_story.html?id=188

HEALTH CARE REFORM

- “Long-term Care Financing in North Carolina: Good Intentions, Ambitious Efforts, Unintended Consequences,” http://www.johnlocke.org/policy_reports/display_story.html?id=145
- “High-Risk Health Insurance Pools: A step towards an individual insurance market,” http://www.johnlocke.org/spotlights/display_story.html?id=145
- “Your Health, Your Choices: Employers and the state fail to meet individual health care needs,” http://www.johnlocke.org/spotlights/display_story.html?id=132
- “Health Savings Accounts: Consumer-driven health care for North Carolina public employees and teachers,” http://www.johnlocke.org/policy_reports/display_story.html?id=64
- “Certificate-of-Need-Laws: It’s time for repeal,” http://www.johnlocke.org/policy_reports/display_story.html?id=62
- “Get Control of Medicaid: Bringing costs into line will help state budget,” http://www.johnlocke.org/spotlights/display_story.html?id=92
- “Jail Diversion Programs: A step toward better mental health reform,” http://www.johnlocke.org/spotlights/display_story.html?id=193
- “Reform the Reform: How mental health reform went wrong and what lies ahead,” http://www.johnlocke.org/spotlights/display_story.html?id=176

CAMPAIGN FINANCE REFORM

- “Political Welfare: Why Taxpayer-Funded Campaigns Are Bad for Taxpayers and Democracy,” http://www.johnlocke.org/policy_reports/display_story.html?id=69

SUGGESTED RESOURCES

BUDGET AND TAXATION

- Americans for Tax Reform, 1920 L Street NW, #200, Washington, DC 20036, 202-785-0266, www.atr.org
- Cato Institute, 1000 Massachusetts Ave. NW, Washington, DC 20001, 202-842-0200, www.cato.org
- Institute for Research on the Economics of Taxation, 1710 Rhode Island NW, Washington, DC 20036, 202-463-1400, www.iret.org
- National Taxpayers Union, 108 N. Alfred Street, Alexandria, VA 22314, 703-683-5700, www.ntu.org
- Tax Foundation, 1900 M Street NW, Suite 550, Washington, DC 20036, 202-464-6200, www.tax-foundation.org

BUSINES AND REGULATION

- American Enterprise Institute, 1150 17th Street NW, Washington, DC 20036, 202-862-5800, www.aei.org
- Americans for Prosperity, 1726 M Street NW, 10th Floor, Washington, DC 20036, 202-349-5880, www.americansforprosperity.org
- Competitive Enterprise Institute, 1001 Connecticut Avenue NW, Suite 1250, Washington, DC 20036, 202-331-1010, www.cei.org
- Consumer Alert, 1001 Connecticut Avenue NW, Suite 1128, Washington, DC 20036, 202-467-5809, www.consumeralert.org
- Heartland Institute, 19 South LaSalle, Chicago, IL 60063, 312-377-4000, www.heartland.org
- Institute for Justice, 1717 Pennsylvania Avenue NW, Suite 200, Washington, DC 20006, 202-955-1300, www.ij.org
- Mercatus Center at George Mason University, 3301 North Fairfax Drive, Suite 450, Arlington, VA 22201, 703-993-4930, www.mercatus.org
- Pacific Research Institute, 755 Sansome Street, Suite 450, San Francisco, CA 94111, 415-989-0833, www.pacificresearch.org
- Reason Foundation, 3415 S. Sepulveda Blvd., Suite 400, Los Angeles, CA 90034, 310-391-2245, www.rppi.org
- Weidenbaum Center, Washington University, Campus Box 1027, St. Louis, MO 63130, 314-935-5630, csab.wustl.edu

EDUCATION

- American Council of Trustees and Alumni, 1726 M Street NW, Suite 800, Washington, DC 20036, 202-467-6787, www.goacta.org
- Center for Education Reform, 1001 Connecticut Avenue NW, Suite 204, Washington, DC 20036, 202-822-9000, www.edreform.com
- Fordham Foundation, 1627 K Street NW, Suite 600, Washington, DC 20006, 202-223-5452, www.edexcellence.net
- Heritage Foundation, 214 Massachusetts Avenue NE, Washington, DC 20002, 202-546-4400, www.heritage.org
- Hudson Institute, P.O. Box 26-919, Indianapolis, IN 46226, 317-545-1000, www.hudson.org
- National Association of Scholars, 221 Witherspoon St, 2nd fl., Princeton, NJ 08542-3215, 609-683-7878, www.nas.org
- Foundation for Individual Rights in Education, 601 Walnut Street, Suite 510, Philadelphia, PA 19106, 215-717-FIRE, www.thefire.org
- The Friedman Foundation for Educational Choice, One American Square, Suite #2420, Indianapolis, IN 46282, 317-681-0745, www.friedman-foundation.org

ENVIRONMENT

- Property and Environmental Research Center, 502 South 19th Avenue, Suite 211, Bozeman, MT 59718, 406-587-9591, www.perc.org
- The Science & Environmental Policy Project, 1600 South Eads Street, Suite #712-S, Arlington, VA 22202-2907, 703-920-2744, www.sepp.org
- The New Zealand Climate Science Coalition, <http://nzclimatescience.net>
- CO₂ Science, Center for the Study of Carbon Dioxide and Global Change, P.O. Box 25697, Tempe, AZ 85285, www.CO2Science.org
- George C. Marshall Institute, 1625 K. Street, NW, Suite 1050, Washington, DC 20006, 202-296-9655, www.marshall.org

- Institute for Energy Research, 601 Pennsylvania Ave., NW, Suite 900, South Building, Washington, DC 20004, 202-434-8200, www.InstituteForEnergyResearch.org
- Capital Research Center, 1513 16th St., NW, Washington, DC 20036, 202-483-6900, www.greenwatch.org
- National Resources Stewardship Project, A 102-1075 Bay St., Suite 405, Toronto, Ontario M55 2B2, 613-234-4487, www.nrsp.com
- Carbon Dioxide Information Analysis Center, Oak Ridge National Laboratory, Bethel Valley Rd., P.O. Box 2008, Building 1509, Oak Ridge, TN 37831, 865-574-2232, <http://cdiac.ornl.gov>
- The Center for Science and Public Policy, 209 Pennsylvania Ave., SE, Suite 2100, Washington, DC 20003, 202-454-5249, www.ff.org
- Climate Strategies Watch, www.climatestrategies-watch.com
- www.JunkScience.com

HEALTH AND WELFARE

- Council for Affordable Health Insurance, 127 S. Peyton Street, Suite 210, Alexandria, VA 22314, 703-836-6200, www.cahi.org
- Galen Institute, P.O. Box 19080, Alexandria, VA 22320, 703-299-8900, www.galen.org
- Pacific Research Institute, 755 Sansome Street, Suite 450, San Francisco, CA 94111, 415-989-0833, <http://health.pacificresearch.org>
- www.statehousecall.org
- National Center for Policy Analysis, 12770 Coit Rd., Suite 800, Dallas, TX 75251, 972-386-6272, www.NCPA.org

OTHER ISSUES

- American Legislative Exchange Council, 1129 20th Street NW, Suite 500, Washington, DC 20036, 202-466-3800, www.alec.org
- Center for Equal Opportunity, 14 Pidgeon Hill Drive, Suite 500, Sterling VA 20165, 703-421-5443, www.ceousa.org
- The Federalist Society, 1015 18th Street, NW, Suite 425 Washington, DC 20036, 202-822-8138, [\[soc.org\]\(http://soc.org\)](http://www.fed-

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- Free Congress Foundation, 717 2nd Street NE, Washington, DC 20002, 202-546-3000, www.freecongress.org
- U.S. Term Limits, 240 Waukegan Road, Glenview, IL 60025, 800-733-6440, www.termlimits.org

NORTH CAROLINA ORGANIZATIONS

- Americans for Prosperity-North Carolina, 200 West Morgan Street, Raleigh, NC 27601, 919-839-1011, www.afpnc.org
- Center for Local Innovation, 200 W. Morgan Street, Suite 200, Raleigh, NC 27601, 919-828-3876, www.localinnovation.org
- Civitas Institute, 1005 Harrington St., Raleigh, NC 27603, 919-834-2099, www.jwpcivitasinstitute.org
- National Federation of Independent Business-North Carolina Chapter, 100 Sawmill Road, Suite 201, Raleigh, NC 27615, 919-844-6342. www.nfib.com
- North Carolina Education Alliance, 200 W. Morgan Street, Suite 206, Raleigh, NC 27601, 704-231-9767 (Charlotte office), www.nceducationalliance.org
- North Carolina Family Policy Council, 343 Six Forks Road, Suite 285, Raleigh, NC 27609, 919-807-0800, www.ncfpc.org
- North Carolina Institute for Constitutional Law, 225 Hillsborough Street Suite 280, Raleigh, NC 27603, 919-838-5313, www.ncicl.org
- Pope Center for Higher Education Policy, 333 E. Six Forks Rd., Suite 150, Raleigh, NC 27609, 919-828-1400, www.popecenter.org
- Stop NC Annexation, P.O. Box 292, Cary, NC 27512, 919-649-9154, www.stopncannexation.com
- Parents for Educational Freedom, 4924 Windy Hill Dr., Suite B, Raleigh, NC 27609, 919-871-1084, www.pefnc.org

20 YEARS OF VITAL STATISTICS ON NORTH CAROLINA PUBLIC POLICY

<i>Fiscal</i>	1988	1998	2002	2003	2004	2005	2006	2007	2008	Change
Total Annual State Budget (Millions, Authorized)	\$9,724	\$20,425	\$25,961	\$26,303	\$27,979	\$29,733	\$33,366	\$35,651	\$43,144	+344%
General Fund Operations (Millions, Authorized)	\$5,805	\$11,259	\$14,706	\$14,321	\$14,872	\$15,898	\$17,162	\$18,674	\$20,428	+252%
Inflation-Adjusted State GF Spending Per N.C. Resident (1995 Dollars)	\$1,211	\$1,505	\$1,713	\$1,621	\$1,625	\$1,655	\$1,691	\$1,752	\$1,839	+51%
N.C. State and Local Tax Burden As a Percentage of Income	9.8%	9.7%	9.6%	9.6%	9.7%	9.8%	10.1%	10.0%	9.8%	+0%
Inflation-Adjusted Public School Spending Per Pupil	\$4,887	\$6,290	\$7,381	\$7,305	\$7,343	\$7,336	\$7,307	\$7,491	—	+53%
State/Local Govt Positions Per 10,000 N.C. Residents	513	558	569	558	532	557	—	—	—	+9%
State Bonded Debt Per N.C. Resident	\$109	\$271	\$422	\$488	\$653	\$753	\$742	\$806	\$791	+624%
Outcomes										
Average SAT Scores of N.C. High School Seniors	1002	982	998	1001	1006	1010	1008	1004	—	+0% ¹
Graduation Rate (percent who finish high school in 4 years)	70.0%	61.0%	59.0%	60.0%	61.9%	65.0%	68.1%	69.5%	—	+1%
Percent of N.C. 8th-Graders Scoring Proficient on NAEP Reading ²	—	—	32%	29%	—	27%	—	28%	—	-3 pctg points
Percent Scoring Proficient on NAEP Math ²	—	20%	32%	32%	—	32%	—	34%	—	+12 pctg pts
Reported Index Crimes Per 100,000 N.C. Residents	4,972	5,452	4,791	4,729	4,639	4,623	4,654	4,659	—	-6%
Percentage of N.C. Births Out of Wedlock	24%	33%	35%	35%	37%	38%	40%	—	—	+67%
National Ranking of the Quality of N.C. Highways	8	33	37	33	35	36	—	—	—	-28 ranks
North Carolinians with 4-yr. Degrees: Percent of National Average	—	—	86.0%	90.0%	87.0%	92.3%	91.9%	—	—	-6 pctg pts
Economic										
Index of Price Inflation (GDP Implicit Deflators)	74.600	96.100	103.600	105.700	108.200	111.700	115.400	118.700	121.300	+63%
Resident Population of North Carolina	6,483,344	7,807,095	8,319,523	8,421,367	8,538,579	8,679,291	8,869,655	9,069,310	9,201,151	+42%
Personal Income Per North Carolinian	\$15,398	\$24,743	\$27,488	\$27,904	\$29,387	\$30,713	\$32,247	\$33,636	—	+118%

Sources: *Fiscal*, General Assembly Fiscal Research Division, the Office of State Budget, Planning, and Management, U.S. Census Bureau; *Outcomes*, Dept. of Public Instruction, State Bureau of Investigation, Dept. of Health and Human Services, UNC-Charlotte Center for Transportation Studies, U.S. Census Bureau, National Center for Education Statistics; *Economic*, U.S. Bureau of Economic Analysis, U.S. Census Bureau.

1. Measures the change since 1996. SAT scores were recentered after 1995.

2. Between 1990 and 2003, the U.S. Department of Education did not administer state NAEP assessments on a regular basis.

ABOUT THE JOHN LOCKE FOUNDATION

The John Locke Foundation is a nonprofit, nonpartisan policy institute based in Raleigh. Its mission is to develop and promote solutions to the state's most critical challenges. The Locke Foundation seeks to transform state and local government through the principles of competition, innovation, personal freedom, and personal responsibility in order to strike a better balance between the public sector and private institutions of family, faith, community, and enterprise.

To pursue these goals, the Locke Foundation operates a number of programs and services to provide information and observations to legislators, policymakers, business executives, citizen activists, civic and community leaders, and the news media. These services and programs include the foundation's monthly newspaper, *Carolina Journal*; its daily news service, *CarolinaJournal.com*; its weekly e-newsletter, *Carolina Journal Weekly Report*; its quarterly newsletter, *The Locke Letter*; and regular events, conferences, and research reports on important topics facing state and local governments.

The Foundation is a 501(c)(3) public charity, tax-exempt education foundation and is funded solely from voluntary contributions from individuals, corporations, and charitable foundations. It was founded in 1990. For more information, visit www.JohnLocke.org.



NOTES



*“To prejudge other men’s notions
before we have looked into them
is not to show their darkness
but to put out our own eyes.”*

JOHN LOCKE (1632-1704)

Author, *Two Treatises of Government* and
Fundamental Constitutions of Carolina



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