Joint Legislative Oversight Committee on Capital Improvements

Report to the 2006 Session of the 2005 General Assembly

April 26, 2006

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Joint Legislative Oversight Committee on Capital Improvements

April 26, 2006

To: Senator Marc Basnight, President Pro Tempore of the Senate
Representative James B. Black, Speaker of the House of Representatives
Members of the 2005 N.C. General Assembly

Attached is the report and recommendations from the Joint Legislative Oversight Committee on Capital Improvements. The Commission submits this report pursuant to G.S. 120-259, which states that, "The Committee may make interim reports to the General Assembly on matters for which it may report to a regular session of the General Assembly. A report to the General Assembly may contain any legislation needed to implement a recommendation of the Committee."

The Joint Legislative Oversight Commission on Capital Improvements submits to you the findings and recommendations stemming from its work following the adjournment of the 2005 Session of the 2005 General Assembly.

Respectfully submitted,

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Senator Linda Garrou
Co-Chair

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Representative James W. Crawford, Jr.
Co-Chair

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Representative Thomas E. Wright
Co-Chair

Joint Legislative Committee on Capital Improvements

2005 - 2006 Membership List

President Pro Tempore's Appointments	**Speaker's Appointments**
Senator Linda Garrou, Co-Chair	Representative James W. Crawford, Jr., Co-Chair
Senator Kay R. Hagan	Representative Thomas E. Wright, Co-Chair
Senator Walter H. Dalton	Representative Wilma M. Sherrill
Senator Charlie S. Dannelly	Representative Bill Owens
Senator Richard Y. Stevens	Representative Paul Luebke
Senator Hamilton C. Horton	Representative Roger West
Senator John A. Garwood	Representative Maggie Jeffus
Senator S. Clark Jenkins	Representative Larry M. Bell

Committee Staff

Jim Klingler, Fiscal Research Division
Mona Moon, Fiscal Research Division
Karen Hammonds-Blanks, Fiscal Research Division
Evan Rodewald, Fiscal Research Division
Marilyn Chism, Fiscal Research Division
Jennifer Hoffmann, Fiscal Research Division
Cindy Avrette, General Research Division

Committee Clerk

Jamilah Sabir-Calloway

Charge of the Committee

The Joint Legislative Oversight Committee on Capital Improvements (the Committee) is established in Article 29 of Chapter 120 of the General Statutes. The charge of the Committee is to examine capital improvement projects of State facilities and to monitor the implementation of the Capital Improvements Planning Act established in Article 1B of Chapter 143 of the General Statutes. According to G.S. 120-259(a), "capital improvements" include repairs and renovations to State facilities. Also, capital improvements in the University of North Carolina are under the oversight responsibilities of the Committee.

The Committee has the authority to submit reports to the General Assembly and include recommended legislation as part of its reports.

The Focus of the Committee

At the first meeting in January, the Committee chose to use the legislative interim to focus on the implementation of the Capital Improvements Planning Act (the Act). In carryout its activities, the Committee looked at the following:

- The Capital Improvements Planning Act
- Existing capital improvements practices in the State
- Capital planning practices in state and local government
- North Carolina's Capital Improvement Program

The Capital Improvements Planning Act

The Capital Improvements Planning Act was written into law in 1997 and directs the Governor to develop a comprehensive process for investing in capital improvements for State operations.

Specifically, the Act directs the Department of Administration to establish and maintain an automated State facility inventory containing information on location, occupying agency, size, condition, parking, maintenance data, and estimated life-cycle costs.

The Act also requires that the Office of State Budget and Management develop a weighted list of criteria for evaluating the need and priority of capital improvement projects identified and requested by State agencies. G.S.143-34.43 specifies that these criteria include: "(1) the Preservation of existing facilities. (2) Health and safety considerations. (3) Operational efficiencies. (4) Increased demand for governmental services."

State agencies are required by the Act to submit a six-year inventory of capital improvement needs by September 1 of each even-numbered year to the Office of State Budget and Management and to the Fiscal Research Division of the General Assembly. The inventory is to include a section for repairs and renovations of existing State facilities and a section for real property acquisitions, new construction, and rehabilitations of existing facilities for new purposes or increased footprints.

The Governor is required to take this inventory of capital needs and transform it into a comprehensive six-year capital improvement plan for the State. The plan should include all capital improvement projects, regardless of source of funding, and should be focused and prioritized by the decision making criteria required in G.S.143-34.43. The Act requires that the six-year capital improvement plan be submitted to the General Assembly on or before December 31 of each even-numbered year. The plan should reflect repair and renovation projects, as well as, property acquisition, new construction, and facility rehabilitation projects.

The Office of State Budget and Management brought to the Committee's attention the work that the Office is currently performing to develop the State's first comprehensive six-year capital improvement plan and reported that the General Assembly could expect to see the plan in December 2006. In an effort the support the Governor and the Office of State Budget and Management, the Committee decided to focus on the implementation of the Capital Improvements Planning Act.

The Committee held a series of meetings to hear from experts in public facilities capital planning, State agencies on their capital planning efforts, local governments with strong capital improvement plans, and a potential capital planning peer for North Carolina, the State of Utah. The Committee also heard presenters on a series of topics that play a role in capital improvements planning, including the activities of the Office of State Construction and the Debt

Affordability Study issued by the Office of State Treasurer. Through these meetings, the Committee sought to shed light on the General Assembly's role in the State's Capital Improvement Program and provide input to the Governor as he develops the Six-Year Capital Improvement Plan.

Existing Capital Improvement Practices in the State

The Committee heard from a series of presenters regarding the current capital planning, budgeting, and facility assessment practices in the State. Presentations to the Committee were made by the Office of State Budget and Management, the University of North Carolina General Administration, the North Carolina Division of Parks and Recreation, the Office of State Construction, and Committee staff.

Jennifer Hoffmann of the Fiscal Research Division provided a historical summary of capital planning and budget in the State. In her presentation, she highlighted the following significant events:

- Starting in 1977, the Office of State Budget and Management has periodically required six-year capital requests from State agencies as part of budget preparation.
- In 1982, the Fiscal Research Division issued a report on State Office Construction Policy and found that the State had a bias for new construction; that the appropriations process neglected maintenance, repairs, and renovations of facilities; and the State lacked any long-term capital planning and budgeting
- In 1983, a statewide reserve for repairs and renovations of State buildings was established.
- In 1987, the State Building Commission was established to oversee the construction and management of State facilities. As part of creating the State Building Commission, the General Assembly established the Facilities Condition and Assessment Program (FCAP) in Office of State Construction. Through FCAP, the Office of State Construction examines State buildings for deficiencies and estimates the cost of repair, renovation, or replacement.
- In 1992, the General Assembly's Government Performance Audit Committee (GPAC) reported that reversions to the General Fund determined the level of capital

appropriations from year to year, and the State lacked any long-term capital planning.

- In 1993, the Fiscal Research Division reported that the General Assembly never reviewed the six-year capital needs schedule submitted to the Office of State Budget and Management. Also, the capital need schedule lacked project prioritization, project scope, or a proposed funding plan.
- In 1993, the General Assembly established the Repairs and Renovations Account within the General Fund and requires the State Controller to reserve 3% of the replacement value of all General Fund supported State buildings at the end of each fiscal year.
- In 1997, the Office of State Construction was required to certify the feasibility of each capital improvement project requested by a State Agency.
- Also in 1997, the Capital Improvements Planning Act was enacted into law.

Based on information provided by the State Property Office, Ms. Hoffman cited that the State currently owns 694,718 acres of property. The largest possessor of State lands is the Department of Environment and Natural Resources, who have 85% of all State lands. In terms of physical plant, the State owns 12,091 buildings at a total area of 103,125,504 square feet. The University of North Carolina possesses both the largest number of buildings (2,937) and the largest amount of building area (59,356,106 square feet). In fact, the University possesses roughly 58% of the State's total square footage in buildings.

According to Ms. Hoffmann, over the past 35 years, the State has depended on a variety of funding sources, including General Fund appropriations, departmental receipts, and the issuance of debt to make capital investments. Since 1970, the General Assembly has appropriated funds for capital improvement projects in every year except in fiscal year 1991-92. As a percentage of the General Fund appropriations, the General Assembly appropriated 3.27% for capital improvements from 1981 to 1990. This percentage dropped to 2.08% from 1991-2000. From 2001 to the present, the General Assembly has appropriated 0.70% for General Fund appropriations to capital improvements. In terms of raw General Fund dollars appropriated to capital improvements, the peak was reached in the late 1990's with \$326.8 million appropriated in FY 1996-97, \$332.3 million in FY 1997-98, and \$367.2 million in FY 1998-99. In the current fiscal year, the General Assembly appropriated the largest raw dollar General Fund appropriation to capital improvements since FY 1999-2000 at $179.9 million.

Prior to FY 2000-01, the State relied on general obligation bonds as the preferred debt instrument for funding capital improvement projects. Between 1971 and 2000, the General Assembly authorized $8.56 billion in general obligation bonds with $4.09 billion going to State owned facilities and property. Since 2000, the General Assembly has relied primarily on authorizing the issuance of special indebtedness, in the form of certificates of participation, to debt finance capital improvements. Since 2000, the General Assembly has authorized the issuance of $1.3 billion in special indebtedness, which does not require a vote of the people.

Since the late 1990's, the use of debt to finance capital improvements has increased, particularly the use of special indebtedness in the past five years. While the use of General Fund appropriations for capital improvements have dropped as a percentage of overall General Fund appropriations, the General Assembly still appropriated $179.9 million to capital projects in FY 2005-06. When debt and appropriations are considered together, the State has allocated significant resources to capital investment. What has been missing is a comprehensive capital improvement plan to prioritize capital expenditures and inform decision-makers of the full extent of capital needs that might be overlooked in the current process.

The Office of State Construction is responsible for certifying whether a proposed capital improvement project is feasible (G.S.143-341). The Office of State Construction presented to the Committee as explanation of their role in the capital budgeting process and their charge of certifying capital projects. When a State agency decides to pursue a capital project, that agency must submit a project description and cost estimate to the Office of State Construction using a form called an OC-25. Through this project description and cost estimate, the Office of State Construction certifies the project feasibility. To certify the project, Office of State Construction examines the project scope, justification of need, building program, site development, detailed design budgets, construction budgets, and equipment budgets, and project scheduling.
Once certified by Office of State Construction, the State agency submits their project certification with the capital budget request made to the Office of State Budget and Management. According to the Office of State Budget Management, the capital budget request must contain a

detailed description of the project, a programmatic justification for the project, a schedule, and an estimate of the impact to the operating budget. The State agency is also required to submit a six-year capital improvement needs schedule. This information, along with the certified project description and cost estimate was typically used to develop the Governor's budget recommendation to the General Assembly. According to the Office of State Budget and Management, this required information now feeds into the Capital Improvement Program for the purpose of developing a six-year capital plan.

The Office of State Construction operates the Facility Condition Assessment Program (FCAP), a program designed to monitor repair, renovation, and replacement needs. FCAP is staff by two teams. Each team is composed of an architect or civil engineer, a mechanical engineer, and an electrical engineer. FCAP examines buildings that are greater than 3,000 square feet and attempts to assess each covered building once every three years. In addition to the building, FCAP assesses site considerations and infrastructure conditions. After an FCAP assessment, the State agency receives a condition report that lists deficiencies, recommended corrections, time priorities, and cost estimates.

Capital Improvement Programming

-Organizations develop capital improvement programs (the CIP) to evaluate capital improvement needs for the subsequent five to ten years. Through the CIP, an organization will analyze all capital projects of sufficient size to determine need, the priority, the estimated cost, source of funding for the project, and the impact on the operating budget. The resulting product is a multi-year capital improvement plan, updated annually or biennially, that informs the organization of capital investment priorities and allows that organization to prepare for those investments. Typically, the first year of the capital improvement plan becomes the organization's capital budget.

The Committee heard a presentation about best practices in capital improvement planning from Jack Vogt of the University of North Carolina at Chapel Hill School of Government. According to Dr. Vogt, a good capital improvement plan should have the following characteristics:

- Cover a multi-year period

- Capital requests that derive from identified needs, such as from a capital asset management system; capital needs assessments; business and strategic plans; legal and regulatory requirements; and request from citizen groups and task forces
- Project detail for each capital request
- Prioritization of capital projects based on established criteria
- Forecasts of appropriations or expenditures for proposed capital projects
- Forecasts of funding for the proposed projects
- Estimates of the impact to the operating budget for each project
- First year represents the capital budget for the upcoming fiscal year, and new projects typically enter in the final year of the plan

Dr. Vogt pointed out that the capital improvement priorities published in the plan are subject to change. Emergencies, unforeseen circumstances, a change in mission for the organization, and availability of resources can affect the ranked order of projects. A strong capital improvement program recognizes and responds to changing circumstances that can alter the authorization, budgeting, and implementation of projects listed in the capital improvement plan.

Identifying Capital Needs

Strong capital improvement programs are built on existing planning activities within the organization. In Wake County's presentation to the Committee, they cited a Comprehensive Master Planning process as the foundation for their CIP. For particular county functions, Wake County staff work with task forces, elected officials, and professional consultants to identify the future mission of county departments, expected service levels, and facilities needs to meet departmental missions. For example, Wake County has developed a 30-year Master Plan for the courts and a 7-year Master Plan for the libraries. Wake County also has county-wide master plans for roof replacements and mechanical system replacements.

The City of Winston-Salem uses a variety of existing plans on which to build their CIP. Types of plans used include: the City Council's 4-year Strategic Plan, the Comprehensive Long-Range Development Plan, the Recreation Center/Park Locator Model, the Fire State Locator Model, and the 5-year Housing Plan. Prior to updating the capital improvement plan, the city staff review all city plans to identify new projects for future years and prioritize projects throughout the plan. The State often makes use of these techniques when identifying capital improvement needs, and the planning activities of many State agencies could support the development of a comprehensive capital improvement program for the State. As stated earlier, the Office of State Construction administers the Facilities Condition Assessment Program (FCAP). FCAP helps to determine the repairs, renovations, and replacement needs of every State facility, on a 3-year cycle. With FCAP, State agencies know the deficiencies for each of their existing buildings and the cost to fix those deficiencies. State agencies also know which facilities are beyond their useful life and need to be replaced.

FCAP does not help State agencies determine future capital needs to meet growing or changing missions. Many State agencies engage in long-range planning and perform capital needs assessments based on their long-range plans. The Committee heard an example of such planning effort from the University of North Carolina General Administration. The 1998 study by Eva Klein and Associates examined the University System for differing missions among the campuses; funding equity across campuses and identified capital improvements necessary to bring campuses to the same level; and FCAP evaluations of University facilities. The consultants developed recommendations on capital improvements necessary to meet the University's growing mission, have facilities appropriate for the diverse mission of the University, and improve the overall quality of facilities in the University. This study became the basis for the University's 10-year capital plan and the foundation for the 2000 Higher Education Bond Program.

The NC Division of Parks and Recreation presented to the Committee on their System-wide Plan for the North Carolina State Parks System. The System-wide Plan establishes the priority characteristics that the State's system of parks should have. These priority characteristics are considered representative of the types of biological, geological, archeological, and scenic systems in North Carolina. The lists of characteristics are generated by Resource Evaluation Committees comprising of conservation experts. The Division then inventories the Parks System for the priority characteristics. The identification and planning for new State parks is determined by extent to which the proposed park land has needed priority characteristics.

If the Division identifies a potential addition to the Parks System, then they will develop a conceptual plan for the new park. Once enough park land is acquired, the Division will develop a master plan for the new park, including the need and timing for facilities. The proposed schedule for land acquisition and facilities construction in the new park's master plan inform the Division of the resources need from the State's Parks and Recreation Trust Fund.

Prioritizing Projects within the Capital Improvement Plan

According to Dr. Vogt, an organization's capital improvement program typically uses a variety of methods to rank projects. The experience of decision-makers, professional or elected, plays a role in ranking projects. Also, the priority of separate departments or agencies submitting capital requests can determine the ranking of projects for that department or agency. Organizations with strong capital improvement programs attempt to set clear and objective criteria for evaluating and ranking projects across functional areas, departments, and agencies. These criteria also force decision-makers to test their own assumptions about which capital projects are of the highest priority. According to Dr. Vogt, typical criteria may include:

- Legal mandates
- Public health and safety
- Governing board's goals
- Improves efficiency and quality
- Maintains standard of service
- Supports economic development
- Supports new services
- Availability of outside funds

Wake County's Capital Improvement Plan is developed by prioritizing projects using ranked criteria. In rank order, Wake County assesses whether a project: (1) meets life, safety, and environmental concerns; (2) provides budgetary cost savings; (3) maintains the integrity of existing capital assets; (4) meets emerging needs or higher service levels; (5) satisfies the objectives of established County plans without expanding the County's mission; (6) meets planned expansion of the County's mission, and; (7) matches contributions by partners for community projects.

As presented by Dr. Vogt, Chatham County takes this method a step further. Within each criterion, a project can be awarded points. For instance, under the criterion for “Safety”, a project can be awarded 0 to 14 points. Under the criterion for “Service addition”, a project can earn 0 to 3 points. With the addition of the point system, Chatham County weighs the criteria against each other and weighs proposed projects within each criterion. Each project gets a total point value which establishes the rank order.

In developing a method for prioritizing projects in the State’s Six-Year Capital Improvement Plan, the Governor and the General Assembly face a real challenge. The State enterprise-wide capital program is immense, and each year, the Governor and the General Assembly must prioritize investments in capital improvement needs. Currently, the capital needs outstrip the State’s ability to fund all facility deficiencies across the enterprise. An objective set of criteria could greatly help the Governor and the General Assembly fund capital priorities with limited resources. The challenge is designing a set of criteria that fairly assesses the diverse mission of the State. It is difficult to establish criteria that will properly rank the need for museums and parks against the need for prisons and mental health facilities.

Funding the Capital Improvement Plan

Plans are often shelved and forgotten if there is not a clear means to implement the plan. Many of the speakers before the Commission stated that for a capital improvement plan to be successful, it must contain a feasible funding proposal. To reiterate the basic characteristics for a good capital improvement plan, the plan should list the appropriations or expenditures for each project, forecast the availability of the sources of funds, and estimate the impact of the proposed projects on the operating budget.

Within their capital improvement plans, the City of Winston-Salem and Wake County list the proposed sources of funding for each project, whether the project is pay-as-go or debt financed. Both the City and the County list anticipated operating impacts to the budget for each project. The City of Winston-Salem, which relies primarily on debt financing to fund its capital improvement plan, uses a financial forecasting model to determine the availability of funding for their capital improvement plan. Winston-Salem takes the projects proposed to be funded pay-as-go, and along with projections for the City's operating budget, the City compares these proposed expenditures against forecasted revenues in future years. For projects proposed to be funded with debt financing, the City assesses the schedule for issuance of authorized debt and capacity in the debt service fund for projects. If the City has insufficient cash reserves or debt capacity to fund projects in the capital improvement plan, then the projects will be added to an unfunded list. This list often becomes the basis for a future bond referendum or debt authorization.

Wake County employs the same type of financial forecast to determine the availability of specific resources for specific projects proposed in the capital improvement plan. The County has also recognized the importance of mixing the sources of funds to strike a balance of resources for the capital improvement program.

As presented by Mona Moon of the Fiscal Research Division, the charts below show the advantages and disadvantages of pay-as-go funding and debt financing:

Pay-as-go Advantages	**Disadvantages**
• Quick implementation • Project is paid-in-full upon appropriation • Minimize construction cost inflation • No financing costs or interest on borrowing • No need for voter approval • Appropriate use of nonrecurring budget Quick availability	• Significant upfront costs • Projects often lose out to high priority operating needs in the budget process • When revenues fall short, funding is easily diverted • Equity – Current taxpayers pay for future users/beneficiaries

Debt Financing Advantages	Disadvantages
• Spreads costs over many years (10-30 years) • With proper planning and debt management, long-term capital needs can be funded with minimal up front costs (i.e. cash flowed) • Equity – Future users/beneficiaries help pay for construction	• Increases overall project costs: administrative and interest expenses • Debt Service requirements are rigid: can crowd out future operating budgets & reduce flexibility • Certain forms require voter approval

Pay-as-go funding is often used by local governments and other organizations to fund smaller projects with shorter life-cycles. Debt is often reserved for financing large, higher priced capital facilities with long life-cycles. The characteristics of the project (e.g. the need, the cost, life-cycle, revenue generation, and the schedule) will often favor either pay-as-go or debt, but overuse by one type of funding across the capital improvement plan can limit fiscal flexibility of the organization. In addition to proposing the source of funding for each project in their capital improvement plan, Wake County has an overall debt-ratio target for their plan. As a stated policy, Wake County maintains a target goal of funding their capital improvement plan with 80% debt financing and 20% pay-as-go funding.

The Committee heard from the State Treasurer regarding the State's capacity to issue debt. The Six-Year Capital Needs Inventory issued by the Office of State Budget and Management cited $1.6 billion in identified capital improvements needs across State government, excluding the University of North Carolina and the Department of Transportation. Based on the analysis by the Debt Affordability Advisory Committee and presented by the State Treasurer, the State does not have sufficient debt capacity to debt finance all of the capital improvement needs in State government. In order to adequately fund the State's Six-Year Capital Improvement Plan, the General Assembly will need to develop ongoing pay-as-go resources and authorize the issuance of debt.

While a debt-ratio policy, like the one used by Wake County, might be helpful to the State, there is no established best practice in states for debt-ratio policies. The Debt Affordability Advisory Committee has offered the targeted policy of keeping General Fund debt service to no more than

4% of General Fund tax revenues, with an absolute maximum of 4.75%. To assist the State with achieving an appropriate balance of pay-as-go and debt, the Governor should not only propose the sources of funding in his Six-Year Capital Improvement Plan, but provide the policies guiding the use of debt financing and pay-as-go funding in the plan. The balance could be based on the policy set forth by the Debt Affordability Advisory Committee or other cited best practices in capital planning.

The State of Utah

The Committee heard from Steven Allred, legislative staff from the State of Utah, regarding that State's capital improvement program. In Utah's CIP, state agencies submit their eligible capital improvement projects directly to the Division of Facilities Construction and Management for evaluation. The higher education agencies first submit their eligible capital improvement requests to the Board of Regents for evaluation and then submit to the Division of Facilities Construction and Management. Once the Division evaluates state agency requests and higher education requests, all proposed capital projects are forwarded to the State Building Board. The State Building Board is an independent eight member board composed of seven members appointed by the Governor and one ex-officio member, the Director of the Governor's Office of Planning and Budget. The State Building Commission is responsible for issuing the State's Five-Year Capital Improvement Plan. The plan is used by both the Governor and the State Legislature.

When the Board of Regents receives capital requests from the higher education agencies, the Board has a specified process for evaluating and prioritizing projects. The Board uses space standards developed by the Division of Facility Construction and Management. The Board then compares existing space, the established space standards, and projected service levels for each institution. A "gap report" is issued for each institution measuring the difference between existing capacity and future need. Proposed capital projects are prioritized by how best the project closes the institution's "gap". Additional points are awarded for life safety and infrastructure considerations and for the availability of private funding.

When the State Building Board receives all requests from state agencies and the Board of Regents, the Building Board evaluates the request on a set of criteria based on six strategic objectives. The criteria of the State Building Board, as presented by Mr. Allred are:

- Life safety and other deficiencies
- Service levels and other program growth considerations
- Program efficiency
- Program effectiveness
- Whether facilities are necessary for critical programs
- Availability of alternative funding sources

Individual members of the State Building Board score each project for each of the first five objectives listed above. The sixth objective is calculated separately. Points are added for life safety considerations, short-term opportunity, and the availability of outside funding. Scores are averaged across the Building Board membership and totaled for each project. Top 10 projects are listed in the first year of the Five-Year Capital Improvement Plan. The second 10 projects are list in the second year, and so on. Neither the State Building Board nor the Board of Regents are bound by the ranking results of the established ranking systems. Both Boards make any necessary adjustments and then approve the plan by vote. The plan is then forwarded to the Governor and the State Legislature for development of the capital budget.

The State of Utah provides an example of a functioning capital improvement program implemented by a state. It should be noted that the successful functioning of Utah's capital improvement program may be aided by its scope. For example, the current version of the Building Board Five-Year Plan lists 10 projects totaling $276 million for FY 2006-07. By comparison, the first year of the Six-Year Capital Needs Inventory released by Office of State Budget and Management in May 2005 listed several hundred projects totaling $824 million, not including the University of North Carolina. Of that amount in identified capital needs, $702 million was for new facility construction. While Utah could provide an example to assist the Governor and the General Assembly to organize the State's capital improvement program, the shear size of North Carolina's capital facility program may present barriers to plan implementation that the example of Utah might not address.

North Carolina's Capital Improvement Program

According to information from the Office of State Budget and Management, the General Assembly can expect to receive a six-year capital improvement plan in December 2006. As a way to test the strengths and weaknesses of the new capital improvement program, the Office of State Budget and Management will attempt to submit a less-developed version of the capital plan for the 2006 Session of the 2005 General Assembly. The Governor's Office hopes to learn from the process of developing and submitting this less-developed plan to strengthen the development of the Six-Year Capital Improvement Plan for December.

The Committee heard from Jim Lora, Assistant State Budget Officer for Capital Projects, regarding the status of the State's Capital Improvement Program. The first step in the State's capital planning process is the development of the Six-Year Capital Needs Inventory. The inventory is required in the Capital Improvements Planning Act and was first developed in 2005. The Office of State Budget and Management is currently updating the Capital Needs Inventory for FY 2006-07. The needs inventory is comprised of capital requests submitted by State agencies. For a project to be considered in the inventory, the State agency must submit a formal budget request for the project with all supporting documentation. For repairs and renovation projects the State agencies must submit any analyses from the Facility Condition Assessment Program. All proposed projects must provide an evaluation based on the Office of State Budget and Management's established criteria.

According to Mr. Lora, the Office of State Budget and Management anticipates developing a funding model to establishing a target for proportioning available funds across either State agencies or broad functional areas. Some agency characteristics that the Office of State Budget is considering include: the replacement value of facilities, the building condition listed in FCAP, total building area, age of buildings, agency office leasing, and changes in demand for the agency.

Within each agency or functional area, the Office of State Budget and Management anticipates prioritizing projects according to established objective criteria. The criteria are organized under two broad categories, “critical” needs and “strategic” needs. As presented by Mr. Lora, critical needs include the following criteria:

- Life safety and emergency issues
- Federal or state mandates
- Timing issues involving binding agreements or sequencing with other capital projects

In addition to these critical needs criteria, Mr. Lora provided a list of strategic needs criteria for ranking capital improvement projects:

- Alignment with the Governor’s agenda or agency’s mission
- Improves service effectiveness or meets program growth/expansion
- Agency priority
- Improves service efficiency or cost effectiveness
- Fiscal considerations, such as the availability of outside funding or the project impact on the State debt capacity
- Environmental impact or energy conservation
- Supports and preserves existing facilities

During Mr. Lora’s presentation to the Committee, he discussed many aspects about funding the Six-Year Capital Improvement Plan, but it remains unclear whether funding for implementation of the plan will be integrated into the plan itself. Mr. Lora recognized the need for balancing pay-as-go sources of funding with debt financing and that debt alone will not meet the State’s extensive capital needs. Where the issuance of debt is planned for capital improvement projects, the issuance should fit with the State’s debt affordability guidelines. The Six-Year Capital Improvement Plan should include a multi-year funding plan to address implementation. Mr. Lora also mentioned that funds should be distributed across State agencies in a fair and equitable manner to meet the capital improvement needs resulting from the State’s diverse mission. It is not clear whether the Six-Year Capital Improvement Plan, as submitted by the Governor, will propose sources of funding for each project or establish~~es~~ clear funding policies and guidelines, such as the targeted use of debt.

Committee Recommendations for the 2006 Session

Through the Committee's work, a number of issues have been brought to light regarding the State's efforts to plan for future capital investments. The Committee feels that for the State to have an effective Capital Improvement Program, (i) the Governor must submit a capital plan that describes how the plan should be funded and (ii) the General Assembly must provide the necessary funding to implement the plan.

Based on information provided by the Office of State Treasurer, Debt Affordability Commission, and other guests of the Committee, the Joint Legislative Oversight Committee on Capital Improvements firmly believes that sole reliance on issuing debt is insufficient to meet the State's capital investment requirements. For the State to meet the current and future needs of its citizens, the General Assembly must look to a mix of funding sources to implement a Capital Improvement Program. In other words, the General Assembly will need to use **cash on hand** as well as **debt** to pay for needed capital investments in State operations.

The Joint Legislative Oversight Committee on Capital Improvements makes the following recommendations for the 2006 Session of the 2005 General Assembly:

1. **Revise the Capital Improvements Planning Act (Article 1B, Chapter 143) to require that the Six-year Capital Improvement Plan, as submitted by the Governor, identify projects in priority order and propose sources of funding for each project.**

2. **Establish a Capital Improvements Reserve Account within the General Fund similar to the Repair and Renovation Reserve Account to fund real property acquisition, construction of new State facilities, and the expansion or rehabilitation of existing State facilities. The General Assembly will designate the capital improvement projects funded from this account based on the State's Six-Year Capital Improvement Plan, the Governor's recommended priorities, and the General Assembly's priorities.**

3. **Transfer 25% of the June 30th unreserved General Fund balance to the Capital Improvements Reserve Account.**

4. **Establish a $50 million recurring appropriation to the Capital Improvements Reserve Account.**

5. **Direct State agencies to use existing plans and specifications for construction projects where feasible. Also direct State agencies to consult with the Department of Administration about the availability of appropriate existing plans and specifications before designing a construction project.**

In addition to these recommendations, the Joint Legislative Oversight Committee on Capital Improvements will continue to study the following issues:

- The percentage allocation, as prescribed by the General Assembly, for repair and renovation funding between the University of North Carolina and all other State agencies
- The design and construction review processes for State facilities. The Committee has asked the Office of State Budget and Management and the State Construction Office to analyze the current review practices and return with recommendations to the next meeting of the Committee.
- The identification of dedicated, recurring revenues to support the implementation of the State's Capital Improvement Program.
- The practices and policies of the State for authorizing debt financing to support the implementation of the State's Capital Improvement Program.

The Committee will bring any findings and recommendations on these issues to the 2007 Session of the 2007 General Assembly.

Appendix

Draft Legislation for Introduction in the 2006 Session

1. Bill Draft 2005-RBz-38 [v.3]: Revise Capital Improvement Plan

2. Bill Draft 2005-RBz-40 [v.4]: Capital Improvements Reserve Account.

3. Bill Draft 2005-RBz-41 [v.4]: Funds for Capital Improvement Reserve Account.

4. Bill Draft 2005-LEz-255 [v.3]: Use of Existing Plans for State Construction

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 2005

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BILL DRAFT 2005-RBz-38 [v.3] (04/25)

(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
4/25/2006 6:05:27 PM

Short Title:	Revise Capital Improvement Plan.	(Public)
Sponsors:	.	
Referred to:		

A BILL TO BE ENTITLED

AN ACT TO INCLUDE IN THE SIX-YEAR CAPITAL IMPROVEMENT PLAN THE RECOMMENDED FUNDING SOURCES FOR THE PROJECTS PROPOSED.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 143-34.45 reads as rewritten:

"**§ 143-34.45. Six-year capital improvement plan.**

(a) The State capital improvement plan shall address the long-term capital improvement needs of all State government agencies and shall incorporate all capital projects, however financed, proposed to meet those needs, except that transportation infrastructure projects shall be excluded. On or before December 31 of each even-numbered year, the Director of the Budget shall prepare and transmit to the General Assembly a six-year capital improvement plan. When preparing the plan, the Director of the Budget shall consider the capital improvement needs estimates submitted by State agencies as required in G.S. 143-34.44. The plan shall be prepared in two parts.

(b) The first part of the capital improvement plan shall set forth repair and renovations requirements that, in the judgment of the Director of the Budget, must be met to protect and preserve existing capital improvement facilities. ~~General Fund expenditure levels anticipated in this part of the plan shall be consistent with the formula establishing the repair and renovation reserve in G.S. 143-15.3A.~~The plan shall identify individual projects in priority order by State agency and shall specify the proposed means of financing.

(c) The second part of the capital improvement plan shall set forth an integrated schedule for land acquisition, new construction, or rehabilitation of existing facilities that, in the judgment of the Director of the Budget, should be initiated within each year of the six-year planning period. ~~The plan shall contain an estimated schedule for each~~

~~project, along with estimates of planning, design, and construction cost.~~ The plan shall contain all of the following for each project:

(1) An estimate of land acquisition and construction or rehabilitation costs.

(2) The proposed means of financing the project. Where the means of financing would involve direct or indirect debt service obligations, the plan shall include a schedule of those obligations.

(3) An estimated schedule for the completion of the project. "

SECTION 2. This act is effective when it becomes law.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 2005

U **D**

BILL DRAFT 2005-RBz-40 [v.4] (04/25)

(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
5/4/2006 11:29:56 AM

Short Title: Capital Improvements Reserve Account. (Public)

Sponsors: .

Referred to:

A BILL TO BE ENTITLED

AN ACT TO ESTABLISH THE CAPITAL IMPROVEMENTS RESERVE ACCOUNT AND TO RESERVE ONE-FOURTH (1/4) OF THE UNRESERVED GENERAL FUND YEAR-END CREDIT BALANCE TO THE ACCOUNT.

The General Assembly of North Carolina enacts:

SECTION 1. Article 1 of Chapter 143 of the General Statutes is amended by adding a new section to read:

"G.S. **143-15.3F. Capital Improvements Reserve Account.**

(a) Account and Use. – The Capital Improvements Reserve Account is established as a reserve in the General Fund. The funds in the Account shall be used only for one or more of the following capital improvement projects supported from the General Fund:

(1) Real property acquisition.

(2) Construction of a new State facility.

(3) Expansion of an existing State facility.

(4) Rehabilitation of an existing State facility to accommodate a use for which the existing facility was not originally designed.

(b) Source of Funds. – The State Controller shall reserve to the Capital Improvements Reserve Account one-fourth of any unreserved credit balance. The General Assembly may appropriate additional funds to the Account.

(c) Appropriation. – Funds in the Capital Improvements Reserve Account shall be expended only by an appropriation by the General Assembly. The General Assembly shall designate the capital improvement projects to be funded from this Account in the Capital Improvements Appropriation Bill or another appropriations bill."

SECTION 2. G.S. 143-15.2 reads as rewritten:

"§ 143-15.2. Use of General Fund credit balance; priority uses.

(a) Definition. -- As used in G.S. 143-15.3, 143-15.3A, and ~~143-15.3B,~~143-15.3F, the term "unreserved credit balance" means the credit balance ~~amount,~~amount remaining in the General Fund at the end of a fiscal year, as determined on a cash basis, before funds are reserved by the State Controller ~~to the Savings Reserve Account or the Repairs and Renovations Reserve Account pursuant to G.S. 143-15.3 and G.S. 143-15.3A.~~in accordance with this section.

(b) Transfers. – The State Controller shall transfer funds from the unreserved credit balance to the following reserve accounts. The Controller must transfer funds to the accounts in the order listed and must satisfy the requirements set for an account before reserving any funds for the next account in the list.

(1) The Savings Reserve Account ~~in accordance with G.S. 143-15.3(a).~~established in G.S. 143-15.3.

(2) The

~~(c) The State Controller shall transfer funds from the unreserved credit balance to the~~ Repairs and Renovation Reserve Account ~~in accordance with G.S. 143-15.3A(a).~~established in G.S. 143-15.3A.

(3) The Capital Improvements Reserve Account established in G.S. 143-15.3F.

(d) Repealed by Session Laws 2000, ch. 67, s. 7.7(e), effective June 30, 2001.

(e) Remaining Balance. – The General Assembly may appropriate that part of the anticipated General Fund credit balance not expected to be reserved only for capital improvements or other one-time expenditures."

SECTION 3. G.S. 143-15.3 reads as rewritten:

"**§ 143-15.3. ~~Use of General Fund credit balance; priority uses.~~Savings Reserve Account.**

(a) There is established a Savings Reserve Account as a restricted reserve in the General Fund. The State Controller shall reserve to the Savings Reserve Account one-fourth of any unreserved credit balance ~~remaining in the General Fund at the end of each fiscal year~~ until the account contains funds equal to five percent (5%) of the amount appropriated the preceding year for the General Fund operating budget, including local government tax-sharing funds, that were directly appropriated. In the event that the one-fourth exceeds the amount necessary to reach the five percent (5%) level, only funds necessary to reach that level shall be reserved. ~~If there are insufficient funds in the unreserved credit balance for the Savings Reserve Account and the Repairs and Renovations Reserve Account, then the requirements of this section shall be complied with first, and any remaining funds shall be reserved to the Repairs and Renovations Reserve Account, in accordance with G.S. 143-15.3A.~~

(a1) If the balance in the Savings Reserve Account falls below the five percent (5%) level during a fiscal year, the State Controller shall, in accordance with subsection (a) of this section, reserve to the Savings Reserve Account for the following fiscal years up to one-fourth of any unreserved credit balance remaining in the General Fund at the end of each fiscal year until the account again equals the five percent (5%) level set out in subsection (a) of this section.

(a2) The transfer of funds to the Savings Reserve Account in accordance with this section or any other provision of law is not an "appropriation made by law", as that phrase is used in Article V, Section 7(1) of the North Carolina Constitution.

(b) The Director may not use funds in the Savings Reserve Account unless the use has been approved by an act of the General Assembly."

SECTION 4. This act becomes effective July 1, 2006.

GENERAL ASSEMBLY OF NORTH CAROLINA

SESSION 2005

U **D**

BILL DRAFT 2005-RBz-41 [v.4] (04/25)

(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
4/26/2006 9:22:07 AM

Short Title:	Funds for Capital Improvement Reserve Account.	(Public)
Sponsors:	.	
Referred to:		

A BILL TO BE ENTITLED

AN ACT TO APPROPRIATE FIFTY MILLION DOLLARS TO THE CAPITAL IMPROVEMENTS RESERVE ACCOUNT AND TO STATE THE INTENT OF THE GENERAL ASSEMBLY TO APPROPRIATE FIFTY MILLION DOLLARS TO THE ACCOUNT EACH SUBSEQUENT FISCAL YEAR.

The General Assembly of North Carolina enacts:

SECTION 1. There is appropriated from the General Fund to the Capital Improvements Reserve Account the sum of fifty million dollars ($50,000,000) for the 2006-2007 fiscal year. It is the intent of the General Assembly that this appropriation be a recurring appropriation.

SECTION 2. Section 1 of this act becomes effective July 1, 2006, only if [Draft Bill 2005-RBz-40], which creates the Capital Improvements Reserve Account, is enacted by the 2005 General Assembly during the 2006 Regular Session. The remainder of this act is effective when it becomes law.

GENERAL ASSEMBLY OF NORTH CAROLINA
SESSION 2005

H **D**

BILL DRAFT 2005-LEz-255 [v.3] (5/1)

(THIS IS A DRAFT AND IS NOT READY FOR INTRODUCTION)
5/8/2006 11:56:09 AM

Short Title:	Use of Existing Plans for State Construction.	(Public)
Sponsors:	Representative.	
Referred to:		

A BILL TO BE ENTITLED

AN ACT TO REQUIRE STATE AGENCIES TO USE EXISTING PLANS FOR STATE CONSTRUCTION PROJECTS WHERE FEASIBLE.

The General Assembly of North Carolina enacts:

SECTION 1. G.S. 143-31.1 reads as rewritten:

"**§ 143-31.1. ~~Study~~ Use of existing plans for State construction projects; study and review of plans and specifications for building, improvement, etc., projects.**

(a) All State agencies shall use existing plans and specifications for construction projects, where feasible. Prior to designing a project, State agencies shall consult with the Department of Administration on the availability of appropriate existing plans and specifications and the feasibility of using them for a project.

(b) ~~It shall be the duty and responsibility of the~~The Director of the Budget ~~to~~ shall determine whether buildings, repairs, alterations, additions or improvements to physical properties for which appropriations of State funds are made have been designed for the specific purpose for which such appropriations are made, that such projects have been designed giving proper consideration to economy in first cost, in maintenance cost, in materials and type of construction. Architectural features shall be selected which give proper consideration to economy in design. The Director of the Budget shall have prepared a complete study and review of all plans and specifications for such projects and bids on same will not be received until the results of such study and review have been incorporated in such plans and specifications, and until economic conditions of the construction industry are considered by the Office of State Budget and Management to be favorable to the letting of construction contracts. The Director of the Budget may, when he considers it in the best interest of the State to do so, terminate design contracts when it is documented that the designer has failed to perform the conditions enumerated in the contract.

Notwithstanding G.S. 143-135, the Director of the Budget may authorize the Department of Health and Human Services and the Department of Correction to use funds necessary for projects that correct deficiencies, improve living conditions, or renovate unneeded patient space for State office space."

SECTION 2. G.S. 116-31.11(a) reads as rewritten:

"(a) Notwithstanding G.S. 143-341(3) and G.S. 143-135.1, the Board shall, with respect to the design, construction, or renovation of buildings, utilities, and other property developments of The University of North Carolina requiring the estimated expenditure of public money of two million dollars ($2,000,000) or less:

(1) Conduct the fee negotiations for all design contracts and supervise the letting of all construction and design contracts.

(2) Develop procedures governing the responsibilities of The University of North Carolina and its affiliated and constituent institutions to perform the duties of the Department of Administration and the Director or Office of State Construction under G.S. 133-1.1(d) and G.S. 143-341(3).

(3) Develop procedures and reasonable limitations governing the use of open-end design agreements, subject to G.S. 143-64.34 and the approval of the State Building Commission.

(4) Use existing plans and specifications for construction projects, where feasible. Prior to designing a project, the Board shall consult with the Department of Administration on the availability of existing plans and specifications and the feasibility of using them for a project. "

SECTION 3. This act becomes effective July 1, 2006, and applies to construction projects on which design is begun after that date.