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How North Carolina intervenes to get local governments on fiscal track

By

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Last week, two troubled North Carolina towns — Spring Lake and Scotland Neck — won praise from state Treasurer Dale Folwell after they stepped up to avoid state oversight by passing what he called responsible budgets in the face of serious financial difficulties.

The two municipalities had voluntarily entered into a financial management agreement with the North Carolina Local Government Commission to help them meet their obligations and duties under the Local Government Budget and Fiscal Control Act.



"We're very glad that Spring Lake and Scotland Neck have made these decisions," said North Carolina Treasurer Dale Folwell.

Folwell said the agreement was part of a multi-step process that included the Local Government Commission, the North Carolina League of Municipalities and the North Carolina Association of County Commissioners.

The goal: "To figure out what's right, get it right and keep it right to determine if these entities were viable concerns going forward," Folwell told The Bond Buyer Tuesday.

Both towns are on the state's Unit Assistance List, a watchlist for troubled local governments facing financial issues involving their general fund or water and sewer funds, internal control deficiencies or other problems such as failure to submit annual audits.

Financial accountability agreements are a relatively new tactic that was developed by staff at the Local Government Commission, which operates out of the state treasurer's office.

The agreements are a step that municipalities on the watchlist can take to avoid a state takeover of their finances. These agreements list the localities' governing board's responsibilities, define the LGC's staff responsibilities and outline what materials and documents the municipalities must provide to LGC staff for review.

Folwell said that just few days before Spring Lake and Scotland Neck approved their budgets, there had been talk that they might regress back to the old way of doing things, which would have caused operating deficits.

"We're very glad that Spring Lake and Scotland Neck have made these decisions," he said. "So hopefully these agreements are a step where they have heard us, understand what we're trying to tell them and they're actually doing something about it."

"The Local Government Commission was created during the Great Depression and [the bankruptcy of Asheville, North Carolina](#)," Folwell said. "For many decades it was one of the only things of its type in the United States."

The LGC, created in 1931, has the responsibility for overseeing over 1,300 entities in the state — 100 counties, 548 cities, and large school districts, airport authorities, universities and hospitals.

In the United States, 22 states make an effort to monitor the fiscal health of local governments, according to Pew Trusts, in that these states "actively and regularly review financial information from local governments with the aim of trying to detect fiscal distress or, more generally, assessing their fiscal conditions."

Out of those 22, Pew said that only eight can be called “early warning” states, which means states which have laws to show when a local government is in fiscal distress and have systems in place to identify the warning signs that a locality is heading in that direction.

“We get calls every few months from states who want to model what we do,” Folwell said.

“North Carolina ranks with New Jersey and Pennsylvania as having the most effective and proactive state municipal oversight bodies,” William Glasgall, senior vice president and director, state and local initiatives at the Volcker Alliance, told The Bond Buyer. “Of the eight states with early warning system for signs of municipal distress (according to Pew Trusts), North Carolina and New Jersey stand out for their systematic reviews of muni budgets and bonding plans. And Pennsylvania, over the years, has strengthened its oversight regime and set deadlines for exiting it as well.”

Folwell chairs the LGC, whose staff come from the Department of State Treasurer’s State and Local Government Finance Division.

“The LGC has provided another layer of protection to investors in local government paper in North Carolina. The intervention is key to preventing a meltdown scenario,” said John Hallacy, founder of John Hallacy Consulting LLC. “Most of the localities have benefited from the direction of the LGC and there have not been many complaints about the LGC being overbearing.”

“We want to borrow money on a tax-free basis with a check-and-balance between the local revenue and borrowing to much money,” Folwell said.

Spring Lake, population 12,000, reported \$1.1 million of general obligation bond debt and \$1.8 million of federal revolving loan debt as of June 30, 2020, according to its most recent audited financial statements.. Scotland Neck, population about 2,000, does not post any financial information [on its website](#).

Folwell said the fiscal problems of the municipalities were exacerbated by the COVID-19 pandemic, but were not the root cause because they had been going on for many years.

There are currently five municipalities in the state under LGC financial control: Kingstown in Cleveland County, the Cliffside Sanitary District in Rutherford County, Robersonville in Martin County, Pikeville in Wayne County, and Eureka also in Wayne County, according to commission's website.

The LGC voted at an [emergency meeting](#) on June 22 to issue a notice of warning to Spring Lake telling it that the commission was going to take over control of the town's finances if its Board of Aldermen did not pass a responsible budget that contained realistic revenue and expenditure estimates.

Spring Lake had a history of running budget deficits and financial difficulties. The LGC's agreement with the town included directive to help it develop a "well thought-out FY2022 budget that is realistic in revenues and expenditure estimations."

The town in Cumberland County had a fiscal 2020-2021 General Fund shortfall of around \$1.2 million, but the originally proposed budget was funding only \$285,000 of that shortfall, LGC Secretary Sharon Edmundson had said earlier.

On June 28, the town's board passed a fiscal 2022 budget that met with approval of LGC staff for compliance with state law, thereby avoiding the need for the LGC to take control of the town's financial affairs.

Scotland Neck has also had its share of budget problems, according to the LGC. It had been overestimating its revenues while it was overspending. Additionally, there had been a lack of clear record keeping.

At present there is no full-time town administrator and the town's part-time finance officer is filling the administrator's slot on a temporary basis.

In early June, LGC staff advised the town commissioners that their preliminary fiscal 2021-22 budget was unacceptable. Town officials worked with the LGC and the North Carolina League of Municipalities to revise the budget documents into one that the LGC staff called one of the best in years. On June 29, town commissioners passed the spending plan.

"We are very pleased with the actions of the towns' governing bodies in finding out what's right, getting it right and now, hopefully, keeping it right for the taxpayers of their communities," Folwell said. "Their constituents pay property taxes with the expectation that essential services they require will be provided with a high degree of governance, transparency and competence from their elected representatives."

Folwell said that if the towns continue to show progress they could be removed from the UAL — a top goal of the financial accountability agreements. A key to that happening is their ability to continue to comply with the budget spending constraints, which has been a shortcoming in the past.

“We don’t have enough staff, sufficient time or, in some instances, the expertise to tackle the growing number of local governments in need of assistance without adopting fresh approaches,” Folwell said. “The financial accountability agreements give us one more tool in our tool box to help steer local governments in the right direction before more drastic action becomes necessary.”

He said the aim of the LCG is to keep things from going from bad to worse by taking proactive action to prevent small financial problems from turning into big ones that municipalities can't handle by themselves.

“At the end of the day we would like the Local Government Commission to be like the Maytag repairman you used to see on TV,” Folwell said. “No one ever calls him, because nothing is broken.”

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