Coates' Canons Blog: A Look at North Carolina's Constitutional Public Purpose Requirement

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In a **post** describing the recently enacted legislation that (potentially) authorizes North Carolina local governments to establish revolving loan funds or impose special assessments in order to finance energy efficiency improvements and distributed generation renewable energy sources permanently affixed to private property, I indicated that one (of many) complicating factors is determining whether or not such "energy financing" programs satisfy the public purpose clause of the North Carolina Constitution. As I stated in that **post**, I think there is a good argument that, at least under certain circumstances, such programs could satisfy this constitutional requirement. The analysis of this issue is fairly extensive and very dependent on the facts and circumstances surrounding a particular unit's program, though. In this post, I describe the current, general framework for evaluating the application of this constitutional provision. Note that this framework applies to the expenditure of public funds for any activity, project, or purpose—thus, the analysis may provide a helpful review for public officials generally.

Defining Public Purpose

Section 2(1) of Article V of the North Carolina Constitution provides that "[t]he power of taxation[] be exercised in a just and equitable manner, for public purposes only . . . ." Known as the public purpose limitation, this provision requires that all public funds, no matter what their source, be expended for the benefit of the citizens of a unit generally, and not solely for the benefit of particular persons or interests. ("Although the constitutional language speaks to the 'power of taxation,' the limitation has not been confined to government use of tax revenues." Madison Cablevision v. City of Morganton, 325 N.C. 634, 386 S.E.2d 200 (1989).)

The North Carolina Supreme Court has not specifically defined the term "public purpose;" instead it has left the issue to be determined on a case-by-case basis. In fact, according to the Court, the "[t]he initial responsibility for determining what is and what is not a public purpose rests with the legislature," and the legislature's determination is "entitled to great weight." *In re* Housing Bonds, 307 N.C. 52, 296 S.E.2d 281 (1982). Whether a particular activity, in a particular context, constitutes a public purpose is a legal issue that ultimately must be decided by the courts, though. The North Carolina Supreme Court has set forth two guiding principles to analyze whether a government activity satisfies the constitutional requirement. First, the activity must involve a "reasonable connection with the convenience and necessity of the particular" unit of government. Second, the activity must benefit the public generally, as opposed to special interests or persons.

Reasonable Connection with Unit of Government

The North Carolina Supreme Court has provided further guidance on the first guiding principle, stating that "whether an activity is within the appropriate scope of governmental involvement and is reasonably related to communal needs may be evaluated by determining how similar the activity is to other which this Court has held to be within the permissible realm of governmental action." Maready v. City of Winston-Salem, 342 N.C. 708, 467 S.E.2d 615 (1996). Thus, as to the first prong, there are two parts to the inquiry. The first is whether or not the activity is an appropriate one for a local government to engage in. North Carolina courts routinely have held that traditional government activities—such as fire protection, street construction, or public health programs—serve a public purpose. There is a notion, however, that there are some activities that should be reserved for the private sector of the economy, and, therefore, are not appropriate for government action. Determining where the line should be drawn is difficult, though. As the Court repeatedly has explained,

> [a] slide-rule definition to determine public purpose for all time cannot be formulated; the concept expands with the population, economy, scientific knowledge, and changing conditions. As people are brought closer together in congested areas, the public welfare requires governmental operation of facilities which were once considered exclusively private enterprises, and necessitates the expenditures of tax funds for purposes which,

in an earlier day, were not classified as public. Martin v. Housing Corp., 277 N.C. 29, 175 S.E.2d 665 (1970).

North Carolina courts, thus, have held that "new" activities that are perceived as outgrowths of more traditional government functions serve a public purpose. For example, in *Martin v. North Carolina Housing Corporation*, 277 N.C. 29, 175 S.E. 2d 665 (1970), the North Carolina Supreme Court held that government funding of low income residential housing served a public purpose. In so holding, the Court tied the government's concern for safe and sanitary housing for its citizens to its traditional role of combating slum conditions. Similarly, in *Madison Cablevision, Inc. v. City of Morganton*, 325 N.C. 634, 386 S.E.2d 200 (1989), the Court held that the municipal provision of cable television services served a public purpose because such services were a natural outgrowth of the types of communications facilities that local governments had been operating for many years, including auditoriums, libraries, fairs, public radio stations, and public television stations.

But, in a few cases, the courts have found that an activity is neither a traditional government activity, nor an outgrowth of a traditional government activity, and, consequently, the activity does not serve a public purpose. For example, in *Nash v. Tarboro*, 227 N.C. 283, 42 S.E.2d 209 (1947), the North Carolina Supreme Court held that it was not a public purpose for a town to issue general obligation bonds in order to construct and operate a hotel, finding that, at least at the time, owning and operating a hotel was purely a private business with no connection to traditional government activities.

And, occasionally, courts have determined that activities that appear to be natural extensions of traditional government activities, nonetheless, do not satisfy the public purpose clause. In *Foster v. North Carolina Medical Care Commission*, 283 N.C. 110, 195 S.E.2d 517 (1973), the North Carolina Supreme Court held that the expenditure of public funds to finance the construction of a hospital facility that was to be privately operated, managed and controlled, did not serve a public purpose, even though the "primary purpose" of a "privately owned hospital is the same as that of a publicly owned hospital." According to the Court, "[m]any objects may be public in the general sense that their attainment will confer a public benefit or promote the public convenience but not be public in the sense that the taxing power of the State may be used to accomplish them." Thus, a court must look not only at the ends sought, but also the means used to accomplish a public purpose.

The first guiding principle also requires that the activity benefit the citizens of the unit that is engaging in the activity, as opposed to citizens in other units. That is, the primary public that is to benefit from an expenditure of public funds must be the citizens of the jurisdiction that is making the expenditure. However, it is the benefit to the unit's citizens that is important rather than the location of the activity. Courts have upheld expenditures of public funds on activities or projects located outside the jurisdiction of a unit as long as the benefit of the expenditures is for the citizens of the unit. Courts also have rejected challenges to government activities because the purported public benefit is too broad; that is, that the benefit extends beyond a unit's citizens. As long as the local benefit accompanies the broader benefit, the activity may serve a public purpose.

Benefits the Public Generally, Not Special Interests or Persons

Even if an activity involves a "reasonable connection" with the unit of government, it does not necessarily mean that it serves a public purpose. The activity also must "primarily benefit the public and not a private party." According to the North Carolina Supreme Court, "[i]t is not necessary, [however], in order that a use may be regarded as public, that it should be for the use and benefit of every citizen in the community. It may be for the inhabitants of a restricted locality, but the use and benefit must be in common, and not for particular persons, interests, or estates." Briggs v. City of Raleigh, 195 N.C. 223, 141 S.E. 597 (1928). In other words, "the ultimate net gain or advantage must be the public's as contradistinguished from that of an individual or private entity." Martin v. Housing Corp., 277 N.C. 29, 175 S.E.2d 665 (1970). But, "an activity does not lose its public purpose merely because it involves a private actor. Generally, if an act will promote the welfare of a state or a local government and its citizens, it is for a public purpose." Parker v. New Hanover County, 173 N.C.App. 644, 619 S.E.2d 868 (2005). Courts often resort to engaging in a balancing test of the public and private benefits; invalidating the expenditure if the private benefit is predominant. Unfortunately, as several courts have noted, "[o]ften public and private interests are so co-mingled that it is difficult to determine which predominates." Martin v. Housing Corp., 277 N.C. 29, 175 S.E.2d 665 (1970).

And, the outcome of the analysis depends largely on how the benefits are characterized. In *Mitchell v. Financing Authority*, 273 N.C. 137, 159 S.E.2d 745 (1973), for example, the North Carolina Supreme Court determined it was not a public purpose to use state funds to acquire sites and construct and equip facilities for private industrial development.

Significantly the Court considered the “benefits” to simply constitute a win-fall to only a few private companies, at the expense of other companies and of the public generally. It, thus, found that the expenditure of public funds for this purpose did not serve a public purpose. Contrast that with a more recent decision in *Maready v. City of Winston-Salem*, 342 N.C. 708, 467 S.E.2d 615 (1996), in which the North Carolina Supreme Court held that economic development incentive grants to private businesses did not violate the public purpose clause. In this case, the Court took a much broader view of the “benefits,” stating that the ultimate goal of providing such incentives to one or more private entities was to improve the community at large—through, among other things, increased tax revenues and job opportunities. The *Maready* case appears to reflect the Court’s recognition of the “trend toward broadening the scope of what constitutes a valid public purpose that permits the expenditure of public revenues” in modern society. (Note, however, as discussed by my colleague Tyler Mulligan **here** and **here**, based on the court’s holding in *Maready,* only certain types of economic development incentives likely satisfy the public purpose requirement.)

Applying Framework to Proposed Government Activity

There is substantial case law analyzing the public purpose clause. The cases cited above, however, are representative of the current framework North Carolina courts are employing to analyze this issue. In the absence of direct court guidance with respect to a particular proposed expenditure of public funds, a unit must determine whether both the means used and the ends sought comprise a traditional government activity, or a natural extension or outgrowth of a traditional government activity. Furthermore, the activity must benefit the citizens of the unit making the expenditure generally. That does not mean it has to benefit all citizens equally. It also does not mean that the proposed expenditure of public funds cannot significantly and directly benefit specific individuals or entities. But the overall purpose of the activity must be to benefit the unit and its citizens; and this broader public benefit ultimately should predominate over the benefit to any single individual or entity. (Of course, there is a great deal of subjectivity in this analysis, which is why the courts appear to be fairly deferential to the Legislature’s or a governing body’s determinination that a particular activity benefits the public.)

Finally, note that even if a proposed activity constitutes a public purpose in the abstract, it does not mean that a unit may engage in the proposed activity. A local government also must have statutory authority to both engage in an activity and expend public funds for that activity. *See* Morgan v. Town of Spindle, 254 N.C. 304 (1961) (“‘Public Purpose’ as we conceive the term to imply, when used in connection with the expenditure of municipal funds from the public treasury, refers to such public purpose within the frame of governmental and proprietary power given to the particular municipality, to be exercised for the benefit, welfare and protection of its inhabitants and others coming within the municipal care.”).

Links

- www.ncga.state.nc.us/Legislation/constitution/article5.html
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