Proposition 101
Income, Vehicle, and Telecommunication Taxes and Fees

Proposition 101 proposes amending the <u>Colorado statutes</u> to:

- ♦ reduce the state income tax rate from 4.63 percent to 4.5 percent in 2011, and to 3.5 percent gradually over time;
- ♦ reduce or eliminate taxes and fees on vehicle purchases, registrations, leases, and rentals over the next four years;
- ♦ eliminate all state and local taxes and fees on telecommunication services, except 911 fees; and
- ♦ require voter approval to create or increase fees on vehicles and telecommunication services.

Summary and Analysis

Proposition 101 reduces or eliminates various taxes and fees on income, vehicles, and telecommunication services. Table 1 shows the annual impact of Proposition 101 on three different households, and Table 2 shows the impact on government budgets.

Some of the reductions in Proposition 101 are phased in over time. The impact will be smaller in the first year and will grow in size over the next 15 to 20 years. Estimates of the impact in the first year, as well as the impact once the reductions are fully implemented, are based on today's dollars. The fully implemented impacts provide the best estimates of the measure's final effects. Although the actual dollar amounts will differ in the future as inflation and growth increase the size of the economy, the comparable budget impacts on taxpayers and governments are expected to remain consistent over time.

In the first year, the tax and fee reductions are expected to be $1.3 billion — $717 million in state reductions and $587 million in local government reductions. Once fully implemented, the impact is expected to be $2.9 billion in today's dollars — $1.9 billion in state reductions and $1.0 billion in local government reductions.

Impact on households and businesses. Table 1 shows the estimated change in tax and fee bills for three different households as a result of Proposition 101, in both the first full year the measure is in effect and when the measure is fully implemented, in today's dollars. Businesses will also experience reductions in taxes and fees. Households and businesses will be impacted differently depending on annual income, vehicles owned, vehicles purchased, and the amount paid for phone and cable service. Households and businesses will experience additional reductions during years in which vehicles are leased or purchased.

Table 1. Annual Change in Representative Households' Tax and Fee Bills Due to Proposition 101, First Year Impact and When Fully Implemented /a

(In Today's Dollars)

	Income Taxes	Vehicle Fees & Taxes	Telecom Fees & Taxes	Total
Household A	*Household Description:* Annual Income: $35,000; owns a 10-year-old car that had an original retail price of $13,000; $60 monthly phone bill.			
First Year	-$20	-$72	-$43	-$135
Fully Implemented	-$185	-$73	-$43	-$301
Household B	*Household Description:* Annual Income: $55,000; owns a 5-year-old car that had an original retail price of $17,000 and a 5-year-old car that had an original retail price of $23,500; $130 monthly combined phone bills.			
First Year	-$40	-$180	-$93	-$313
Fully Implemented	-$320	-$295	-$93	-$708
Household C	*Household Description:* Annual Income: $110,000; owns a 2-year-old car that had an original retail price of $37,500 and a 3-year-old car that had an original retail price of $26,000; $180 monthly combined phone bills.			
First Year	-$90	-$327	-$128	-$545
Fully Implemented	-$780	-$883	-$128	-$1,791

/a This analysis assumes a 7.0 percent combined state and local sales tax rate. Telecommunication tax and fee reductions are fully implemented in 2011. Some vehicle tax and fee reductions are fully implemented in 2011 and some are phased in between 2011 and 2014. It will take an estimated 15 to 20 years for the income tax rate reductions to be fully implemented.

Impact on government budgets. Table 2 shows the estimated impact of Proposition 101 on tax and fee collections used for local government budgets, the state's general operating budget, and transportation budgets in the first year and once it is fully implemented. All of these impacts are shown in today's dollars. More information on the impact on each type of budget follows. As a result of the decrease in tax and fee collections, state and local governments will have to consider options such as decreasing spending and services, increasing fees to pay for services, or some combination of both.

Table 2. Annual Change in Government Tax and Fee Collections Due to Proposition 101, First Year Impact and When Fully Implemented
(In Today's Dollars)

Government Budget	Collections under Current Law	Collections under Prop 101	Change*
Local Governments Vehicle Specific Ownership Taxes and Sales Taxes	$3.9 billion	$3.4 billion First Year	-$489 million First Year
		$3.0 billion Fully Implemented	-$872 million Fully Implemented
State Government General Operating Budget Sales Taxes, Income Taxes, and Telecommunication Fees	$7.2 billion	$6.8 billion First Year	-$422 million First Year
		$5.5 billion Fully Implemented	-$1.6 billion Fully Implemented
City, County, and State Government Transportation Budgets Vehicle Registration Fees and State Rental Fee	$440 million	$50 million Fully Implemented During First Year	-$390 million Fully Implemented During First Year

** Totals may not sum due to rounding.*

Impact on local government budgets. Local governments will collect less money from vehicle specific ownership taxes and sales taxes. Local governments affected by the measure include school districts, cities, counties, and special districts such as recreation, fire, water, sewer, and public transportation districts. The money collected in taxes and fees pays for different services depending on the local government. Most of the money is used for education, public safety, roads, trash service, and parks and recreation. State law requires that school districts be reimbursed by the state for most of their loss in tax collections.

Impact on the state government operating budget. The state government will collect less money from sales taxes, income taxes, and telecommunication fees. The state spends 96 percent of its general operating budget on: preschool through higher education; health care; prisons; the courts; and programs that help low-income, elderly, and disabled people. Proposition 101 will reduce the amount of money available to pay for the state's general operating budget by an estimated 6 percent in the first year and by an estimated 23 percent once fully implemented.

The state will also be required to reimburse school districts for most of their loss of vehicle specific ownership taxes. This obligation increases the total impact on the state general operating budget during the first year from the $422 million shown in Table 2 to $470 million, and when fully implemented, from $1.6 billion to $1.7 billion.

Impact on state and local government transportation budgets. Proposition 101 reduces funding dedicated to transportation budgets. The state constitution requires that vehicle-related fees collected by the state be spent on road safety, construction, and maintenance. This money is shared between the state, cities, and counties. The state's transportation budget will decrease by an estimated 28 percent from these fee reductions. The impact on city and county government transportation budgets will vary by government. Because cuts affecting transportation budgets are immediate, the full impact shown in Table 2 will occur in 2011.

State Income Tax

Households and businesses pay taxes on their income to both the state and federal governments. The state's income tax rate is a flat 4.63 percent and is the same for all income levels and for both households and businesses. The state income tax is the largest source of money the state receives to pay for its main programs.

Proposition 101 gradually lowers the state income tax rate from 4.63 percent to 3.5 percent over time. The rate is first lowered to 4.5 percent starting in 2011. This will reduce income tax collections to the state by an estimated $145 million, a decrease of 3 percent. The tax bill for a household with an annual income of $55,000 will be reduced by $40 in 2011. In the future, the rate is reduced by 0.1 percentage point each year in which state income tax collections grow by more than 6 percent. For example, if tax collections increase fast enough, the income tax rate will decrease from 4.5 percent to 4.4 percent in 2012. This will occur until the income tax rate decreases to 3.5 percent. When the tax rate is fully reduced, income tax collections to the state will be an estimated 26 percent less, or a decline of $1.3 billion in today's dollars. The tax bill for a household with an annual income of $55,000 will be reduced by $320 when the cut is fully phased in. Because income tax collections historically have not grown by more than 6 percent every year, it will likely take 15 to 20 years for the tax rate to reach 3.5 percent.

Vehicle Fees and Taxes

Proposition 101 reduces several types of vehicle fees and taxes as shown in Table 3. The amounts in the table show the impact when the reductions are fully implemented—sales tax reductions on vehicle purchases and specific ownership tax reductions are phased in over a four-year period, while all other fee and tax changes occur in 2011. The total amount of the reduction in vehicle fees and taxes, when fully implemented, is estimated at $1.3 billion in today's dollars.

Table 3. Vehicle Fees and Taxes Under Current Law and Proposition 101, When Fully Implemented
(In Today's Dollars)

	Average Payment		**State & Local Govt. *Change in Yearly Collections***
	Current	***Prop. 101***	
Vehicle Owners			
Sales Tax /a *Four-year Phase-in (2011 to 2014)*	$2,100 one-time payment	$1,400 one-time payment	-$285 million total for state and local
Registration and Licensing Fees /b *Fully Implemented in 2011*	$81 paid once per year	$10 paid once per year	-$300 million total for state and local
Specific Ownership Tax *Four-year Phase-in (2011 to 2014)*	$87 paid once per year	$2 (new cars) or $1 (used cars) paid once per year	-$345 million total for all school districts /c and local governments
Vehicle Lessees			
Sales Tax /a *Fully Implemented in 2011*	$1,080 total ($30 paid monthly during lease term)	$0	-$60 million total for state and local
Registration and Licensing Fees /b *Fully Implemented in 2011*	$81 paid once per year	$10 paid once per year	-$75 million total for state and local
Specific Ownership Tax *Fully Implemented in 2011*	$87 paid once per year	$0 paid once per year	-$86 million total for all school districts /c and local governments
Vehicle Renters			
Sales Tax /a *Fully Implemented in 2011*	$2.45 per rental day	$0	-$80 million total for state and local
State Car Rental Fee *Fully Implemented in 2011*	$2 per rental day	$0	-$19 million total for state and local

/a This analysis assumes a 7.0 percent sales tax rate. For vehicle owners and lessees, it assumes a $30,000 car is purchased or leased for 36 months. For vehicle renters, the analysis assumes a vehicle is rented for $35 a day.
/b Currently, the average registration and license fees are lower than the average payment shown in the table, but are estimated to increase to the amounts shown over the next year. The collections numbers represent registration and license fee impacts assuming what the fees will be when they are increased.
/c State law requires the state to reimburse school districts for most of their loss of specific ownership taxes.

Vehicle owners. Upon purchase, vehicle buyers are required to pay sales tax. In addition, each year vehicle owners must register their vehicle(s) with the state and pay registration fees and a specific ownership tax. Proposition 101 reduces all three taxes and fees.

Vehicle sales tax. Sales taxes are paid on the purchase of a new or used vehicle. The tax is applied to the price of the vehicle, including any manufacturer's rebate. The total tax rate is a 2.9 percent state rate plus any applicable local government sales tax rates. Because different local governments have different tax rates, the sales tax a buyer pays differs depending on where the buyer lives. The average combined sales tax rate is close to 7 percent.

Proposition 101 reduces the sales taxes due on vehicle purchases by exempting the first $10,000 of the vehicle's price and any manufacturer's rebate from the sales tax. The $10,000 exemption is phased in over a four-year period beginning in 2011. When fully implemented, vehicles worth $10,000 or less will not have a sales tax bill. Vehicles with greater values will receive a $10,000 "write-off." For example, a vehicle purchased for $18,000 will be taxed only on $8,000 of the value. This sales tax cut will reduce local government tax and fee collections by an estimated $165 million, or 5 percent, and state government tax and fee collections by an estimated $120 million, or 6 percent.

Vehicle registration and licensing fees. Vehicle owners pay registration fees each year. Most fees vary according to vehicle weight, age, and value. While most of the money pays for roads and bridges, some pays for services like emergency medical services, vehicle emissions reduction programs, the Colorado State Patrol, and snow plowing.

Beginning in 2011, Proposition 101 combines all registration, licensing, and titling fees into a single $10 annual fee, with the exception of vehicle inspection and new license plate fees. As shown in Table 3, the average registration and licensing fee for vehicle owners would fall from $81 to $10 and the amount collected by state and local governments would decrease by about $300 million, or 88 percent.

Vehicle specific ownership tax. Vehicle owners also pay a specific ownership tax each year when registering a vehicle. The specific ownership tax is a property tax on a vehicle. The tax ranges from 0.45 percent to 2.10 percent of the vehicle's taxable value, based on the vehicle's original recommended retail price. As a vehicle ages, the tax rate is reduced. The minimum specific ownership tax is either $3 or $5 per vehicle, depending on the type of vehicle. Counties collect specific ownership taxes and distribute them to schools, cities, counties, and special districts within their boundaries.

Proposition 101 phases in a cut to specific ownership taxes over four years, beginning in 2011. It also requires permission from voters to create or increase future registration and licensing fees. Table 3 shows the change in vehicle owners' bills and state and local government collections.

Vehicle lessees. Like vehicle owners, persons who lease vehicles must pay sales taxes, registration fees, and specific ownership taxes each year. Proposition 101 reduces all three taxes and fees for vehicle leases.

<u>Vehicle sales tax and specific ownership tax.</u> Proposition 101 eliminates sales taxes and annual specific ownership taxes on leased vehicles beginning in 2011. This will reduce state and local sales tax collections by an estimated $60 million per year, or 1 percent. It will also eliminate all specific ownership taxes collected by local governments on leased vehicles.

<u>Vehicle registration and licensing fees.</u> Leased vehicles are also required to be registered with the state and lessees must pay annual registration fees. Beginning in 2011, Proposition 101 eliminates all registration fees and imposes a single $10 fee per vehicle, resulting in a reduction of $71 for vehicle lessees. The measure reduces state collections by approximately $75 million per year.

Vehicle renters. The state charges a fee of $2 per day for car rentals. The money is shared by the state, cities, and counties to build, repair, and maintain roads and bridges. Sales tax is also applied, with revenue going to the state and local governments. Proposition 101 eliminates the fee and all sales taxes beginning in 2011. As a result, state and local transportation budgets will have an estimated $19 million less per year in fee collections and $80 million less in sales tax collections.

Other vehicle fees. The state also charges use and permitting fees for large and overweight vehicles that use Colorado roads. A passenger mile tax is also charged for passenger bus or shuttle businesses. Proposition 101 eliminates these fees beginning in 2011, resulting in $56 million less in state funds, reducing charges to trucking and carrier companies by a like amount.

Telecommunication Fees and Taxes

Proposition 101 eliminates state and local sales tax and other fees on customer bills for any kind of telecommunications service, except for existing 911 fees. The measure lists the following as telecommunication services, even though some of them are not currently taxed: phone, pager, cable, television, radio, Internet, and computer services. Currently, the state and some local governments charge sales tax on a portion of the cost of phone and pager services, and some local governments charge sales tax on cable services. State fees that are eliminated include fees that help telephone companies provide access to phone service in rural areas of the state, to the blind or deaf, and to low-income people. Local governments may have other fees, such as television franchise fees, that may be eliminated.

Proposition 101 freezes 911 fees at their 2009 level. These fees differ from county to county and ranged from 43 cents to $1.25 per month in 2009. The 911 fees are charged by local governments to help pay for 911 emergency services.

The reduction in a household or business's telecommunications bill depends on how much it spends on taxable phone and cable. Tax and fee collections by local governments would be reduced by at least $194 million each year. Tax and fee collections to the state government would be reduced by an estimated $183 million each year.

New voter approval requirements. Proposition 101 redefines all telecommunication fees and most vehicle fees as taxes. Because the state constitution requires a vote to increase taxes but not to increase fees, governments will need to ask voters for permission to create new or increase existing vehicle or telecommunication charges in the future. Proposition 101 excludes vehicle-related fines, parking fees, tolls, vehicle impound fees, vehicle identification and emission inspection fees, and new license plate fees from this requirement.

How does Proposition 101 interact with two other measures on the ballot? Proposition 101 along with Amendment 60 (see page x) and Amendment 61 (see page x) contain provisions that affect state and local government finances by decreasing taxes paid by households and businesses and restricting government borrowing. How these measures work together may require clarification from the state legislature or the courts.

Proposition 101 reduces state and local government taxes and fees. Amendment 60 reduces local property taxes, while requiring state expenditures for K-12 education to increase by an amount that offsets the property tax loss for school districts. Amendment 61 requires state and local governments to decrease tax rates when debt is repaid, and is assumed in this analysis to apply to the existing debt of state and local governments.

Since portions of these measures are phased in over time, the actual impacts to taxpayers and governments will be less in the initial years of implementation and grow over time. Assuming that all three measures are approved by voters, the first-year impact will be to reduce state taxes and fees by $717 million and increase state spending for K-12 education by $385 million. Once fully implemented, the measures are estimated to reduce state taxes and fees by $2.1 billion and increase state spending for K-12 education by $1.6 billion in today's dollars. This would commit almost all of the state's general operating budget to paying for the constitutional and statutory requirements of K-12 education. Tax and fee collections by local governments are estimated to decrease by $5.0 billion, but the net impact on local government budgets would be $3.4 billion after the state reimburses school districts.

Households and businesses are estimated to save $1.6 billion in the first year and $7.1 billion per year in today's dollars when the measures are fully implemented. The measures reduce the taxes and fees owed by an average household making $55,000 per year that owns a $295,000 house by an estimated $400 in the first year and $1,750 per year when fully implemented.

Arguments For

1) Allowing citizens and businesses to keep more of their own money helps support the economy. A family with a yearly income of $55,000 could save $313 in the first year of Proposition 101 and $708 per year when its fully implemented. Most businesses will also have more money, allowing them to invest in their companies and create new jobs.

In addition, people who buy or lease cars will save even more from lower sales taxes. Reducing taxes and fees helps businesses and lower- and middle-income families who are struggling in this difficult economy. Consumer spending and business investment tend to increase when the tax burden is lower.

2) Proposition 101 will require state and local governments to eliminate unnecessary spending. Governments will look more closely at how they spend money, ensuring that taxpayer dollars are used in the best and most efficient way. State and local governments already spend about $40 billion a year, which amounts to an average of $20,000 per household in the state. Also, government spending continues to grow in most years. The amount of spending by governments in the state has increased by about 14 percent since 1990, even after accounting for inflation and population growth. Even with Proposition 101's reductions in tax and fee collections, revenue to governments will continue to grow in most years, although at a slower rate. Governments can prioritize and fund the most important services with less money by making better choices about how they spend money.

3) Proposition 101 gives people a voice in decisions about fees on phones and vehicles. Rather than asking voters for more money for transportation projects, the state recently increased vehicle registration fees by about $220 million, an average of approximately $44 per car. The state did this even though registration fees exceed what it costs the government to process vehicle registrations. Proposition 101 will require governments to seek voter approval for more money rather than adding more fees. Further, some telecommunication fees raise the cost of basic services for everyone but help only a small part of the state's population. Proposition 101 simplifies and eliminates these fees—lowering all vehicle registration fees to a flat $10 per year and ending state and local taxes and fees on phone and cable bills.

Arguments Against

1) Colorado's economic success depends on services that governments provide, such as education and a safe transportation system. Proposition 101 will force cuts to these services which people rely on for a high quality of life and that businesses need to succeed. Services that have already been reduced because of the economic downturn, such as schools, colleges, prisons, firefighters and police, and water and sewer systems, will be cut further. These cuts could further weaken the already slow economy, reduce jobs, and, over time, hurt the quality of the state's workforce. Rural economies may also be affected because money currently dedicated to phone and Internet service for rural areas will be eliminated. The state's operating budget is estimated to be cut by $1.6 billion, or about 23 percent, when the measure is fully implemented, an amount greater than what the state currently spends on prisons, courts, and the Colorado State Patrol combined. Further, local governments will have about $1 billion less. State government spending as a percentage of the economy is already third lowest among all states and combined state and local government spending is eighth lowest.

2) Proposition 101 will hurt the ability of the state and local communities to maintain already inadequate roads and bridges and provide public transportation. Studies show that Colorado needs more than twice as much money each year than it currently spends just to maintain existing roads and bridges. Proposition 101 would cut state transportation funding by an estimated 28 percent each year. In 2009 alone, the state and local governments maintained more than 193,000 lane miles of roadway and 8,000 bridges. The state also snow-plowed and sanded 5.6 million miles of highway, repaired 77,000 street signs, and monitored 278 avalanche paths. Public health and safety may also be affected due to fewer resources for emergency medical services, vehicle emission programs, and road maintenance.

3) Cuts to government services may result in hardship for families who have to pay for services that governments will no longer be able to afford. For example, tuition will likely increase, putting college out of reach for many households. Higher-income people, who are better able to absorb these cost increases, will benefit the most from the reduced taxes and fees in Proposition 101. Low- and middle-income people will be less able to absorb the costs. Those with lower incomes and people who are deaf or blind will also lose a source of money that helps them communicate within society.

Estimate of Fiscal Impact

State revenue. Proposition 101 contains several provisions that decrease revenue to the state government. Because some of the reductions are phased in over time, the reduction in revenue will be lower at first. The first year reduction is estimated to be $717 million, which includes $295 million less in vehicle fees that are constitutionally-required to be used for transportation-related spending. When fully implemented, state tax and fee collections would decrease by an estimated $1.9 billion in today's dollars.

State spending. The state will have less money available for spending on its operating programs and transportation budget. Though the reductions to the transportation budget will be immediate, the reductions to operating programs will occur over time as the cuts to the income and sales tax are phased in. The state will have $422 million, or 6 percent less, in the first year to spend on operating programs, such as education, prisons, and social services. Further, the state will have about $295 million, or 28 percent, less to spend on transportation. When fully implemented, the state would have $1.6 billion, or 23 percent, less in today's dollars to spend on operating programs. The impact on the state's operating programs depend on the future budgeting decisions of the state legislature.

Proposition 101 will also create some additional costs for the state. The state will be required to replace most of the loss of vehicle specific ownership taxes for school districts. This will cause the state to spend an additional $48 million in the first year and $121 million annually when the measure is fully implemented.

Also, Proposition 101 increases state administrative costs by about $185,000 in budget year 2010-11 and $34,000 in the following few years to implement the reductions in taxes, fees, and charges, and to audit compliance with the measure's provisions. The state's administrative costs will decrease in subsequent years as the tax and fee reductions are fully implemented. It is estimated that the measure will require the addition of 0.5 new staff in budget year 2010-11 and 0.25 new staff in the following few years to administer the auditing of governments' tax and fee reductions.

Local revenue and spending. Because reductions in the local sales tax on vehicles are phased in over four years, revenue decreases in the first few years will be lower than when the measure is fully implemented. Local government revenue is estimated to be reduced by $587 million in the first year, with $99 million of this amount for transportation projects. When fully implemented, local government revenue would decrease by an estimated $1.0 billion in today's dollars.

The extent to which each local government program will be affected will vary depending on what services the government provides and its budget decisions. Local governments may also have increased administrative costs to comply with the auditing requirements of Proposition 101.

Impact on taxpayers. Proposition 101 will reduce households' and businesses' tax and fee bills by different amounts depending on their income, the number and type of vehicles they have, the costs of their phone and cable bills, and whether they purchase or lease vehicles in a given year. In the first year, before all the tax and fee reductions are fully implemented, an average household with an annual income of $55,000 would experience a reduction in their tax and fee bill of about $313. When fully implemented, the total tax and fee bill for this household would be reduced by about $708 annually in today's dollars. There would be additional reductions if the household purchases or leases a vehicle. Businesses will also experience reductions in taxes and fees.