Final Staff Document

Referendum C — State Spending

Referendum C is an amendment to the *Colorado Revised Statutes* that:

- permits the state to spend the money it collects over its limit for the next five years on health care, public education, transportation projects, and local fire and police pensions;
- eliminates, for the next five years, refunds that taxpayers receive when the state collects more than it is allowed to spend, and reduces these refunds thereafter;
- uses the highest amount of money the state collects in any year during the next five years to calculate allowable state spending THEREAFTER; and
- caps annual increases in the new state spending amount at inflation plus population growth, beginning in 2011.

Background

How does the constitution limit state spending? A constitutional provision commonly known as TABOR limits the amount of money the state may spend each year. It limits the annual increase for some state revenue to inflation plus the percentage change in state population. Any money collected above this limit is refunded to taxpayers, unless the voters allow the state to spend it. Referendum C asks voters if the state may spend ~~the~~ money it collects above the limit ON HEALTH CARE, PUBLIC EDUCATION, TRANSPORTATION PROJECTS, AND LOCAL FIRE AND POLICE PENSIONS.

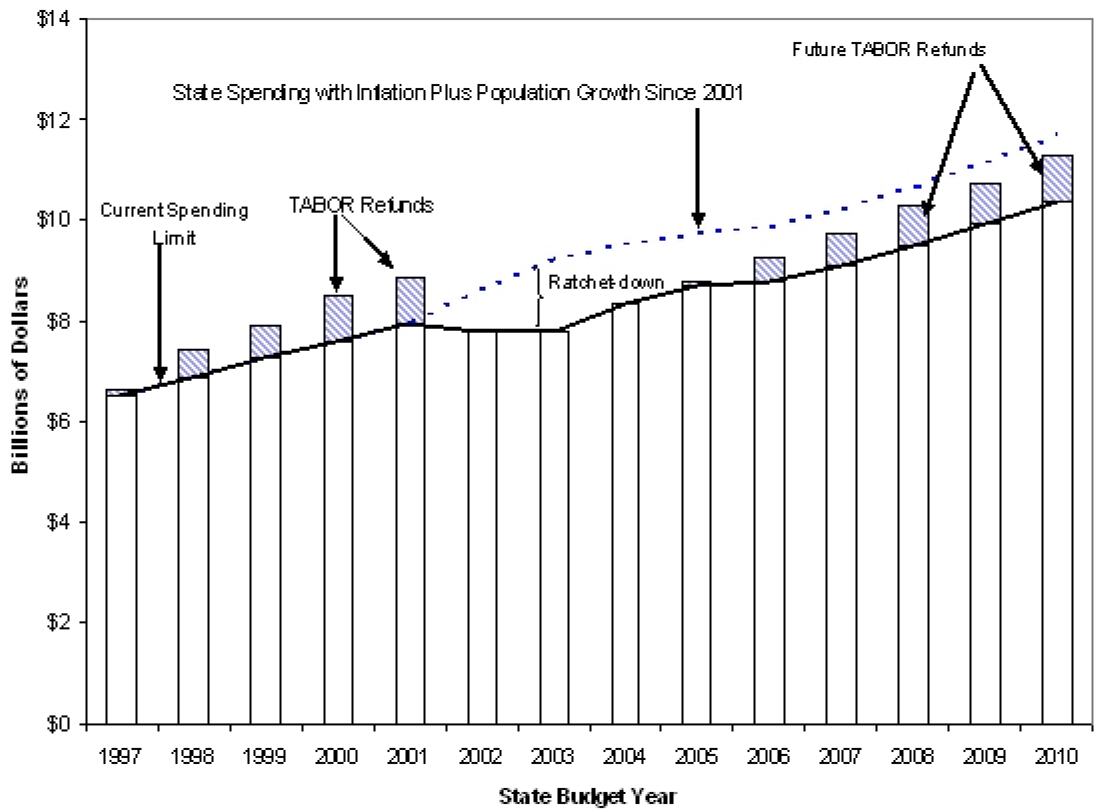
What money is included within the limit? The constitutional spending limit applies to about 60 percent of the money collected by the state, including income taxes, sales taxes, fees, fines, and interest earnings. Money received from the federal government, enterprises, lawsuits, and gifts is not covered by the spending limit AND IS NOT INCLUDED IN THIS ANALYSIS.

How has the spending limit worked? Between 1997 and 2001, the state collected money above the spending limit. For instance, in 2001, the state was allowed to spend $7.9 billion, but $8.9 billion was collected. The difference of about $1.0 billion was refunded to taxpayers.

When the state collects less money than the spending limit allows, there are no refunds. The next year's limit is calculated from the amount of money actually collected in the prior year. For example, the state experienced a recession during 2001 and the amount of money collected in 2002 was $7.8 billion, while inflation plus population growth would have allowed spending of $8.1 billion. The next year's limit grew from the $7.8 billion, not the $8.1 billion. This lowering of spending is known as the "ratchet-down" effect. The amount the state can spend under TABOR is now permanently below what it would ~~have been~~ BE if no recession had occurred and spending had grown by inflation plus population each year.

Figure 1 shows how the spending limit has operated and is projected to operate from 1997 through 2010. The solid line is the state spending limit, the dotted line shows what state spending would have been with inflation plus population growth, and the shaded areas represent refunds. Beginning in 2006, the shaded area is the money that Referendum C is asking voters to allow the state to spend.

Figure 1
State Spending ~~Limits~~ LIMIT and Refunds



How does Referendum C change state spending? Referendum C has three major provisions. First, it allows the state to keep the money it collects above the limit for five years, BEGINNING ON JULY 1, 2005, and to spend it on:

- transportation projects;

- health care for low-income, disabled, and elderly Coloradans;
- health insurance premiums for individuals and small businesses;
- preschool through twelfth grade public education;
- community colleges and other public institutions of higher education; and
- local fire and police pensions.

Legislative economists estimate that Referendum C ~~will~~ ALLOWS the state to increase spending by about $3.741 billion during the five-year period. The exact amount of the spending increase could be higher or lower, depending on the economy and the amount of money collected. Legislative staff is required to prepare an annual report detailing how the money is spent.

Second, beginning in 2011, Referendum C creates a new state spending cap equal to the highest amount of money ~~collected~~ THE STATE COLLECTS in any year between 2006 and 2010. This ~~cap~~ DOLLAR AMOUNT ~~is allowed to~~ INCREASES annually by inflation plus population growth. This provision in Referendum C prevents future drops in the state spending limit. All money collected above the new cap will be refunded to taxpayers.

Third, Referendum C allows the state to spend an additional $100 million ~~per~~ EACH year if Referendum D passes. This change, WHICH begins in 2011, ~~and it~~ reduces refunds EACH YEAR BY THE AMOUNT OF ADDITIONAL SPENDING. ~~by the same amount each year. The additional~~ THIS money may be used to repay debt permitted by Referendum D. Referendum D allows the state to borrow up to $2.1 billion to be used for transportation, capital projects in public education facilities, and local fire and police pensions. Referendum D ~~takes~~ CAN ONLY TAKE effect ~~only~~ if Referendum C passes.

What happens to the money if Referendum C fails? If Referendum C fails, the money the state collects above its spending limit will be refunded to taxpayers. The legislature, with approval of the governor, determines how the money is refunded. There are currently 16 methods to refund money. One of the methods is the sales tax refund, which almost all taxpayers receive. The sales tax refund accounts for about 42 percent of all TABOR refunds and is distributed based on income levels. Taxpayers are expected to receive A TOTAL OF BETWEEN $350 AND $1,021 OVER THE NEXT FIVE YEARS, OR an average of $491 in sales tax refunds. ~~over the next five years,~~ Figure 2 shows the estimated sales tax refund for a taxpayer in the highest and lowest income levels, and the average sales tax refund for all taxpayers from 2007 through 2011.

Figure 2
Estimated Sales Tax Refunds Per Taxpayer UNDER CURRENT LAW

Income Level	2007	2008	2009	2010	2011	Five-Year Total
Lowest	$35	$53	$88	$79	$95	$350
Highest	$102	$154	$258	$231	$276	$1,021
Average	$49	$74	$124	$111	$133	$491

Examples of the remaining 15 refunds include a reduction in vehicle registration fees, a rebate for local property taxes paid by businesses, and ~~a credit for child care expenses~~ A CREDIT FOR LOW-INCOME INDIVIDUALS. The total refund a taxpayer receives is the sales tax refund plus any of the other refund methods for which a taxpayer qualifies. Not all refund methods are available every year; the methods available depend on the amount of money being refunded. While the sales tax refund was distributed to almost 2.8 million taxpayers in 2001, most of the other 15 methods were distributed to a much smaller number of taxpayers. The appendix contains more information on the refund methods.

Does Referendum C impact annual income tax refunds? A taxpayer receives a state income tax refund when the taxpayer pays more in state income taxes than he or she owes. Income tax refunds are not affected by Referendum C.

What are other impacts of Referendum C? Under current law, low-income families receive an income tax credit for child care expenses when the state collects money above the limit. Passage of Referendum C eliminates this child care tax credit for at least five years. In addition, beginning in 2011, a new TABOR refund method is created that reduces the state income tax rate from 4.63 percent to 4.50 percent. The tax rate reduction takes effect in years in which the state collects enough money above the limit to pay for it. It reduces the amount of money refunded through other methods.

Arguments For

1) Referendum C provides money for critical investments in Colorado's future: improving the safety of roads and schools, providing ~~better~~ ADDITIONAL health care for Colorado families, and supplying an educated workforce for Colorado businesses. These investments ~~are necessary to~~ WILL HELP generate new jobs and retain existing jobs in the state. Based on income, Colorado ranks among the bottom ten states for funding K-12 and higher education. In addition, 39 percent of Colorado's roads and highways are in poor condition. Repairing highways now is cheaper than replacing them later.

2) Referendum C allows the state to recover from economic downturns while preserving the right of citizens to vote on all future tax increases. Under current limits, the state can never fully recover from an economic downturn. In the past few years, the state has added students and prisoners, and experienced more traffic congestion while TABOR revenue fell. Even if Referendum C passes, the state will be spending less in the future than inflation and population growth would have allowed since 2001. After five years, the state will once again have the strictest spending limit in the nation.

3) Without raising taxes, Referendum C provides the state with money to fund programs and services that were cut during the recent recession. The money will be generated from job growth, increased sales, higher salaries, and tourism spending. Colorado will still be a low tax state. Without Referendum C, the state will have to reduce funding for items such as higher education, programs that assist seniors like the senior homestead exemption, and programs that benefit low-income families and the disabled.

Arguments Against

1) Referendum C is effectively a tax increase. It eliminates TABOR refunds for five years and reduces them each year thereafter. The state will spend roughly $3.741 billion that could be better used by Colorado's citizens and businesses. This reduction in private spending could dampen the economic recovery that began in 2003, making the state a less desirable place for business relocation. NOT ONLY ARE TAXPAYERS GIVING UP THEIR SALES TAX REFUND, THEY ARE ALSO GIVING UP 15 OTHER REFUNDS, SUCH AS A CHILD CARE CREDIT, LOWER MOTOR VEHICLE FEES, AND CAPITAL GAINS CREDITS, WHICH AVERAGE $1,105 PER TAXPAYER OVER THE NEXT FIVE YEARS. ~~When the $3.741 billion is divided by the number of Colorado taxpayers, it amounts to $1,163 per taxpayer over five years.~~

2) Referendum C allows state spending to expand without being specific about the programs for which the money will be spent. The broad spending categories outlined in Referendum C cover 83 percent of state government. The new money could replace current spending on health care and public schools, essentially allowing the money to be spent for any purpose. The legislature can change the spending priorities anytime after the election. In addition, suspending the TABOR limit might lead to increases in fees and charges during the next five years because there is no limit on state spending and no requirement ~~for voter~~ THAT THESE INCREASES BE APPROVED BY VOTERS ~~approval~~.

3) The perceived budget shortfall could be handled in other ways. TABOR allows government growth at inflation plus population, but it does not ~~require~~ GUARANTEE it. ~~It is acceptable for government to grow at a slower rate~~ GOVERNMENT GROWTH AT A SLOWER RATE IS ACCEPTABLE AND COULD ENCOURAGE GREATER PRODUCTIVITY AND EFFICIENCY. Since TABOR passed in 1992, state spending has increased each year. Rather than spending more, the state could save money by eliminating inefficiencies, consolidating government

functions, privatizing certain services, and reforming the state purchasing system. ~~Slower growth could encourage greater government productivity and efficiency.~~

Estimate of Fiscal Impact

State impacts. Referendum C is estimated to increase state spending by $3.741 billion over the next five years. Figure 3 summarizes the estimated ADDITIONAL annual revenue the state can spend IF ~~under~~ Referendum C PASSES.

Figure 3
Estimated Increase in State Spending from Referendum C

State Budget Year:	2006	2007	2008	2009	2010	TOTAL
State Spending Increase Under Referendum C	$507 million	$653 million	$836 million	$823 million	$923 million	$3.741 billion
Additional Spending as a Percentage of Total Spending Capped by TABOR	6.0%	7.4%	8.9%	8.4%	9.0%	8.0%

Beginning in 2011, Referendum C is estimated to increase state spending by $923 million, plus annual increases for inflation and population growth. If Referendum D passes, the state will also be allowed to spend an additional $100 million each year beginning in 2011.

REFERENDUM C APPENDIX
TABOR Refund Methods and Amounts Distributed in 2001

The following table lists the refund methods available when the state collects money above its spending limit. For 2001, the last year refunds were issued, the table displays the average amount refunded per taxpayer and the number of taxpayers claiming each refund.

Sales Tax Refund		
Federal Adjusted Gross Income Group (income tiers in 2001)	**Estimated Number of Taxpayers in 2001**	**Average Amount Per Taxpayer in 2001**
Less than $26,000	949,357	$144
$26,001 to $53,000	816,139	$187
$53,001 to $78,000	474,271	$220
$78,001 to $103,000	248,190	$252
$103,001 to $126,000	112,248	$283
More than $126,000	196,482	$451
Total Sales Tax Refund	**2,796,687**	**$206**

Other TABOR Refund Methods (listed in the order available)		
	Number of Taxpayers Claiming Refund in 2001	**Average Amount Per Taxpayer in 2001**
Earned income credit	210,942	$156
Foster care	431	$487
Business personal property tax /A	77,726	$1,291
Capital gains for CO assets purchased before 5/9/94	9,296	$5,433
Child care credits	194,924	$131
Research and development	/B	/B
Lower motor vehicle registration fees C/	4,006,000	$7
High technology scholarship program	38	$88
Pollution control equipment	0	$0
Contribution to telecommunication education	/B	/B
Trucks at 0.01 percent sales tax rate	/D	/D
Interest, dividends, and capital gains	1,055,713	$42
Agriculture cooperative tax credit	237	$2,138
Health benefit plans	6,442	$376
Capital gains for CO assets purchased after 5/9/94	5,967	$4,636

/A 42,651 taxpayers received less than $200 each, while 250 taxpayers received more than $40,588 each.

/B New method that was not available in 2001

/C Estimated average refund per vehicle registration

/D Data not available