Amendment 61
Limits on State and Local Government Borrowing

Amendment 61 proposes amending the <u>Colorado Constitution</u> to:

- prohibit all new state government borrowing after 2010;
- prohibit new local government borrowing after 2010, unless approved by voters;
- limit the amount and length of time of local government borrowing; and
- require that tax rates be reduced after borrowing is fully repaid.

Summary and Analysis

Amendment 61 places new restrictions on government borrowing. Currently, the state and local governments borrow money to build or improve public facilities like roads, buildings, and airports and repay the money over multiple years. Borrowing is also used for other purposes, such as financing loans for small businesses.

Beginning in 2011, Amendment 61 prohibits all future borrowing by state government and limits future borrowing by local governments, including cities, counties, school districts, special districts, and enterprises. The measure also requires that governments lower tax rates after borrowed money is fully repaid, even if the borrowing was repaid from a source other than taxes. In certain cases, governments borrow money on behalf of private entities. Because the private entities are solely responsible for repayment, it is unclear if this borrowing is covered by the provisions of Amendment 61.

Impact of Amendment 61 on state government. Amendment 61 affects Colorado's state government by prohibiting any future borrowing and requiring a tax cut when certain borrowing is fully repaid. Current borrowing will be unaffected, but future projects, programs, and services that would have otherwise been financed through borrowing will have to be eliminated or paid for by increasing fees or using money currently budgeted for other purposes. Table 1 provides examples of projects funded through state government borrowing and the requirements and restrictions under current law compared to Amendment 61.

The state and all of its enterprises issue an average of $2.9 billion in new borrowing annually and spend about $2 billion annually to repay borrowing. State agencies, excluding enterprises, make annual payments of about $200 million on borrowing. At the end of 2010, the state and all of its enterprises will owe about $17 billion for assets financed through borrowing.

Under current law, the state borrows money in the following ways, which will no longer be permitted by Amendment 61:

- *Long-term borrowing* — Long-term borrowing is money borrowed for a period of more than one year that is repaid from a specific source of money like dedicated taxes or fees over a fixed period of time. Voters must approve non-enterprise borrowing. For example, in 1999 voters approved borrowing for state highway projects. The money that was borrowed for the projects is repaid with state and federal highway funds.

- *Short-term borrowing* — In Colorado, the state sometimes borrows money early in the year to cover costs for its day-to-day operations and repays the money later in the year, as revenues are collected.

- *Lease-to-own agreements* — Lease-to-own agreements allow the state to make annual payments for new buildings or equipment over a number of years until the cost is repaid. The state legislature authorizes lease-to-own agreements and approves payments every year during its annual budget process. Once the cost is paid, ownership is typically transferred to the state. The state is currently using lease-to-own agreements to build a prison, a museum, a court building, and several academic buildings at state colleges and universities. The state is also using these types of agreements for K-12 school construction and renovation.

- *Enterprise borrowing* — Publicly owned enterprises are currently permitted to borrow for projects and programs without voter approval. Generally, enterprises generate their own revenue through fees charged for the services they offer. Enterprises usually borrow with long-term borrowing repaid from grants or fees for services. Enterprises do not have a defined voter base, and do not hold public elections.

  Most public colleges and universities are enterprises and have recently borrowed money to build classroom buildings and other facilities. This borrowing is repaid from sources such as tuition money, student fees, donations, and federal grants. Other state-level enterprises, such as the Colorado Housing and Finance Authority, act as financing authorities to borrow money that is lent to local governments, private businesses, and individuals.

Table 1. State Government Borrowing Requirements and Restrictions Under Current Law and Amendment 61

Examples of Existing Projects Funded Through Borrowing	Restrictions and Requirements	
	Current Law	**Amendment 61**
Long-term borrowing — money borrowed for a period of more than one year that is repaid from a specific source of money like dedicated taxes or fees over a fixed period of time.		
State Departments ***Department of Transportation*** State highways and roads	• Voter approval required • No dollar limit on borrowing	• Prohibited
State Enterprises **Public universities and colleges** Classroom buildings, dormitories, and student centers **Colorado Housing and Finance Authority** Loans to home buyers, businesses, ranchers, and farmers **Colorado Water Resources and Power Development Authority** Improvements to water and wastewater treatment plants	• No voter approval required • No dollar limit on borrowing • Legislative authorization required	
Other borrowing — including short-term (repaid within one year) borrowing, and lease-to-own agreements where authorized by state law and the state legislature approves payments annually.		
State Departments and Enterprises **Department of Corrections** Prisons **Department of Higher Education** Academic facilities **State Treasurer** Short-term borrowing and K-12 school construction and renovation	• No voter approval required • No dollar limit on borrowing • Legislative authorization required	• Prohibited

Impact of Amendment 61 on local governments. Amendment 61 applies new borrowing limits to all local governments and requires that all future borrowing be submitted for voter approval. Similar to the impact on state government, Amendment 61 will require local governments to either increase fees, reduce construction, or reduce programs or services. Table 2 provides examples of projects funded through local government borrowing and the requirements and restrictions under current law compared to Amendment 61.

Local governments and their enterprises issue an average of $4.9 billion in new borrowing annually, and spend about $4.3 billion annually to repay borrowing. Local governments, excluding enterprises, make annual payments of about $2.2 billion on borrowing. Currently, local governments and their enterprises owe about $36 billion for assets financed through borrowing. Some local government borrowing is repaid from voter-approved tax increases. After this borrowing is fully repaid, tax rates will be reduced, regardless of the outcome of Amendment 61.

Amendment 61 limits allowable local government borrowing in the following ways:

- *Borrowing is limited to bonded debt*. Bonded debt is money that is borrowed through the sale of government bonds for a period of more than one year. Under current law, local governments may borrow money through bonded debt as well as other forms of borrowing, such as short-term borrowing or lease-to-own agreements. Amendment 61 prohibits all forms of local government borrowing except bonded debt.

- *Voter approval is required for all borrowing*. Under current law, not all borrowing requires voter approval, and elections for bonded debt occur at various times throughout the year depending on the type of local government. Amendment 61 requires that all future borrowing first be submitted for approval by voters at a November election. In addition, enterprises, which were not previously required to seek voter approval for borrowing, will be required to hold elections.

- *For all local governments,* except enterprises*, borrowing is limited to 10 percent of the assessed real property value within their borders.* Generally speaking, this cap is less than what is allowed under current law. A local government that has already borrowed an amount more than the 10 percent cap would be prohibited from additional borrowing until it repays enough of its borrowing or real property values increase enough to drop its total borrowing below the 10 percent cap.

- *Borrowing must be repaid within 10 years and may be repaid early without penalty*. The typical term of current borrowing is 20 to 30 years. Borrowing for a shorter length of time requires higher annual payments because the loan is spread over fewer years; however, total interest costs over the term of the loan are lower.

Table 2. Local Government Borrowing Requirements and Restrictions Under Current Law and Amendment 61

<table>
<tr><th rowspan="2">Examples of Existing Projects Funded Through Borrowing</th><th colspan="2">Restrictions and Requirements</th></tr>
<tr><th>Current Law</th><th>Amendment 61</th></tr>
<tr><td colspan="3">Bonded debt — money borrowed for a period of more than one year that is repaid from a specific source of money like dedicated taxes or fees over a fixed period of time.</td></tr>
<tr><td>School Districts
School construction or improvements</td><td>• Voter approval required
• Borrowing capped at 20% of assessed property values for most districts</td><td rowspan="4">• Voter approval required
• Future borrowing capped at 10% of assessed real property values
• Term of future borrowing is limited to 10 years</td></tr>
<tr><td>Counties
Roads, public buildings, and vehicles</td><td>• Voter approval required
• Borrowing capped at 3% of actual (market) property values</td></tr>
<tr><td>Cities
Public buildings such as jails and recreation centers</td><td>• Voter approval required</td></tr>
<tr><td>Special Districts

Water and sewer districts: improvements to water and wastewater treatment plants

Fire protection districts: buildings, vehicles, and equipment

Regional Transportation District (RTD): mass transit facilities and vehicles</td><td>• Voter approval required in some instances</td></tr>
<tr><td>Enterprises

Denver International Airport: airport facilities and runways</td><td>• No voter approval required
• No dollar limit on borrowing</td><td>• Voter approval required
• No dollar limit on borrowing
• Term of borrowing is limited to 10 years</td></tr>
<tr><td colspan="3">Other borrowing — including short-term (repaid within one year) borrowing, and lease-to-own agreements where authorized by a local board and the local board approves payments annually.</td></tr>
<tr><td>Local Governments and Enterprises
Short-term borrowing, lease-to-own agreements</td><td>• No voter approval required
• No dollar limit on borrowing
• Subject to local board approval</td><td>• Prohibited, unless in the form of bonded debt</td></tr>
</table>

Impact of Amendment 61 on taxpayers. Amendment 61 requires that after borrowed money is fully repaid by a government, taxes must be reduced in the amount of the average annual payment. Assuming this requirement applies to current borrowing, and once the measure is fully implemented, state taxes will be reduced by about $200 million. Local government taxes are estimated to be reduced by about $940 million. Some tax reductions will occur in the first few years after the measure takes effect, but the full reduction will not occur until all borrowed money is repaid, which could take up to 40 years.

If the entire state tax reduction is applied to the state income tax, an average household earning $55,000 annually will pay about $49 less per year in today's dollars once the measure is fully implemented. If the entire local tax reduction is applied to property taxes, the owners of a home valued at $295,000 will pay about $225 less per year in today's dollars. The impact of the local tax reduction will vary based on the location of a taxpayer's residence.

How does Amendment 61 interact with two other measures on the ballot? Amendment 61 along with Amendment 60 (see page x) and Proposition 101 (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.

Amendment 61 requires state and local governments to decrease tax rates when debt is repaid, which is assumed in this analysis to apply to the existing debt of state and local governments, and it prohibits any borrowing by state government. 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. Proposition 101 reduces state and local government taxes and fees.

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 $744 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, leaving little for other government services. In addition, the prohibition on borrowing will increase budget pressures for the state if it chooses to pay for capital projects from its general operating budget. This would further reduce the amount of money available for other government services.

Tax and fee collections for local governments are expected to fall by at least $966 million in the first year of implementation and by $3.4 billion when the measures are fully implemented. However, after the state reimburses school districts, the net impact on local government budgets would be at least $581 million in the first year and $1.8 billion when fully implemented.

Total taxes and fees paid by households and businesses are estimated to decrease by $1.7 billion in the first year and $5.5 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 $1,360 per year when fully implemented.

Arguments For

1) Borrowing is expensive because it includes interest payments and fees. Limits are needed to help ensure that borrowing costs do not reduce money for public services in the future.

2) Amendment 61 encourages fiscal restraint through a pay-as-you-go approach to government spending. This approach limits government from passing on debt to future generations.

3) Because the public is responsible for repaying government borrowing through taxes and fees, voters should be asked before money is borrowed. The existing limits on government borrowing are not strict enough because the government can still borrow large amounts without voter approval. Amendment 61 requires any future local government borrowing to be submitted to voters for consideration at a November election.

4) Amendment 61 reduces taxes when borrowing is fully repaid, giving individuals and businesses more money to spend. Tax rates should go down when borrowing is repaid because the government no longer needs money for the annual payments.

Arguments Against

1) Borrowing is a crucial tool for financing large public investments such as prisons, schools, and water projects. Similar to private citizens using a loan to buy a home or car, borrowing is often the only way governments can afford to build and maintain safe bridges, roads, and other public infrastructure. Amendment 61 makes it harder to manage public finances and to respond in a timely manner to the needs of citizens.

2) Amendment 61 limits the ability of communities to meet the demands of a growing economy. Colorado's population has grown almost 20 percent in the last decade, requiring new roads, schools, hospitals, and water treatment plants. These public investments are needed by communities to operate and to attract residents and businesses. In addition, the measure may reduce private sector jobs, for instance

businesses may be awarded fewer construction contracts.

3) Amendment 61 places the full burden of paying for public buildings built to last 30 years or more on today's taxpayers. Also, Amendment 61 may force governments to set aside money for several years before construction can begin on a new facility. As a result, current taxpayers may never benefit from a facility they paid to construct. Taxpayers may realize a greater benefit from borrowing than from a tax-rate reduction.

4) Some governments will face serious financial disruptions as a result of Amendment 61. For example, the Colorado unemployment fund may be unable to pay unemployment benefits for a period of time if the state is no longer able to borrow to pay for benefits. Also, starting in 2011, school districts that rely on short-term borrowing may have cash flow disruptions until spring tax collections are received. These districts will have to consider options such as reducing or suspending teacher pay, selling buildings, or closing schools.

Estimate of Fiscal Impact

The measure contains provisions that reduce the amount of taxes paid by most taxpayers over time, while reducing future construction of publicly owned facilities and restricting the ability of the state and local governments to provide other programs and services.

Impact on the state and local governments. The measure will impact the state and local governments in the following ways.

- Borrowing restrictions will require that the state and local governments either raise fees, reduce construction, or reduce programs and services. Additionally, the measure affects cash flow management for the state and school districts, which in the past have borrowed money to finance current operations in anticipation of taxes collected later in the year.

- Assuming the tax reduction applies to current borrowing, the measure requires state and local governments to cut spending. The state will gradually cut spending after each borrowing is fully repaid by about $200 million over the course of the next 40 years beginning in 2018. Local governments will also cut spending after each borrowing is fully repaid by about $940 million over the course of the next 20 or 30 years. These amounts reflect the estimated average annual repayment for money currently borrowed by the state and local governments.

- Like government agencies, publicly owned enterprises will have to either raise fees, reduce construction, or reduce programs and services. Current borrowing by state-level enterprises accounts for an estimated $15 billion; borrowing by local enterprises accounts for about

$11 billion.

- The cost of future local government borrowing will likely be affected by the new 10-year maximum term on borrowing, as well as the early repayment provisions. However, the impact will vary by locality.

Taxpayer impact. The measure will impact taxpayers in the following ways.

- Based on the average annual repayment amount and assuming the tax reduction provision applies to current borrowing, Amendment 61 is expected to reduce taxes by about $1.1 billion per year when fully implemented over the next 40 years. This estimate includes about $940 million in local taxes and about $200 million in state taxes. The actual reduction for individuals, businesses, and others will depend on which taxes are reduced by the state and local governments and where the taxpayer lives. To illustrate the reduction, if the state reduced income taxes and local governments reduced property taxes, Amendment 61 is estimated to reduce the total taxes paid by an average household earning $55,000 per year and living in a $295,000 home by about $274 per year in today's dollars.

- Amendment 61 could make it difficult for Colorado to pay unemployment benefits, which could cause the state to be in violation of federal law. Unusually high unemployment has forced the Colorado Unemployment Insurance Fund to borrow money from the federal government to pay unemployment insurance benefits. Amendment 61 could prohibit this borrowing. As a result, the federal government could choose to increase federal unemployment insurance taxes on businesses in the state.

Table 3 summarizes the impact of the tax reductions required by Amendment 61 once all current borrowing is repaid.

Table 3. Annual Estimated Tax Impacts Based on Current Borrowing, Once Amendment 61 is Fully Implemented

	Total Outstanding Borrowing (Excluding Enterprises)	**Total Tax Reduction**	**Taxpayer Impact*** Tax Reduction
State Government	$2.2 billion	$0.2 billion	$49
Local Governments	$24.8 billion	$0.9 billion	$225
Total	$27.0 billion	$1.1 billion	$274

**Based on a household earning $55,000 per year living in a $295,000 home.*