

## HB05-1194 (TABOR Changes) Bill Analysis

for the Health District of Northern Larimer County Board of Directors

March 25, 2005

**Bill Title:** Concerning an adjustment to the amount of state revenues in excess of the limitation on state fiscal spending in section 20(7) of Article X of the state constitution in order to provide a more stable means of funding state budgetary needs...

**Bill Summary:** Creates General Fund Exempt Account in GF, consisting of moneys equal to the amount of state revenues in excess of the limitation on state fiscal year spending that the state retains for a given fiscal year. Voter reauthorization in 5 years, with rolling reauthorizations every five years. Money is to be appropriated for the broad purposes of reducing health care costs; funding public education and paying for strategic transportation projects.

**Sponsors:** House: Romanoff. Senate: Johnson and Groff, Anderson, Entz, Fitz-Gerald, Gordon, Isgar, Keller, Kester Tapia, Taylor.

**Committees:** Finance

**History:** Passed Senate Third Reading 3/23

**Date of Analysis:** March 24, 2005

### Background

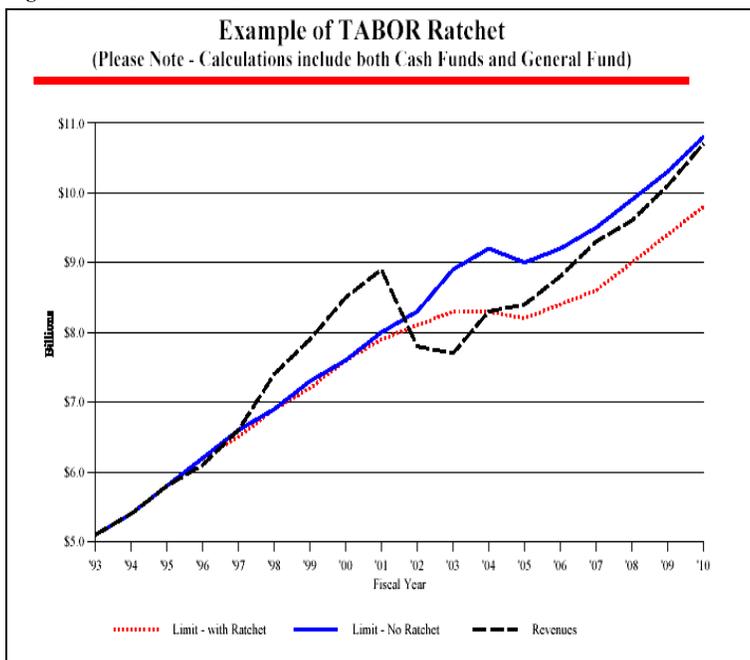
Discussions of the Taxpayer's Bill of Rights (TABOR), the Colorado constitutional amendment that limits state government revenues, often begins with its passage by the voters in 1992. However, attempts at TABOR-style reform earnestly began in 1986 with Amendment 4, which proposed mandatory voter approval for tax increases. Amendment 4 and other attempts at tax reform failed throughout the 1980s and early 1990s, facing strong opposition from both parties as well as business leaders who argued that flexibility in maintaining government infrastructure was necessary to attract business investments in the state. An adaptation of earlier proposals, TABOR was approved by the voters in 1992.<sup>i</sup>

What does TABOR do? This question cannot be answered simply. Indeed, the Legislative Council of the Colorado General Assembly issued a 126-page report in 2003 analyzing the impact of TABOR and other constitutional amendments that affect Colorado's fiscal situation. Even with the publication of this comprehensive study, debate continues over the effects of TABOR on the government and economy of Colorado. Given that caveat, TABOR can be conceptually reduced to several key points:

- (1) **Voter approval for tax increases.** All Colorado tax districts must ask voters to approve tax increases, including: a new tax; a tax rate increase; a local mill levy increase; an increase in a property assessment valuation ratio; an extension of an expiring tax; or, a tax policy change causing a net revenue gain. Voter approval is not required for a tax decrease.<sup>ii</sup>
- (2) **Revenue limits.** TABOR limits revenue by setting a cap on the amount of tax revenue that the state can budget each year. Under TABOR, state government cannot grow faster each year than inflation (market-basket prices) plus population growth (referred to as the TABOR limit). All revenues collected above the cap (referred to as TABOR surplus) are returned to the taxpayers as either refunds or credits, unless the voters approve a plan to spend surplus revenues. Specifically, government revenue spending in one fiscal year is limited to the level of spending in the prior year plus combined percentages of inflation in the Denver-Boulder area and statewide population growth.<sup>iii</sup>
- (3) **Ratcheting down.** TABOR limits annual growth in most state revenue to inflation plus population growth. If annual revenues fall below the TABOR limit, actual revenues rather than the applicable TABOR cap determine the base for the next year, permanently reducing the following year's TABOR limit.<sup>iv</sup> In addition, TABOR limits government's ability to spend the revenue it retains, by requiring voter approval to weaken existing limits. As a result of this provision, the statutory 6% limit on growth in general fund expenditures was locked in place.<sup>v</sup> Assuming continued economic growth, the logical conclusion is that the cap would keep government growth in check. However, in times of economic downturn, the TABOR limit has the unintended consequence of "ratcheting down" the TABOR revenue base, so that the limit is permanently reduced for subsequent years. For example, following the economic recession in 2001-02, actual state revenues were \$365.7M less than the TABOR limit for that fiscal year, resulting in a permanent

reduction of the TABOR base.<sup>vi</sup> **Figure 1**, compiled by the Joint Budget Committee Staff, demonstrates the cumulative effect of this type of ratcheting down on the state budget.<sup>vii</sup> As a recent article in the magazine *State Legislatures* describes, “Think of it, for example, like a reservoir that falls by half during a drought. When the rains return, the basin can’t refill to its pre-drought capacity. Instead, the amount of water the reservoir can keep is based on drought levels.”<sup>viii</sup>

**Figure 1: JBC Demonstration of “Ratchet” Effect**



**(4) Spending limits.** Although TABOR does not limit spending directly, revenue limits imposed by TABOR do work to limit government appropriations, as explained above. Since Colorado is a balanced budget state, when the ratcheting down effect occurred at the beginning of the decade, the Colorado General Assembly (induced by the combination of reduced revenues plus the constitutionally-locked 6% limit on government spending) was forced to fund governmental programs and operations with a significantly decreased revenue base, inducing funds transfers and spending cuts for certain programs. Consequently, the legislature has undertaken several types of actions to balance the budget in recent years, including: transferring funds into the general fund; implementing one-time accounting measures to lessen the impact in a given year; reducing capital appropriations; reducing general fund transfers for transportation projects; reducing

operating appropriations; not providing typical funding increases (i.e., caseload, medical, food, employee raises); and refinancing General Fund programs with cash funds or federal funds.<sup>ix</sup>

Overall, between 1992 and 2002, overall state and local spending in the state of Colorado decreased from 16.4% to 15.6%.<sup>x</sup> Notably, Legislative Council staff estimates a \$92.6M budget shortfall in FY 2005-05 and a \$248M shortfall in FY 2005-06. The likely result being an addition of programs to the Joint Budget Committee “cut list” so that General Fund savings may be achieved.<sup>xi</sup> Please note that certain programs retain statutory protection, largely insulating them from spending cuts prompted by TABOR. For example, K-12 funding is protected by Amendment 23, which constitutionally guarantees funding increases for public elementary and secondary education. Likewise, Medicaid is protected as a federally mandated program. Demonstrating the relative insulation of these programs from spending cuts, K-12 education was appropriated 42.2% of General Fund (GF) dollars in FY89-90 budget and 42.7% FY 05-06, while Medicaid was appropriated 13.1% of GF dollars in FY89-90 and 22.9% in FY05-06.<sup>xii</sup> During the same time-span, higher education, corrections, the judicial department and “other programs,” respectively, have suffered the most significant decreases in GF appropriations.<sup>xiii</sup>

**(5) De-Brucing.** Voters may let a state or local government retain revenues in excess of the TABOR limit; as well, they may exempt government from TABOR limits for a set number of years. According to the Association of Colorado County Administrators, 70% of counties have de-bruced some or all of their revenue streams since the passage of TABOR. Larimer County, in particular, passed eight of ten debrucing ballot initiatives between 1997 and 2000.<sup>xiv</sup> The Health District was de-bruced in 2000. Amendment 35 provides that the state legislature may refer a debrucing proposal to the state ballot with a simple majority vote.

***Why is this issue important to the Health District?***

Although federal law protects Medicaid, both the Department of Human Services (DHS) and the Department of Health Care Policy and Finance (DHCPF) have been compelled to apply cost-saving actions to health related programs (including Medicaid) due to TABOR. Since the Health District is committed to providing quality, affordable and timely health care services to its constituents, the District has a vital interest in protecting state and local services that support

these health-care priorities. Listed below (**Figure 2**) are the budget actions taken by DHS and DHCPF that directly impact health care services throughout the state.

**Figure 2: DHS and HCPF Actions to Balance the Budget**

DHS ACTIONS	DHCPF ACTIONS
<ul style="list-style-type: none"> <li>❖ Reduced support services for individuals with developmental disabilities (\$9.5M)</li> <li>❖ Reduced Medicaid mental health capitation rates (\$8.6M)</li> <li>❖ Shifted mental health clients to local programs (\$7.1M)</li> <li>❖ Reduced mental health funding for indigent clients (\$6.8M)</li> </ul>	<ul style="list-style-type: none"> <li>❖ Reduced Medicaid reimbursement rates for Medicaid providers (\$39.1M)</li> <li>❖ Used refinancing mechanisms (\$30.6M)</li> <li>❖ Changed eligibility requirements, capped Children’s Basic Health Plan, and limited the scope and duration of certain client services (\$19M)</li> <li>❖ Reduced administrative overhead (\$5.4M)</li> <li>❖ Increased cost recoveries through audits and estate recoveries (\$4.7M)</li> <li>❖ Implemented drug utilization and generic substitution (\$1.3M)</li> <li>❖ Increased co-payments for Medicaid clients (\$0.5M)</li> </ul>

Source: Colorado JBC Staff General Fund Budget Overview Presentation to the Joint Session of the General Assembly (January 12, 2005)

JBC staff have identified two ways for the legislature to resolve the long term fiscal situation in Colorado: (1) decreasing expenditures, such as reducing K-12 funding by a vote of the people or reducing or eliminating on-going operating needs; or (2) increasing the amount of revenues available for GF expenditure under TABOR, which would require a legislative referendum. Clearly, the Health District maintains an interest in sustaining health-care programs. However, health care and other vital governmental services, like higher education, criminal justice, and elementary and secondary education are not mutually exclusive. Therefore, the Health District retains substantial interest in sustaining governmental expenditures generally. HB05-1194 systematically addresses the fiscal problems evident in Colorado by proposing state-level de-bribing, rather than imposing even further program-level spending cuts.

**Review of HB05-1194**

HB05-1194 proposes reductions in the state income tax rate as well as TABOR relief at the state level. Listed below (**Figure 3**) is a review of the key provisions of this bill.<sup>xv</sup>

**Figure 3: Review of key provisions in HB05-1194**

	HB05-1194	
REFERENDUM?	Yes	
INCOME TAX RATE REDUCTION?	No	
SPENDING LIMIT?	Yes, 5-year time-out from TABOR (July 1, 2005 – June 30, 2010). State authorized to retain and spend capped amount of state revenues in excess of TABOR limitation from FY2010-11 and each succeeding fiscal year, based on a formula including adjustments for inflation and change in state population	
EXCESS REVENUE CAP?	Yes, defined for a given fiscal year to mean either: (1) if the voters approve a bonded debt increase at the 11/2005 state election, an amount equal to the highest total state revenues for a fiscal year from FY2005-06 – FY 2009-10, adjusted for inflation plus % population change, plus \$100M, and adjusting for the qualification or disqualification of enterprises and debt service changes; or (2) if the voters do not approve a bonded debt increase in 11/2005, the definition would not include \$100M	
EARMARKED FUNDS?	Yes	
PREPARATION OF ANNUAL FINANCIAL REPORT?	Yes, Director of Research of LC that annually identifies amount of excess state revenues retained in prior FY and how they were spent. Link to report on GA website.	
STATE REVENUE	<u>FY 2005/06</u>	<u>FY2006/07</u>
◆ INCOME TAX REDUCTION REVENUE	N/A	N/A
AMOUNT RETAINED FROM EXCESS		
◆TABOR REVENUE AFTER REDUCTION	\$393,800,000	\$579,700,000
State Expenditures	<u>FY2005-06</u>	<u>FY2006-07</u>
	\$0	\$0
Impact to TABOR Refund Mechanisms	<u>FY 2005-06</u>	<u>FY2006-07</u>
	\$393,800,000	\$579,700,000
ELIMINATE FUTURE RATCHET DOWN?	Yes	

HB05-1194 would allow the General Assembly to adequately fund programs and avoid program cuts, thus crafting potential solutions to TABOR-related fiscal constraints. Below, **Figure 4** lists arguments for and against TABOR reform, generally, and for and against HB05-1194 specifically.

**Figure 4: Summation of arguments for and against TABOR reform**

	ARGUMENTS FOR	ARGUMENTS AGAINST
TABOR REFORM	<ul style="list-style-type: none"> <li>▶ According to JBC staff, one-time sources of revenue only delay the inevitable, allowing the state to fund existing programs for a limited amount of time, but not changing revenue restrictions once those funds are exhausted.</li> <li>▶ TABOR opponents state that almost every possible savings mechanism, including centralization, has been realized in Colorado. It has been demonstrated that nothing short of TABOR reform will provide long-term relief and prevent additional program cuts.</li> <li>▶ As it stands, TABOR is contributing to an ineffective, inefficient, and increasing irrelevant government structure in Colorado.<sup>xvi</sup> Likewise, TABOR opponents cite that Colorado has some of the worst managed state finances in the country and is forty-nine among the states in job growth.<sup>xvii</sup></li> </ul>	<ul style="list-style-type: none"> <li>▶ According to the Independence Institute, Colorado can apply cost-saving spending measures to increase government efficiency, allowing significant changes to be realized without altering TABOR.</li> <li>▶ To achieve savings without reforming TABOR, they state that state services could be centralized, realizing significant savings.</li> <li>▶ TABOR proponents argue that by constraining state government growth, TABOR actually contributed to Colorado’s strong overall economic growth during the 1990s and should serve as a model of economic efficiency for the federal government and the states.<sup>xviii</sup></li> </ul>
HB05-1194	<ul style="list-style-type: none"> <li>▶ Allows for a five-year time out during which time solutions to TABOR-related fiscal constraints could be addressed.</li> <li>▶ As a result, HB05-1194 could potentially (subject to voter approval for bonded debt increase in 2005) raise the TABOR spending cap by \$100M, allowing potentially for a longer-term solution for funding essential services and avoiding the ratchet down effect in the future.</li> <li>▶ HB05-1194 earmarks funds for public education, transportation, pension funds for firefighters and police officers and health care.</li> </ul>	<ul style="list-style-type: none"> <li>▶ Voters may choose to vote against the referred measure, viewing it as substantially undermining the taxing limitations set forth in the state constitution.</li> <li>▶ HB05-1194 does not address the TABOR provision that locks 6% GF growth in place.</li> <li>▶ If voters choose not to approve a bonded debt increase in 2005, we would not see an increase in the revenue cap beyond the standard TABOR calculation. In the event of another recession, ratchet down could occur – likely resulting in further cuts in higher education and optional services under Medicaid.</li> </ul>

**Board Position**

The Board of Directors for the Health District of Northern Larimer County voted to support HB05-1194 on March 30, 2005.

**About this Analysis**

This analysis was prepared by Health District of Northern Larimer County staff to assist the Health District Board of Directors in determining whether to take an official stand on various health-related issues. Analyses are based on bills or issues at the time of their consideration by the Board and are accurate to the best of staff knowledge. It is suggested that people check to see whether a bill has changed during the course of a legislative session by visiting the Colorado General Assembly web page at [www.state.co.us/gov\\_dir/stateleg.html](http://www.state.co.us/gov_dir/stateleg.html). To see whether the Health District Board of Directors took a position on this or other policy issues, please visit [www.healthdistrict.org/policy](http://www.healthdistrict.org/policy).

**About the Health District**

The Health District is a special district of the northern two-thirds of Larimer County, Colorado, supported by local property tax dollars and governed by a publicly elected five-member board. The Health District provides medical, mental health, dental, preventive and health planning services to the communities it serves. Their mission is to improve the health of the community.

For more information about this analysis or the Health District, please contact Katherine Young at (970) 224-5209 or [kyoung@healthdistrict.org](mailto:kyoung@healthdistrict.org).

**Notes**

<sup>i</sup> Legislative Council Staff, “An Analysis of 1992 Ballot Proposals”, Publication No. 369 (1992)

<sup>ii</sup> Legislative Council Staff, “HJR 03-1033 Study: TABOR, Amendment 23, the Gallagher Amendment, and Other Fiscal Issues,” Publication No. 518 (September 2003)

<sup>iii</sup> Ibid

<sup>iv</sup> Ibid

<sup>v</sup> TABOR constitutionally locked the 1991 Arveschoug-Bird statute into place. The statute limits general fund spending in each year to prior year spending level plus six percent or 5.5% of state personal income, whichever is lower. The Arveschoug-Bird restriction applies only to the state’s operating budget (funding for state

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programs and agencies) and does not apply for capital items such as highways, prisons and other state provisions. Capital expenditures are limited only by the TABOR spending limit. John Straayer, *The Colorado General Assembly* (Boulder: University Press of Colorado, 2000)

<sup>vi</sup> Ibid

<sup>vii</sup> Colorado JBC Staff General Fund Budget Overview Presentation to the Joint Session of the General Assembly (January 12, 2005)

<sup>viii</sup> Chris Frates, "Fiscal Folly?" in *State Legislatures*, Volume 31, Issue 1, p. 20 (January 2005)

<sup>ix</sup> Colorado JBC Staff General Fund Budget Overview Presentation to the Joint Session of the General Assembly (January 12, 2005)

<sup>x</sup> Ronald K. Snell, "Nuts and Bolts of TABOR" in *State Legislatures*, Volume 31, Issue 1, p. 24 (January 2005)

<sup>xi</sup> Colorado JBC Staff General Fund Budget Overview Presentation to the Joint Session of the General Assembly (January 12, 2005)

<sup>xii</sup> Note that during the cited economic downturn, more Colorado citizens were forced onto Medicaid, therefore inflating General Fund expenditures for the program as well as increasing federal match dollars. Colorado JBC Staff General Fund Budget Overview Presentation to the Joint Session of the General Assembly (January 12, 2005)

<sup>xiii</sup> Colorado JBC Staff General Fund Budget Overview Presentation to the Joint Session of the General Assembly (January 12, 2005)

<sup>xiv</sup> "De-Brucing-County Summary," Association of Colorado County Administrators, [www.coadmin.homestead.com/files/DE-BRUCING\\_IN\\_COUNTIES\\_-\\_spreadsheet.htm](http://www.coadmin.homestead.com/files/DE-BRUCING_IN_COUNTIES_-_spreadsheet.htm)

<sup>xv</sup> Legislative Council Staff, "Comparison of Proposals to Reform TABOR and Amendment 23, as of 2/18/2005 Assuming Passage of the Base Change and Over Refund Carry Forward"

<sup>xvi</sup> Ronald K. Snell, "Nuts and Bolts of TABOR" in *State Legislatures*, Volume 31, Issue 1, p. 24 (January 2005)

<sup>xvii</sup> Bill Kraus, "Sure, TABOR is simple – a little too simple" in *Madison Magazine* (March 2005)

<sup>xviii</sup> Ronald K. Snell, "Nuts and Bolts of TABOR" in *State Legislatures*, Volume 31, Issue 1, p. 24 (January 2005)