



UNIVERSITY OF
DENVER

Center for Colorado's
Economic Future

**Legislative Briefing
February 25, 2011**

State Government Financing Study

1. The study responds to SJR 10-002, requesting DU to examine state and local taxes, and report to the General Assembly by January 31, 2011.
2. The resolution asked DU to raise funds for the study from private sources.
3. Nine Colorado Foundations provided support for the study.
 - *Boettcher Foundation*
 - *Bonfils-Stanton Foundation*
 - *Colorado Health Foundation*
 - *Colorado Trust*
 - *El Pomar Foundation*
 - *Gates Family Foundation*
 - *Kaiser Permanente*
 - *Piton Foundation*
 - *Rose Community Foundation*
4. DU is providing substantial direct support of the study.
5. Due to funding and time constraints, an examination of the financing of the General Fund programs of state government is our first priority.

Briefing Outline

- Study Parameters
 - More has been done than will be presented today
 - The purpose of today's briefing is to look at the work we have done on the state General Fund
 - Our focus is not on the immediate problem, but on long term structural dynamics
- We will continue our work, in consultation with DU's Strategic Issues Panel on the Future of State Government
- Today's briefing is preliminary in nature, and we hope to issue a final report on the General Fund by mid-summer
- Today we will review our observations and findings as well as categories of options we intend to investigate further
- Our final report will model options for consideration by policymakers and citizens

Study Approach

- Our study approach was to forecast the major components of the General Fund
 - Forecasting allows us to examine the long term dynamics of the structural features of the General Fund
 - Component Forecasts also provide the platform to model options over the long term
- Our forecasts are consolidated – they are all based on the same set of underlying assumptions
- We forecast the Colorado economy based on a baseline national forecast from Moody's Economy.com, and forecast General Fund revenues by source, as well as rebates and expenditures

Study Approach (continued)

- We combined the General and State Education Funds to obtain a more holistic picture of General Fund components
- In order to address revenue adequacy, it was necessary to forecast state spending drivers
- Programs initially chosen were based on the fastest growing components from the past two decades: school finance, Medicaid, and Corrections
- Each forecast was done by component and results combined. For example, school finance forecasts were done by forecasting enrollments, inflation, and assessed values by class
- We believe the results give us a strong picture of the direction and health of our current financing system

Study Approach (continued)

- Our analysis is not a budget forecast – it is a straightforward comparison of expenditures versus revenues over time
- Our revenue forecast shows a healthy recovery beginning in full force in 2012 and continuing for 3 years, before returning to a more steady rate of growth through the forecast horizon
- Over the 3 year period of 2012 through 2014 our forecast shows the addition of about 280,000 jobs – about twice the number gained as were lost during 2009 and 2010
- Expenditure forecasts are made based upon current constitutional and statutory provisions

Study Findings and Observations

- **General Fund Revenues**

- Colorado's General Fund has become more reliant on income taxes and that reliance will continue throughout the forecast horizon
- Revenue system is only slightly unproductive
- Revenues are becoming increasingly volatile
- General Fund revenues are mildly regressive, despite the progressivity of Colorado's income tax
- General Fund revenues are becoming increasingly inadequate when compared to stronger expenditure growth

Study Findings and Observations (continued)

- General Fund Spending

- School Finance

- The state's share of school finance spending will continue to outgrow the local share of funding
 - The local share of school funding is slowed by conflicting constitutional and statutory provisions
 - Despite the levy freeze, the local share will grow slower than assessed value growth
 - The state share of school finance funding will grow faster than General Fund revenue through FY 2024-25

Study Findings and Observations (continued)

- **Corrections**

- Changes in sentencing laws and slower growth in the 18 to 30 year old population cohort are leveling off the growth in inmates
- Strong growth over the past 3 decades in inmate populations and appropriations for the Department of Corrections are expected to slow in the future
- The Department of Corrections budget will grow more slowly than General Fund Revenues
- The share of revenues consumed by the Department of Corrections will decline from 8.8% to 7.3% by FY 2024-25

Study Findings and Observations (continued)

- **Medicaid**

- Medicaid caseloads will grow strongly due to population and age demographic growth as well as expanded eligibility
- Growth in medical inflation for the constituent parts of the Medicaid population will combine with caseload growth in the Medicaid population to drive costs
- Medicaid funding will grow more than twice as fast as General Fund revenue through the 2024-25 forecast horizon
- Growth in Medicaid costs will grow at faster rates after the forecast horizon due to the impacts of long term care for the aged

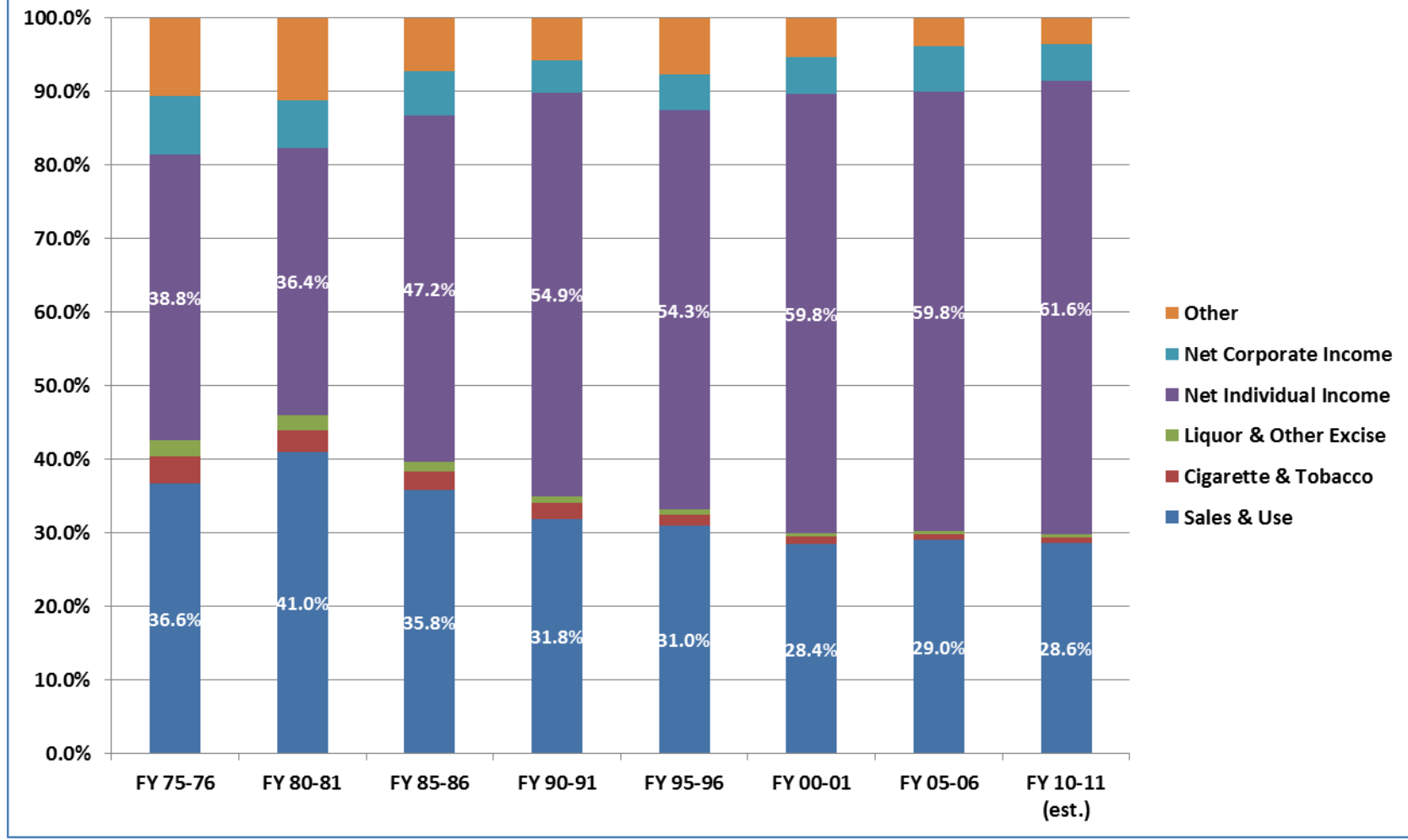
Revenue Adequacy

- Growth in Medicaid, education, and corrections spending will outpace revenue growth through FY 2024-25
- From period from FY 2012-13 through FY 2024-25, more than all of the “new money” the state will receive from revenue growth will be needed for school finance, Medicaid, and corrections
- For FY 2012-13 and each year from FY 2016-17 on, more than all of the “new money” each year will go to the 3 programs
- The percentage of revenues available for the remainder of General Fund activities will drop by about 60% throughout the period
- In 2010 constant dollars, amounts available for the remainder of the General Fund will shrink by more than 46%

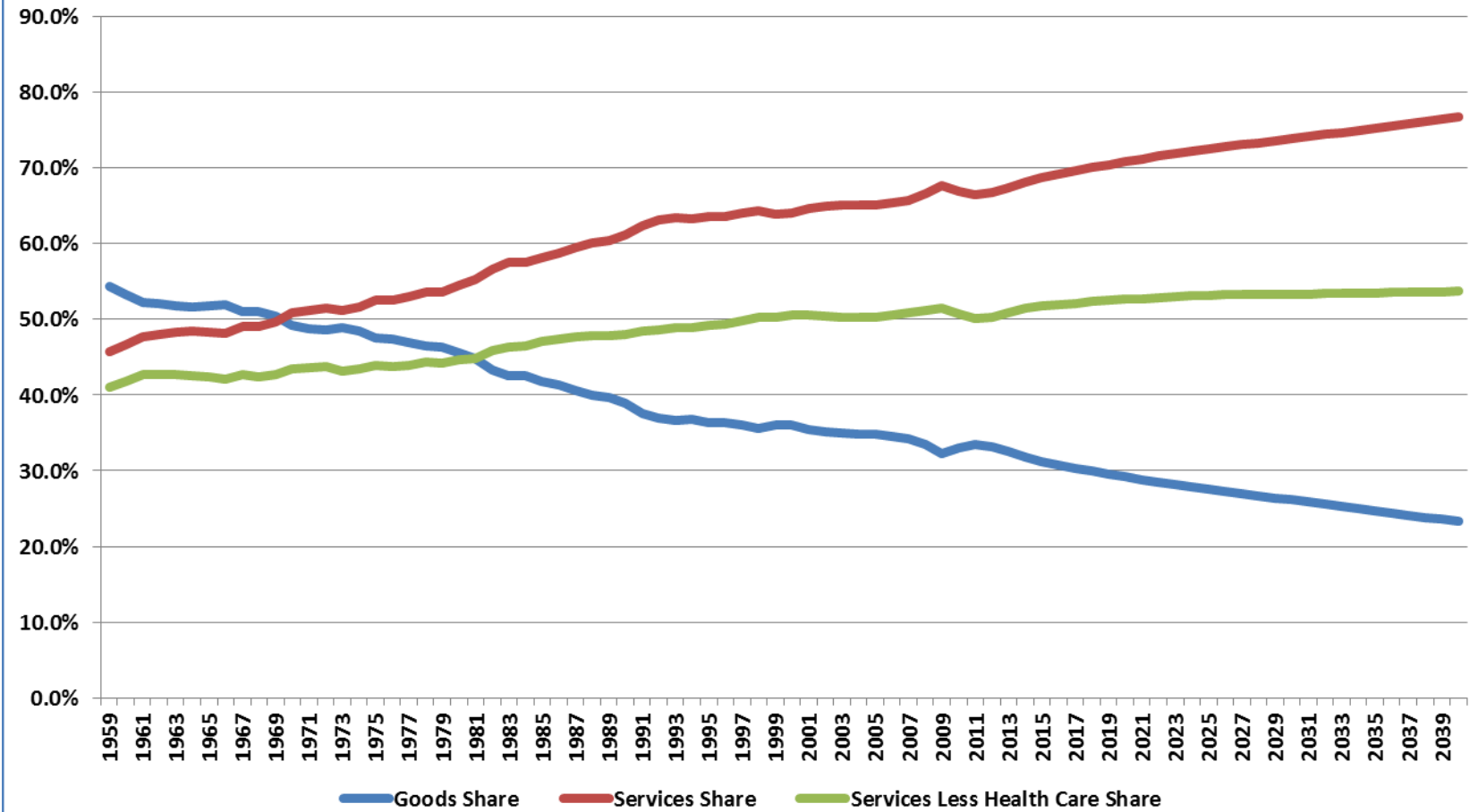
Revenue Adequacy (continued)

- Also in 2010 constant dollars, the amount of general fund available on a per capita basis will shrink by about 60% from FY 2007-08 levels by FY 2024-25
- On the basis of these observations, we find that Colorado's General Fund financing system is becoming increasingly structurally imbalanced and unsustainable.
- We will pursue a more rigorous analysis of “the gap” in the next phase of our work

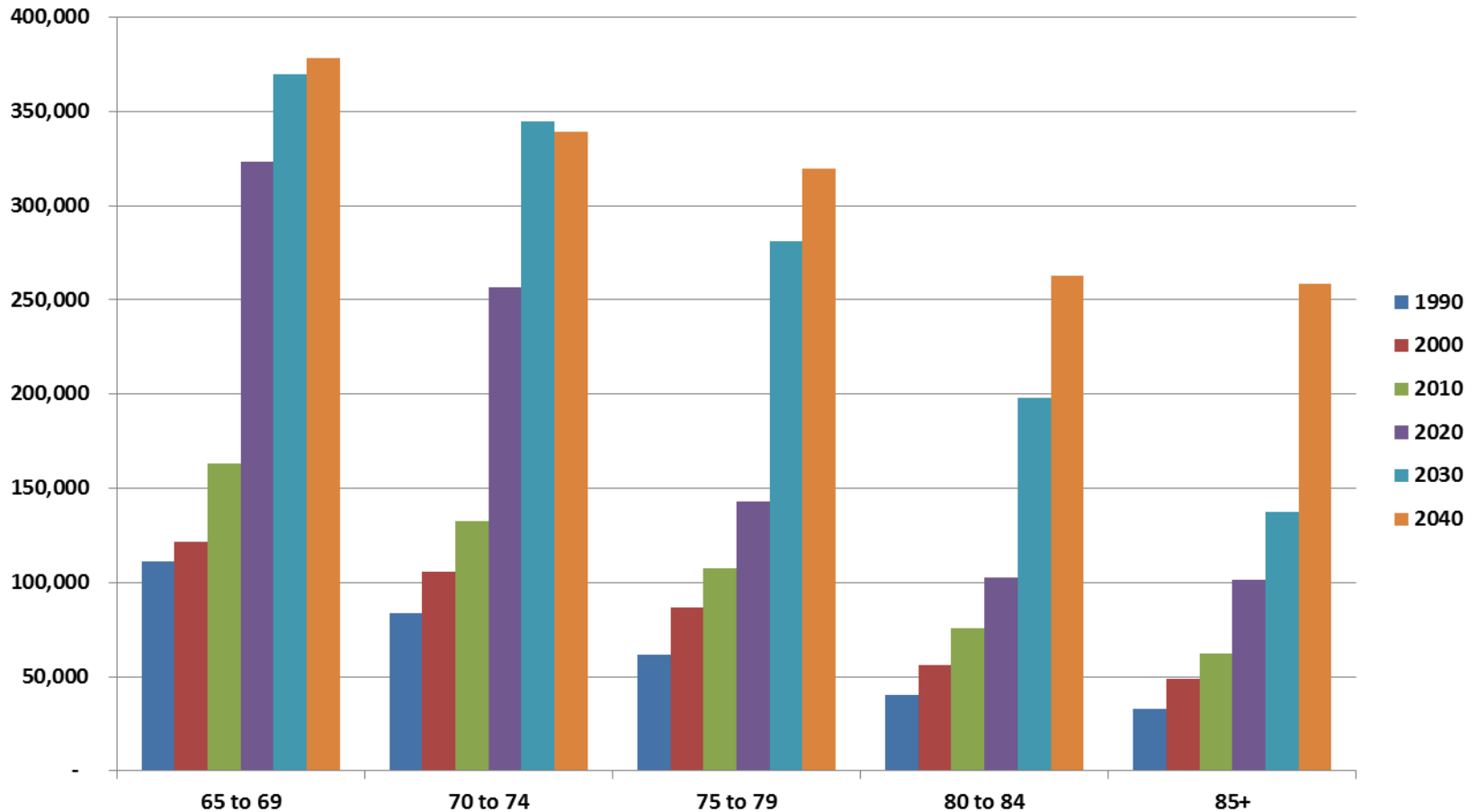
Colorado General Fund Revenues* By Source



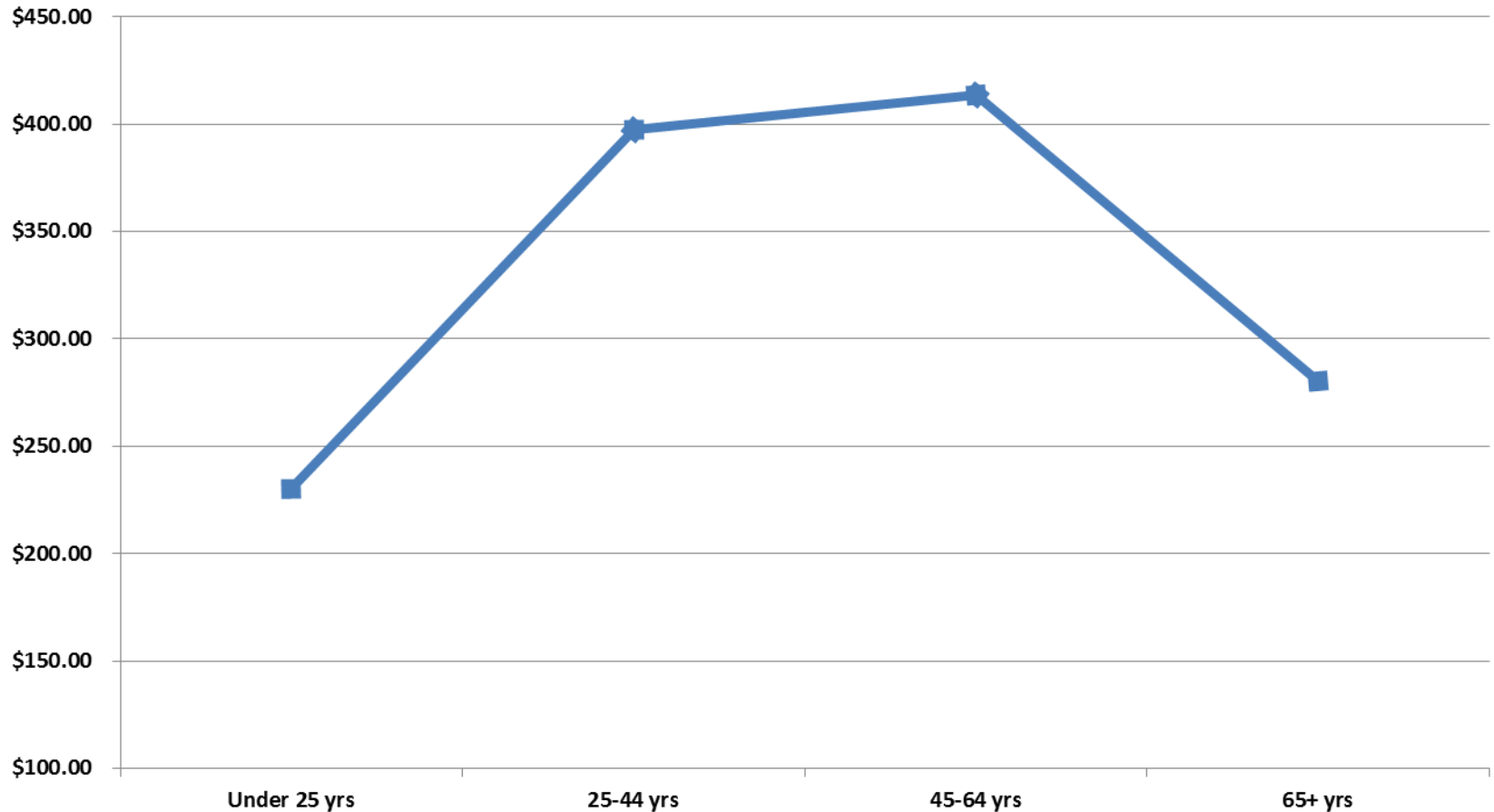
Personal Consumption Expenditures for Goods and Services as a Share of Total: U.S. History and Forecast



Colorado's Population by Five-year Age Groups 65+ 1990 to 2040



Patterns of Household Contribution to the Sales Tax Base by Age of Householder



Measuring Revenue Productivity

Percentage Increase in Revenue Source from a 1 Percent Increase in Total Personal Income

	Colorado (1976–2009)	Colorado (1992–2009)	50 States (1992–2009)
Individual Income Tax	1.15%	1.02%	1.046%
Sales Tax	0.795%	0.685%	NA
Use Tax	0.685%	0.892%	NA
Sales and Use Tax	0.786%	0.702%	0.867%
Selective Excise Taxes	0.163%	No significant relationship	0.893%

Measuring Revenue Volatility

Percent Change in the Rate of the Growth Rate of Revenue Sources Resulting From a 1 Percent Change in the Rate of the Growth Rate of Total Personal Income

	Colorado (1976–2009)	Colorado (1992–2009)	50 States (1992–2009)
Individual Income Tax	1.63%	3.06%	2.71%
Sales Tax	1.22%	1.80%	NA
Use Tax	1.70%	1.88%	NA
Sales and Use Tax	1.25%	1.82%	1.24%
Selective Excise Taxes	No significant relationship	0.03%	1.0%

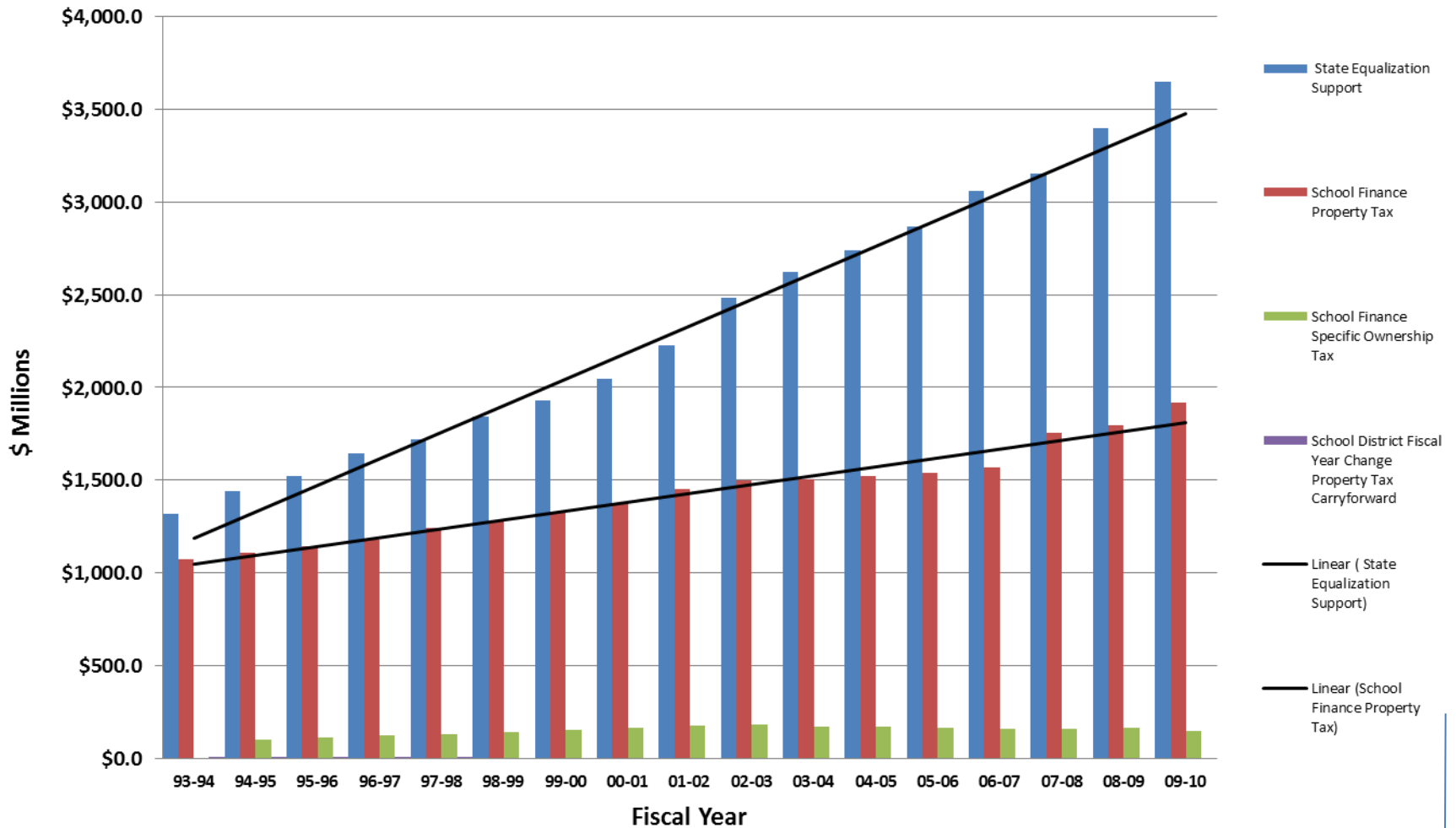
Taxes as percent of income, FY 2007-08

Adjusted Family Money Income

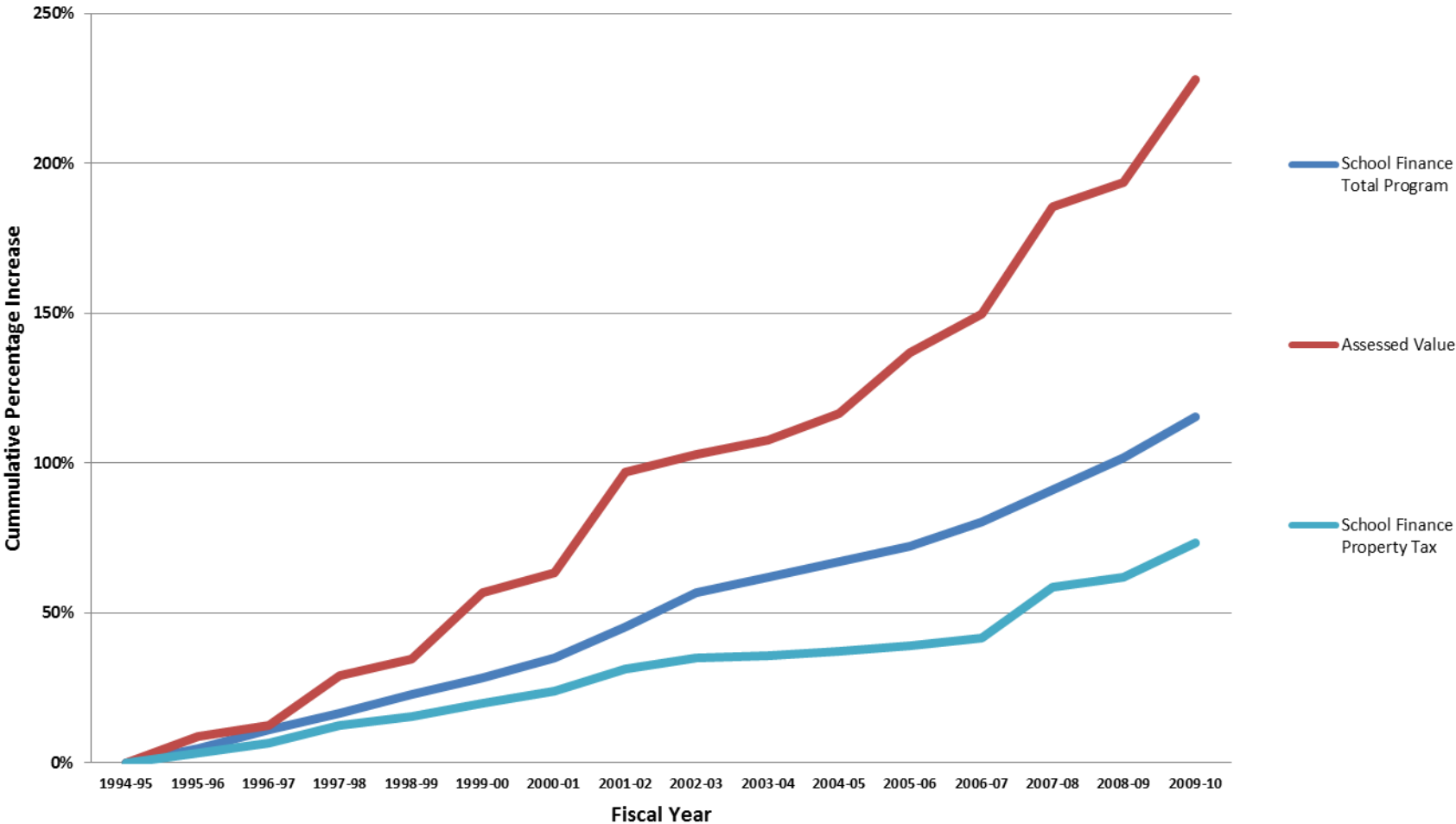
	Less than \$10,000	\$10,000 to \$14,999	\$15,000 to \$19,999	\$20,000 to \$29,999	\$30,000 to \$39,999	\$40,000 to \$49,999	\$50,000 to \$69,999	\$70,000 to \$79,999	\$80,000 to \$99,999	\$100,000 and over	Total
State taxes:											
Individual Income	0.6%	0.7%	1.1%	1.7%	2.0%	2.3%	2.4%	2.7%	2.8%	3.0%	2.7%
Sales and Use	1.9%	1.5%	1.3%	1.2%	0.9%	0.9%	0.9%	0.8%	0.8%	0.5%	0.7%
Fuel tax	0.7%	0.5%	0.5%	0.5%	0.4%	0.3%	0.3%	0.3%	0.2%	0.1%	0.2%
Licenses and Registrations	0.3%	0.2%	0.2%	0.2%	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%
Liquor tax	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Tobacco taxes	0.8%	0.5%	0.5%	0.4%	0.3%	0.2%	0.2%	0.1%	0.1%	0.0%	0.1%
Total state taxes	4.3%	3.5%	3.6%	3.9%	3.9%	4.0%	4.0%	4.0%	4.1%	3.7%	3.8%
Local Taxes:											
Residential Property	3.0%	3.0%	3.6%	3.1%	2.4%	2.3%	2.7%	2.3%	2.0%	1.1%	1.7%
Sales and Use	2.8%	2.2%	1.9%	1.7%	1.4%	1.3%	1.3%	1.2%	1.2%	0.7%	1.0%
Specific Ownership	0.5%	0.6%	0.4%	0.5%	0.4%	0.4%	0.3%	0.3%	0.3%	0.1%	0.2%
Occupation	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total local taxes	6.4%	5.8%	6.0%	5.5%	4.3%	4.1%	4.4%	3.7%	3.5%	2.0%	2.9%
Total Taxes	10.7%	9.3%	9.6%	9.3%	8.2%	8.1%	8.4%	7.7%	7.6%	5.7%	6.7%

School Finance Act Funding Components

FY 1993-94 through FY 2009-10



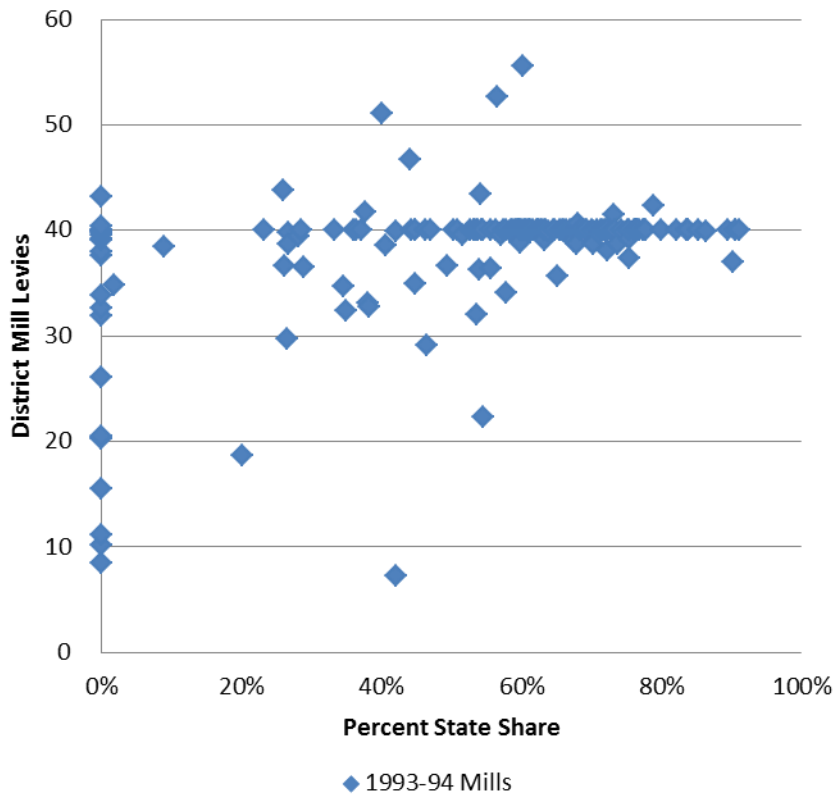
Comparison of Increases in Assessed Value, School Finance Total Program, and School Finance Property Taxes



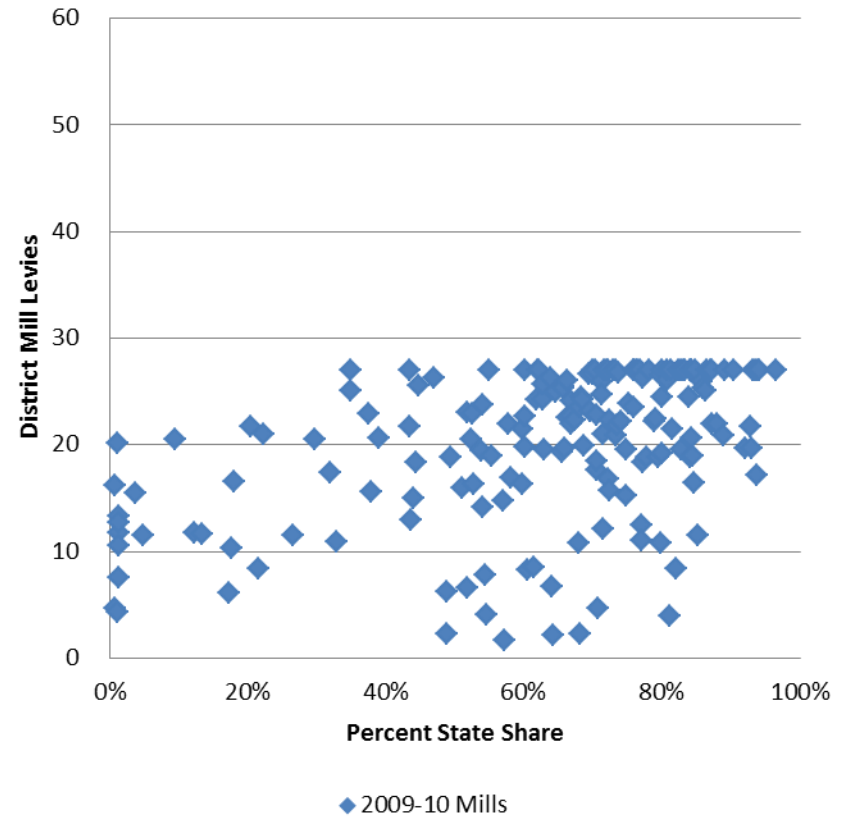
Comparison of School District Mill Levies by State Share

FY 1993-94 and FY 2009-10

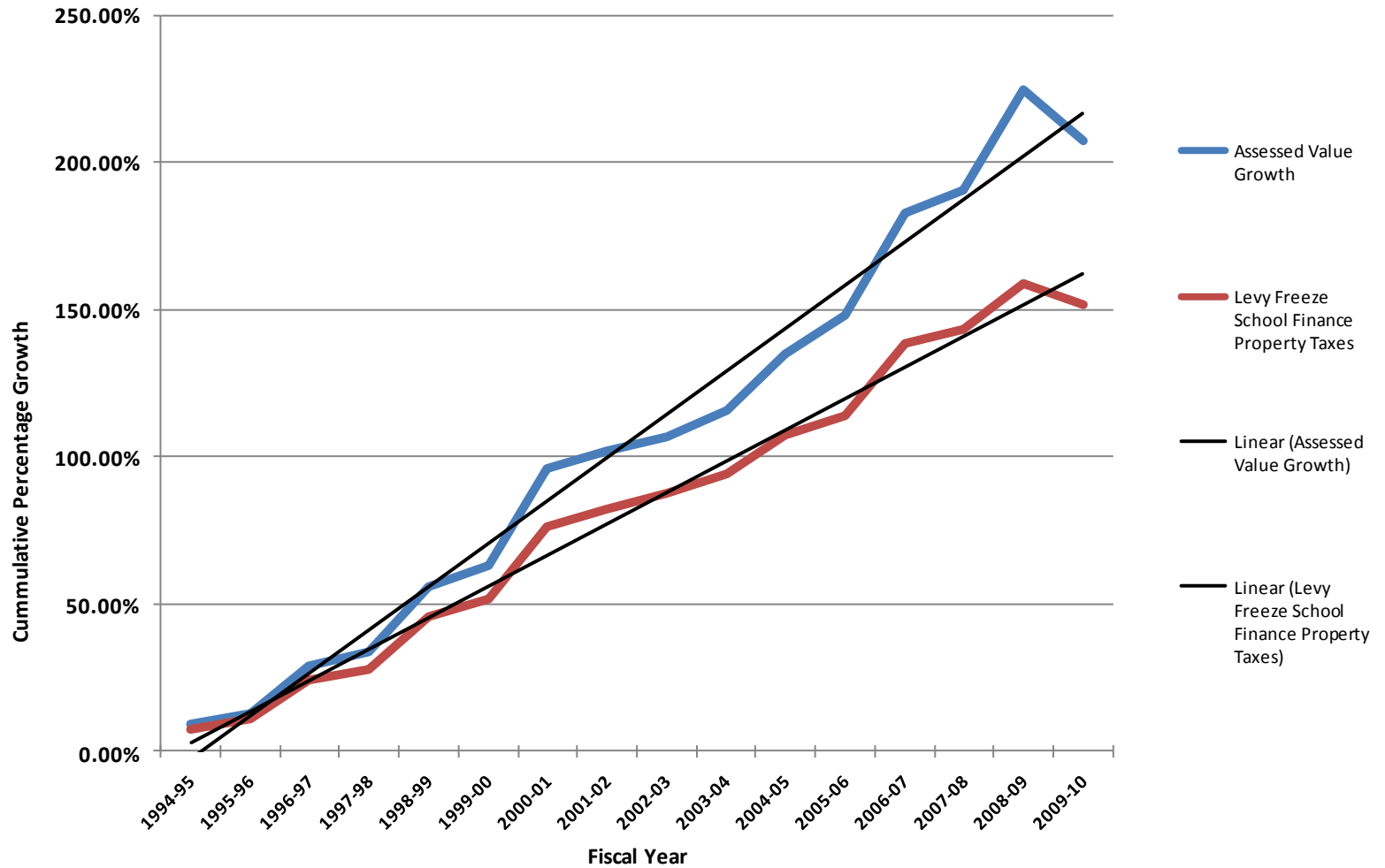
1993-94



2009-10



Simulated Cumulative Growth Rates of Assessed Value and School Finance Property Taxes with Levy Freeze



School Finance Act Funding Shares

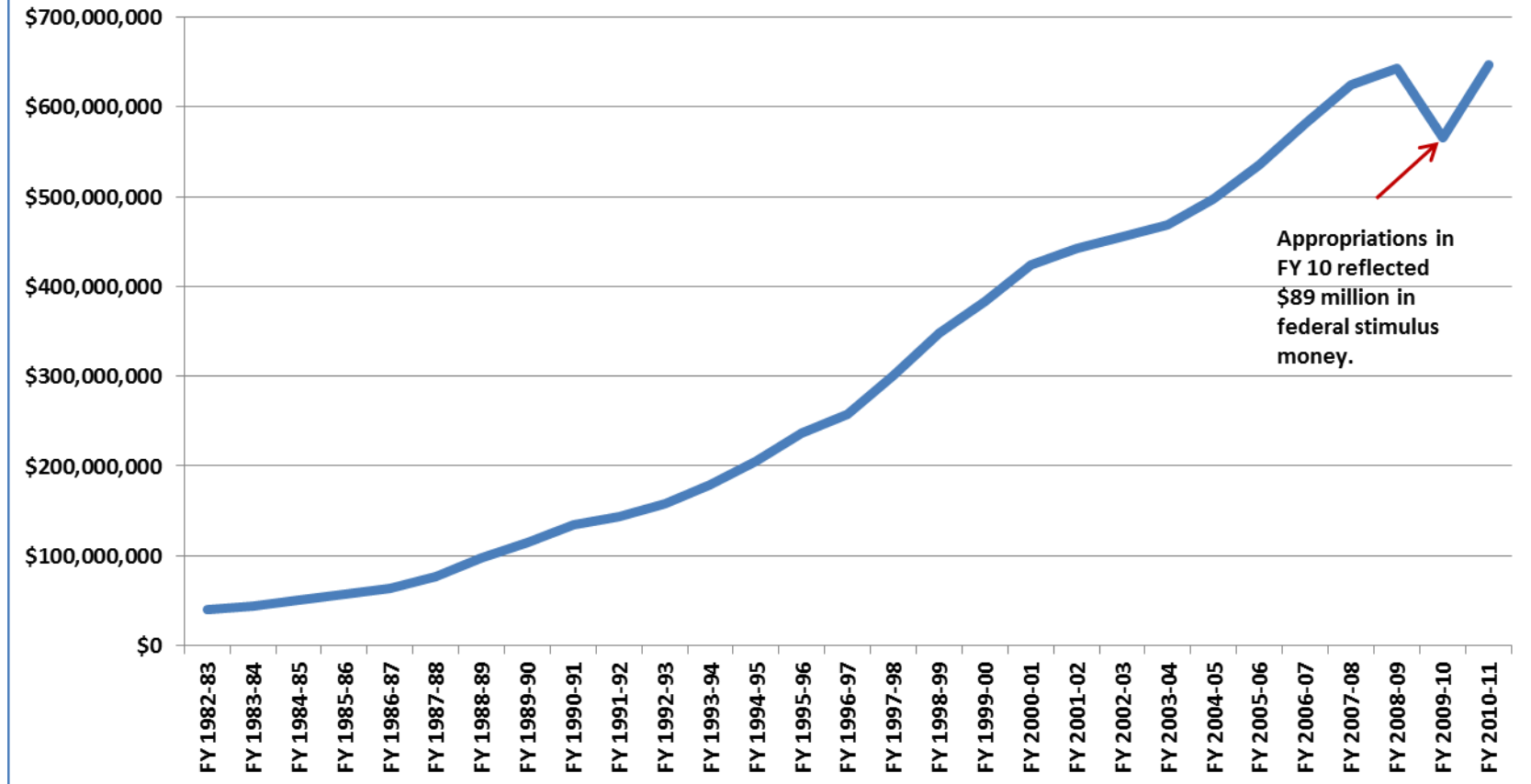
FY 2010-11 through FY 2024-25

<u>Fiscal Year</u>	<u>Funded Pupils</u>	<u>Pupils Percent Change</u>	<u>Total Program Cost</u>	<u>Total Local Share (Includes SO Tax)</u>	<u>Local Share Percent</u>	<u>State Share</u>	<u>State Share Percent</u>
FY 10-11	798,676	n/a	\$5,441,404,230 *	\$2,018,856,003	37.52%	\$3,422,548,227 *	62.90%
FY 11-12	808,382	1.22%	\$5,438,295,823 **	\$1,955,451,923	35.96%	\$3,482,843,900 **	64.04%
FY 12-13	819,814	1.41%	\$6,206,046,097	\$2,025,415,751	32.64%	\$4,180,630,346	67.36%
FY 13-14	833,245	1.64%	\$6,560,027,691	\$2,133,141,785	32.52%	\$4,426,885,906	67.48%
FY 14-15	846,421	1.58%	\$6,963,629,875	\$2,249,864,945	32.31%	\$4,713,764,930	67.69%
FY 15-16	861,994	1.84%	\$7,311,602,370	\$2,362,430,173	32.31%	\$4,949,172,197	67.69%
FY 16-17	881,443	2.26%	\$7,656,003,322	\$2,460,100,737	32.13%	\$5,195,902,586	67.87%
FY 17-18	899,918	2.10%	\$8,019,702,016	\$2,559,079,102	31.91%	\$5,460,622,914	68.09%
FY 18-19	918,239	2.04%	\$8,395,728,602	\$2,642,686,792	31.48%	\$5,753,041,810	68.52%
FY 19-20	934,770	1.80%	\$8,760,554,906	\$2,734,158,456	31.21%	\$6,026,396,450	68.79%
FY 20-21	950,790	1.71%	\$9,124,543,264	\$2,816,754,908	30.87%	\$6,307,788,357	69.13%
FY 21-22	966,176	1.62%	\$9,494,730,516	\$2,909,616,245	30.64%	\$6,585,114,272	69.36%
FY 22-23	981,002	1.53%	\$9,862,160,353	\$2,993,144,924	30.35%	\$6,869,015,429	69.65%
FY 23-24	996,511	1.58%	\$10,238,470,262	\$3,084,214,259	30.12%	\$7,154,256,002	69.88%
FY 24-25	1,012,596	1.61%	\$10,622,214,240	\$3,166,027,105	29.81%	\$7,456,187,135	70.19%
Change	213,920	26.78%	\$5,180,810,010	\$1,147,171,102	-7.71%	\$4,033,638,908	7.30%

* Both the total program cost and state share for FY 10-11 include \$216.4 million of federal funds.
 ** Total program and state share funding for FY 10-11 and FY 11-12 are prorated pursuant to the budget stabilization factor created by HB 10-1369.

Department of Corrections - Annual General Fund Appropriations

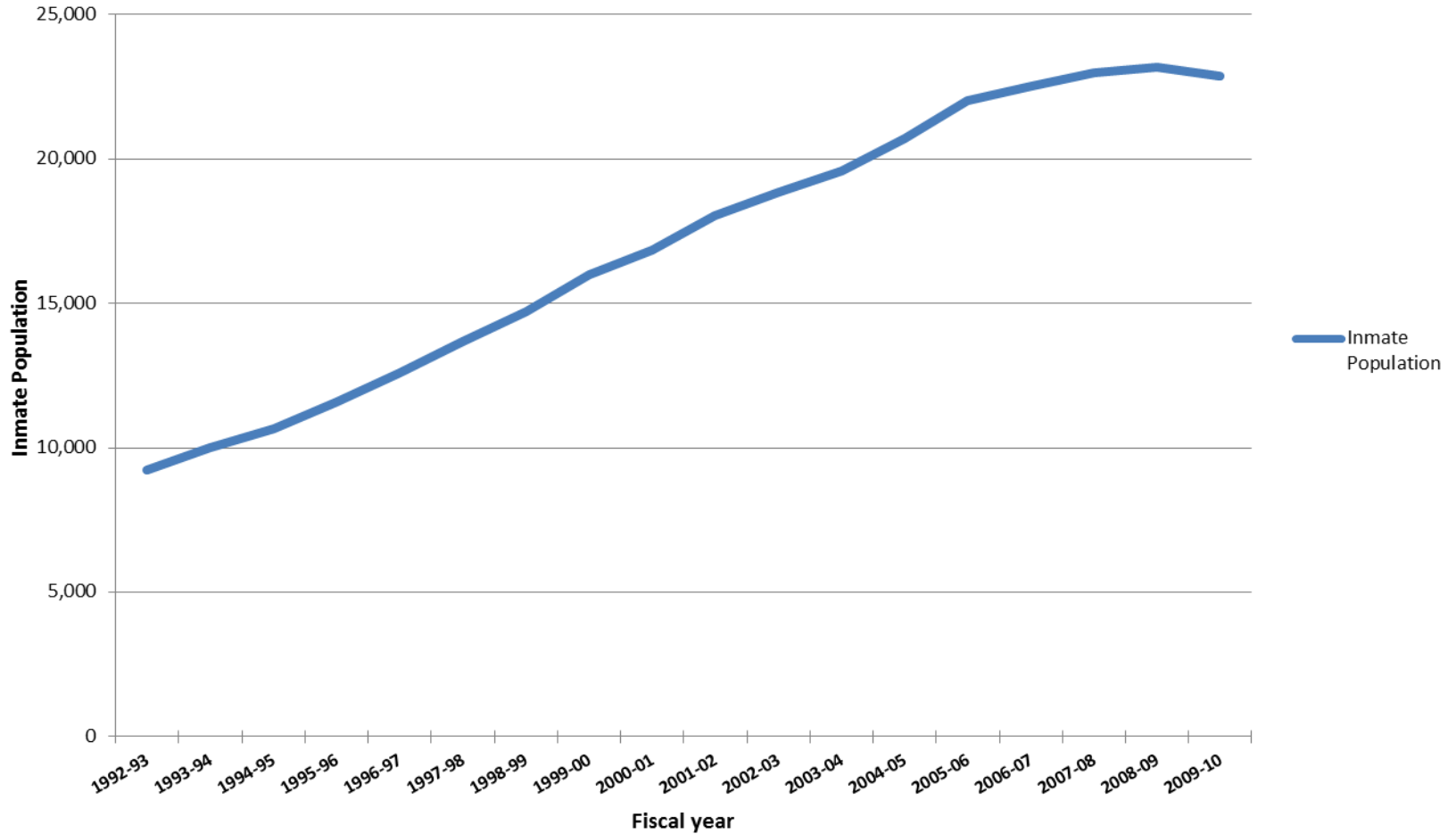
FY 1982-83 to FY 2010-11



Appropriations in FY 10 reflected \$89 million in federal stimulus money.

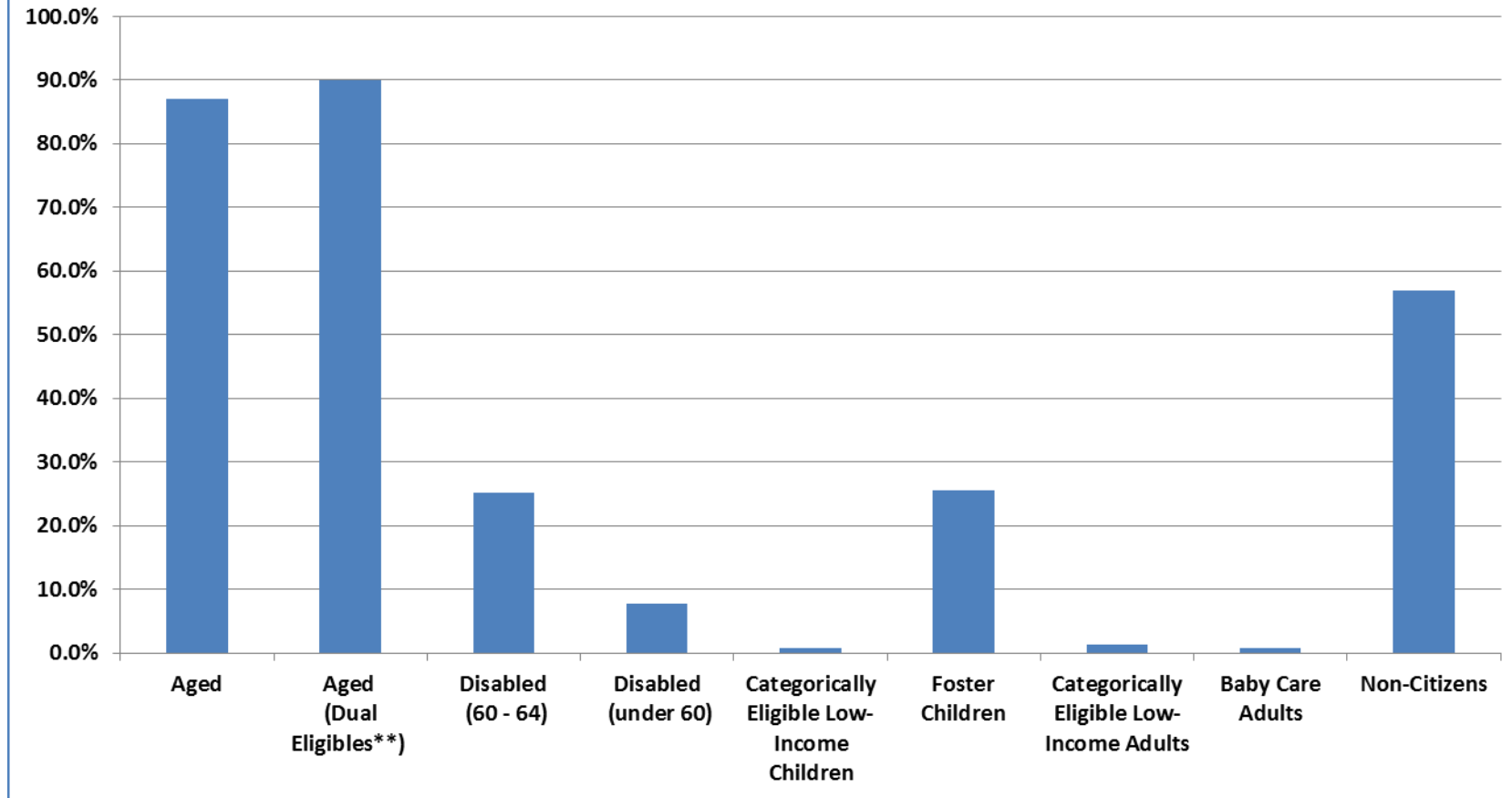
Growth in Inmate Population

FY 1992-93 through FY 2009-10

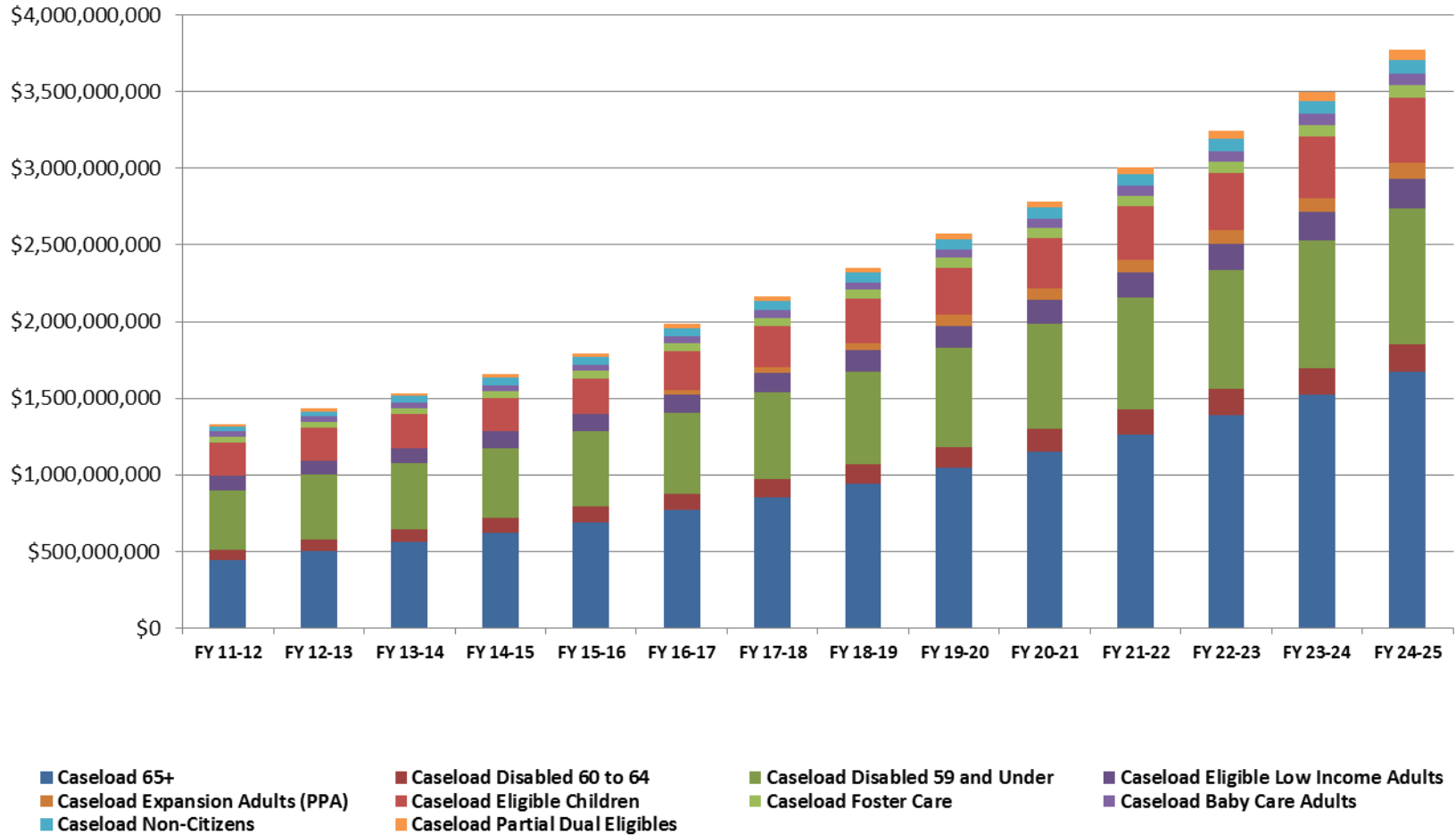


Medicaid Medical Services Premiums Caseload Growth Forecast

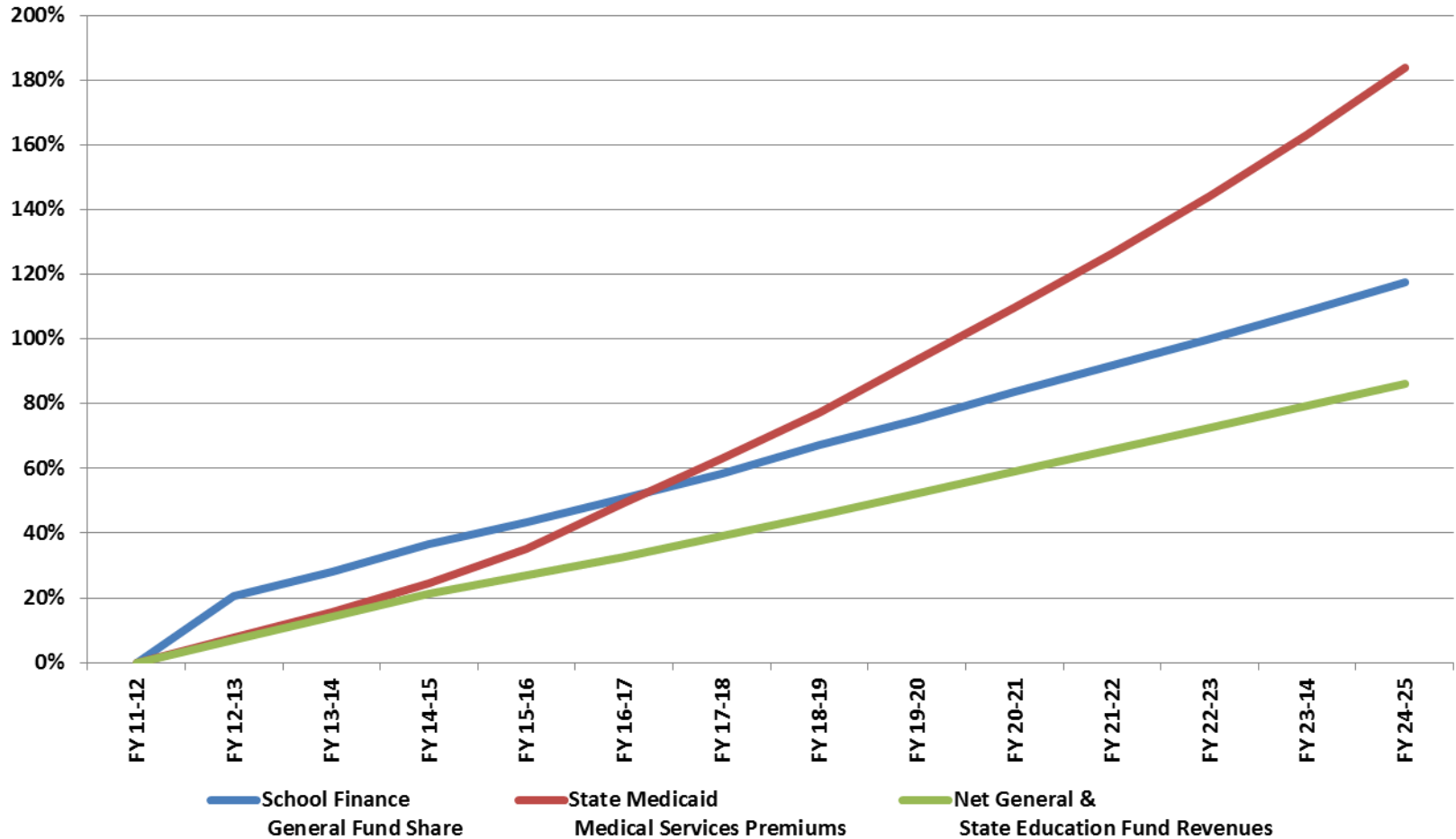
FY 2011-12 to FY 2024-25



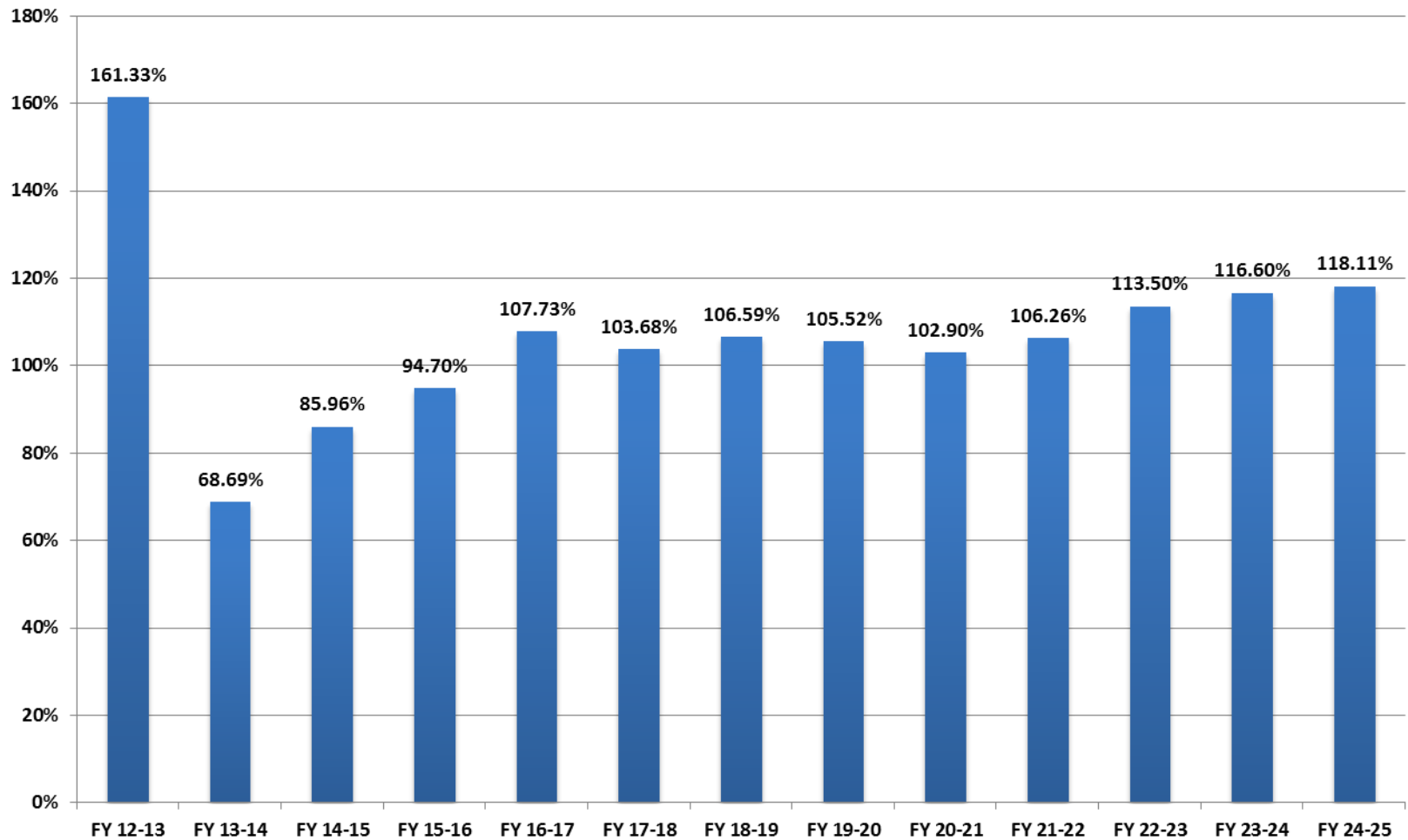
Contributions to Future Medicaid Medical Services Premium Growth by Caseload



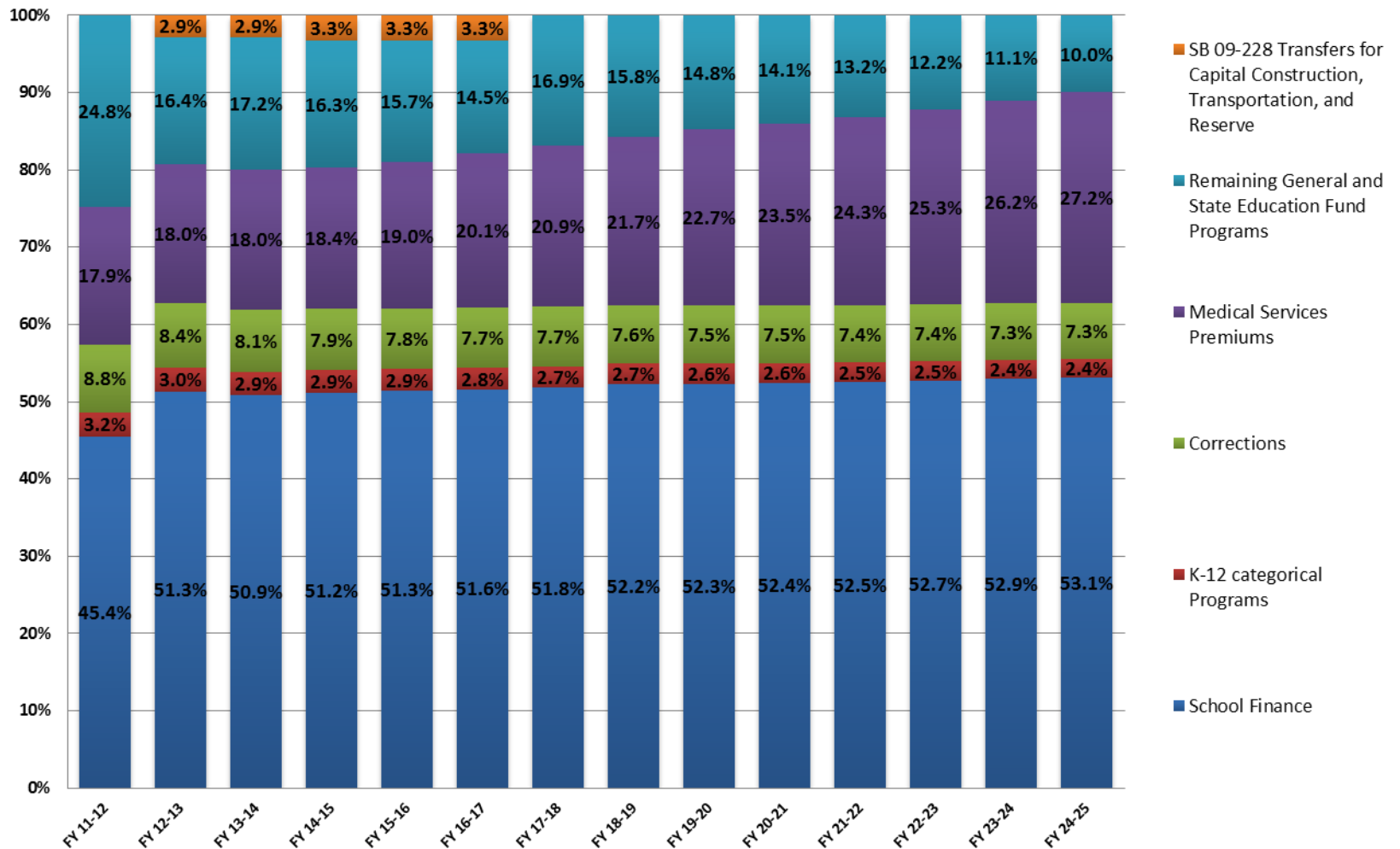
Cumulative Growth Rates from FY 2011-12: School Finance & Medicaid Appropriations vs. General Fund Revenues



Share of Incremental Annual Revenue that will be Consumed by Incremental Growth in K-12, Medicaid, and Corrections

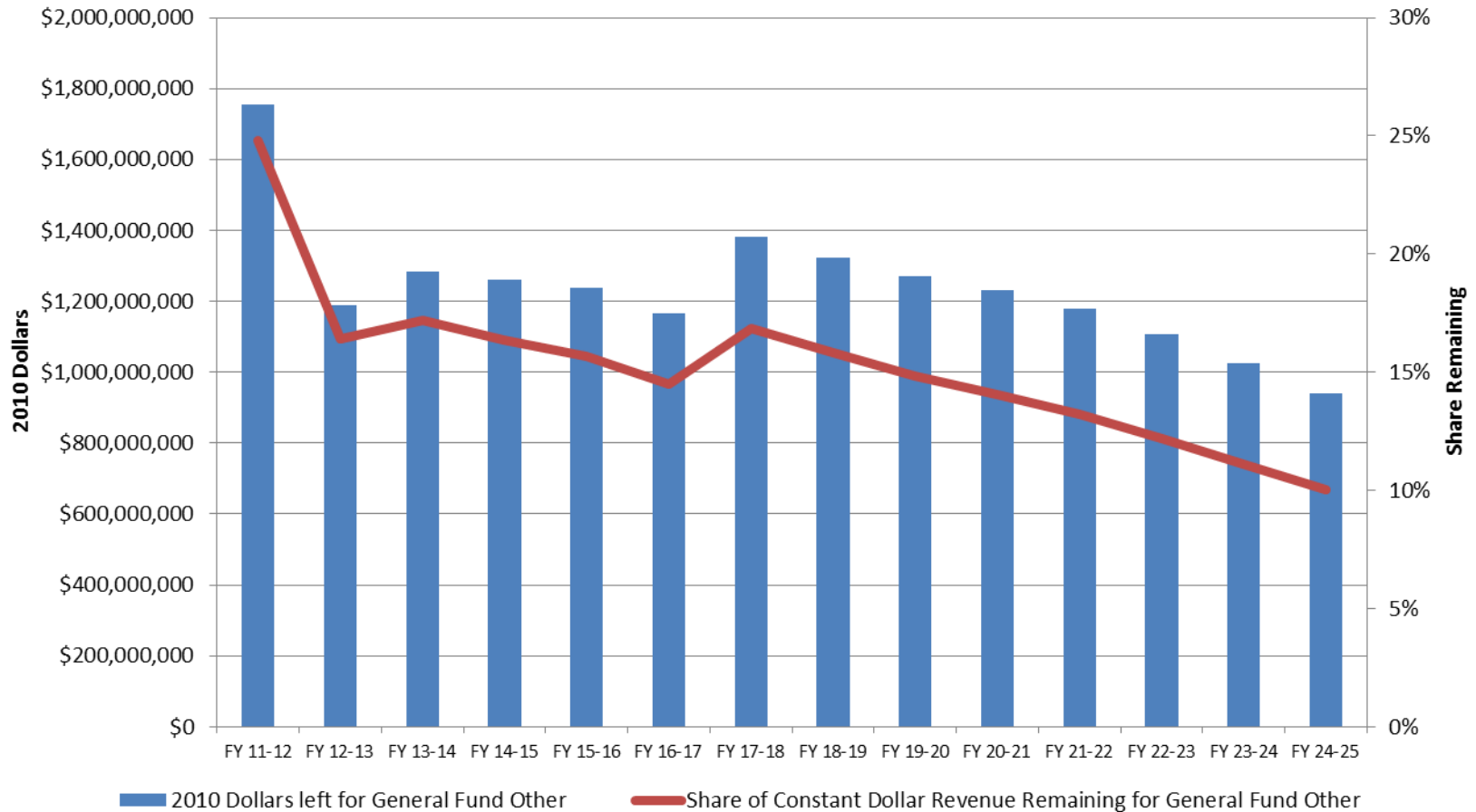


Percentage Shares of Net General and State Education Fund Revenues FY 2011-12 through FY 2024-25



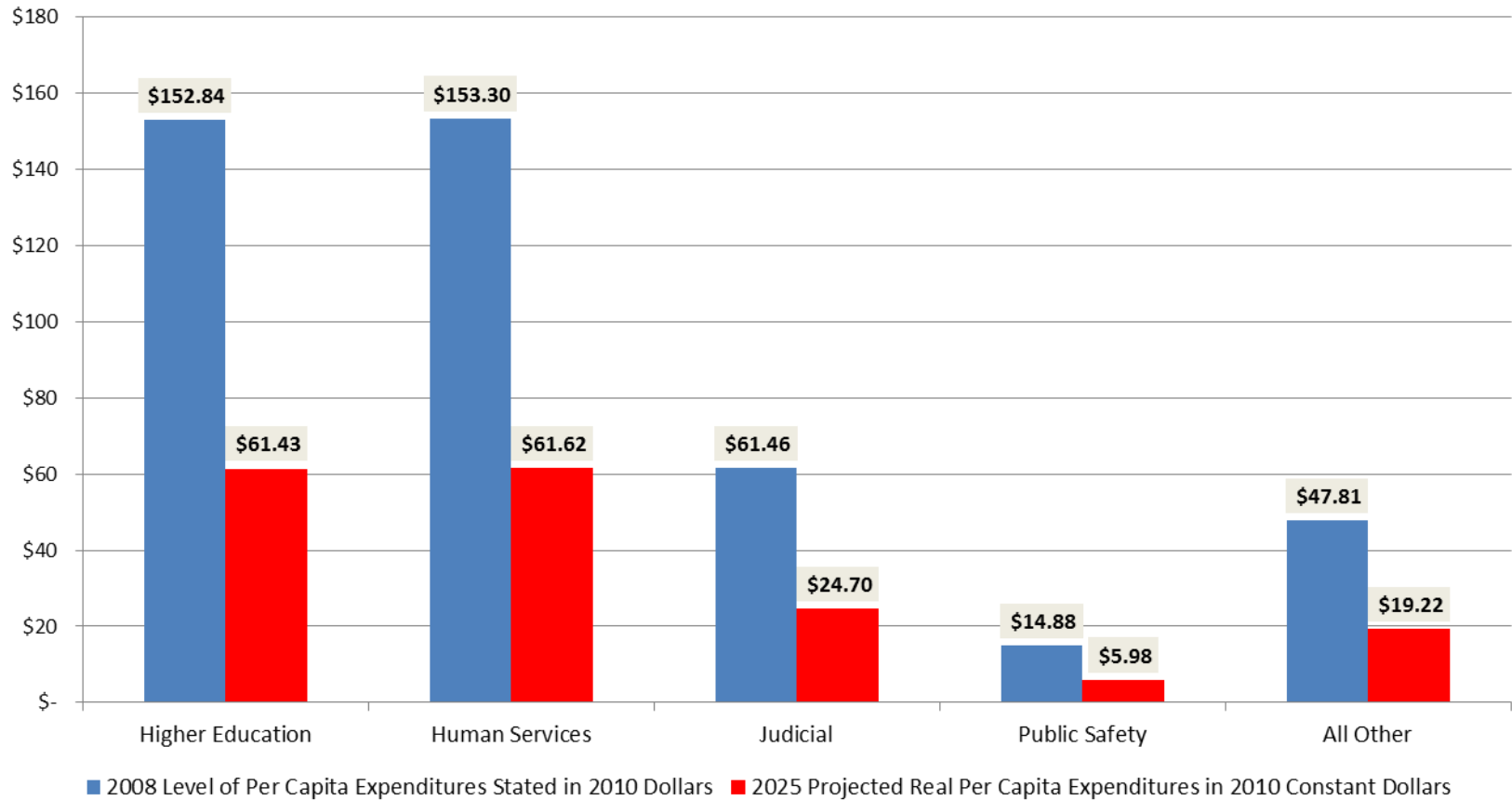
General Fund Revenue Available for "All Other" and Share of General Fund Revenues Available for "All Other"

2010 Constant Dollars



FY 07-08 and FY 24-25 Projected Per Capita General Fund Remaining for Major Departments Assuming FY 07-08 Pro Rata Shares

Stated in 2010 Constant Dollars



Policy Directions to Explore in Phase 2

General Fund Revenue Volatility

1. Creation of planning processes aimed at
 - Monitoring changes in long range spending drivers
 - Identifying business cycle driven revenue fluctuations relative to revenue norms
 - Informing decision-makers regarding spending and revenue policies
 - Preparing for and managing cost growth
2. Establishment of budgetary rules aimed at establishing a meaningful budget stabilization fund to address both upside and downside volatility and business cycle issues

Policy Directions to Explore in Phase 2 (continued)

General Fund Spending

1. Redefining the state/local financial partnership for future school finance costs, including ways to shore up existing local sources or looking for a new way to finance schools
2. Identifying ways for the state to finance the cost trajectory of Medicaid
 - Improving revenue productivity
 - Creation of savings to help pay for cost increases
 - Managing cost growth
3. Finding funding mechanisms for capital construction, controlled maintenance, and transportation that are not dependent on General Fund surpluses

Policy Directions to Explore in Phase 2 (continued)

Revenue Adequacy

- Evaluation of methods to make the General Fund more productive and flexible
 - Base and rate adjustments to improve performance
 - Examination of non user-related earmarked revenue
- Modeling the performance of selected revenue options over the forecast horizon