COLORADO ECONOMIC FUTURES PANEL · FINAL REPORT

PRINCIPLES FOR PROGRESS:
SHAPING THE ECONOMIC FUTURE OF COLORADO

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LETTER FROM THE UNIVERSITY OF DENVER CHANCELLOR

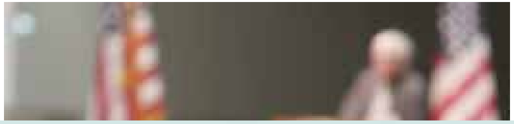
For more than a year now, the Colorado Economic Futures Panel has worked diligently to analyze the state's difficult fiscal situation. Sixteen accomplished business and civic leaders from across Colorado, acting as a nonpartisan task force and assisted by a talented research staff, have examined the state's fiscal structure. They scrutinized expenditures for major state and local government functions and agencies, including public (K-12) and higher education, health care, human services, corrections, transportation, courts and capital construction. This is the Panel's final report. In it, you will read of their serious concerns and comprehensive recommendations.

The University of Denver established the Colorado Economic Futures Panel and hosted its work in the belief that, as an independent institution, we are in a unique position to invest in the state that has been home to the University since our founding in 1864. Supporting the Panel's work at this critical time in Colorado's history has been an expression of our institutional commitment to work for the public good, and our belief that together we will surmount the challenges we face.

The Colorado Economic Futures Panel has completed its work. What comes of its findings and recommendations depends on the will and resolve of our leaders and the citizens of Colorado—indeed, all of us.

Robert D. Coombe

Robert D. Coombe
Chancellor, University of Denver



PRINCIPLES FOR PROGRESS:
SHAPING THE ECONOMIC FUTURE OF COLORADO

Overview from the Panel Chair

REPORT OF THE COLORADO ECONOMIC FUTURES PANEL

The economic future of Colorado will be written in the choices we make.

The outcome is not preordained and the stakes are high. The quality of life in Colorado is built on the foundation of the state's economy. In years to come, economic and fiscal decisions made by elected officials and voters will affect the state's success in attracting new businesses and creating jobs, navigating in a highly competitive global economy and maintaining reasonable tax levels.

These public decisions will shape nearly all aspects of life in Colorado. The quality of education, roads, mass transit, water, public health, open space, environmental protection, public safety, corrections, social services and the administration of justice all are affected by economic and fiscal policy decisions. Finding ways to make such decisions effectively has been the focus of the Colorado Economic Futures Panel (CEFP).

The Colorado Economic Futures Panel began its work with a detailed examination of the fiscal and economic characteristics of the state as a whole. As the Panel studied a broad range of issues, it became apparent that rebuilding public trust and improving the processes used for public decision-making and governance are fundamental to the long-term economic success of the state. These processes form the framework for decisions that will shape the economic future of Colorado.

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No one, including the Panel, knows exactly what decisions Coloradans will face in the future. We do know, however, that the only certainty is change and that difficult and complex public policy choices inevitably lie ahead. We also are quite certain that, in a highly competitive world, the margin for error is small, and timely action is essential. To shape a successful economic future for Colorado, fiscal policy decisions will need to be made wisely, based on sound information, and capable of adjustment when conditions change, as they surely will.

In creating what we hope will be a roadmap for decision-making and governance, the Panel does not intend to tell elected representatives and citizens *what* decisions to make in the future. Rather, our focus is on *how* to build public trust and improve the processes of decision-making in a way that will enhance the economic future and quality of life in Colorado.

SUMMARY OF FINDINGS

Any study of the state must begin by recognizing that Colorado is a place of great promise, with much to celebrate. Overall, Colorado is a high-income state with relatively low tax levels and an educated citizenry. It is a state with a diverse and growing population. It is a place of breathtaking physical beauty. All that, and more, is the Colorado of today.

But what about the Colorado of tomorrow? After a year of study, the Colorado Economic Futures Panel has concluded that the promise of Colorado is in peril. Without fundamental changes to the processes of fiscal policymaking and governance, the Panel believes that the Colorado of tomorrow may be at much greater risk than is apparent on the surface today.

The threat comes not only from the immediate fiscal crises that make headlines and occupy the attention of public officials and the media. Rather, and more fundamentally, the risk comes from underlying procedural, systemic and other factors that shape the way in which problems are understood and decisions are made. These are the drivers that determine the degree to which Colorado governments and institutions are able to meet the needs of citizens and respond to the inevitable changes that lie in our future. These are the forces that will shape the economic future of Colorado.

Over the course of its study, the Panel concluded that to create a sound economic future, and thus a favorable quality of life, four conditions are desirable. These are, in effect, principles for the progress of Colorado. They are:

- An informed, flexible process for making public decisions;
- A strong and effective system of representative government;
- A renewal of public trust through increased government accountability;
- A competitive fiscal policy based on information, shaped by an investment perspective and grounded in equity.

In relation to these principles, the Panel has identified several major impediments to effective public decision making and developed a number of recommendations. The procedural roadblocks to developing sound fiscal and economic policy in Colorado include: *A tangled, haphazard fiscal policy process; the weakening of representative government; and an erosion of public trust.*

UNTANGLING FISCAL POLICY

A most serious issue facing Colorado is its tangled fiscal policy process. Central to the problem is the practice of making fiscal policy by public referendum through amendments to the Colorado Constitution. It is a haphazard approach where citizens are asked to make major fiscal decisions in isolation, based on one-sided "facts" provided by proponents and opponents. Making fiscal policy by referendum is a process where over-simplification

> Making fiscal policy by referendum is a process where over-simplification and under-analysis are the established norms; where conflicting policies and unintended consequences are the logical outcomes.

and under-analysis are the established norms; where conflicting policies and unintended consequences are the logical outcomes.

In Colorado, creating fiscal policy is a process that can be initiated by the legislature, an in-state or out-of-state interest group or anyone else. The signature threshold to place a measure on the ballot in Colorado is lower than other states, and proponents can hire people to obtain signatures. There is no requirement to inform voters in a thoughtful and balanced way about the long-term implications of the proposal. Proponents and opponents need only present their own points of view.

While newspapers and other media may try to provide analysis, their work is often overwhelmed by 30-second sound bites, last minute barrages of pre-recorded telephone calls to voters and mountains of electioneering mail. The marketing system for public policymaking by constitutional amendment is biased against providing voters with anything resembling complete disclosure.

Once a policy has been established by this idiosyncratic process it is, effectively, cast in concrete. No one, not even duly elected officials, can change the policy except by going through another cumbersome election process, which can take years, as well as millions of dollars, to complete. The policy can't be changed—even if it doesn't work as intended. It can't be adjusted to recognize unintended consequences or the existence of other, conflicting policies. It can't be amended to meet new circumstances such as a constantly changing economic landscape or competition from other states or nations.

The result is the worst of all worlds—a random decision-making process that denies citizens meaningful information and then produces results that are extremely difficult to change. In a highly competitive world, this process of decision-roulette is unlikely to result in a winning number for Colorado citizens or businesses. For these reasons the Panel recommends that *future fiscal policies not be placed in the Colorado Constitution* but be enacted statutorily where they can more easily be adjusted as changing conditions require.

The decision-making straitjacket created by placing fiscal policies in the constitution is so dangerous that the Panel further recommends that existing *fiscal limitations and mandates be removed from the constitution*, as difficult as that process may be, and reestablished by statute. This might be done through a process of sunsetting existing constitutional provisions and converting them to statutes, either by constitutional convention or other appropriate means.

The Panel believes that the Colorado Constitution should contain only the fundamental rules of governance and, like the U.S. Constitution, should not be easy to change. Therefore the CEFP recommends *more rigorous standards to amend the Colorado Constitution*.

Although the Panel believes that the Colorado Constitution should not be easy to amend, and is not the proper vehicle for fiscal policy, the Panel does believe that the right of citizen initiative and referendum should be protected. The issue here is, of course, one of balance. Citizens must have the right to initiate action when necessary, but the process should not be so easy as to encourage inappropriate use.

STRENGTHENING REPRESENTATIVE GOVERNMENT

The practice of establishing fiscal policy by constitutional amendment has weakened representative government in Colorado by taking the most important fiscal decisions out of the hands of elected officials. We have put the state on autopilot, locked into a long-term course based on ideas of

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yesterday that have been frozen into the Colorado Constitution. It is a system in irons that deserves to be freed.

The Panel believes, as we think most Coloradans do, that taxpayers should approve all new taxes and tax-rate increases. To balance taxpayer control over the establishment of taxes with a fiscal policy process that is flexible and reinforces the concept of representative government, the CEFP recommends *that fiscal policies be established by statute*, not placed in the Colorado Constitution. Therefore, the Panel recommends *less* rigorous standards for statutory citizen initiatives as compared to constitutional initiatives. By so recommending, the Panel hopes to facilitate fiscal policy via statute and discourage fiscal policy via constitutional amendment.

The Colorado Economic Futures Panel believes that strong and responsive representative government is at the heart of effective governance. To support this concept, representative government in Colorado should be strengthened in two ways. First, the CEFP recommends that, after voters approve tax levels, elected officials should be allowed to make expenditure allocation decisions unencumbered by constitutional revenue limits or expenditure mandates. Second, the Panel believes that term limits are arbitrary and inhibit effective leadership and institutional continuity. Thus, the Panel recommends *eliminating term limits for state and local elected officials*.

REBUILDING PUBLIC TRUST

As the disjointed process of creating fiscal policy through constitutional amendment has removed key decisions from elected officials, it has weakened representative government, diffused accountability and strained public trust.

The Colorado Economic Futures Panel recommends that government accountability and public trust be strengthened by significantly improving the flow of relevant, understandable information to citizens. It is certainly true that Colorado governments, agencies and institutions already produce many reports. Even amid this flurry of reporting, however, taxpayers interested in understanding where their money goes and how it is used by each taxing entity are forced to conduct a major research project. The result, not surprisingly, is a skeptical citizenry.

To provide citizens with understandable information, the CEFP offers a number of related recommendations. The Panel recommends that all major state agencies, the courts, educational and other public institutions and local governments *be required to provide citizens with an annual performance report*. Such a report would show, among other things, the *comparative* performance of the unit benchmarked against similar units of government in terms of per capita revenues, service costs and subsidy levels. Importantly, a description of results achieved from the taxpayer's investment also would be included. In addition, the report should provide clear information as to *why the entity should not be consolidated* with similar or overlapping governments and describe how taxpayers benefit from the lack of consolidation.

The Panel also recommends that all major state agencies, the courts, educational and other public institutions and local governments be required to cooperate with the state of Colorado to produce an *online taxpayer information system*. Such a system would allow citizens to quickly estimate the total amount they are paying in taxes, which governments are receiving their tax dollars, the major services provided by those governments and the per capita costs, principal funding sources and amount of general tax subsidies, if any, for those major services.

The quality of education, roads, mass transit, water, public health, open space, environmental protection, public safety, correction, social services and the administration of justice are affected by economic and fiscal policy decisions.

Finally, the Panel recommends the establishment of an *ongoing fiscal research and reporting center*. This would be an independent, non-government and nonpartisan organization that conducts ongoing research and provides regular updates *to the public* on matters related to Colorado's fiscal health, state economy and other significant trends affecting the state. It could be called upon to provide the type of thoughtful, balanced, impartial analysis of issues and proposals that is so noticeably absent from the Colorado's fiscal decision-making processes.

INFORMATION, PERSPECTIVE AND EQUITY

Improving the processes of public decision-making, strengthening representative government, and rebuilding public trust by providing citizens with useful information are the foundation of a competitive fiscal policy for Colorado. To be successful, however, the fiscal policy built on this foundation needs to be based on information, shaped by an investment perspective and grounded in equity.

Developing a competitive fiscal policy begins by gaining a shared understanding of the problem to be solved. One source of impartial research to inform the policy process might be the independent, nonpartisan fiscal research and reporting center described in this report, although other sources could be used as well. However finally organized, the Panel believes the use of such an information-based approach would improve the quality of both representative and direct-democracy decisions in Colorado.

Developing effective fiscal policy also would be aided if proposed governmental expenditures were viewed from an investment perspective. A public investment perspective encourages a hardheaded analysis about how funds should be used and what returns should be insisted upon. It also facilitates thinking about how smaller preventive investments today might avoid large remedial expenditures tomorrow. Perhaps most importantly, such a perspective focuses the legislative and public discussion on results. A *public investment perspective focusing on results* changes the dialogue and directs attention to issues of efficiency, effectiveness and the public's right to insist upon a return on tax dollars invested.

A strong economic future in Colorado requires sound policy decisions based on solid information and a businesslike return-on-investment perspective. It also requires consideration of issues of equity and disparity.

The first of these issues relates to the need to improve the external competitiveness of the state *by creating a balance between residential and non-residential (business) property taxes*. While businesses clearly must carry their fair share of the tax burden, a disproportionate reliance on non-residential property for tax revenue can reduce the attractiveness of Colorado as a place in which to do business. This, in turn, could make the state less competitive in its efforts to attract desirable companies, making it more difficult to build a strong economic future. To enhance the long-term competitive position of Colorado, consideration should be given to a policy where property taxes are equitably distributed between residential and non-residential property.

The research presented to the Panel also suggests that there are dramatic disparities in resources among counties in the state. Perhaps even greater variations exist among cities. There are many reasons for this, including the winner-take-all competition for sales tax among local governments. Sales tax battles among local governments can adversely impact land-use decisions and allow public entities to be played off against one another, often at high cost.

The economic future of Colorado,
and the quality of life our children enjoy tomorrow,
may hinge on our collective resolve today.

At times, local governments "win" the competition for a new sales tax source by offering expensive tax breaks or other inducements to developers and retailers. Such inducements may, or may not, serve the best interest of residents and other taxpayers in the community. In any event, one long-term effect of this process is the creation of a governmental class system where some local governments in Colorado are resource-rich while others are much poorer.

The external competitiveness of Colorado on the world economic stage is not served by a sales tax structure that creates classes of rich and poor local governments within a single state, leaving some able to serve businesses and residents well and some with much less capacity to do so.

Therefore, the Panel recommends that consideration be given to implementing a mechanism that would share incremental resources among local governments in Colorado. For example, the state could establish a mechanism to share a portion of incremental sales tax revenue increases regionally among cities and counties in Colorado while still retaining incentives for entrepreneurial local government action. Another approach might involve a general revenue sharing or equalization process utilizing state funds. Whatever approaches are used, the Panel recognizes that achieving some measure of resource balance or revenue sharing among cities and counties in the state is a complex matter. Nevertheless, it is an important issue to address.

INTERCONNECTIONS

Our study suggests that there are strong interconnections among the impediments to effective fiscal decision-making identified by the Panel. The disjointed process of placing fiscal limits and mandates in the Colorado Constitution removes key decisions from the hands of elected officials, weakening representative government, diffusing responsibility and accountability and eroding public trust. The implications include errant and inflexible public decision-making, posing possible serious risks to Colorado's economic future. This is not a situation that anyone chose; it simply came into being—one disconnected step at a time.

MOVING FORWARD

The Colorado Economic Futures Panel recognizes that implementing the suggestions put forth in this report will not be easy. Indeed, doing so will require an uncommon coalition and a particular determination. Yet, the economic future of Colorado, and the quality of life our children enjoy tomorrow, may hinge on our collective resolve today.

Jim Griesemer, Chair
Colorado Economic Futures Panel

REPORT OF THE COLORADO ECONOMIC FUTURES PANEL

> Just as running a business in the 21st century requires the ability to adapt to rapid change, so does running a government.

CREATING THE FUTURE

The Colorado of tomorrow will be significantly different from the Colorado we know today. In the past, our economic competition came from neighboring states, but as interstate highway and air transportation improved, our competition widened to include the Western United States, then the national field of play. Today, the explosive growth of telecommunications and electronic commerce is forcing Colorado to compete globally, and this competition will intensify in the years ahead.

While it is impossible to predict the impact of future changes, we can anticipate that change will occur far more rapidly than in the past. Advances in technology and telecommunications have brought the global economy to our doorstep, changing the way the world does business and further hastening the pace of change.

No longer is it necessary for all workers to be located in one place—or even in one country. Instead, many jobs, particularly knowledge-based jobs, may be performed virtually anywhere in the world, and many knowledge-based products may be transmitted instantaneously to the other side of the globe. Businesses have begun to adapt to these changes, making their organizational structures flexible, adaptable and responsive in taking advantage of all that the global economy has to offer.

Just as running a business in the 21st century requires the ability to adapt to rapid change, so does running a government. State taxes in Colorado, which rely predominately on earnings and the proceeds of sales, will generate relatively less revenue when future knowledge-based jobs are located elsewhere in the world and purchases are made in cyberspace. State government must be able to respond to such structural changes in the economy. Unfortunately, Colorado's fiscal structure is difficult and slow to change because it is locked into the Colorado Constitution.

Why should Coloradans be concerned about the ability of state and local governments to adapt in the future? One answer lies in the connection between the sustainability of governmental services and our economic health. To remain healthy and competitive, current and future Colorado businesses look to state and local governments to provide an educated workforce, efficient transportation systems, a streamlined regulatory environment and public health and safety.

In addition, Coloradans expect their governments to meet the challenges awaiting us over the decades ahead. Preserving our environment, coping with our state's continued population growth, addressing the growing traffic congestion in Front Range and mountain areas and improving our education system to maintain the high skill level of our work force and educating the growing number of young people who enter our schools without communication and other skills is essential. In short, governmental flexibility is critically important to all Coloradans because of its impact on our quality of life for years to come.

We have determined that there are significant barriers that must be overcome to improve governmental flexibility. Overcoming these barriers is not impossible, but will take work—work largely dedicated to restoring public trust in representative democracy through better public information and accountability, and to restoring flexibility in making fiscal policy through the use of statutory rather than constitutional methods.

For these reasons, this report is focused on our fiscal policymaking processes rather than making recommendations for specific changes in tax or spending.

The inability of our state and local governments to address these and other important issues is, we feel, the result of structural rigidities and inflexibilities in our government structure.

THE PAST AND PRESENT

Colorado historically has been the envy of other states. Our natural beauty, recreational amenities and clean environment have attracted new residents each year. In addition, the stewards of our governmental institutions have provided state and local governments that are open, clean and relatively efficient. As a share of income, our combined state and local taxes rank 46th, which is low compared to other states, and our citizens have the right to vote on any new or increased taxes. Coloradans also have the right to petition their government directly through the initiative powers provided in our constitution.

From the time it was adopted, Colorado's Constitution has required its state and local governments to balance their budgets each year, and delegated to elected officials the authority to allocate public funds. *We strongly affirm the right of citizens to vote on new and increased taxes, the right of citizens to petition their government through the initiative process, the power of elected officials to allocate public funds and the requirement that our governments balance their budgets.* These distinctive qualities of Colorado policymaking must be retained as important components of the way we do public business.

But these great strengths also have opened the door to problems that must be addressed. The ease with which we can initiate constitutional amendments has resulted in explosive growth of detailed provisions in our constitution that normally would be found only in statutory law. Since 1990 alone, the Colorado Constitution has grown by more than 21,000 words, the equivalent of nearly three United States Constitutions, including its preamble and all 27 amendments. Adding to the problem, Colorado's constitutional amendments were adopted independently over time and contain many provisions that overlap or conflict with one another. Changing any of these provisions is a very time-consuming and costly process. Most problematic is Colorado's inability to respond to a rapidly changing future because of the constitutional straitjacket these provisions have created.

It is natural to ask why initiated constitutional amendments have become the policymaking tool of choice for citizens. It appears that over the course of the past few decades, there has been a steady erosion of public trust in government, especially at the levels of government farthest removed from the everyday lives of citizens. The constitution has become a favorite and frequently used policy-making tool because currently there is nothing to prevent initiated statutes from being amended by a simple majority of the legislature. By contrast, elected officials cannot change the constitution without voter consent. Addressing and reversing this erosion of trust is of primary importance to our future. Only then can we begin to consider ways to provide the flexibility necessary for our state and local governments to thrive and prosper in the 21st century global economy.

REBUILDING THE PUBLIC TRUST

Since the founding of our nation, our form of government has been based on a system of representative democracy. We look to our elected representatives to exercise leadership in the development and protection of our physical and human infrastructures—schools, roads, public safety, health care, environmental protection and higher education. Trust and accountability are the building blocks of effective representative government.

There is evidence over the past few decades of a growing lack of trust in our elected officials. Among the ways our lack of trust has been shown is through citizen-initiated constitutional amendments and term limits.

First, we have tied the hands of state and locally elected officials with increasingly strict limitations on their powers to budget, tax and spend—among the most critical tools of public policy and governance. Second, we have imposed term limits to restrict the amount of time elected officials may serve—in the process restricting our own ability to re-elect those we trust for leadership positions. Fiscal limitations vastly reduce the array of options policymakers can consider to address state and local priorities. Term limits reduce the experience and leadership needed to understand and navigate extremely complex problems.

The "unintended consequence" of these initiatives is that our elected officials are increasingly unable to resolve major fiscal policy issues. This, in turn, further erodes citizens' confidence in our elected representatives. Knowledgeable observers of Colorado's representative institutions believe that heightened polarization also has been an unintended consequence of these limits. Polarization leads to the appearance that politicians are able to do little more than bicker and posture over critically important issues which, in turn, causes the public to have less confidence in our

Better information leads to better decisions—for individual voters and for their elected representatives.

representative government, fosters the desire for even tighter controls and further fuels the downward spiral in public trust.

How can this spiral be reversed? We recommend a two-pronged approach. First, we increase accountability by providing more practical and accessible information to the public so that citizens can better evaluate the performance of their elected representatives. Second, we return to the voters the right to exercise a more targeted and effective tool for limiting terms through the ballot box. We believe eliminating rigid term limits will give voters the right to retain those elected officials who have earned their trust through demonstrated leadership and expertise, while allowing voters to replace those officials they feel are neither responsive nor effective.

BETTER AND MORE ACCESSIBLE INFORMATION TO THE PUBLIC

We make three recommendations to improve the public's ability to track and evaluate the value they receive for their tax dollars. First, information that is provided to the public should be clear, easily understood and focused on comparative performance information. Second, the information should be made available through an online citizen information system. Third, we recommend the establishment of an ongoing nonpartisan fiscal research and reporting center.

Provide Information to the Public that is Clear and Informative. With nearly 2,600 taxing entities and an array of complex governmental accounting systems, Colorado's decentralized structure of government makes it difficult to understand how much tax is paid, to whom it goes, how the money is used and what services are provided. Our examination of these problems has led to the conclusion that trust in government would be increased if the public could more easily understand which governmental agency provides the services and how much those services cost so they can evaluate the worth of services received for their tax dollars.

Each governmental agency in Colorado is required by law to produce a variety of detailed financial plans and reports, but most citizens are unaware of what reports are created or where those reports can be found. Further compounding the problem, these documents tend to be technical and difficult to understand. While the reports usually are presented at public meetings, these events often are not well-publicized or attended. These challenges must be overcome.

Many local governments in Colorado print copies of "budget briefs," a general non-technical summary of their annual financial plan, or budget, to make it easier for citizens to understand their goals. Performance measurement, an increasingly common practice in government, can help citizens understand how well their governments are managing public resources. Incorporating these practices into an annual performance report required of every governmental agency and public institution, and distributing that information to the public, would help reverse the spiral of mistrust by highlighting performance, or lack thereof.

The Panel recommends that all major state agencies, courts, public institutions, local governments and other public entities provide citizens with a clearly worded annual performance report covering, among other things:

- *The comparative performance of the entity benchmarked against similar units of government or institutions in terms of per capita revenues, service costs, subsidy levels, etc.;*
- *A description of principal results achieved by the entity;*
- *Information as to why the entity should not be consolidated with similar or overlapping governments or institutions.*

Create an Online Citizen Information System. As noted above, it is very difficult for taxpayers to know which unit of government is receiving what portion of their tax dollars, the purpose for which the funds are used, the services received and the results achieved, particularly in light of Colorado's multiple layers and highly decentralized system of government. Citizens pay sales taxes almost daily, income taxes (paid regularly through payroll deductions), property taxes (paid at least once annually, but often less visibly through mortgage escrow accounts) and specific ownership taxes paid annually with automobile registrations. Each of these individual tax streams supports different and at times multiple levels of government as well as a myriad of services within those levels. It is no wonder that most taxpayers do not know what they pay, to whom and for what.

We believe that improved transparency and access to this information can help reverse the continuing downward spiral of public trust. This is important for at least two reasons. First, citizens have a right to know what they pay, to whom, and for what; and second, governments are missing an opportunity to better inform the taxpayer about the value received for each tax dollar. Twenty years ago, communicating information about such a complex system would have been extremely cumbersome. Today, thanks to significant increases in communications and data management technologies, it is feasible to make such information available.

We believe that better information leads to better decisions—for individual voters and their elected representatives. To that end, *we recommend the development of an Internet-based, interactive taxpayer information system that will provide a taxpayer with an estimate of that individual's annual tax burden, as well as a summary of the programs and services at all levels of government that are supported by those tax dollars.* Such an application would provide the public with information about the linkage between revenues and expenditures for public programs.

Establish an Ongoing Fiscal Research and Reporting Center. We further recognize that Colorado's complex system of state and local government and active participatory democracy demand ongoing, nonpartisan research. Such research would allow a better understanding of emerging issues before they become crises, as well as provide a method to evaluate proposed changes to the current system. It is critical that we address systemic questions concerning the fiscal health and tax system in the state, as well as respond with well-researched information and analysis about specific fiscal policy measures.

As a means of implementing the multiple tax policy research functions necessary to provide clear information and analysis, *we recommend that an independent, nonpartisan, non-governmental organization be established to conduct ongoing research and provide regular updates to the public on matters related to Colorado's fiscal health, other significant trends affecting the state's economy and on proposed initiatives and major legislation relating to taxation and public spending.*

Other states such as Florida, Ohio and Tennessee have independent, nonpartisan governmental research groups who work to inform the public debate on issues of public tax policy. These groups complement rather than replicate the resources already available within state and local governments. In our system of combined direct and representative democracy, unique state-local interactions and multiple and overlapping limits and mandates that complicate the system of governance, ongoing research will contribute significantly to better inform the public, as well as its elected officials.

The goals of this organization should include:

- Examining the long-range impacts of proposed initiatives and major legislation relating to taxation and public spending and reporting to the public *prior* to any citizen referendum or legislative action;
- Performing a thorough tax burden analysis that addresses the distribution of burdens among economic sectors and individuals in Colorado. A better understanding of this will contribute to the development of a more efficient and equitable tax system for the state;
- Developing a careful and well-researched periodic evaluation of the manner in which Colorado's economy has changed and is likely to change in the coming years, and recommending ways to update our systems of financing public services to ensure that the current system remains productive and competitive in light of structural changes to the economy;
- Examining the structure of government in Colorado and recommending improvements, with a goal of maximum effectiveness, efficiency and citizen support.

ELIMINATE TERM LIMITS FOR ELECTED OFFICIALS

Colorado has a long tradition of instituting reforms to ensure that lawmaking is not the playground of special interests and that elected representatives are responsive to their constituents. Examples over the past 40 years include such laws as the Open Meetings Act (1968), The Sunshine Law (1972), and the GAVEL Amendment (1988 – *"Give A Vote to Every Legislator"*). These reforms have kept Colorado's system of state and local representative democracy relatively free from issues of fraud, conflicts of interest and other political scandals.

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SUMMARY OF PANEL RECOMMENDATIONS

CURRENT PROVISIONS TO BE RETAINED

The Colorado Constitution contains important fiscal policymaking requirements that should be retained.

The Panel strongly affirms the right of citizens to vote on new and increased taxes, the right of citizens to petition their government through the initiative process, the power of elected officials to allocate public funds and the requirement that our governments balance their budgets.

REBUILDING THE PUBLIC TRUST

In order to rebuild the public trust in government, better information needs to be provided to the public and elected officials need to be allowed time in office to develop expertise on complex fiscal issues.

The Panel recommends that all major state agencies, courts, public institutions, local governments and other public entities provide citizens with a clearly worded annual performance report covering, among other things:

- *The comparative performance of the entity benchmarked against similar units of government or institutions in terms of per capita revenues, service costs, subsidy levels, etc.;*
- *A description of principal results achieved by the entity;*
- *Information as to why the entity should not be consolidated with similar or overlapping governments or institutions.*

The Panel recommends the development of an Internet-based, interactive taxpayer information system that would provide a taxpayer with an estimate of that individual's annual tax burden, as well as a summary of the programs and services at all levels of government that are supported by those tax dollars.

The Panel recommends that an independent, nonpartisan, non-governmental organization be established to conduct ongoing research and provide regular updates to the public on matters related to Colorado's fiscal health, other significant trends affecting the state's economy and on proposed initiatives and major legislation relating to taxation and public spending.

The Panel recommends that the effectiveness and efficiency of representative democracy, and the right of voters to select representatives of their choosing, be restored by eliminating term limits for state and local elected officials.

CREATING FLEXIBILITY AND RESPONSIVENESS

State and local governments need to be flexible and adaptable in responding to the rapid pace of change in the 21st century.

The Panel strongly recommends that any future fiscal limits or mandates be statutory rather than constitutional.

Additionally, the Panel recommends that:

Detailed fiscal provisions be moved from Colorado's Constitution to statutory law, and that protections be created for these statutes so that they can be amended only under extraordinary circumstances.

Any index used in establishing limits or mandates be relevant to the revenue or expenditure affected.

The use of statutes rather than the constitution should be encouraged for fiscal provisions by making the following changes:

For all initiated measures, either constitutional or statutory:

- *Change the basis of the signature requirement for initiatives from votes cast for the secretary of state to votes cast for governor in the most recent gubernatorial election.*

For initiated statutory measures:

- *Require signatures equal to five percent of the total votes cast in the last state election for governor;*
- *Require a simple majority of voters to approve;*
- *Require a supermajority vote of the legislature to change any statutory measure after its enactment through direct democracy.*

For initiated constitutional measures:

- *Require signatures equal to 10 percent of the total votes in the last state election for governor;*
- *Assure a geographical distribution of those signatures by requiring that the proponents collect signatures equal to 10 percent of the district-wide vote for governor in a majority of the state's congressional districts (currently four of the seven districts);*
- *Require a supermajority of voters to approve.*

For referred constitutional measures:

- *Require a supermajority of legislators to refer a measure to the voters;*
- *Require a supermajority of voters to approve.*

OTHER IMPORTANT ISSUES THAT MUST BE CONSIDERED

Three of the most important other issues the Panel recommends be considered include: improving equity among taxpayers; addressing local and regional fiscal disparities; and developing strategies for public investment and cost avoidance.

Taxpayer Equity: There is a substantial disparity between the property taxes paid by business and by other taxpayers. Disparities in the burden of other taxes may exist as well. *Since both businesses and other taxpayers are beneficiaries of services provided by various levels of government, issues of fairness, as well as the future business climate and economic competitiveness of Colorado, require that taxes be equitably distributed.*

Fiscal Disparities: *The Colorado General Assembly and local governments should consider implementing the following recommendations:*

- *Share sales taxes regionally among local governments in order to mitigate resource disparities;*
- *Dedicate a portion of state funds for general revenue sharing to local governments;*
- *Expand regional cooperation to lessen the tax base competition between local jurisdictions.*

Investment and Cost Avoidance: There is an increasing tendency to think of all government expenditures simply as costs to be reduced. While there is much to be said for careful scrutiny of all public expenditures, thinking of taxes simply as something to be cut, rather than an investment to be optimized, is not wise public policy. This concentration on costs instead of returns takes the focus off government performance and achieving a return on taxpayer investments. From a policy perspective, it cripples the legislative and public dialogue about how governments or institutions will achieve their objectives. It also dampens the process of linking public resources to public outcomes. *For these reasons, elected officials should strategically identify budget investments that will produce a significant return for tax dollars invested, generate long-term public benefits, or avoid future costs.*

The most significant change resulting from term limits has been the loss of experience.

(continued from page 11)

Despite the fact that Colorado has one of the most open and fair systems of representative government in the nation, we also were at the forefront of the term limit movement. Oklahoma and California joined Colorado in 1990 as the first three of 21 states to impose term limits to date. Six of those 21 states have since eliminated term limits, either through state court or legislative action. Currently, 15 states have term limits on their elected officials.

Colorado voters adopted an eight-year term limit for state and federal elected officials via a constitutional initiative in 1990; a second initiative in 1994 added local officials. The language imposing term limits for local elected officials allowed for a local override by a vote of the people within that local governmental jurisdiction. Voters have used that option to eliminate or extend term limits for some local government offices across the state; however, that option is not available for state officials. The federal courts have voided term limits for federal officials by declaring that state-enacted term limits on federal officials conflict with the U.S. Constitution. Term limits, however, remain in place for state and local elected officials.

As we studied the effects of term limits in Colorado, we discovered they have not accomplished the goals originally intended by the proponents, but instead have weakened the effectiveness of representative democracy. For example, a stated goal of term limit supporters was to reduce "careerism" and get rid of long-serving but ineffective elected officials. While the public careers of some ineffective officials undoubtedly fell victim to term limits, the impact also caused the loss of many skilled and valued leaders.

A paper presented by the former director of the Legislative Council at a 2003 legislative symposium examined the length of terms for legislators newly elected since 1990 who had the opportunity to serve their full eight-year term of office under term limits. It showed that the average tenure for members of the General Assembly actually *increased* after the implementation of term limits. From 1960 through 1988, the election year before term limits were adopted, the average tenure was 5.2 years. Since 1990, the year term limits were enacted, the tenure increased to six years, an increase of 15.4 percent.

There also has been virtually no effect on another major goal of the proponents of term limits—the rate of turnover. According to a 2004 study conducted by Professor John Straayer of Colorado State University, the turnover rate averaged about 30 percent each election cycle prior to term limits. After an initial jump in 1998, the year term limits first went into effect, our rate has returned to about the same as before. Re-election of those seeking another term averaged 92 percent in the decade prior to the adoption of term limits in 1990, and reached 94 percent from 1992-2002. Nor has there been much change in the composition of the legislature based on the members' gender, ethnicity, education, occupation or age.

However, the most significant change resulting from term limits has been the loss of experience—especially that of legislative leadership. The following chart compares 1997, the year before legislators were forced from office by term limits, to 2003, five years after the impact of term limits was first felt. The turnover is felt most starkly in leadership and committee expertise.

Legislative Experience of Members of the Colorado General Assembly

Representatives with 6+ years of service, and Senators with 10+ in the House & Senate

Year	House	Senate
1997	18 of 65 members *(27.7 %)*	18 of 35 members *(51.4%)*
2003	8 of 65 members *(12.3%)*	9 of 35 members *(25.7%)*

Speaker of the House and President of the Senate: In the 18 years prior to 1998, there were two Speakers of the House, while three Senate Presidents served the prior 21 years. Since 1998, every Speaker and President has served no more than two years.

Joint Budget Committee: The turnover on the six-person Joint Budget Committee, the committee with the most influence on the day-to-day functioning of state government, averaged just one new member following each of the three election cycles prior to term limits. Continuity of membership on this important committee allowed for growth of teamwork, bipartisanship and detailed knowledge. Post-term limits, there were four new members in 1999; three new members in both 2001 and 2003; and four new members again in 2005 on the six-member committee.

While term limits have introduced new personalities, Professor Straayer's survey of a broad cross-section of legislative staff, lobbyists, legislators, members of the press and others who had in-depth knowledge of Colorado's legislature from before and after term limits identified significant problems. These close observers of Colorado's legislative process believe the consequences are visible and mostly negative. Four-fifths of those individuals surveyed believed that:

- Leaders are weaker;
- Partisanship is up;
- Civility and procedural order have suffered;
- The clout of lobbyists, staff and the governor has increased;
- Legislators are less inclined and able to address the state's major problems in a long-term fashion.

Rather than diversifying and reinvigorating Colorado's legislative body, the inflexible eight-year term limit has deprived it of experience and expertise, and deteriorated its norms, procedures and problem-solving capacity. A recent national study *(the "Joint Project on Term Limits")* reported that other states also have experienced many negative effects on the functioning of their state legislatures. As reported in the 2005 edition of ***The Book of States***, "Term limited legislatures report more general chaos, a decline in civility, reduced influence of legislative leaders and committees…." In sum, according to Professor Straayer, the data show clearly that term limits were designed to solve a problem that did not exist and, in the process, have weakened Colorado's system of representative government.

Recognizing that the voters have expressed their support for term limits, we carefully considered our recommendation. The studies convinced us that constitutionally imposed term limits, especially at the state level where there is no option for voter override, inhibit the learning of new officials and the continuity and effectiveness of legislative and executive leadership. Since we cannot elect those who cannot run, the long-established constitutional right of voters to make a choice at the ballot box also is restricted by term limits. From a private sector perspective, no business forces its employees and leaders to resign as soon as they reach the peak of their knowledge and performance. Therefore, *the Panel recommends that the effectiveness and efficiency of representative democracy, and the right of voters to select representatives of their choosing, be restored by eliminating term limits for state and local elected officials.*

CREATING FLEXIBILITY AND RESPONSIVENESS

Over the past few decades, Colorado's citizens increasingly have sought to place fiscal policy directives in the state's constitution. The state's flexibility and responsiveness have been significantly compromised, since amending these provisions of the constitution is a cumbersome, expensive and difficult process. We struggled with the issue of how to develop needed flexibility while continuing to honor the will of the people in restraining the fiscal powers of state and local governments. After much consideration, we recommend that this dilemma be addressed through three actions.

First, *we recommend that detailed fiscal provisions be moved from Colorado's Constitution to statutory law, and that protections be created for these statutes so that they can be amended only under extraordinary circumstances.* Options to accomplish this objective include convening a constitutional convention, individually addressing each provision to be moved in a series of constitutional amendments, or amending the constitutional single-subject requirement to allow for a package of amendments to be proposed. The second action is the creation of requirements that any newly proposed limits and spending mandates must meet in order to allow some flexibility. The third action is to revise the initiative process to maintain the role of the constitution as the broad framework of our system of government, and not as the vehicle of choice for detailed fiscal policymaking.

MOVE DETAILED FISCAL PROVISIONS FROM THE COLORADO CONSTITUTION TO STATUTORY LAW

The fiscal provisions to be removed from the state constitution or transferred into statutory law include, but may not be limited to:

- The State Debt Limit, (Article XI, section 3), enacted in 1876;
- The Gallagher Amendment, (Article X, section 3), enacted in 1982;
- The Taxpayers Bill of Rights (TABOR), (Article X, section 20), enacted in 1992;
- Amendment 23, (Article IX, section 17), enacted in 2000.

The State Debt Limit, enacted as a part of Colorado's original 1876 constitution, prohibits state government from incurring general obligation debt. General obligation debt is backed by the credit and taxing power of the issuing jurisdiction rather than a specific revenue source. Interest expenses for general obligation debt are normally reduced by pledging the "full faith and credit" of the issuing entity. Since general obligation debt is prohibited, other mechanisms have been devised for the state to incur debt. These mechanisms generally make repayment subject to annual appropriation by the general assembly, so the debt is not viewed as a legally enforceable obligation of the state.

For this reason, the bond market views these instruments as a higher risk, driving up the interest rate. These financing mechanisms have been used since the 1980s to finance some of the state's key capital construction investments, such as prisons, highways and higher education facilities. We concluded that for the last 25 years, the state constitutional debt limit has not prevented the state from incurring debt for major capital construction projects, but simply has served to increase financing costs to the state general fund. For this reason, it should be moved to state statute, where ways can be considered by the legislature to reduce its negative impact on the general fund.

The Gallagher Amendment provides for a mechanism to reduce the property tax valuation of residential property as growth occurs, but not commercial and other classes of property. The result is that although residential property comprises nearly 78 percent of the value of all taxable property in Colorado, it bears only about 47 percent of the tax burden. Under TABOR, mill levies cannot be increased to make up for the valuation reduction without a vote, so the property tax burden on residential properties is gradually reduced and the property tax revenue for many local governments is unable to keep pace with the rate of growth in property values. Property taxes are a major funding component of the state's Public School Finance Act, so the state must "backfill" this reduction in property taxes by increased general fund spending for schools. In addition, Amendment 23 requires per-pupil funding for public schools to increase each year. The Gallagher Amendment in combination with TABOR and Amendment 23 have teamed to increase state general fund appropriations for schools at rates greater than the rates of growth for the general fund, forcing reductions in other general fund appropriations.

The Taxpayers Bill of Rights (TABOR) limits all state spending, including general fund spending to a formula growth rate based on inflation and population. As explained above, this limit, coupled with the Gallagher Amendment and Amendment 23, results in a significant restriction of general fund flexibility.

Amendment 23 requires the state to increase per-pupil funding for the state's Public School Finance Act at the rate of inflation plus one percent through 2011, and at the rate of inflation each year thereafter. When combined with TABOR and the Gallagher Amendment, these three provisions interact to place the state general fund in a fiscal vise.

CREATE CONDITIONS THAT NEW LIMITS AND MANDATES MUST MEET

Once items are moved from the constitution to statutory law, it is critical that conditions be created to prevent the state from returning to a posture of inflexibility. To prevent this, *we strongly recommend that any future fiscal limits or mandates be statutory rather than constitutional.* The constitution should be reserved for broad statements of policy, with procedural detail placed in statutes. Fiscal limits and mandates must not be placed in the constitution. In addition to these parameters, *we recommend that any index used in establishing limits or mandates be relevant to the revenue or expenditure affected.*

MODIFY THE INITIATIVE AND REFERENDUM PROCESSES

Coloradans have an active history of direct democracy. Since 1910, the year the initiative and referendum process were adopted, there have been only six even-year elections at which voters were not asked to decide an initiated measure. Since 1980, every even-year election has included at least one initiated measure.

In the 25 years since 1980, Coloradans have amended our state constitution 47 times. By contrast, the U.S. Constitution has been amended only 27 times in more than 217 years.

The process of initiating ballot language requires collecting signatures sufficient to meet the state's mandated signature requirement. Every state that allows for initiatives requires the collection of signatures; however, the number of signatures varies from state to state. Colorado's signature threshold for constitutional initiatives of five percent of the votes for Secretary of State is the lowest in the nation when measured as a percentage of population.

Furthermore, among the direct initiative states, Colorado is the only state that does not maintain a different signature requirement for constitutional changes versus statutory changes. In our state, it is as easy to initiate constitutional amendments as it is statutory changes. Coupling this ease of amending our constitution with the general level of mistrust in government, it is no wonder that the majority of initiated measures are for constitutional change—and once language is in the constitution, the legislature cannot amend it.

Since 1980, 77 percent of all measures submitted to the voters in Colorado have been constitutional: of those, 53 percent passed. In the 25 years since 1980, Coloradans have amended our state constitution 47 times. By contrast, the U.S. Constitution has been amended only 27 times in more than 217 years, and 10 of those were passed at the same time as the Bill of Rights.

While we recognize and respect Coloradans' deeply held value for participatory democracy, we also recognize that numerous citizen-initiated constitutional amendments have had unintended consequences. Especially when they contain detailed fiscal limits and mandates that are more appropriate for statutory law, these amendments greatly impede the flexibility of representative government. To strike a balance between respecting direct democracy and the need for legislative flexibility, we recommend procedural changes to the process of direct democracy in the state, particularly when proposing constitutional measures.

Consistent with our recommendation concerning the preferred use of the statutes over the constitution—and with due respect for the tradition of direct democracy—we recommend changes be made to the citizen initiative process, particularly in the area of proposed constitutional change. Currently there is no incentive to initiate a statutory measure when it is procedurally equivalent to initiating a constitutional one, so the following recommendations seek to make the requirements for amending the constitution more stringent than those for statutory change, providing an incentive for initiated and referred measures to be statutory rather than constitutional.

For all initiated measures, either constitutional or statutory:

- *Change the basis of the signature requirement for initiatives from votes cast for the secretary of state to votes cast for governor in the most recent gubernatorial election.*

For initiated statutory measures:

- *Require signatures equal to five percent of the total votes cast in the last state election for governor;*
- *Require a simple majority of voters to approve;*
- *Require a supermajority vote of the legislature to change any statutory measure after its enactment through direct democracy.*

For initiated constitutional measures:

- *Require signatures equal to 10 percent of the total votes in the last state election for governor;*
- *Assure a geographical distribution of those signatures by requiring that the proponents collect signatures equal to 10 percent of the district-wide vote for governor in a majority of the state's congressional districts (currently four of the seven districts);*
- *Require a supermajority of voters to approve.*

For referred constitutional measures:

- *Require a supermajority of legislators to refer a measure to the voters;*
- *Require a supermajority of voters to approve.*

The state is operating in a 21st century economy with a mid-20th century tax system.

The change in the basis for the signature requirement from votes cast for secretary of state to votes cast for governor is consistent with requirements in other direct-initiative states. Because the gubernatorial race is the highest and most visible statewide race, it better reflects the number of active voters in Colorado.

It is important to note that the change to votes cast for governor as the basis for the signature requirement would result in an increase in the signature requirements for both statutory and constitutional initiatives. The table below summarizes the impact of that change based upon the 2002 election. If our recommendations had been in place at the time of the 2002 election, the current signature requirement for *statutory* initiatives would be 2,802 signatures higher—a 4.1 percent increase, and the signature burden for constitutional initiatives would have increased by 73,432. The increase in signatures for *constitutional* initiatives would have resulted from a combination of the change from 5 percent to 10 percent and the change of base from votes for secretary of state to governor.

OTHER IMPORTANT ISSUES TO CONSIDER

We believe that the process-oriented recommendations presented earlier hold the highest priority because, unless the structural problems in Colorado's government are addressed, dealing with urgent fiscal problems will be nearly impossible. This does not diminish the importance of also addressing fiscal problems. The panel has identified three priorities in fiscal policy that need to be addressed, including tax issues, resource disparity and development of a public investment and cost avoidance strategy.

Tax Issues

Colorado's state and local tax system is comprised of three major taxes: sales, property and income taxes. In addition, state and local governments also are financed through the imposition of a variety of fees. These taxes and fees have changed considerably in structure and relative importance over the past few decades.

Summary of 2002 Votes for Governor and Secretary of State and Resulting Actual and Recommended Signature Requirements

Votes cast for Governor	Votes cast for Secretary of State *(SOS)*	Current Requirement: 5% of votes for SOS	Statutory Recommendation: 5% of votes for Governor	Increase in Signature Requirement for Statutory Initiatives	Constitutional Recommendation: 10% of votes for Governor	Increase in Signature Requirement for Constitutional Initiatives
1,412,602	**1,356,561**	**67,828**	**70,630**	**2,802**	**141,260**	**73,432**

Source: Colorado Secretary of State.

Sales Taxes

- When the last comprehensive analysis of Colorado's public fiscal system was completed in the late 1950s, only two municipalities levied a sales tax in addition to the state's 2 percent tax; the highest combined rate in those two cities was 3 percent.
- Today there are 299 different sales taxes being levied, ranging from one-tenth of 1 percent to 5 percent, in 48 counties, 211 municipalities and 17 special districts; the overall rate (including the state's 2.9 percent rate) reaches 10.1 percent in one jurisdiction.
- Over the years, 67 separate exemptions from the state sales tax have been made. Local governments also have enacted some of these exemptions, but not others. The exemptions are estimated annually to total $538 million in decreased state revenue. They increase the complexity of administering the sales tax system and alter the distribution of tax burden among individuals and sectors in the state's economy.
- When the state sales tax was first introduced in 1935, a service tax also was enacted which imposed a levy on professional and personal services, but it was repealed in 1945. Services make up one of the fastest growing sectors of the economy, and sales taxes on services increasingly are considered in other states as a way to maintain the productivity of the system while reducing the regressivity of the sales tax.

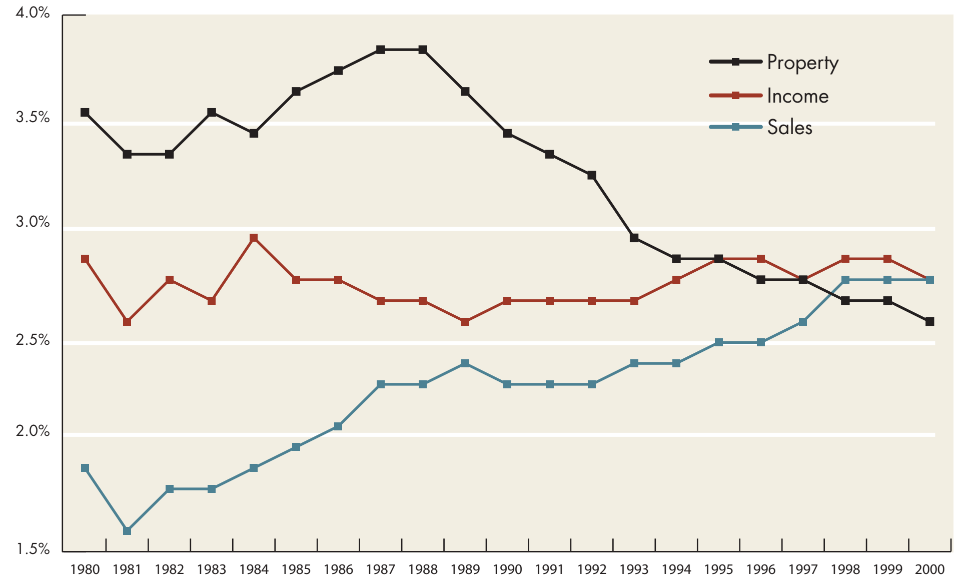
Property Taxes

- The property tax share of total municipal tax revenue has declined from 28 percent in 1985 to 17 percent in 2001. (During that same period, the share of municipal sales tax revenue increased from 64 percent to 72 percent.)
- Colorado is thought to have a low residential property tax burden compared to other states, and the "Gallagher" amendment has caused a shift in the burden from residential to other classes over the past 25 years. Given the same value, a residential property pays about one-fourth of the tax burden of a nonresidential property.
- Residential personal property and business inventory have been exempted from the tax, while business-owned personal property remains taxable, discouraging industries such as manufacturing that make heavy use of equipment.

Income Taxes

- Income tax is the major source of state general fund revenue (52 percent), more than double that of the sales tax.
- Income tax is more volatile than other taxes in responding to economic changes, growing faster in good times and falling more precipitously in bad.
- Colorado's definition of net taxable income is largely based on the federal definition, so when the federal definition is modified, Colorado's income tax collections either rise or fall, depending on the nature of the federal change, without any state direction or control.

THREE MAJOR TAXES AS A PERCENT OF PERSONAL INCOME:
BY TYPE OF TAX
YEARS 1980-2000



Source: Colorado Department of Revenue, Division of Property Taxation, Division of Local Government, CPEC, Bureau of Economic Analysis - revised income, September, 2004.

There are dramatic disparities in available tax base resources among Colorado counties.

User Fees and Taxes

- There is a need to evaluate the impact of user fees on individual and business taxpayers.
- User fees have grown considerably over the last 25 years to replace tax revenue that is bound by the various statutory and constitutional limits.

Little is known about how these changes have affected the structure and funding of state and local governments. Essentially, the state is operating in a 21st century economy with a mid-20th century tax system. Taxes may serve as either incentives or disincentives to economic growth; without careful attention, disincentives often emerge. Over time, the failure to modernize the tax system to match the emerging structure of the economy will contribute to these disincentives and weaken our state's ability to compete.

The Panel concluded that Colorado's state and local tax system needs to be examined to determine how it should be modified to meet the goals of *equity* in the distribution of the financial burden of government on citizens and among businesses; *efficiency* in minimizing negative effects of the tax system on the economy; and *productivity* in generating sufficient tax revenues with a minimal administrative burden on the taxpayer. There is a substantial disparity between the property taxes paid by business and by other taxpayers. Disparities in the burden of other taxes may exist as well. *Since both businesses and other taxpayers are beneficiaries of services provided by various levels of government, issues of fairness, as well as the future business climate and economic competitiveness of Colorado, require that taxes be equitably distributed.*

It has been more than 10 years since any study has been done to examine Colorado's state and local tax burdens. A *comprehensive* analysis of Colorado's structure of state and local government and taxes has not been done in nearly 50 years. To our knowledge, there has never been an examination of the total tax burden on and among businesses.

ADDRESS LOCAL RESOURCE DISPARITIES IN FUNDING ESSENTIAL SERVICES

There are dramatic disparities in available tax base resources among Colorado counties—about a 20-to-1 disparity in per capita county tax bases. More significant resource disparities are suspected among city governments, and the result is a state where regions vary significantly in the level of core public services available to citizens. Many other states mitigate these local differences through a state government revenue sharing system. With the notable exception of K-12 school funding, Colorado does very little at the state level to mitigate such differences.

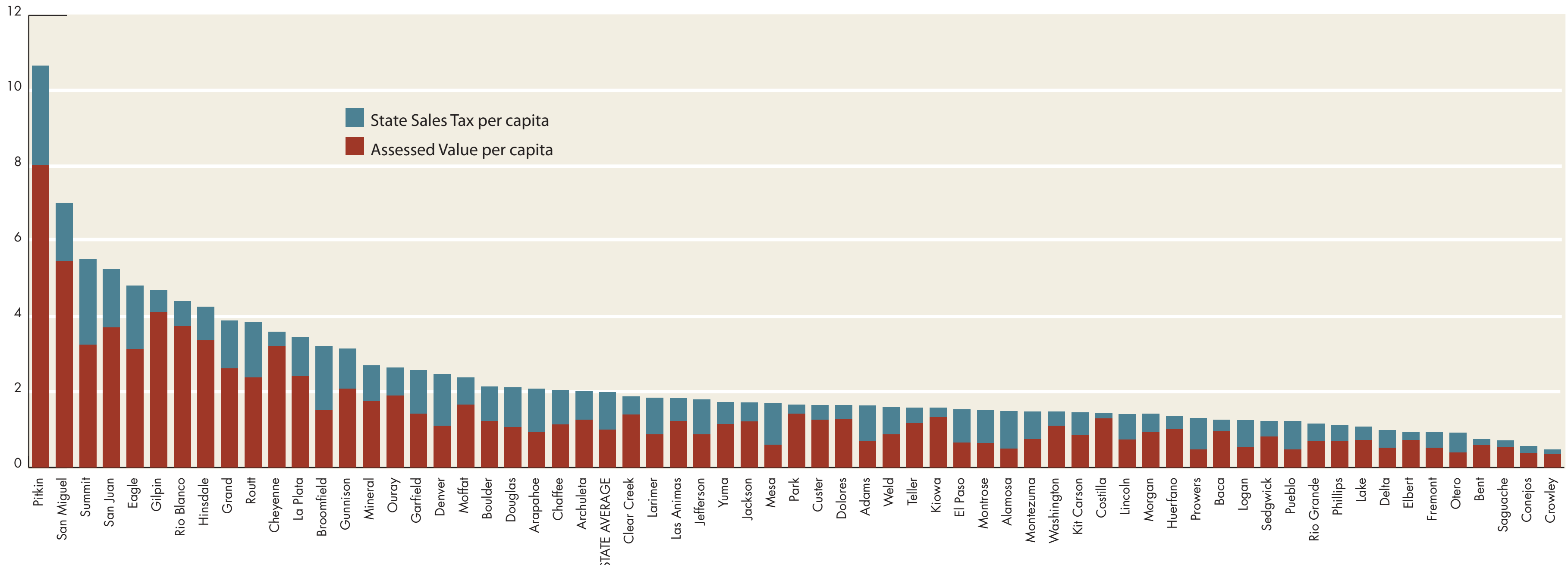
These disparities are further exacerbated by the degree to which municipal government in the state is reliant on locally levied and collected retail sales taxes. As a result of sales tax revenue dependence, fierce competition exists among municipalities for the tax base brought about by new retail developments. This frequently leads to annexation battles, poor land use planning between jurisdictions, and in some cases, sprawl and lawsuits.

There are ways to lessen this winner-take-all practice. Several local governments have entered into intergovernmental agreements for revenue sharing. This arrangement usually has been between a county and municipalities within its boundaries involving county sales taxes generated within municipalities. Recently, some municipalities have implemented sales tax revenue sharing through intergovernmental agreements on revenues generated within specific areas. These agreements have attempted to mitigate sales tax base competition. If this practice were encouraged, more efficient land use patterns could emerge, reducing subsequent infrastructure costs, and perhaps beginning to mitigate some of the resource disparities.

The Colorado General Assembly and local governments should consider implementing the following recommendations:

- *Share sales taxes regionally among local governments in order to mitigate resource disparities;*
- *Dedicate a portion of state funds for general revenue sharing to local governments;*
- *Expand regional cooperation to lessen the tax base competition between local jurisdictions.*

COUNTY ASSESSED VALUE AND SALES TAX BASE:
INDEX BY STATE AVERAGE
YEAR 2003



SOURCE: Colorado Department of Property Taxation and Department of Revenue, 2003.

Concentrating solely on tax levels instead of returns on public investment takes the focus off government performance.

DEVELOPMENT OF PUBLIC INVESTMENT AND COST AVOIDANCE STRATEGIES

In recent years there has been significant publicity about cuts in state programs due to the recession. Many of the cuts have adversely affected those who are most vulnerable. Additionally, from a public investment point of view, many of these expenditure cuts have come from areas of the budget where investing now results in long-term public benefits and avoids more substantial spending in the long run.

Many of the cuts have been in programs that encourage individuals to become productive members of society. Investments in early childhood care and education, K-12 and higher education pay handsome returns in helping to build the productive workforce sought by business. Expenditures on preventive services, such as immunizations, substance abuse treatment, mental health services, community alternatives to incarceration of juveniles, probation supervision and in-home care for persons with disabilities have long-term fiscal and societal benefits. They also help avoid the substantial future costs to support these individuals later in life through welfare, incarceration or more expensive medical care.

When the economy falters and revenues fall, funding for other programs often takes precedence. For example, during the budget process, state spending on prisons and matching funds for mandated Medicaid services take priority. Unfortunately, cutting investments in other programs that have a long-term benefit to the state creates even greater future governmental expenses. The connection of current spending to investment and future cost avoidance is not always obvious, but must be considered to provide future benefits that far outweigh the initial expenditure.

There is an increasing tendency to think of all government expenditures simply as costs to be reduced. While there is much to be said for careful scrutiny of all public expenditures, thinking of taxes simply as something to be cut, rather than an investment to be optimized, is not wise public policy. This concentration on costs instead of returns takes the focus off government performance and achieving a return on taxpayer investments. From a policy perspective, it cripples the legislative and public dialogue about how governments or institutions will achieve their objectives. It also dampens the process of linking public resources to public outcomes. *For these reasons, elected officials should strategically identify budget investments that will produce a significant return for tax dollars invested, generate long-term public benefits, or avoid future costs.*

THE ROAD AHEAD

MEETING THE CHALLENGE

We recognize that the recommendations made in this report do not follow the most popular lines of thinking in the state today, but to capitalize on the many advantages to attain a bright future for Colorado, hard decisions must be made and politically difficult actions taken. We also recognize that while the legislature must play a leading role in removing the impediments to a bright future, the business community and the citizenry must also be fully engaged in the process. A strong nonpartisan effort uniting all of the regions of our vast and diverse state will be required to accomplish what must be done. The task is daunting, but Colorado has not become the place we all love by shrinking from a challenge.

The stakes are high. Failure means that our state will be relegated to a place of mediocrity—an unacceptable legacy. While the task will be difficult, the result will benefit generations of Coloradans for years to come. We must take action.

OUR THANKS

We wish to thank the University of Denver, the Chairman of its Board of Trustees Chancellor Emeritus Daniel L. Ritchie, and Chancellor Robert D. Coombe, for their sponsorship and support of the Panel during the past year. In addition, we are grateful for the financial contributions made by the following foundations:

- *Bonfils-Stanton Foundation*
- *Castle Rock Foundation*
- *The Denver Foundation*
- *Dobbins Foundation*
- *Donnell-Kay Foundation*
- *Joseph Henry Edmondson Foundation*
- *Gates Family Foundation*
- *David and Lucille Packard Foundation*
- *Piton Foundation*
- *Rose Community Foundation*

By contributing to the Panel's efforts, these Colorado charitable foundations recognize the importance of long-term analysis of Colorado's past and present, as well as the need for realistic planning for the future. Colorado is fortunate to have an active and dedicated not-for-profit sector as a full partner in its deliberations on its future.

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