BRIEFED BY THE BELL: **FISCAL POLICY**

The Issue

Colorado's economy is flourishing — low unemployment rates continue as our state attracts more talent and investment from all corners. Even still, Colorado has real fiscal problems, spurred by constitutional measures put in place more than two decades ago. These provisions — including the Taxpayer's Bill of Rights (TABOR) — have made funding for public services, like education, housing, and transportation, extremely difficult.

Because of TABOR's constitutional prohibition on the legislature's ability to raise taxes, the Gallagher Amendment that makes property tax cuts the norm, and our low and regressive state tax system, too many public programs have atrophied.

According to Governor Hickenlooper's 2018-2019 budget request, "From calendar year 2000 through 2016 the combination of inflation and population growth totaled 70.5 percent, compared with General Fund revenue growth (converted to calendar year) of 58.2 percent." This means our revenues have not kept pace with our economic growth, leaving the state in a fiscal hole.

The consequences of this underfunding aren't abstract. They impact families in very real ways that have a direct impact on household budgets:

- Half of Colorado school districts are on four-day weeks and Colorado teachers rank 46th in the nation in average pay, according to the National Education Association
- Colorado's transportation needs are projected to exceed its revenues by $25 billion over the next 25 years
- About one-third of 4-year-old students who qualify for Colorado Preschool Program aren't served because of lack of funding
- Colorado families pay twice as much for tuition costs at public colleges and universities than they did in 2000

The Facts

- The amount of Colorado state General Fund spending as a share of the overall economy has decreased by about 20 percent since the 1990s
- At 3.7 percent of the overall economy, General Fund spending in 2017-2018 on state services such as transportation, education, and health care, is lower than nearly every other non-recessionary year
- Coloradans in the bottom 20 percent of income pay an effective state and local tax rate of 8.7 percent, while those in the top 20 percent pay an effective rate of only 4.6 percent
- According to the Colorado Fiscal Institute, the average tax rate, including state and local taxes, on middle-income families — those earning between $42,000 and $62,000 annually — is 8.5 percent, about two times the rate of the wealthiest Coloradans

Education funding is at the center of much of this. Because local property tax revenue has gone down, in part due to the Gallagher Amendment adopted in 1982, schools are now largely funded by state taxes, but the amount required has squeezed out other important services that rely on state funding.

In 2010, the state enacted the "budget stabilization factor," formerly known as the "negative factor," to cut per-pupil funding after adjusting for "factors" in the school finance formula as a method to balance the state budget. From 2010-2018, $6.69 billion has been cut from school funding, and despite efforts to reduce this amount, the state is still $672 million short in FY 2018-2019.

Due to tax revenue restrictions, it has become extremely difficult to close this gap and support the many other priorities that need state funding. Another challenge worth highlighting is the state's inability to keep all of the tax revenue it receives due to TABOR's revenue limits.

If revenue collected by the state is above the limit set by TABOR, as revised by Referendum C (discussed below), then this amount is returned to taxpayers in the form of small rebates. Given that the state has a difficult time funding its current obligations — especially given our low and relatively regressive tax rates — it's especially harmful that Colorado cannot even keep all of the revenue it collects under its existing tax rate and must make cuts to services that are not only needed now, but in the future.

Next fiscal year it's expected that the state will exceed TABOR revenue caps and begin to issue rebates. Under state law, these rebates will go to counties, school districts, and special districts to offset their loss in property taxes associated with the senior homestead and disabled veteran property tax exemptions.

The Solutions

The conversation about our fiscal challenges cannot solely revolve around TABOR. The arbitrary limits and rules established in 1992 help the wealthy pay less in taxes and ensure Coloradans get less from their government, but there are a number of different ways to improve our situation. The solutions below focus on two different approaches. The first are actions we can take within the current status quo; the second are ways to reimagine the system that allows Colorado to adequately fund public priorities and enable all Coloradans to thrive.

Under the Status Quo

Stop Cutting Taxes: Colorado doesn't have enough revenue to properly provide important services, like education, transportation, and health care. Cutting taxes only reduces the state's ability to fund those and other services. In 2000, Colorado cut income tax rates from 5 percent to the current 4.63 percent. According to Governor Hickenlooper's FY 2018-2019 budget request, the state was left with $610 million less in General Fund revenues during FY 2016-2017 as a result of the tax cuts.

The 2001-2003 recession depleted revenues even further and put the state in an enormous hole that it was just starting to dig out of when the Great Recession hit in 2008. Funds lost due to the tax cuts could have gone to education, transportation, and other crucial public services. If we continue to cut taxes, the next recession — whenever it happens — will put us in an even deeper hole.

Raise the Referendum C Cap: Referendum C, passed by Colorado voters in 2005, has significantly softened the roughest edges of TABOR by allowing the state to retain more revenue for public investments. The Ref C cap is tied to the highest revenue received between 2005-2010, adjusted for inflation and population growth.

To get an agreement to not count revenue from the Hospital Provider Fee under the TABOR limit, the legislature cut the Ref C cap by $200 million in 2017. This revenue should never have been counted toward the TABOR limit in the first place and we should restore the Ref C cap to its voter approved level.

We should also tie future adjustments in the Ref C cap to changes in Colorado's Total Personal Income, a measure of state economic growth, rather than inflation and population growth. Tying the cap to a measure of economic growth means it more accurately reflects our ability to support needed public investments.

Adopt Targeted Tax Increases to Fund Important Priorities: Every election season there are measures on the ballot to help plug holes in the state's budget. While not every tax increase and funding opportunity makes sense, we should be looking at ways to have smart and targeted ways to increase revenue for education, health care, transportation, and other important priorities for Coloradans. The new revenue streams help, but unless the cap on state revenues is lifted, the state will be in the position of cutting some services while expanding others.

Reimagining Colorado's Fiscal Policy

Abolish Bans on Certain Tax Increases: There are particular taxes banned by TABOR. For example, the real estate transfer tax cannot be raised above where it stood in January 1993. Many states use these taxes to fund affordable housing and other land-use policy. Even as many Colorado cities face housing crises, this tax cannot legally be raised without a constitutional amendment. Increasing it from .01 percent, where it currently stands, to 0.1 percent could raise $55.6 million of state revenue to be used to fund a state housing trust fund. Allowing some taxes to be raised and not others isn't smart public policy, especially when some of these taxes could be used to fund important priorities, like affordable housing.

Remove the Ban on a Progressive Income Tax: Part of TABOR that has led to significant income inequality in our state is the ban on a progressive income tax. Many people are unaware that enshrined in the Colorado Constitution is a prohibition on income tax rates that rise with income. Currently, Colorado has a flat tax rate of 4.63 percent for all Coloradans. But 4.63 percent is much more of burden for those at the low end of the income spectrum than those at the top.

Research shows we could adequately fund more public programs within the state by reducing tax rates for low- and middle-income people and raising rates for those at the very top. That would lead to better funded services, like education, child care, and health care which help people advance economically, and reduce inequality throughout the state. However, we cannot even consider doing this until the progressive income tax ban is lifted.

Allow the State to Keep Revenue It Has Collected: An outdated formula determines how much revenue the state gets to keep. If more revenue than that is collected, taxpayers could receive small tax rebates. Of course, this benefits those at the top significantly more than those at the bottom. Colorado should be able to retain all of the revenue it collects based on the current tax system to fund core public services that broadly benefit everyone in the state. In order to make this happen, we need to remove the TABOR cap on state revenues.

Give Legislature Ability to Raise Taxes: Electing a democratic representation of our collective views is why we entrust legislators to do the people's business. However, Colorado representatives have their hands tied — they cannot raise taxes and can only reduce them. It doesn't make policy or economic sense to have one area off limits to legislators, especially as they look to improve our state for the future. There are many critical areas where state revenue is spent, and it's up to communities to let their representatives know what's needed. In some cases, more revenue might be necessary, and our legislature should have that option. Until that's the case, the ledger will be stacked in favor of tax cuts for people who don't need them.

The Takeaways

- TABOR hamstrings Colorado's ability to make public investments that benefit all Coloradans
- Investment in state services are near historic lows compared to the growing economy
- Due to the state's largely regressive tax rates, those in the lower income tax brackets pay much more of their money in taxes than those in the top tax brackets
- Changing parts of TABOR need to be part of the solution, we should raise the current caps, and look at targeted tax increases to help fund important services

The Bottom Line

Colorado is growing because people value the Colorado way of life, but with that lifestyle comes certain challenges. Policies adopted more than two decades ago haunt our state, making things difficult for many families. To serve all Coloradans, we need to invest in our future and our state. Doing so will fulfill the real promise of Colorado and all Coloradans. To do this, we need real changes to our tax structure, starting by making it less regressive and more tailored to the needs of today.