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MEMORANDUM

September 21, 2015

TO: Interested Persons
FROM: Kate Watkins, Senior Economist, 303-866-3446
SUBJECT: State Revenue Changes and the Colorado State Budget

Summary

This memorandum provides an overview of how changes in tax and fee revenue impact Colorado's state budget. Pursuant to the Taxpayer Bill of Rights (TABOR) Amendment, the State of Colorado is limited in the amount of revenue from taxes and fees that it can retain and spend. The TABOR Amendment requires voter approval for tax increases, while fees can be changed by the state legislature without voter approval.

Tax and fee revenue changes impact the state budget differently. These differences influence the availability of moneys for general operating expenditures.

The TABOR Limit

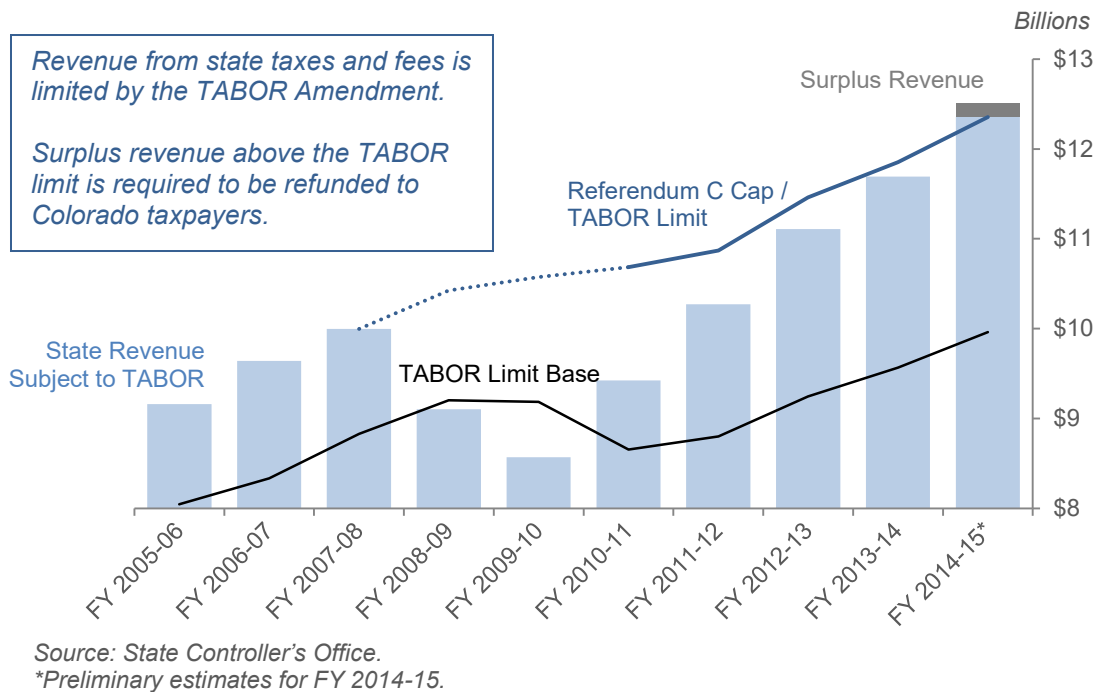
The **TABOR Amendment**, which was approved by voters in 1992, limits the amount of revenue the State of Colorado can retain and spend. The TABOR limit "base" is equal to the lesser of the prior fiscal year's revenue limit grown by Colorado inflation and population growth.¹ **Referendum C**, which was approved by voters in 2005, allows the state to retain and spend an amount of revenue above the TABOR limit base. This amount is limited by the Referendum C "cap," which grows by inflation plus population growth from FY 2007-08 revenue subject to TABOR.²

Surplus revenue in excess of the Referendum C cap must be refunded to Colorado taxpayers. The money is refunded from the state's general operating fund, known as the "General Fund." Revenue subject to TABOR, the TABOR limit, and surplus revenue above the limit are shown for the past ten fiscal years in Figure 1.

¹ Colo. Const. art. X, § 20.

² Section 24-77-103.6, C.R.S.

Figure 1
Revenue Subject to TABOR and the TABOR Limit



Voter-Approved Tax Increase

The TABOR Amendment requires voter approval for tax increases. Fees can be increased by the state legislature without voter approval. Voter approval is also required to increase the TABOR limit, which constrains state revenue from both taxes *and* fees.

Tax versus Fee Revenue

Most state tax revenue goes to the General Fund, including revenue from state individual and corporate income taxes, sales and use taxes, and excise taxes on liquor, cigarettes, and tobacco (Figure 2). General Fund revenue is spent on general operations, including funding for K-12 education, health care, corrections, and higher education.

Most fee revenue is collected in a number of different cash funds, where it is held for spending on specific programs as required by state law. Cash funds also receive revenue from certain earmarked taxes, including gasoline, severance, marijuana, and gaming taxes. Transportation-related fees and taxes represent the largest share of cash fund revenue. These sources of revenue are required to be spent on transportation-related projects.³

³Colo. Const. art. X, § 18.

Figure 2
Revenue to and Spending from the General Fund and Cash Funds



Sources:

* Preliminary FY 2014-15 estimates of revenue subject to TABOR from the State Controller's Office.

† Based on budgeted expenditures for FY 2014-15 Appropriations Report published by Joint Budget Committee Staff.

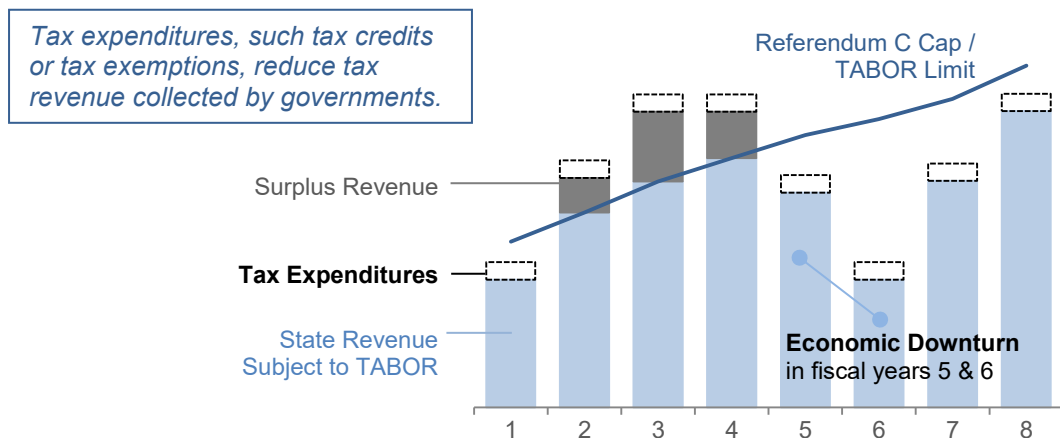
** Cash fund revenue is by law dedicated to specific programs.

Tax Expenditures

Tax expenditures include tax credits, deductions, subtractions, and exemptions. They reduce the amount of taxes owed by taxpayers, thereby reducing the amount of tax revenue collected by federal, state, and local governments.

In a surplus revenue situation, tax expenditures reduce the amount of the TABOR surplus and subsequent refund to taxpayers, as illustrated in years 2, 3, and 4 in Figure 3. When revenue is below the TABOR limit, tax expenditures reduce the amount of revenue available to be spent on state operations. This is likely to occur during an economic downturn, when tax revenue declines, as illustrated in years 5 and 6 in Figure 3.

Figure 3
An Illustration: Tax Expenditure Impacts on Revenue



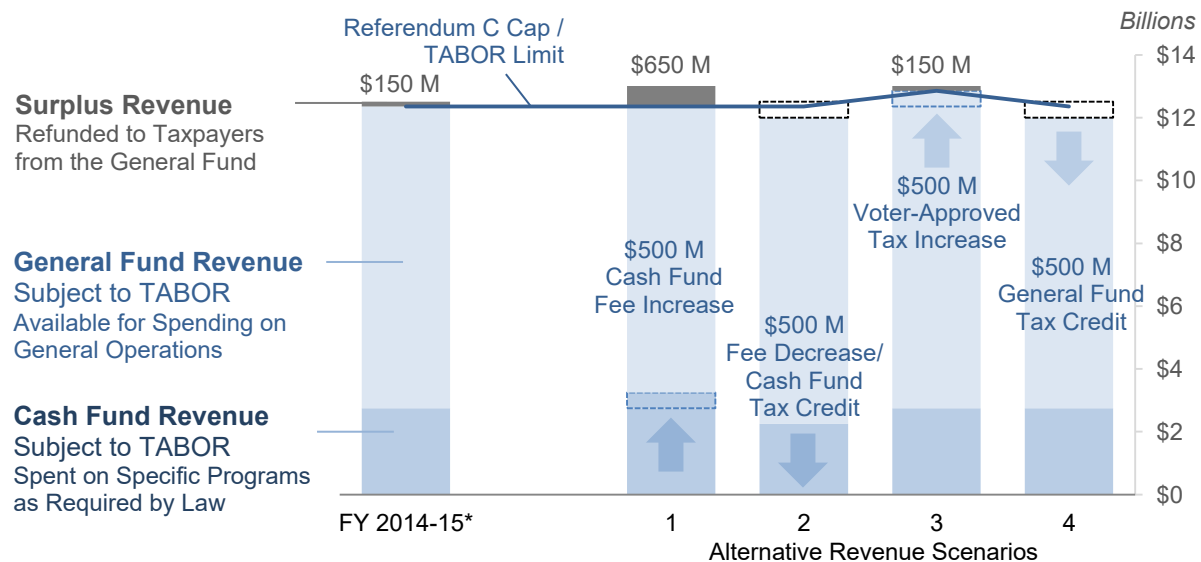
This figure is for illustrative purposes and does not reflect actual state revenue or tax expenditures.

Tax versus Fee Revenue Changes and the Budget

Tax and fee changes have different budgetary impacts. A change in cash fund revenue changes the availability of General Fund revenue in a TABOR surplus situation. If the state legislature increases fees but does not receive voter approval to retain the additional revenue, the state will be required to refund an amount equal to the fee revenue increase from the General Fund. In other words, when cash fund revenue increases, the availability of General Fund revenue decreases.

To illustrate these dynamics, Figure 4 provides four hypothetical scenarios compared to preliminary estimates of revenue and the TABOR surplus of \$150 million in FY 2014-15. A narrative explanation of each is provided below Figure 4.

Figure 4
Alternative Revenue Scenarios to FY 2014-15



	Revenue Increase	Revenue Decrease
Cash Funds	Scenario 1: Fee Increase If the state legislature had increased fees to cash funds by \$500 million in FY 2014-15, the TABOR surplus and subsequent refund would have been \$500 million larger. Because refunds are paid from the General Fund, this would have reduced available General Fund revenue by \$500 million.	Scenario 2: Fee Decrease/Tax Expenditure If fees had been decreased by \$500 million, this would have reduced revenue below the TABOR limit, eliminating the TABOR refund. This scenario would make \$150 million in General Fund revenue available to the budget. A \$500 million cash fund tax expenditure, such as a tax credit, would have the same impact as a fee decrease.
General Fund	Scenario 3: Voter-Approved Tax Increase If voters had approved a \$500 million tax and TABOR limit increase for FY 2014-15, the surplus would have remained at \$150 million, and the state would be allowed to retain \$500 million in additional revenue for general operations.	Scenario 4: General Fund Tax Expenditure A tax expenditure reducing General Fund revenue by \$500 million in FY 2014-15 would have eliminated the TABOR surplus and would have reduced moneys for general operations by \$350 million.